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Impact of Overseas Private Investment Corporation Activities on U.S. Employment

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Comptroller General
of the United States

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To the President of the Senate and the
Speaker of the House of Representatives

The Overseas Private Investment Corporation Amendments Act of 1985 (Public Law 99-204) requires the General Accounting Office to determine the impact of the Overseas Private Investment Corporation's activities on employment in the United States. This report responds to the legislative requirement.

The Overseas Private Investment Corporation is a U.S. government agency established to encourage and facilitate private U.S. investment in developing countries by providing political risk insurance and loans and loan guaranties. Existing legislation directs the Corporation to decline assistance to proposed overseas investments if it determines that they are likely to have significantly adverse impacts on U.S. employment.

We are sending copies of this report to the President of the Overseas Private Investment Corporation; the Administrator of the Agency for International Development; the Director of the Office of Management and Budget; the Secretaries of State, Labor, Commerce, and the Treasury; and the Chairman of the International Trade Commission.

Frank C Conahan

for Charles A. Bowsher
Comptroller General
of the United States

Executive Summary

Purpose

The Overseas Private Investment Corporation (OPIC) is a U.S. government agency established to encourage and facilitate private U.S. investment in developing countries by providing loans and political risk and loan guaranty insurance. OPIC seeks to complement the development assistance objectives of the United States while supporting U.S. economic interests. Existing legislation directs OPIC to decline assistance to proposed overseas investments if OPIC determines that they are likely to have significantly adverse impacts on U.S. employment.

The Overseas Private Investment Corporation Amendments Act of 1985 (Public Law 99-204) requires GAO to determine the impact of OPIC activities on employment in the United States. This report responds to the legislative requirement and examines

- the direct impact of selected OPIC projects on employment in the United States and
- OPIC's methodology for determining, evaluating, and quantifying the effects on U.S. employment of OPIC-assisted projects, including procedures for screening and monitoring projects that may adversely affect U.S. employment.

Background

Since 1971, OPIC has issued some $29 billion in political risk insurance coverage and about $1.1 billion in direct loan and guaranty commitments to 2,100 investment projects in more than 80 developing countries. OPIC has assisted investments abroad in agribusiness, light industry, high technology, sales and distribution, and service banking. Investments assisted by OPIC in 1985 represented less than 5 percent of total U.S. private investments abroad.

OPIC screens proposed offshore investments prior to granting assistance and monitors ongoing approved projects to determine development effects on the host country and to help ensure that there will be no significantly adverse impact on U.S. employment. Increases in U.S. employment resulting from OPIC-assisted overseas projects are among the major benefits cited by OPIC in annual reports to the Congress.

Results in Brief

GAO found that some OPIC-assisted projects have direct negative impacts on U.S. trade and potentially negative impacts on U.S. employment. OPIC's methodology for computing the economic impact on the United States of the projects it assists obscures the direct effects of these projects (effects caused by trade flows directly to or from the overseas

project) and results in overly optimistic reports to the Congress regarding the magnitude of economic benefits to the United States. OPIC needs comprehensive policies and procedures for use in its project screening and monitoring functions.

Principal Findings

Employment Impact

GAO calculations, using investor application data, showed that the direct effects on U.S. employment of 20 of 33 projects GAO examined could have been expected to be potentially negative. (See p. 40.) In addition, responses to a GAO questionnaire show that the 1985 operations of projects that OPIC had approved in 1981 and 1982 had a net potentially negative direct effect on employment of about 2,100 employee-years. Fifteen of the 32 projects that continued to trade with the United States in 1985 were producing a direct negative effect on U.S. trade and a potentially negative effect on U.S. employment. (See pp. 45-46.)

It is prudent for OPIC—in its analyses of proposed overseas projects—to make certain assumptions concerning the possible effects of a project. However, when OPIC uses these assumptions to mathematically compute the effects on U.S. trade and employment of a proposed project, it obscures the direct adverse effects of a project. For example, OPIC may assume that if it does not assist a proposed U.S. investor project, the goods of a hypothetical foreign competitor will replace U.S. domestic production and displace U.S. sales to other countries. OPIC uses this assumption to justify mathematically offsetting (reducing or cancelling) any adverse direct effects on trade and employment of the proposed project. OPIC does not report that the direct effects of the project and those of a hypothetical alternative are being combined. Thus, the Congress and other interested parties may be misled concerning the magnitude of U.S. economic benefits from OPIC-assisted projects. (See pp. 32-37.)

Other problems in OPIC's methodology include (1) obscuring annual effects on employment of project operations by combining them with the effects of project start-up procurements, (2) not considering all pertinent exports to the United States, and (3) using inappropriate labor-output per worker ratios in estimating employment. (See pp. 38-40.)

Screening and Monitoring

GAO identified weaknesses in OPIC's ability to screen out projects that could have adverse economic effects on the United States. For example,

- OPIC lacked formal guidance for the screening process, which was often done without adequate documentation;
- little contact occurred between OPIC and labor unions, trade associations, and sometimes the Department of Labor; and
- inadequate attention was given to Labor Department job loss data when OPIC evaluated proposed projects and monitored ongoing projects. (See pp. 19-24.)

The usefulness of OPIC's monitoring of ongoing projects is limited because

- results of monitoring are inadequately documented and apparently are not systematically used to improve the screening process or to determine if U.S. employment has been adversely affected and
- OPIC has not determined the appropriateness of and circumstances for discontinuing assistance to future approved projects whose operations are found to have adverse impacts on the U.S. economy. (See pp. 24-28.)

Recommendations

GAO recommends that the President of OPIC, in consultation with the Administrator of the Agency for International Development,

- develop formal policies and a comprehensive system for OPIC's screening and monitoring functions, including a methodology that more clearly and accurately estimates the direct economic effects on the United States of proposed projects and calculates the actual effects of ongoing projects and
- in OPIC's annual reports to the Congress on newly approved or ongoing projects (1) report aggregate positive trade and employment effects on the United States (without offsetting assumptions and alternatives) separately from aggregate results of projects with expected negative impacts (without offsetting assumptions and alternatives) and (2) report separately the economic effects on the United States of any alternatives and assumptions considered in OPIC's analyses.

GAO's report also contains other recommendations to improve OPIC's screening and monitoring methodology and associated procedures. (See pp. 54-55.)

Agency Comments

The Overseas Private Investment Corporation did not agree with GAO's conclusions and recommendations, characterizing them as irrelevant to its operations. OPIC stated that no changes are needed in screening and monitoring procedures. GAO is concerned, however, that existing OPIC procedures provide only limited assurance that an adequate determination has been made to show that no significantly adverse effects on the United States would occur or are occurring as a result of OPIC-assisted investments.

OPIC also stated that it disagreed with GAO's recommendation to improve its reporting to the Congress because it believes current reports present fair assessments of project benefits. To the contrary, GAO notes that OPIC's methodology for mathematically computing the economic effects on the United States obscures the direct adverse effects of the projects it assists. Unless its methodology is clarified in its reports to the Congress, OPIC's claims of project benefits to the United States can be misleading. Accordingly, GAO believes its recommendations remain valid. (See pp. 52-55.) The full text of OPIC's comments is in appendix III.

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Abbreviations

AFL-CIO	American Federation of Labor and Congress of Industrial Organizations
GAO	General Accounting Office
NSIAD	National Security and International Affairs Division
OPIC	Overseas Private Investment Corporation
TAA	Trade Adjustment Assistance

Introduction

The Overseas Private Investment Corporation (OPIC) was established in 1971 as an agency of the U.S. government under the Foreign Assistance Act of 1969 to encourage and facilitate private U.S. investment in developing countries by making available political risk insurance, loans, and loan guaranties. Through this assistance, OPIC seeks to complement the development assistance objectives of the United States while supporting U.S. foreign policy and economic interests. Accordingly, it is OPIC's purpose to encourage U.S. private investments that benefit both the host country and the United States and to decline assistance to "investments that are likely to cause harm to domestic employment levels or the U.S. balance of payments." The concerns of the Congress and others, particularly with respect to the effects on U.S. employment of OPIC assistance, are reflected in 1985 amendments to Section 240A of the Foreign Assistance Act of 1961, which call for separate analyses by OPIC and GAO.

Since OPIC began operations, it has issued some $29 billion in political risk insurance coverage and about $1.1 billion in direct loan and guaranty commitments to some 2,100 investment projects in more than 80 developing countries. These projects include conventional equity projects, goods and services projects, licensing and technical assistance agreements, production sharing agreements, and joint venture agreements. OPIC has assisted offshore investment (investment not within the United States) in agribusiness, light industry, high-technology industry, sales and service distribution, and service banking.

OPIC's insurance program protects investors against the political risks of

- the inability to convert local currency gained through the overseas investment into U.S. dollars;
- full or partial loss of the investment through seizure by the foreign government;
- loss due to war, revolution, insurrection, or civil strife; and
- loss due to interruption of business caused by any of the above risks.

Investors pay premiums for this coverage, which can last for up to 20 years.

OPIC also makes or guarantees overseas investment loans on terms not generally available from private lenders. The loans and guaranties are intended to be of particular assistance to small U.S. businesses and to the poorer countries.

Commitments for all OPIC programs are backed by (1) OPIC capital and financial reserves totaling $1.08 billion as of September 30, 1986, and (2) the faith-and-credit pledge of the United States for full payment. According to OPIC, its maximum potential liability for possible insurance claims was $3.1 billion as of September 30, 1986, and its loan and loan guaranty portfolio totaled $588.5 million.

OPIC is required to annually report to the Congress the details of its operations, including assessments of the economic benefits to the United States and the development impact resulting from projects or activities OPIC assists. OPIC's activities are carried out under the authority of its Board of Directors whose chairman is the Administrator of the Agency for International Development.

Foreign Investment Versus U.S. Employment

U.S. private companies and individuals invest billions of dollars overseas each year. How these overseas investments affect employment in the United States has long been studied and debated without resolution. Organized labor has been the main proponent of the idea that caution should be used in offshore investment lest U.S. jobs be lost to less expensive offshore labor. Investors claim, however, that they must move offshore to remain competitive with other U.S. and foreign companies.

Although organized labor's complaint is against U.S. private investment overseas in general, it also argues that the U.S. government helps to foster U.S. job losses through the activities of OPIC and other agencies. OPIC contends, however, that investments it assists create jobs in the United States through increased exports to these offshore projects, to which labor counters that U.S. imports from these OPIC-assisted projects cause U.S. job losses. In addition, OPIC-assisted investment is small compared with total U.S. private investment overseas. For example, overseas capital expenditures by U.S. companies having a majority interest in affiliates totaled over $36 billion in 1985 compared with about $2 billion in capital expenditures by U.S. investors in overseas projects insured or financed by OPIC.[1]

To help prevent U.S. job losses resulting from OPIC activities, existing legislation directs OPIC to decline assistance to proposed investments if OPIC determines that they are "likely to cause a significant reduction in the number of [U.S. employees..." (22 U.S.C. 2191). In the absence of

[1]OPIC notes that its participation in the flow of U S investment to third world countries is close to 20 percent

any definition of these terms or other explanation in the legislation as to how OPIC is to make this determination, from a legal standpoint OPIC has, and in fact exercises, a wide degree of judgment in making such decisions. Administratively, OPIC analyzes (screens) proposed investments of its prospective clients prior to granting assistance and monitors ongoing approved projects to help determine whether there will be a significant adverse impact on U.S. trade or employment.

Prior GAO Reviews of OPIC

In addition to our annual financial audits of OPIC, we have reviewed OPIC activities in three previous reports at the request of the Senate Committee on Foreign Relations. In 1973, we reviewed OPIC's program management.[2] In 1977, we reported on (1) OPIC's success in obtaining private participation in its program and potential financial risks in certain industries and countries, (2) the extent of U.S. government involvement in claims disputes, and (3) the participation of small investors in OPIC programs.[3] In 1981, we reviewed (1) the effect of OPIC's programs on development, (2) the extent to which OPIC-supported investments stimulate U.S. exports and how these investments affect U.S. employment, and (3) the participation of small U.S. businesses in OPIC's programs.[4] The 1973 and 1977 reports noted the heavy concentration of OPIC insurance in a small number of countries, the clear predominance of large U.S. investors, and weaknesses of OPIC's project monitoring.

The 1981 report also noted weaknesses in OPIC's monitoring of projects and in screening proposed projects for possible adverse economic effects on the United States. As a result, we recommended that OPIC (1) routinely consult with appropriate U.S. government officials and industry experts when assessing investor project proposals and (2) develop industry-specific operational guidelines for assessing projects. In response to these recommendations, OPIC took steps to improve its consultations with some U.S. government agencies and also indicated that it planned to improve its system for monitoring ongoing projects. However, OPIC stated that it did not believe that industry-specific guidelines for assessing projects were needed.

[2]Management of Insurance, Loan Guaranties, and Claim Payments by the Overseas Private Investment Corporation (B-173240), July 16, 1973

[3]The Investment Insurance Program Managed by the Overseas Private Investment Corporation (ID-77-49), July 26, 1977

[4]The Overseas Private Investment Corporation Its Role in Development and Trade (ID-81-21), Feb 27, 1981

Objectives, Scope, and Methodology

The Overseas Private Investment Corporation Amendments Act of 1985 (Public Law 99-204), reauthorizing the activities of OPIC, required GAO to determine the impact of OPIC's activities on employment in the United States. Shortly after the legislation was signed, we talked with pertinent committee and subcommittee representatives to help identify and clarify the specific issues our report should focus on to comply with the requirements of the legislation and to respond to the information needs of the Congress. From agreements reached during these discussions and a review of the legislation and supporting documentation, our main objectives were to examine

- the effect on employment in the United States of selected OPIC projects;
- OPIC's methodology for determining, evaluating, and quantifying the effects of its projects on U.S. employment, including procedures for screening out prospective projects that might adversely affect U.S. employment (referred to as project screening); and
- OPIC's methodology for determining whether ongoing projects are benefiting U.S. employment as anticipated in initial applications for OPIC assistance (referred to as project monitoring)

Based on our discussions with committee and subcommittee representatives, it was evident that they are particularly concerned with the actual "direct" effects[5] that OPIC-assisted projects are having on the United States. These representatives were especially concerned about whether OPIC's quantification and reporting of the effects of the projects it assists accurately represent the direct effects of these projects. We, therefore, concerned ourselves primarily with these direct effects.

We did not examine the effect on U.S. employment resulting from the transfer of technology overseas via OPIC-assisted projects. Neither did we examine the development benefits to the host country resulting from OPIC activities or benefits to the United States that may accrue from such financial inflows as interest and principal payments, dividends, profits, royalties, and fees. We also did not consider the secondary positive effects on the United States that may result from host-country development.

[5]The "direct" effects on U S. trade of an offshore project are measured by the trade flows between the project and the United States These quantified trade flows are accounting figures and thus are measurable If U S exports to the project exceed project-connected U S imports plus previous U S exports displaced by project sales, the direct impact of the project on U S trade is positive When the trade flows are converted to equivalent employee-years, we refer to them as the direct effects of the project on U S employment

To examine OPIC's procedures for screening prospective projects and monitoring ongoing projects, we interviewed officials of OPIC; the Departments of Labor, Commerce, and Treasury; the International Trade Commission; and organized labor and trade associations. In examining a number of OPIC-assisted projects, we attempted to determine the extent and reliability of sources of information and types of analyses OPIC used to screen and monitor these projects. (See chapter 2.)

We analyzed OPIC's methodology and procedures for computing and reporting trade and employment benefits to the United States attributable to OPIC's projects. We then calculated the effect on U.S. employment of 33 selected projects, using data provided to OPIC by U.S. investors before their projects were approved for assistance. (See chapter 3.)

To examine the relatively current (1985) effect of specific OPIC projects on employment in the United States, we developed a questionnaire for parent companies concerning the production activities of their OPIC-assisted overseas investment projects and their effects on U.S employment. We mailed this questionnaire to parent companies of the 109 active projects approved by OPIC in 1981 and 1982, which we identified based on available data from OPIC. This time period allowed us to focus on current projects that had been operating at least 3 years. We used the data obtained from these questionnaires to compute the effect that OPIC projects approved in 1981 and 1982 are having on U.S. trade and employment. (See chapter 4.)

We used a generally accepted methodology to mathematically estimate the labor content of U.S imports from OPIC-assisted projects and exports to OPIC-assisted projects, and we refer to this as an estimate of potential effect on employment of these projects. It describes U.S. job opportunities that may be created by production of goods to be exported or lost due to imports displacing U.S. production. However, potential effect on employment may not translate into actual impact on employment because real employment changes depend on a number of additional factors whose effects are difficult to quantify. For example, factors such as business cycles, monetary and fiscal policies, and exchange rate movements may affect the demand for U.S. labor and thus actual employment. To determine whether 1985 trade flows and the resulting potential effects on employment of OPIC-assisted projects were related to actual impacts on employment, we examined whether job losses were

occurring in pertinent industries due to imports and whether the products produced by OPIC-assisted overseas projects compete with goods made by U.S. employees.[6]

We also visited 33 projects in 7 countries—3 in the Far East, 2 in the Middle East, and 2 in the Caribbean. Twenty-four of these projects had been approved in 1981 and 1982, and nine had been approved in 1980 or 1983. Because of congressional concerns, we selected most of these projects from "import-sensitive" industries (industries whose imports are more likely to have an adverse impact on U.S. employment, such as those manufacturing electronic components, textiles, and certain items of apparel).

At overseas locations, we discussed the projects with company representatives and, where possible, examined accounting and other records to obtain information on trade between the projects and the United States. We compared these data with estimates made by the parent companies in their applications for OPIC assistance. We also used the results of our site visits to help verify the accuracy of parent company responses to our questionnaire.

To enhance our response rate and obtain certain trade data from OPIC clients, we assured them that their confidential and proprietary business information would not be released outside of GAO (except to OPIC) in a form that could be identified with a specific U.S investor. Accordingly, we have not identified companies or affiliates and, where appropriate, we have aggregated identifying data.

The legislation mandating our study also requires OPIC to do a similar study, and the conference report for this legislation specified that we share with OPIC "raw data" obtained from OPIC clients. We gave OPIC data obtained from its clients through our mailout questionnaire and the data obtained from clients during our overseas fieldwork.

Our conclusions and recommendations are set out in a final chapter because of their interrelationship with the results of our analyses of OPIC procedures and the economic impact of OPIC-assisted projects on the United States presented in earlier chapters. (See chapter 5.)

[6]For a further discussion of this methodology see United States International Trade Commission, U S Trade-related Employment 1978-84, May 1986

We obtained OPIC's comments on a draft of this report, which have been evaluated and addressed within the report where appropriate and are included as appendix III. We also received more extensive comments from OPIC which have been addressed as needed. In addition, we employed a consultant who has expertise in international trade and investment and is familiar with OPIC's project analysis procedures to review our draft report and OPIC's comments.

Our work was performed between February 1986 and March 1987 in accordance with generally accepted government auditing standards.

Improvement Needed in Procedures for Screening and Monitoring

OPIC needs to improve project screening and monitoring by more thoroughly and systematically performing and documenting the results of both of these critical functions.

Project Screening Not Systematic or Well Documented

OPIC analyzes the data in investor applications for assistance to assess the possible economic impact on the United States of a proposed project. OPIC's authorizing legislation directs it to decline political risk insurance and/or financing for projects that are likely to have significantly adverse impacts on U.S. employment.

Our evaluation of OPIC's project screening process showed the following problems:

- OPIC has not (1) developed formal guidance for evaluating projects, (2) established criteria to determine whether the adverse impact that OPIC-assisted projects may have on the U.S. economy is "significant," or (3) developed some needed industry-specific guidelines to evaluate proposed projects.
- OPIC has not routinely contacted key parties in the public and private sectors to discuss and obtain input on project proposals or adequately considered evidence of job losses in specific industries or at U.S. parent companies of firms seeking OPIC assistance for their overseas projects.
- Inadequate documentation of the screening process makes it impossible to determine whether the expected economic effects of projects on the United States are being accurately and systematically analyzed.

How Projects Are Screened

OPIC's Economic Impact Analysis Unit consists of a director and one full-time analyst. Three other officers and five interns spend part of their time analyzing economic impact. The unit analyzes the economic impact on the United States of each proposal that reaches the application stage; its analysis is used as the basis for approving the project for OPIC assistance. OPIC refers to this as a "sectoral" analysis.

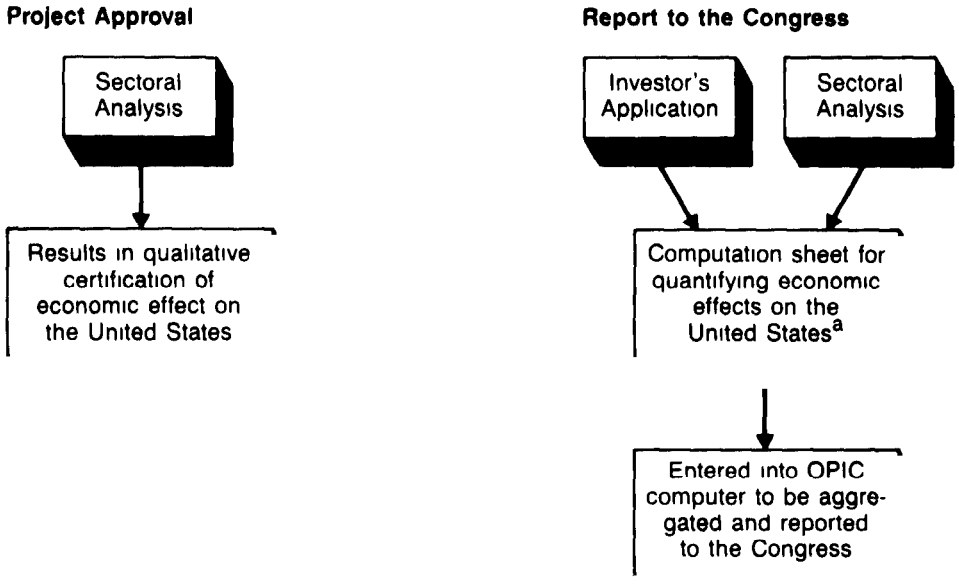
According to OPIC officials, OPIC sectoral analyses are based on investors' estimates and projections of future economic trends, including an examination of (1) the condition of a project's specific U.S. industry, including production, consumption, demand, and employment trends, (2) the industry's market share both in the United States and overseas, and (3) the U.S. import and export trends for the project's output. From this analysis, OPIC makes a qualitative assessment of the project's potential effect on the U.S. economy and employment. For example, exports from

the United States to the project may have the potential for a positive effect on U.S. employment, and displacement of U.S. production by the project through imports to the United States or displacement of U.S. exports to other countries may have the potential for a negative effect.[1] The analysis unit performed 200 sectoral analyses in 1985.

We found that OPIC's sectoral analysis contains some quantified economic data, but it is mainly a qualitative assessment of a proposed overseas project's potential economic impact on U.S. trade and employment. This analysis results in a qualitative certification that the proposed project "does not/does appear to have the potential for a significant negative effect on the U.S. economy or employment." The sectoral analysis does not quantify the impact on U.S. trade and employment of the OPIC-assisted project. OPIC does this later, using data from the investor's application, bolstered by the results of the sectoral analysis (see fig. 2.1). OPIC reports annually to the Congress the economic effects on the United States of the projects OPIC assists. A detailed discussion of OPIC's procedures for computing economic effects on the United States is included in chapter 3.

[1]Taken from OPIC's September 1986 report to the Congress on The Effects on U S Employment and Economic Conditions of OPIC Insured or Financed Programs Active As of September 30, 1986 Proposed Methodology

Figure 2.1: OPIC's Project Approval Analysis and Subsequent Quantification and Reporting of Economic Effects on the United States



[a]During the period of our audit, OPIC used a formal computation sheet OPIC officials told us that in the future they will not use a formal sheet but will enter figures into the computer from an informal work sheet

OPIC analysts make certain assumptions in assessing the U.S. economic impact on the United States of a proposed overseas investment. OPIC's assumptions include the following (depending on the individual project):

- Even if project goods will compete with goods made by U.S. employees, the project will not displace U.S.-made goods but instead will displace existing U.S. imports from a foreign country, thus (according to OPIC) negating any possible adverse import effect from the U.S. investor project.
- If OPIC does not assist the U.S project, a foreign company may undertake the investment, and the effect on the United States will be worse than if the U.S. investor undertakes the project.
- The U S market is growing rapidly enough to absorb the negative effect of a project on employment.
- The project's product is not made in the United States; thus, there is no negative effect on employment.

For example, OPIC may believe, based on its sectoral analysis, that even though OPIC-assisted project goods compete with those made by U.S.

workers the project will not displace U.S. production but will instead displace foreign imports, such as Japanese or Korean goods that compete with U.S. goods. OPIC then uses this assumption to determine that the direct effects of the U.S. imports from the proposed overseas project will not have an adverse effect on the U.S economy.

OPIC's sectoral analysis does not investigate other information having a bearing on the potential impact on the economy of the United States. For example, OPIC analysts give no consideration to other viable alternatives to assisting the overseas investment, such as (1) the U.S. investor proceeding without OPIC assistance, (2) the investment being made by another U.S. investor, or (3) the investment being made in the United States instead of overseas. OPIC officials told us that they are required by law to analyze only the possible adverse effects of the proposed investor's project and thus are not concerned with these other possible alternatives, which may or may not be advantageous to the U S economy.

Screening Process Needs More Procedural Guidance

OPIC has not developed step-by-step formal guidance for performing sectoral analyses. In December 1985, an OPIC staff member prepared informal draft guidelines and general procedures for performing economic analyses of proposed projects. This staff member saw a need for such guidelines to aid the interns who do many of OPIC's sectoral analyses. However, these guidelines had not been approved, as of March 1987, by OPIC's management. OPIC officials told us that new analysts learn primarily by experience and by studying finished cases. We believe that interns and other OPIC analysts would benefit from detailed written guidance and checklists for performing these analyses

Although, OPIC is mandated to screen out projects that are likely to cause "significant" adverse impact on U.S. employment, it has developed no written definition or guidance on what constitutes a "significant" impact. According to a 1978 consultant's report,[2] OPIC has left the term "significant" undefined in order to permit some latitude for projects with marginally adverse effects on the United States that may be counterbalanced by strong benefits to the host country's development.

[2]OPIC Assessment of Project Impact on U S Employment Review and Analysis of Policies, Procedures, and Evaluative Methods, 1978 The consultant was hired by OPIC to analyze OPIC's method of determining impact on U S employment

On occasion, this lack of definition has led to disagreement between analysts and management. For example, in 1980, OPIC's Office of Development recommended that a proposed cut-flower project be rejected because it would have a significant adverse effect on the cut-flower industry in one region of the United States. Nevertheless, the project was approved because OPIC's president believed that the impact on the United States would not be significant.

Although guidance exists concerning the evaluation of some import-sensitive industries (such as textiles and certain segments of agribusiness), OPIC has not developed similar guidance for other import-sensitive industries, principally electronics We believe that guidelines geared specifically to the evaluation of electronics projects are necessary because overseas projects in the electronics sector have great potential for causing U.S. job losses; Department of Labor files contain numerous petitions for assistance from electronics companies' employees who have lost their jobs because of competitive imports. To prevent such job losses, analysts need to be extremely thorough in covering all aspects of proposed projects in this industry.

OPIC Should Improve Its Contacts With the Department of Labor, Labor Unions, and Trade Associations

OPIC analysts solicit opinions of and data from pertinent government and non-government experts to verify investor-provided application information and put it into U.S.-industry and economic perspective. We found that, while contact has improved somewhat since our 1981 report, further improvements in OPIC consultations with the Department of Labor, labor unions, and trade associations are possible. These agencies have important views and information that OPIC needs to consider in its project analyses.

Contact With the Department of Labor

OPIC's contact with the Department of Labor appears to have been inconsistent since we recommended in our 1981 report that this contact be improved, although we do note improvement in these contacts since we started our current review in 1986. However, we are concerned that this contact improve even further and be maintained consistently.

For example, it is especially important for OPIC to maintain ongoing contact with the Department of Labor's Trade Adjustment Assistance (TAA) Group since it has specific information bearing on the legislative directive that requires OPIC to screen out projects likely to have significantly adverse impacts on the U.S economy and to monitor these projects to help ensure that project operations are not having adverse impacts. The

TAA Group investigates petitions for U.S. government assistance payments filed by workers who have lost their jobs because of increases of imports that (1) are like or directly competitive with articles produced by the workers' U.S. plant (or appropriate subdivision) and (2) have contributed "importantly" to the decline of production and sales and to the total or partial job losses of workers at U.S. facilities. The TAA Group maintains lists of these petitions (by firm and industry) and files containing the details and results of their investigations.

A key TAA Group official said that OPIC had contacted the Group twice in 5 years—once in 1981, shortly after our 1981 report (recommending more contact) was issued, and once in early 1986, when we started this study. However, it appears that OPIC has recently increased its contacts with the TAA Group. According to OPIC officials, the TAA Group was contacted as part of OPIC's analyses of six recently approved (1986) projects that we reviewed We confirmed these contacts with two TAA Group members who said that they had provided information about Trade Adjustment Assistance cases to OPIC. One stated that OPIC officials had contacted him recently on several occasions. In addition, according to a TAA group member, he now sends OPIC a copy of the monthly TAA petitions list.

OPIC analysts told us that they use the results of TAA's investigations in their analyses of overseas projects being considered for OPIC assistance. However, we found that OPIC analysts were not aware of some important TAA investigations involving the parent companies of our case study projects approved by OPIC in 1980-83.

Our analysis of TAA files revealed that a significant number of employees from parent companies of 8 of the 33 case study OPIC-assisted projects we selected had lost their jobs between 1976 and 1986 and had been awarded significant TAA payments due to the adverse impact of imports. These TAA petitions involved the same, similar, or related product lines as those manufactured by projects OPIC was assisting or considering for assistance. We also found that some employees of other companies in the same industries as OPIC-assisted projects had also filed TAA petitions However, except for one case,[3] we found no evidence in OPIC's sectoral analyses, general project, or other files that OPIC was aware of or considered any of this TAA information at the time of project

[3]We found that OPIC had considered and dismissed TAA data in its analysis for one of these cases

approval. Similarly, there was no evidence that OPIC used this TAA information during project monitoring to determine whether the operations of these projects are having adverse impacts on the U.S. economy.

We cannot say that the OPIC-assisted projects we reviewed were directly responsible for any of these job losses and resulting TAA awards to employees of these parent companies, since some of the petitions had been filed before the projects were approved or during the time projects were being considered. Also, two OPIC projects did not in fact export to the United States. In cases where TAA petitions were filed before OPIC project approval, we believe that OPIC should have considered these petitions in its project approval analyses. There is no evidence that OPIC did this. In cases where TAA petitions were filed after the project had been approved by OPIC, there is no evidence that OPIC monitored or considered this information to determine if OPIC-assisted projects were having adverse effects on the U.S. economy. We acknowledge that OPIC projects that do not export to the United States could not have contributed to TAA petitions.

Although OPIC has more recently increased its contacts with the Labor Department's TAA Group, we are still concerned that OPIC may not always make itself aware of or consider pertinent TAA information. For example, in one recent case where we knew OPIC was considering the large expansion of an insurance policy for a particular company, we made OPIC aware of a recent large TAA certification involving this company. As far as we could determine, OPIC officials were not aware of this information. In addition, OPIC does not appear to place much emphasis on historical TAA petitions. According to OPIC such TAA petitions by employees of companies seeking OPIC's assistance are not important in its decision to approve a project because it is highly unlikely that a prospective project could have led to layoffs of workers in the past. We believe, however, that past TAA petitions are important evidence for OPIC to consider because prospective projects if approved might lead to further layoffs if there is a history of such layoffs.

OPIC Contacts With Labor Unions

Our 1981 report recommended that OPIC have more contact with labor unions; however, we found that OPIC still has almost no such contact. OPIC has not found it particularly useful to confer with union officials because, according to OPIC's Vice President for Development, these

sources generally have been either unable or unwilling to provide information on the impact on employment of proposed investments. Nevertheless, he added, it continues to be OPIC policy to contact unions, when necessary, while screening investment proposals.

OPIC recently contacted an economist on the staff of the American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) about a proposed project. According to the economist, this was the first such contact with AFL-CIO headquarters in 4 years. We contacted six other officials of unions representing workers in the textile and electronics industries, including two unions that OPIC officials specifically told us they had contacted. All said that they had never been asked by OPIC to comment on project proposals. Many of the union officials with whom we spoke complained that the U.S. economy had been damaged by the U.S. government's promotion of overseas investment through programs such as OPIC's. One garment union official told us that his union had lost about 8,500 members in recent years due to U.S. overseas investments. An official of a union representing electrical workers said that, since 1982, a period of overall economic recovery, his union has had a net membership loss of 36,000 (18 percent) due to the closing of 206 electrical manufacturing plants. Several of these officials said that they would like to share such information with OPIC and would welcome any discussions with OPIC's analysts concerning proposed overseas projects

Contacts With Trade Associations and Organizations

OPIC officials also said that they regularly consult with trade associations and organizations. However, when we contacted seven of the trade organizations that OPIC told us it has contacted, only one confirmed that the organization had ever been contacted by OPIC. The others were unsure of, could not remember, or specifically denied having contact with OPIC.

OPIC officials told us that—to obtain "more candid" answers from government and private agencies—OPIC analysts sometimes represent themselves as graduate students doing research. Thus, OPIC said, some of those contacted may not remember the contact. Irrespective of the propriety of this practice, we found no documentation in OPIC's files to substantiate such contact.

Inadequate Documentation of the Screening Process

Our analysis of OPIC's screening process was hindered because OPIC maintains few records documenting and supporting the results of its project screening analyses. Analysts may keep informal files, but these are usually discarded soon after project approval. According to OPIC officials, even current analysis files may not contain complete records of the analyses performed or contacts made. In examining these recent (1986) files, we found that they often provide only sketchy evidence of contacts made and information obtained, making it impossible, even for an immediate supervisor, to check the work performed by an analyst and to determine whether the results accurately portrayed and thoroughly considered expected economic benefits to the United States. Once these files are discarded, OPIC must rely on the memory of its analysts who, in the case of interns, remain at OPIC for only a few months. For example, when OPIC officials told us that they had contacted two unions to discuss a textile project, they could not provide the names of the people contacted since the individual who had analyzed the proposed project was no longer employed by OPIC and had left behind no records of his contacts.

Changes Needed in the Monitoring Process

OPIC selectively monitors operating projects to determine whether they are benefiting the United States and host country to the extent anticipated by the investor in the application for assistance. We reviewed OPIC's current monitoring procedures and found a number of problems, including (1) inadequate documentation of monitoring results and of the reconciliation of these results with investor application data, (2) insufficient analysis and use of monitoring data, (3) a lack of on-site verification of monitoring data, and (4) no determination of the appropriateness of and circumstances for discontinuing assistance to future projects found (through monitoring) to have adverse effects on the U.S. economy.

How Projects Are Monitored

Project monitoring is conducted by officers from all OPIC offices, usually as add-ons to other work being conducted in a country. However, the analysis and summary of monitoring results are the responsibility of one individual—the "monitoring" officer in the Office of Development. To evaluate a project's effect on the U.S. economy, OPIC gathers the same type of information via a monitoring questionnaire that was originally requested on the application for assistance (i.e., project procurement, production, and distribution data).

The monitoring officer in Washington, D.C., reviews the monitoring questionnaire results. In many cases, this officer must contact the U.S.

investor for additional or clarifying information. Monitoring data indicating the impact on U.S trade of OPIC-assisted projects is then aggregated and reported to the Congress.

nadequate Documentation of Monitoring Results

OPIC must reconcile differences between investor application and operating data before reporting the results of OPIC's project monitoring to the Congress. It is important that OPIC document its reconciliation of such differences to help ensure that the projects affecting the U.S. economy are correctly identified. We found that data in OPIC's reports to the Congress often does not match the actual monitoring data obtained from OPIC investors and that OPIC does not document the reasons for these differences.

OPIC officials told us that they sometimes must contact investors in an effort to reconcile differences in application data and project operating data obtained during monitoring and that the reconciliation process may result in changes to the monitoring data provided by investors. We found that OPIC has little, if any, documentation explaining the differences between monitoring and application data. For example, a note on one of the 20 monitoring questionnaires that we selected for examination indicated that OPIC had asked the investor to explain some data provided in 1985, which showed the project was having a negative impact on the U.S economy The data was subsequently changed without explanation to reflect a neutral effect on the United States. It was not possible to determine who had made the change, the validity of the change, or the basis upon which the change had been made. OPIC officials could not remember the details of this case

We found that the data on project monitoring forms often does not match project monitoring data reported to the Congress. We requested documentation reconciling all three pieces of information for the OPIC-monitored projects that we examined—the investor's application data, OPIC's project monitoring data, and the data entered into the OPIC computer and later reported to the Congress. OPIC officials told us that there is no written documentation reconciling this data; the monitoring officer makes any necessary data changes "in his head" and records only the results. The monitoring officer told us that he does not have the time to design and institute a formal record-keeping system.

OPIC did not formally comment on this issue. Nonetheless, according to other recent information received from OPIC, it does intend to improve its documentation for both its screening and monitoring results.

Insufficient Time Devoted to Analysis and Little Use Made of Monitoring Data

In addition to its project screening, OPIC's monitoring of projects can help ensure that assistance is being given only to those private investments that will benefit both the host country and the United States. It is therefore important that OPIC sufficiently analyze and use monitoring results in pertinent policy decision-making processes, especially in its future project approval decisions. According to OPIC officials, higher priorities for limited staff resources preclude devoting additional time to analyzing monitoring results.

We believe that one reason more time is not spent on analysis and documentation of monitoring results is that there may be too few resources dedicated to this function. OPIC doubled its monitoring workload in 1986 but did not increase resources. The monitoring officer estimates that he spends about 20 to 33 percent of his time on monitoring, or about a day and a half to analyze and reconcile the data for each project. We observed that he is kept very busy doing other analyses for OPIC's Office of Development. He is occasionally assisted by a summer intern who spends approximately the same proportion of time on monitoring

We also found that, although OPIC prepares summary reports of monitoring results, it has no formal system to feed monitoring results back into its decision-making process concerning the policies and procedures for screening projects. The monitoring officer responsible for analyzing project monitoring data told us that no formal link exists between the screening and monitoring functions, although an informal feedback system does exist. We believe that the current informal system, like some of OPIC's other procedures, depends too much on individual initiative. Thus, unlike a formal system, informal feedback may or may not occur, and if it does occur it may not occur in a useful, organized manner. For example, if an analyst believes it is important to check monitoring results when evaluating a proposed project, he or she alone determines which previously approved projects might be relevant to the proposed one, checks to see if they have been monitored, and then tries to locate the appropriate files or people who monitored the projects to determine if these projects have any relevance to the one being screened. We believe that a formal system would ensure that important monitoring results are used by OPIC to help make project approval decisions concerning a project proposed by the same investor or an investor in the same industry. For example, one requirement under a formal system would be that an analyst check the monitoring results for projects in the same industry as that of the proposed project. A review

of monitoring results would also enable OPIC analysts to check the accuracy and relevancy of OPIC's assumptions during previous project evaluations in the same industry (see pp. 18-19). This review would be a checklist requirement not left to the discretion of the analyst. In addition, monitoring results should be easily categorized by industry so that they can be used in analyses and subsequent decision-making.

Monitoring Not Verified

OPIC does not verify data by examining records during the monitoring process because, according to an OPIC official, verification would be too time consuming and could create ill will with the investors. We found from our field work at 33 OPIC-assisted projects that there were differences (sometimes large) (1) between actual operating data and investor application estimates of project trade data (see app. I), (2) in some cases, between data provided by project representatives and data in project files, and (3) in some cases, between operating data obtained directly from the projects and operating data provided by parent companies of these projects (see ch. 4). We believe it is advisable to at least selectively check project records to ensure that data obtained during project monitoring is accurate

No Formal Po icy to Deal With Adverse Projects

OPIC has not determined the appropriateness of and circumstances for discontinuing assistance to future projects whose operations are found to have significantly adverse impacts on the U.S. economy. OPIC officials stated that they regularly find that projects may do better or worse than expected by the U.S. investor. Current OPIC policy, however, penalizes investors only if OPIC finds during project monitoring that the investors willfully misrepresented data on their applications. OPIC officials told us that no investor has ever been penalized.

OPIC believes that it should not be required to penalize U.S. investors whose success abroad inadvertently causes adverse impacts on the U.S. economy. In addition, OPIC believes that its primary job is to facilitate development and that any contingencies built into a contract for assistance that would tend to make OPIC's insurance policies less valuable could impact adversely on its development mandate. We recognize OPIC's dilemma in attempting to fulfill its development mandate while at the same time ensuring that there is no adverse impact on the U.S. economy. We also recognize that OPIC has contractual obligations involving existing projects. Nevertheless, we question the usefulness of project monitoring if OPIC has not determined the appropriateness of and circumstances for discontinuing assistance to future projects if they are

subsequently found to have significantly adverse impacts on the U.S economy.

Agency Comments and Our Evaluation

The following summarizes OPIC's major comments on the material in this chapter and our evaluation

Formal Procedures for Evaluating Projects

OPIC believes that formal guidelines for performing complex sectoral analyses of unique projects are not necessary because it has informal guidelines and the director of the analysis unit oversees and reviews all sectoral analyses. OPIC also stated that our audit contains no evidence that a single sectoral analysis carried out by OPIC was inaccurate or resulted in a project that harmed the U S. economy

As discussed in our report, the informal guidelines OPIC refers to have existed only since December 1985, and OPIC management told us that these are draft guidelines and should not be considered official guidance.

We believe these draft, or "informal," guidelines are a good step toward needed formal guidance. They should be tested, modified as needed, formally approved by OPIC management, and updated as needed. It is important that such guidance be designated by OPIC management as "formal" guidance (not "informal"); otherwise, its use may be considered optional and its interpretation subjective. Formal guidance will also help ensure that the same procedures and standards are followed and understood by all.

We agree that we did not isolate problems with specific sectoral analyses resulting in the approval of individual projects that were harmful to the U.S. economy. However, we believe that efficient management and good analytical practice dictate the need to develop and use formal institutional guidance to better ensure the accurate and consistent analysis of project proposals. This formal guidance is especially needed, given OPIC's use of inexperienced interns to perform many of these analyses.

Criteria for "Significant" mpact

OPIC stated that the Congress has given it discretion in determining when projects are likely to cause "significant" adverse impacts on U.S. employment and emphasizes the importance of analyzing each project on its own merits, given the difficulty of defining "significant" broadly enough to cover all situations encountered in its analyses. We agree that a project should be evaluated on its own merits, but we continue to believe that without specific uniform criteria, such as a standard definition of "significant economic impact," OPIC cannot ensure and demonstrate that it is being objective and consistent in its project approval decisions.

Industry-Specific Guidance

OPIC believes that formal guidance for the electronics industry is unnecessary because the industry involves a rapidly changing range of products, and therefore guidelines would quickly become obsolete. We believe that, because this field is complex and rapidly changing, specific guidance is necessary for these types of projects. For example, the guidance should contain steps unique to the analysis of projects in the electronics industry to ensure that the effects of rapid change in the industry and products are being considered for the product in question. In addition, overseas manufacturing of electronic goods has caused U.S. job losses and continues to be a major threat to U.S. employment according to OPIC and other U.S. government agencies. We believe that specific guidance in evaluating projects in the electronics industry would improve the analyses and subsequent decisions on proposed projects.

We also believe OPIC should use consultant studies and contacts with experts in and outside of government to keep electronics-industry guidance current, just as it does for textile and agriculture guidelines, which are over 10 years old.

Contact With Organizations

OPIC says that it routinely contacts government agencies and, when appropriate, consults with non-government agencies, such as trade associations and labor unions. Based on our review of OPIC's most recent (1986) sectoral analyses, it appears that OPIC has increased its frequency of contacts with U.S government and some non-government agencies. However, we could not accurately verify the actual extent of OPIC's contacts because they were not adequately documented. Moreover, our review of sectoral analyses for projects approved in 1980-83 showed little or no indication of contact with labor unions or trade associations and only sporadic contact with the Labor Department.

OPIC objected to what it said was our conclusion that it had failed to maintain contact with Labor's TAA Group, a failure that resulted in the loss of jobs by employees of companies receiving OPIC assistance. OPIC discounted the relevance of the TAA case information we present because, in some cases, OPIC believed the product in the TAA finding did not exactly match the output of the project OPIC is assisting; in other cases, OPIC could not determine whether there was such a match; and finally, in two cases, the OPIC-assisted projects did not export to the United States, and therefore there could be no linkage between job layoffs and the projects. Lastly, OPIC emphasized that it does consult TAA data and uses it when appropriate in screening projects.

We did not state that a direct link existed between OPIC's failure to consider TAA data and a loss of U.S. jobs at these companies and have further clarified our report to avoid such an inference. After considering OPIC's comments, we have also deleted three of the cases we used in our analysis. However, we continue to believe that the other cases we cited should have been thoroughly investigated and considered by OPIC's analysts in their initial screening and/or subsequent project monitoring because of the similarities of the products and/or industries involved. Contrary to what OPIC has stated, we found no evidence to suggest that OPIC was aware of any of these TAA cases involving the companies it assisted. It was only after we presented OPIC analysts with the information that they investigated these TAA cases.

Resources Devoted to Reconciliation and Analysis of Monitoring Results

OPIC stated that it does not devote too few resources to monitoring projects and that we had not cited any cases where the numbers or types of OPIC staff had resulted in less than adequate monitoring. In our report, we did not focus on the OPIC resources devoted to actual field monitoring at OPIC-assisted projects. Instead, we reviewed the staff resources allocated to the tasks of reconciliation and analysis of monitoring results. OPIC did not address this We continue to believe, for the reasons noted in our report, that OPIC needs to devote more resources to this function.

On-Site Verifications of Monitoring Results

OPIC stated that it believed that, as a general rule, auditing investors' records during field visits is unnecessary and that we did not find any "misrepresentations" between what project representatives told us and what we found in their records during our fieldwork. For the projects we visited, we did find discrepancies between data provided to us by

many of the project representatives and their actual records, due generally to a misunderstanding of our data needs. For example, some project representatives gave us data for the entire foreign enterprise instead of data only for the OPIC-assisted portion of the enterprise, as we had requested. In addition, in some cases we found differences between data provided by project representatives and data provided by parent companies.

Similarly, we found that in fiscal year 1981 when OPIC officials had monitored a group of electronics projects, it had accepted the project representative's figures without checking records. These figures turned out to be for the entire enterprise, not the OPIC project, and as a result OPIC reported incorrect data to the Congress. Thus, we continue to believe that it is important for OPIC to test the data provided by project representatives and parent companies against actual records.

Policies for Terminating Projects

OPIC stated that we had used a hypothetical case—in which an overseas investor's production of greater quantities of goods than expected has harmful effects on the U.S. economy—as the basis for asserting that OPIC, in such cases, could not legally cancel an investor's contract. We did not in fact present such a hypothesis, nor are we suggesting that OPIC should terminate a contract simply because an investment is doing better or worse than expected. We do believe, however, that OPIC should formulate a policy addressing such situations in future assistance arrangements. If appropriate, procedures should be formulated to discontinue assistance to projects having significantly adverse impacts on the U.S. economy, after the advantages and disadvantages to all parties involved (i.e., the U.S investor, host country, and U.S. economic sector) have been considered.

OPIC's Calculations of Employment Benefits to the United States Are Overly Optimistic

OPIC reports to the Congress each year that OPIC-assisted projects increase employment in the United States. For example, its 1984 report estimated that, for the projects approved between fiscal years 1981 and 1984, "some 109,000 man-years of employment will be generated in the United States in connection with the manufacturing, mining, growing, processing or shipping of additional U.S. exports" during the first 5 years of operations. In this chapter we analyze the methodology that OPIC uses to estimate effects on U.S. employment.

Benefit of Project to U.S. Employment Obscured by Methodology

The generally accepted method for determining the potential impact on U.S. employment of a U S foreign investment project is to subtract employment lost as a result of project-connected U.S imports and displaced U S. exports (i.e , sales by the project that replace previous U.S. exports) from employment generated as a result of project-connected U.S. exports. Export and import trade flows, which are measured in dollars, are converted to employment estimates (employee-years) by dividing the trade flows by a labor-output ratio (dollar value output per employee-year) for the specific industry involved. If the calculated export-generated employment is more than the calculated employment lost due to imports and displaced exports, the project's impact on the U.S. economy is potentially positive. The calculated effects on U.S. trade, resulting from the trade flows directly to or directly from the project in question are referred to as the direct trade effects of the project, and the resulting effect on employment is referred to as the direct employment effect of the project.

To investigate OPIC's methodology for computing the effects on the United States of projects it assists, we concentrated on the formal worksheets that OPIC uses to compute these effects. We verified that the trade and employment figures in the computation sheets (with a few minor exceptions mainly due to arithmetic and data transfer errors) represent the data ultimately reported to the Congress; we did this by tracing computation sheet figures to the computer file where OPIC aggregates these figures for its reports to the Congress. OPIC officials told us they check the accuracy of these computations when they are entered into the computer for ultimate reporting to the Congress. We also checked these computation sheets against investor application data and OPIC's sectoral analyses.

We found that, when OPIC computes the economic benefits to the United States of a proposed project, it generally follows the method described above; however, as part of its methodology, OPIC also makes certain

assumptions involving the project and the market in which the project will compete. These assumptions are based on the U.S. investor's application data and OPIC's sectoral analysis (see ch. 2). We believe it is appropriate for OPIC analysts to make plausible assumptions when they evaluate a project for OPIC's assistance. However, the way OPIC analysts use these assumptions to mathematically calculate the economic effects on the United States of a project inadvertently obscures the negative direct effects of the project.

Our review of OPIC's computation sheets showed that OPIC most often uses a hypothetical alternative to the proposed project to justify offsetting (mathematically reducing or totally canceling) the predicted direct adverse effects of the project. A hypothetical alternative often assumed by OPIC is that a non-U.S. company would produce and sell to the United States the product in question if OPIC does not assist the U.S. investor.[1] OPIC often assumes that, in that event, the non-U.S. competitor would make sales to the United States equivalent to sales that would occur as a result of the proposed U.S. investment, and, unlike the proposed U.S. investment, would make no purchases from the United States. Thus, when OPIC computes the effects on the U.S. economy of the proposed project, OPIC's analysts mathematically cancel the negative direct effects of the project's sales (U.S. imports) to the United States on the assumption that it is preventing (or displacing) sales from the non-U.S. alternative. However, when OPIC reports the effects of this project, it does not stipulate that it uses assumptions in its computation of these effects. Thus, interested parties such as the Congress may mistakenly assume that OPIC is reporting the direct effects of the project, not the net effects of the project based on OPIC's assumptions.

Illustrative Example of OPIC's Methodology

Because OPIC's computational methodology is complex, we believe it is helpful to demonstrate this methodology with an example taken from OPIC's project files. In this example, OPIC reported that the project would generate 104 employee-years of employment (See appendix II)

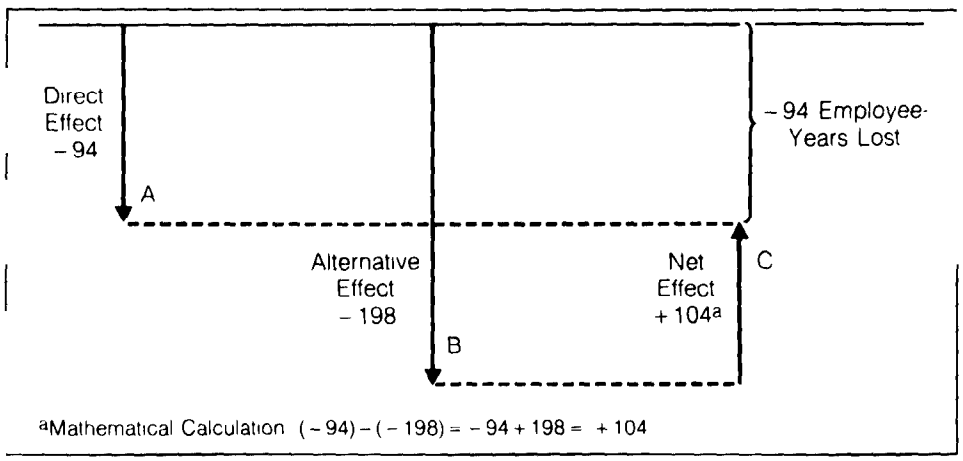
OPIC calculated that the operation of the project would generate 104 U.S. employee-years of work annually from related U.S. exports. OPIC also calculated that no employee-years would be lost due to related imports. This latter result was obtained by mathematically offsetting the

[1]OPIC, in other cases, may assume that the U S market is growing rapidly enough to absorb any negative effect of the project on employment or that the project's product is not made in the United States and thus has no direct negative effect on employment in the United States

expected negative U.S. import trade flow from the project with the potential trade flow of a hypothetical alternative, thus reducing the project's calculated negative effect on employment to zero.

Figure 3.1 illustrates OPIC's implicit calculations; it also shows that the predicted direct effect of this project on employment is actually negative.

Figure 3.1: Illustration of OPIC's Calculation of the Effect on U.S. Employment of a Sample Project
(Annual Average Employee-Years)



This illustration shows that the expected direct effect on U.S. employment of the project is an annual work loss of 94 employee-years (represented by the downward arrow labeled A). This represents a positive effect on employment of 104 employee-years due to U.S. exports to the project and a negative effect on employment of 198 employee-years due to project imports by the United States.

Based on application data solicited from the investor (sometimes supplemented by OPIC's sectoral analysis), an import offset of 100 percent for the alternative scenario (arrow B) is calculated, showing an estimated job loss of 198 employee-years resulting from trade flows between the United States and a hypothetical foreign competitor. As a result, by assisting the project, OPIC assumes it is completely preventing (or displacing, in the case of U.S. sales by an existing foreign competitor) job loss (arrow B) and thus credits itself with creating 104 U.S. employee-years (arrow C) of work annually—the mathematical difference (arrow C) between the estimated effect of the project and the non-U.S. alternative scenario's effect on employment.

Using plausible alternatives and assumptions in computing effects on the United States may be prudent; however, OPIC, by not disclosing in its reporting that it uses a hypothetical alternative, suggests that 104 employee-years of new employment will be directly generated annually by the project. To the contrary, as figure 3.1 shows, there is still an estimated direct loss of employment of 94 employee-years annually.

The example presented in figure 3.1 is representative of the 33 case study projects we analyzed. Our analyses of the investors' application data for OPIC assistance, the OPIC computation sheets, and sectoral analyses show that many of the projects should have been predicted to have direct negative effects on U.S. employment.

Methodology May Provide Misleading Monitoring Results

OPIC also uses the methodology described above to analyze information gathered when monitoring ongoing projects, thus perpetuating an overly optimistic picture of the effects of the projects on the U.S. economy.

OPIC uses the hypothetical trade flows of an assumed non-U.S. competitor to reduce, if not totally cancel out, any negative real trade flows between OPIC-assisted projects and the United States. Thus, OPIC reports to the Congress that the monitored project is having a positive effect on U.S. trade when the project's actual direct effect on U.S. trade and employment may be negative.

We believe it would be more meaningful for OPIC to present the actual direct effect that these operating projects are having on the U.S. economy However, we recognize that OPIC, in its presentation of the actual results of its monitoring, may wish to also show why it initially approved these projects using its hypothetical alternatives or other assumptions. We believe this fuller presentation would be especially useful for those projects whose operations may be found to have direct negative impacts on the U.S. economy.

Reports to the Congress Are Overly Optimistic

In summary, we found that OPIC's methodology for calculating the economic effects on the United States of its projects obscures their direct effects. This methodology results in reports to the Congress that provide overly optimistic impressions of what may be assumed to be the direct effects of OPIC-assisted projects. That is, OPIC's methodology does not calculate and report the direct economic effects on the United States of the projects it assists but instead mathematically reduces or cancels these direct effects with those of hypothetical alternatives—with potentially

worse effects than those of the proposed project—that OPIC believes are preventable by assisting the U.S. investment. OPIC implicitly assumes that the impact on U.S. trade and employment will be worse if it does not help the U.S. investor to operate overseas. In other words, many of the employee-years of employment that OPIC reports as being generated by assisted projects do not, in fact, represent employment generated by these projects. Instead, this figure reflects the number of employee-years of employment that OPIC estimates will not be lost if OPIC provides assistance to these projects

Implicit Assumptions in OPIC's Alternative Scenarios Seem Unrealistic

The premises underlying OPIC's use of hypothetical alternative scenarios are based on assumptions that seem unrealistic. That is, OPIC implicitly assumes that if it does not provide assistance, the U S. project will not be undertaken by any U S. investor; a non-U.S. foreign competitor will displace (or is displacing) U.S. production and sales and will buy nothing (or is buying nothing) from the United States; and the U.S investor will not put his funds in any alternative investment that benefits U.S. production and employment. The latter part of this assumption seems particularly unrealistic; it is doubtful that profit-seeking U.S. businesses will withdraw their investment funds from the U.S. economy and forego earning profits.

Regarding the first part of OPIC's assumption, evidence suggests that many proposed overseas investments may go ahead without OPIC assistance. The issue of the need for OPIC assistance was addressed by a 1982 study commissioned by OPIC.[2] The report found that in only 25 percent of the cases studied the overseas investment would clearly not have been undertaken by the investor without OPIC assistance.

In computing the effect on employment as it does, OPIC generally assumes that there are non-U.S. alternatives to the investor's proposed overseas project. However, it does not ask the U.S. investor whether other alternatives, such as investing in the United States to expand, modernize, or automate existing facilities, have been considered or whether (if denied assistance) the investor may invest overseas without OPIC assistance. We believe that OPIC should attempt to identify more likely alternatives For example, rather than constructing an alternative scenario based on general assumptions about an investor's possible actions, OPIC should solicit information regarding an investor's likely

[2] A Study of Additionality of OPIC Assistance to U S Private Investment in Developing Countries, Arthur Young and Company, May 28, 1982

behavior if OPIC were not to provide assistance. Questions that might be considered include whether the investor will undertake the same or a similar overseas investment if OPIC assistance is denied, whether a competing U.S. or non-U.S. based firm will undertake this investment, or whether investment in the United States will be undertaken if OPIC denies assistance. Using such information, OPIC could base its analysis on the investor's more likely behavior rather than on general assumptions.

Previous Recommendations to Improve Methodology

In 1978, a consultant commissioned by OPIC to review its methodology for computing impact on U.S. trade and employment made specific recommendations that could have alleviated many of the problems we found.[3] The consultant criticized OPIC for too generously offsetting the calculated negative effects of proposed projects and warned that

"Displacements [of U S. exports] due to non-U S alternatives have been too generously used [by OPIC] to offset actual U S export displacements (particularly in the electronic industries, where the argument has been that if the U.S does not go offshore, Japanese or other imports will displace the U.S production) . U S. import effects have been grossly understated in projects involving offshore manufacture of parts and components .. Even direct imports from LDCs [less developed countries] are generally discounted to '0' on the grounds that if the U S firm did not go offshore, those products would be sold by other foreign suppliers. This reasoning explains why many projects that would otherwise show negative effects on U S balance of payments and employment are turned into 'positive effect' projects." (Underscoring added.)

The consultant concluded that "the current procedures, policies, and evaluative methods used by OPIC to prepare U.S. effects analysis suffer from significant deficiencies, and in many instances a lack of serious attention and analysis by OPIC staff." As recommended by this consultant, OPIC did set up a small group to analyze project evaluations, but it did not implement the consultant's specific recommendations regarding the calculation and presentation of expected project effects. The consultant recommended that the direct project effects be calculated separately from the alternative effects and that a broader range of alternatives to offshore manufacturing be considered. OPIC officials told us that they had not incorporated these recommendations into their calculations and presentations of the economic effects on the United States

[3]OPIC Assessment of Project Impact on U.S. Employment· Review and Analysis of Policies, Procedures and Evaluative Methods, prepared by Developing World Industry and Technology, Inc , Washington, D C , Apr 5, 1978

but had generally incorporated them into their qualitative sectoral analyses. We found no evidence that the consultant's recommendations have been incorporated into OPIC's sectoral analysis.

Other Aspects of OPIC's Methodology Further Obscure Direct Effects on Employment

OPIC's methodology further obscures the direct effects on employment by (1) combining project effects on employment resulting from start-up procurement with those resulting from annual operating procurement, (2) failing to consider the effects of all pertinent imports from projects to the United States, and (3) using inappropriate labor-output per worker ratios to convert the value of project-connected imports into employee-years of U.S. employment.

Types of Procurement Need to Be Treated Separately

OPIC combines the investor's estimates of initial (one-time) procurement to start the project (for example, machinery and equipment) with estimates of annual operating procurement (for example, spare parts and raw materials) and reports the total combined effect on U.S. employment of these two different types of project procurement. This procedure obscures the fact that, although exports of initial procurement materials and equipment from the United States to the project will have a one-time positive potential effect on employment, normal operations may have a positive or negative effect on the United States that may continue for many years.

The following hypothetical example illustrates OPIC's methodology. OPIC reports that a project is expected to create 300 employee-years in the United States during the first 5 years of operation. In reality, initial procurement (lasting only a short time) may temporarily create 800 employee-years, but normal operations may cause an annual loss of 100. However, OPIC reports only that 300 employee-years are generated (800 minus (5 times 100)). Combining the initial procurement and operating procurement effects obscures the fact that the annual operations of these projects may cause adverse impacts on U.S. employment, giving the impression that the effect on employment of the project is continuously positive.

This procedure also suggests that the U.S. employment generated by the project occurs entirely in the proposed project's industry (for example, chemicals) when in fact much of it does not. Since most of the initial procurement (and some of the operational procurement) is U.S. exports of major machinery and equipment and spare parts, the employment these exports generate is not necessarily in the project's industry. Even

if the project causes no change in overall U.S. employment, there may still be significant sectoral changes. For example, while employment in the machinery and equipment industry may increase due to initial procurement, employment in the project's industry (for example, textiles and electronics) may decrease because it has been adversely affected by imports during project operations.

OPIC, in commenting on this section of our report, did not respond to the need to compute and report the economic effects on the United States resulting from initial construction and start-up procurements separately from those resulting from the annual operations of projects. OPIC instead commented on its use of a 5-year time frame in reporting project effects. We do not take issue with using a 5-year time horizon.

Effects of Indirect Imports Not Considered

OPIC's calculations do not include the indirect U.S. imports from a project that would decrease the calculated positive effect on U S. employment; thus, OPIC's calculations overestimate positive effects on U.S. employment. Indirect imports are goods produced by the project, usually components, sent to affiliates or other firms abroad and subsequently shipped to the United States as part of a finished product. For example, in the representative project discussed on page 33, OPIC's computations did not include the U.S. investor's estimate of $4.6 million worth of electronic components to be shipped annually from the project to the United States through an affiliate, causing an estimated loss of 98 employee-years of work annually in the United States from this one project.

OPIC has routinely obtained information about indirect U.S. imports from investors for the past 10 years but has not generally used this information even though the 1978 consultant's report specifically recommended that OPIC use this information when computing effects on the United States. According to OPIC, it will now use information on indirect imports, as suggested by its 1985 reauthorization legislation.

Appropriate Output-Per-Worker Ratios Should Be Used

In estimating effects on employment, OPIC converts the dollar value of trade flows into employee-years by dividing the trade flows by a labor-output ratio (dollar value of production per worker per year). However, OPIC generally uses the same ratio of U.S. production per worker for both exports and imports, even though U.S. exports of initial or operating procurement materials and imports of the finished products from the OPIC-assisted project may come from different industries OPIC told us

that it believes the labor-output ratios it currently uses in its computation of project effects on employment provide reasonable estimates of these effects. We found many cases where the labor ratios OPIC used provided overly optimistic portrayals of projects' effects on U.S. employment.

Our Calculation Shows Expected Negative Impact on U.S. Employment of 33 Case Study Projects

We computed the expected effects on U.S. employment for our 33 case study projects, using a methodology that estimates the potential direct effects on U.S. trade and employment of OPIC-assisted projects. Our procedure, which corrects problems in OPIC's methodology,

- calculates the net direct trade flows of proposed U.S. investor projects (that is, we do not use hypothetical trade flows to offset those of the proposed project);
- separates initial effects from those of operating procurement;
- uses investor-supplied information concerning indirect imports to the United States from the project;
- uses appropriate industry-output ratios to convert trade flows into employee-years of employment; and
- calculates and reports separately the effects on trade and employment of the offsets resulting from OPIC's assumptions about these 33 projects.

In applying this methodology, we used the same information that OPIC had at the time it undertook its project approval analyses—the information provided to OPIC by the applicants and OPIC's sectoral analyses. Using this methodology we found that, in the aggregate, these 33 projects should have been expected to have a one-time gain of 2,283 employee-years from the manufacture of project start-up machinery and equipment purchased from the United States. During project operations, 20 of the 33 projects should have been expected to generate a negative U.S trade flow and a direct negative effect on U.S. employment The aggregate operations of all 33 projects had the potential to cause an annual direct loss of 2,635 employee-years of U.S. employment.

In comparison, OPIC calculated that during their first 5 years of operations these projects would generate approximately 7,586 employee-years, or 1,517 annually. The difference between OPIC's figures and ours is due primarily to the fact that OPIC mathematically offsets the direct negative effects of the projects with those of alternative scenarios [4]

[4]The calculated aggregate value of these offsets is 3,263 employee-years of annual U S employment

Agency Comments and Our Evaluation

OPIC stated that our findings concerning its methodology for computing the effects on the United States of its projects are of limited value because (1) the OPIC computation sheets we used to develop our findings do not form the primary basis for OPIC's decisions to approve a project or for its reports to the Congress; (2) the methodology (a "worst case alternative")[5] that we said OPIC always uses is one that OPIC only rarely uses and in fact was used in only 4 of 22 projects we analyzed from import-sensitive industries; and (3) we failed to sufficiently consider the role of OPIC's sectoral analyses. OPIC also disagreed with our suggested methodology for calculating the projects' direct effects, characterizing it as "totally inadequate."

GAO maintains, however, that OPIC's computation sheets do form the basis for OPIC's reports to the Congress. We verified this by tracing most of the individual computations for our case study projects to the reported data Computation sheet data matched data reported to the Congress with a few minor exceptions due primarily to arithmetic or data transfer errors. Moreover, during our review, OPIC officials specifically directed us to these computation sheets as the documents used to quantify effects on U S. employment.

We agree that OPIC does not always use a "worst case alternative" and have modified our report to note that OPIC uses not only this hypothetical scenario but others in computing the effects of its projects. We have substituted the term "hypothetical alternative" to encompass the various alternatives OPIC uses to compute economic effects. In our review of OPIC's computation sheets and computer files containing data reported to the Congress, we found that OPIC used hypothetical alternatives to completely offset (mathematically cancel) the direct negative effects of most of the projects we examined However, regardless of the type of alternatives or assumptions used or the reasons for their use, our main concern is that OPIC's methodology obscures (mathematically reduces or cancels) the direct adverse effects of these projects and results in reports to the Congress that are overly optimistic concerning the magnitude of the direct benefits to the United States of OPIC-assisted projects.

We disagree that we have not adequately considered the importance of OPIC's sectoral analyses; we discuss these analyses in chapter 2. We are

[5]In our draft report we defined a "worst case alternative" as a hypothetical alternative to U S investment based on the assumption that a non-U S company will undertake a similar new investment if OPIC does not assist the U S investor, resulting in a least favorable outcome for the U S economy

concerned in chapter 3 with the methodology OPIC uses to quantify and report the effects of its projects to the Congress.

Finally, we did not suggest our methodology as a substitute for OPIC's sectoral analysis. Rather, we presented a way of determining a project's direct effects, which we believe should be calculated and reported separately from any calculations using hypothetical alternatives.

Some Responses to Our Questionnaire Show Possible Negative Impact on U.S. Employment

We used 1985 operating data obtained from our mailout questionnaires to parent firms to compute the impact that projects approved by OPIC in 1981 and 1982 are having on the U.S. economy. Our analysis of U.S. parent companies' responses shows that some ongoing OPIC-assisted overseas investments may be having a negative impact on the U.S. economy. While U.S. employment opportunities might have been created by the start-up procurements of OPIC-assisted projects, a number of projects had a negative impact on U S. trade and a potentially negative impact on U.S. employment once they began to operate.

The U.S. investors' responses to our questionnaires also revealed that some parent companies' responses did not match data obtained from their project representatives and verified by us in the field and that many projects changed their product lines or methods of operation after they had received OPIC insurance.

In our calculation and discussion of the effects of the operations of OPIC-assisted projects on U.S. trade and employment, we focused on the direct effects of these projects. Our objective was to determine and present the direct effects on U.S. trade and employment of OPIC-assisted projects, using the actual operating data from these projects

Our calculations of trade impact on the United States by OPIC-assisted projects are based on measurable 1985 trade flow data provided by respondents. Employment impact, although computed from these actual trade flow data, is a calculated figure and does not necessarily depict what actually might have happened to U.S. employees as a result of these OPIC-assisted projects. The calculated effect on employment represents the potential effect on U.S. employment resulting from the trade flows of these OPIC projects in 1985; thus, we use the term "potential" effect or impact on employment. In cases where we found a potentially negative effect on employment, we did further analyses in an attempt to determine whether these potential losses are related to real job losses for U S. employees.

Respondents to Our Questionnaire

We mailed our questionnaires to the parent companies of 109 OPIC-assisted projects, including the 33 in our case studies, and received 85 responses (78 percent), including 24 from our case studies. Of the 85 firms responding, 28 (33 percent) had actually terminated their OPIC insurance. These firms were eliminated from our analysis of active projects. Thus, we analyzed a total of 57 projects, including all 24 case study projects.

After evaluating the responses, we believe that the projects in our study adequately represent the types of projects that were approved by OPIC in 1981 and 1982 and were still active in April 1986. In 15 cases, we were able to compare parent companies' questionnaire responses with verified project data we had obtained during our overseas case study site visits.[1] These comparisons allowed us to gauge the accuracy of parent companies' responses to our questionnaires (see p. 48).

Potential Negative Effect on Employment of Some OPIC-Assisted Projects

We estimated the impact on U S. employment of the 57 OPIC-assisted projects, using 1985 operating data and the methodology described in chapter 3 (p. 40). We estimate that potential U.S. employment was generated by 40 projects that had made initial procurements from the United States. Also, 32 of the 57 projects (56 percent) continued to trade with the United States after start-up; 18 of the 32 sold more to the United States than they purchased. These 18 projects had a negative direct effect on trade, and 15 of these had the potential for a negative direct effect on employment in the United States (see table 4.1).[2]

Table 4.1: Potential Effect on U.S. Employment of OPIC-Assisted Projects

Project phase	Total projects	Potential effect		
		Positive	Negative	No direct
Start-up procurement	57	40	0	17[a]
1985 operations	57	17	15	25[b]

[a]Sales, service, and manufacturing projects, which purchased start-up equipment and supplies from foreign countries

[b]Mainly construction projects requiring no operating supplies, manufacturing projects trading only with foreign countries, or service banks requiring few operating purchases

We estimated total potential U.S. employment generated during the initial start-up of these projects at 11,034 employee-years. Potential employment gained from U.S. exports to the projects in 1985 is estimated at 780 employee-years. Potential U.S. employment lost due to direct and indirect U S. imports and to U.S. exports displaced in 1985 is 2,854 employee-years. Total estimated net potential employment lost in the United States due to the operations of these overseas projects is estimated at 2,074 employee-years Although the computed potential gain in employment resulting from initial start-up purchases is substantial, the

[1]We were able to compare data from only these 15 because some of the data obtained was incomplete and not comparable

[2]We obtained this result by using appropriate industry labor-output ratios to convert export and import trade flows to employee-years

estimated potential loss in employment resulting from ongoing operations could continue for an indefinite number of years. OPIC estimated, based on its analysis of investor application data, that these projects would generate 24,180 U.S. employee-years during their first 5 years of operation, or 4,836 annually.

The 57 projects had a significant net negative impact of -$218.8 million on U.S. trade in 1985; this negative trade impact translates into an estimated potential net U.S. employment loss of 2,074 employee-years. The 57 projects had an estimated $285.7 million in direct sales and $13.5 million in indirect sales[3] to the United States and purchases of about $85.6 million in materials and supplies from the United States. According to responses to our questionnaires, these projects also displaced an estimated $5.2 million in sales that would have been made by U.S. firms to foreign markets in 1985

Parent companies also estimated that $28 million of their $285.7 million in project sales to the United States in 1985 had replaced foreign competitors' sales to the United States.[4] This estimate reflects a much smaller percentage (10 percent) of project sales to the United States than OPIC used in computing the estimated economic effects on the United States of these projects That is, OPIC assumed that virtually all of these projects' sales to the United States would be offset by the projects' replacement of foreign competitor sales to the United States. (See chapter 3.)

OPIC, in commenting on our report, disagreed with our characterization of the impact of these projects. OPIC cited two projects—one involving the trans-shipment of Alaskan crude oil and one involving the manufacture of electronic recording equipment in the Far East—to support its comments. In the former case OPIC stated that it is "clearly fallacious" to conclude that pipeline trans-shipment services had led to U.S. unemployment. In fact, OPIC contends, the pipeline indirectly stimulates employment in oil-related industries. According to OPIC, this project accounts for a substantial amount of the direct import sales for the 57 projects we analyzed and its exclusion would "virtually wipe out" the aggregate negative effects on trade and employment we present.

[3]These are sales by projects to third parties who then export the goods to the United States

[4]The $28 million in estimated offsets translates into a potential effect on U.S employment of 311 employee-years

This project does account for a significant proportion of our figures (for both positive and negative effects on employment), but we disagree that it could not have been expected to have negative effects on trade and potentially negative effects on employment. Our review of available data suggests that the project did in fact have a negative impact on U.S. trade flows and might have had some adverse impact on employment. That is, the payment to a non-U.S. company (the pipeline operator) for shipment services should be treated as a negative trade outflow from the United States in calculating the impact of this project on U.S. trade and employment. OPIC did not recognize this in its calculations. Furthermore, trans-shipment of Alaskan crude oil through the pipeline has displaced shipments through the Panama Canal on U.S. flag ships.[5] According to the U.S. Maritime Administration, such shipments through the canal decreased by 94 percent during the pipeline's first year of operations (1983). In addition, a Maritime Administration representative told us that there has been a significant annual reduction (about 500 thousand tons) of required U.S. oil tanker capacity due to the OPIC-assisted pipeline. Moreover, the Panama Canal Commission (a U.S. government agency that operates the canal), in its 1983 Annual Report, attributed a loss in revenues to the opening of the pipeline. Finally, it is difficult to ascribe a positive effect of the pipeline on U.S. oil-related industry employment in isolation from other factors influencing the industry because the volume of crude oil trans-shipped through the pipeline has been less than that shipped previously by U.S. ships through the canal.

In the recording equipment case, OPIC stated that few, if any, U.S. workers could have been displaced by imports, because it is standard practice in this industry to perform assembly overseas. Our review shows that this project is in an industry in which the U.S. government has (through the TAA process) determined that U.S. workers have lost their jobs due to imports. Moreover, OPIC approved this project at a time when, according to OPIC's own sectoral analysis, competing firms were considering alternatives to offshore assembly that would retain manufacturing (and jobs) in the United States.

Negative Impact Was Predictable

We believe that the negative economic impact on the United States of many of these projects could have been predicted had appropriate analyses been made of the investors' initial application data. The results of

[5]Only U S flag ships are permitted to ship Alaskan North Slope crude oil to the Gulf and East Coasts These flag ships are crewed by U.S citizens

our analysis of the direct effects that OPIC-assisted 1985 project operations have had on the U.S. economy correlate with our calculation of the expected direct impact on employment of case study project applications data (see ch. 3). We found that 1985 operations of 10 of the case study projects, whose parent companies had responded to our questionnaires, had had a negative impact on U.S. trade and a potentially negative impact on U.S. employment. Our analyses of investor application data in chapter 3 predicted that 9 of these 10 projects would have a potentially adverse impact on the U.S. economy. The parent companies of the case study projects that we predicted would have the greatest adverse aggregate impact on the U.S. economy did not respond to our questionnaires.

Impact on Employment May Be Worse Than Shown by Questionnaire Responses

We found differences between parent companies' responses and those obtained from the overseas projects in 10 of the 15 cases that we were able to compare. The 10 parent companies' responses estimated that their project operations had positive effects on U.S. trade. However, the verified data obtained from these 10 projects showed a negative trade flow between the project and the United States, suggesting a potential loss in U.S. employment. Further investigation revealed that some of the parent companies had made legitimate mistakes in the trade flow data they had provided us. Re-computing the effect on U.S employment of the 1985 operations of these projects, using the verified on-site project data, showed a potential loss of 197 U.S. employee-years in addition to the potential loss of 2,074 as computed from parent companies' responses.

Estimated Potential Employment Losses May Be Related to Actual Job Losses

The Labor Department's TAA files show that most of the U.S. industries related to the 15 projects we estimated to have a potentially negative impact on U.S. employment (see table 4.1) experienced actual job losses between 1980 and 1985. In addition, the parent companies of 9 of these 15 projects told us that the products of their overseas projects compete with similar goods made by U.S. workers. Thus, the potential employment losses that we calculated using the operating data of these projects might have contributed to real job losses or lost job opportunities for some U S. workers in pertinent industries since these projects began operating.

Questionnaire Information Also Emphasizes Need for Project Monitoring

We found that many projects have terminated their OPIC insurance and that active projects have either added new products to their product lines or changed their modes of operation or both. Termination of projects can affect the risk profile of OPIC's insurance portfolio and the integrity of its premium base, and changes in a project's product line and mode of operations may affect U.S. trade and employment in a manner not originally considered by OPIC. These changes in the status, product lines, and operations of OPIC-assisted projects again emphasize the need for accurate and timely monitoring of these projects. We found that a total of 57 percent (or 143 of 249) of the projects insured in 1981 or 1982 were no longer covered by OPIC insurance. We asked most of the 28 firms that responded to our questionnaires why they had terminated their OPIC insurance, and the reasons ranged from having abandoned their overseas projects to deciding that OPIC insurance was too expensive. Most of these firms told us they had terminated their insurance in 1984.

Agency Comments and Our Evaluation

OPIC commented that the methodology we use to calculate impact on employment assumes "that any project which generates exports to the United States will, ipso facto, result in U.S. unemployment" and that it is too simplistic to equate U.S. imports with loss of U.S. jobs. OPIC also noted that our 1981 study did not find a direct relationship between OPIC-assisted projects and U.S. job losses.

Our calculation of a project's direct effects on trade, and the use of this data to estimate effects on employment, were not intended to imply that all imports automatically result in job losses, and, where appropriate, we have clarified the report to say that our figures represent the potential effect on employment of the projects. We agree that further analysis has to be done to determine whether the projects have actually resulted in job losses. Nonetheless, as we noted in our report, Labor Department employment data and parent company responses do suggest that our calculations of potential employment losses may correlate to actual job losses. Furthermore, the methodology we used to calculate potential economic effects on the United States is the same methodology that OPIC said (in a 1986 report to the Congress) it would use to determine the potential effects on employment (excluding any offsetting assumptions OPIC may use) in its forthcoming mandated study of effects on U S. employment.

Lastly, in our 1981 report we did not, for our eight case study projects, find a direct correlation between the OPIC-assisted projects and subsequent job losses, but we did find two cases indicating possible job losses involving OPIC projects We further observed that OPIC's screening process was not thorough enough to ensure that an adequate determination was made to show that no job losses would occur from the OPIC-assisted investments.

Other OPIC comments on this chapter have been incorporated into our report where appropriate.

Conclusions and Recommendations

Conclusions

OPIC has approved a number of projects that should have been predicted to have direct negative impacts on trade and potentially negative impacts on employment when the proposed investments were evaluated Moreover, some ongoing projects that continue to receive OPIC assistance are having negative impacts on U.S trade and potentially negative impacts on U.S. employment.

We are concerned that existing OPIC procedures provide limited assurance that adequate determinations have been made during screening and monitoring to show that no significant adverse effects on the United States will occur or are occurring as a result of OPIC-assisted investments. In addition, we believe that OPIC's methodology for computing and presenting the economic effects on the United States of its projects has led to overly optimistic reports to the Congress concerning the magnitude of the direct economic benefits to the United States of OPIC-assisted projects.

Our analyses, using initial investor estimates and current operating results, show that a number of projects approved by OPIC might have had direct adverse impacts on U.S. employment. We believe that better screening and monitoring procedures would help OPIC to better identify such projects before and after they are approved. At present, OPIC evaluates proposed and ongoing projects using few, if any, formal policies and procedures. For example, there are no specific guidelines for evaluating projects in the sensitive electronics industry and no parameters defining what constitutes a "significant" adverse impact.

We did note some recent improvement in OPIC's government and non-government contacts and information gathering. However, we found little evidence that some organizations directly concerned with OPIC's actions, such as labor unions and trade associations, are routinely consulted and solicited for information in OPIC's screening and monitoring processes.

While we believe that OPIC has recently improved its contact with Labor Department officials, we are concerned that this contact be consistently maintained. According to Labor Department officials and our review of OPIC files, this contact has been inconsistent in the past For example, there is little evidence in OPIC's files that some important information—such as the Labor Department's TAA job loss data—had been considered in OPIC's project approval and monitoring processes for the projects we examined. Regarding OPIC's consideration of TAA information, we are not saying that OPIC's project approval decision should be based on whether

a company's employees have or have not filed TAA petitions—there are other considerations. However, we believe that OPIC should (1) be aware of and thoroughly investigate a company's TAA history before it grants assistance to a company and (2) track the TAA profiles of the companies and industries it is assisting. Furthermore, when OPIC analysts do their TAA analyses, they should thoroughly document the results of these analyses so that other analysts will be aware of them and can use them in evaluating future projects and in monitoring the economic effects of existing projects on the United States.

Other needed improvements in OPIC's screening and monitoring functions include more complete documentation of actions taken, increased level of effort devoted to screening and monitoring, verification and use of monitoring data, and determination of the appropriateness of and circumstances for discontinuing assistance to future projects found to have adverse effects on the U.S. economy.

OPIC currently uses a methodology that produces overly optimistic project evaluation results that are reported to the Congress. These reports to the Congress overestimate projects' creation of employment in the United States, reflecting to a large extent the number of U.S. job losses that might be prevented when compared to hypothetical alternatives.

OPIC should use a methodology that permits it to evaluate and report the effects of a proposed project on its own merits, apart from any offsetting alternative analysis. Any alternatives used for comparison with the proposed project should be realistic and complete and should be considered, evaluated, and reported separately.

The results produced by OPIC's methodology further obscure the direct effects on U.S. trade and employment of projects because OPIC analysts do not

- calculate and report the effects on U.S. employment expected from a project's initial procurement separately from the expected effects of its annual operations,
- gather and use information from the U.S. investor and other sources concerning the amount of indirect exports to the United States expected to be generated by the project, and
- use appropriate labor-output ratios to convert trade flow information into employee-years of employment.

OPIC's analysts also use this computational methodology to calculate and report the effects of ongoing projects on the U.S. economy. Thus, the results of OPIC's analyses and the reporting of these results to the Congress also may present an overly optimistic portrayal of the magnitude of the projects' impact on the U.S. economy

Recommendations

We recommend that the President of OPIC, in consultation with the Administrator of the Agency for International Development, take the following actions.

- Develop formal policies and a comprehensive system for screening and monitoring the economic effects on the United States of OPIC-assisted projects, including a methodology that more clearly and accurately (1) estimates the direct economic effects on the United States of projects being considered for OPIC assistance (separate from any possible alternatives) and (2) calculates the actual effects of ongoing projects on the economy of the United States. This methodology should include proper treatment of start-up and operating procurements, indirect exports to the United States, and appropriate labor-output ratios. Also needed are specific guidance for sensitive industries, parameters for identifying "significant" adverse impact, requirements for routine consultations with concerned public and private organizations, and thorough, consistent consideration of the Department of Labor's Trade Adjustment Assistance Group's actions.
- In annual reports to the Congress concerning the effects of OPIC-assisted projects on the U S. economy, (1) report (without offsetting alternatives) the aggregate results of the operations of projects expected to have (or having) positive direct impacts on U.S. trade and employment separately from the aggregate results of those expected to have (or having) negative direct impacts, (2) report separately the economic effects on the United States of any alternatives (including the presumed actions of non-U.S. investors) and assumptions that were considered and analyzed as part of the project approval process, and (3) report separately the effect on trade and employment of project construction and start-up procurement. (A suggested format for OPIC's reporting of economic effects on the United States is included in appendix IV.)
- Determine the appropriateness and circumstances for including in future assistance arrangements authority to discontinue assistance to projects whose operations are found to have adverse impacts on the U.S economy.

- Establish a documentation system for screening and monitoring that will record actions taken, help ensure the accuracy of results obtained, and be useful in performing future screening and monitoring analyses.
- Assess the adequacy of staff resources devoted to the screening and monitoring processes.
- Provide for selection verification of monitoring data and improved use of monitoring results through formal feedback to the screening process.

Agency Comments and Our Evaluation

OPIC disagreed with our conclusions and recommendations, which it characterized as irrelevant to its operations, given the methodological errors and misconceptions in our analysis. Specifically, OPIC (1) does not believe that formal guidelines or policies—including sector-specific guidance for sensitive industries—for screening projects are necessary and (2) considers that its current methodology for assessing its projects accurately estimates their impact on the U S. economy and provides a fair statement to the Congress of the effects of its projects.

We believe that we have been accurate in describing OPIC's project screening and monitoring procedures and its methodology for calculating and reporting to the Congress on the economic effects of its projects. Existing procedures—notably OPIC's failure to adequately document its screening and monitoring functions and a lack of formal guidance to govern its analyses—do not ensure that OPIC is making appropriate and consistent judgments about the projects it is screening and monitoring and therefore need to be improved.

As noted in our report and OPIC's comments, OPIC uses assumptions and alternatives to compute the benefits to the United States of the projects it assists. We recognize the justification for OPIC's use of such alternatives and assumptions in its project approval process, but we note that their use in mathematically computing the economic effects of projects obscures any direct adverse effects of these projects. Unless this methodology is clarified in OPIC's reports to the Congress, OPIC's claims of benefits to the United States gained from the projects it assists can be considered overly optimistic Accordingly, we believe our recommendations remain valid.

Verification of Claims of Trade Benefit to the United States

We visited 33 OPIC-assisted projects in 7 countries to verify whether trade benefits to the United States that were claimed on applications for OPIC assistance were valid and to observe operations and obtain testimonial evidence from project representatives regarding the impact of the project on the United States. We also wanted to use verified data obtained during these visits to help test the accuracy of parent companies' responses to our questionnaires.

Our 33 case studies included 22 projects from 6 "import-sensitive" industries or sensitive segments of industries such as electronics, textiles/apparel, certain agricultural products, certain chemical products, vehicles, and steel. We also visited 11 non-sensitive industry projects. During our visits to the projects, we reviewed accounting records showing the amount and source of production inputs (mainly equipment, supplies, and raw materials) and the amount and distribution of production outputs. In our review of these projects, we found that

- estimates of trade benefits to the United States made when projects were approved in 1980-83 varied widely from actual benefits realized during project operations and
- other industrialized countries sometimes benefit as much or more than the United States from the procurement activities of these projects

Investor Application Estimates Vary Widely From Actual Operations Data

Although we expected to find differences between the estimates on applications for OPIC assistance and the actual operating data for the project after it got started, some of these differences were quite large. For seven electronics projects for which we were able to obtain and compare data, we found that actual operating data were higher or lower than investors' estimates by more than twenty-fold in some cases. For example, we found that an investor had listed on its application that its Far East project would sell about $3 million in goods annually to the United States but was selling about $25 million and had estimated about $0.6 million in annual purchases from the United States while purchasing an average of about $19 million per year. Another investor that had anticipated that it would buy $18 million in raw materials annually from the United States was buying an average of about $6 million and exporting about $12 million in goods to the United States after estimating exports would be $64 million. Differences are to be expected, and reasons can be found for such differences, e.g., company policy changes, market changes, conservative or optimistic initial application estimates, and others. For example, we found that much of the large differences we discovered in data for the first project cited were due to

the investor's not including in its application the value of consigned raw materials manufactured in the United States—only the value added by the project was included in estimates of U.S. imports and exports. We reported this case to OPIC when we returned from our overseas visits. As far as we could determine, OPIC was unaware of this situation and had used the investor's incomplete estimates in its calculation of the impact on trade and employment, which was subsequently reported to the Congress.

The initial U.S. procurements by these electronics projects were substantial and could be expected to have potential one-time positive effects on the U.S. economy. However, the net annual trade flow between these projects and the United States was negative; that is, these projects sold more annually to the United States than they purchased from it. Total one-time initial procurement was $77 million (about $17 million less than estimated). Total actual annual average imports to the United States were nearly twice the amount of the average exports from the United States of production supplies and materials—$99 million in U.S. imports compared with $53 million in operating exports. Moreover, many project officials told us that their products are also indirectly exported to the United States by other foreign firms after being used in the manufacture of finished products, such as television sets or stereo equipment. We also analyzed data from other sensitive industries (textiles/apparel, chemicals, certain agricultural products, stainless steel, and vehicles) and found results similar to those for electronics.

We visited 11 other projects producing a variety of products, such as plumbing fixtures, paper products, dry cell batteries, drugs, detergent, and poultry. These projects are from industries considered non-sensitive, because exports of their products to the United States are not considered likely to adversely affect U.S. employment. We found that only one of the 11 projects exported to the United States and its exports represented only a small portion of its total production.

For seven non-sensitive industry projects for which we were able to compare actual data with investor estimates, we found that four investors had underestimated initial and operating procurements from the United States. In the three other cases the investors had overestimated procurement from the United States Annual purchases from the United States by these non-sensitive industry projects were much greater than their exports to the United States, about $7.6 million versus $8,000.

OPIC, in commenting on the two electronics projects we used as examples in this section, stated that the first example incorrectly compared data from different accounting systems. Thus, OPIC contends, our example drastically overstates the amount of value added to the product by the project. According to OPIC, the dollar amount of net imports to the United States was only $5 million to $6 million. Regarding the second example, OPIC commented that we omitted the fact that the project did not sell to the United States any of the substantial amount of exports originally projected. OPIC calculated that there has been a 95 percent decrease in anticipated imports of electronic components to the United States from the seven projects. Thus, the U.S. economy was not harmed by these projects as GAO claimed.

We agree that both import and export data for these two projects should have been included to avoid misconceptions. We also agree that we should have noted that the investor's estimates for the first project did not include the value of consigned goods. We have modified our report to incorporate these changes. We also agree that the annual sales by the first project to the United States exceeded its purchases from the United States by about $6 million ($25 million-$19 million), which resulted in a negative trade flow between the project and the United States In the second example, actual project exports to the United States were substantially less than estimated—totaling $12 million rather than $64 million, about one-fifth of the investor's application estimate. In this case, average annual sales to the United States ($12 million) also exceeded purchases ($6 million) from the United States.

With respect to the electronics projects' exports to the United States, OPIC's calculated 95 percent decrease includes a project that had not begun to operate, total exports to the United States in 1985 from the remaining six projects were about 40 percent less than the investors had estimated. However, this still represents a substantial direct negative trade flow accruing to the United States from these projects. Nonetheless, our point in presenting this material is to emphasize that differences between investor application estimates and actual project operating data exist and should be considered in determining whether OPIC's projects are having an unanticipated adverse impact on the U S economy. We did not conclude that such differences in themselves are harmful.

Procurement Benefits Other Industrialized Countries

Other industrialized countries (mainly Japan and the European Community) are benefiting as much and, in some cases, more than the United States from the procurement resulting from OPIC-assisted projects. In our case studies, except for the electronics industry, we found that other countries had sold more to the projects than had the United States. This greater benefit to other countries was the case overall for initial procurements, as well as subsequent operating procurements, as shown in table I.1.

Table I.1: Comparison of Procurement Sources for Case Study Projects

Figures in Percent

	Procurements from		
	United States	Host country	Other countries[a]
Initial procurement			
Sensitive industries			
Electronics	70	25	5
Other	6	50	43
Non-sensitive industries	27	42	31
Operating procurement for 1985			
Sensitive industries			
Electronics	50	10	40
Other	34	25	40
Non-sensitive industries	29	31	40

[a]Mostly Japan and European countries

Project representatives told us that they generally search for the least expensive source for procurement, which includes cheaper shipping rates from countries closer to the project than the United States. OPIC pointed out that, once a project is established, OPIC cannot control where production inputs are obtained.

OPIC Computation Sheet for Determining Effects of OPIC-Assisted Projects

Note Explanatory comments appear at the end of this appendix

See comment 1

See comment 2

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ADDENDUM NO 1 TO
ACTION MEMORANDUM OF
INSURANCE CONTRACT NO ____

Analysis of Effects Upon the U S Balance
of Payments and U S Employment 1/ & 2/

1 U S Export Effects

Net Direct U S Exports

(A) List gross exports of U S capital goods, materials, and production inputs to the project in the first 5 years

Initial U S Procurement	$ 7,592,697
Exports of Production Inputs	17,000,000
Total for 5 Years	$ 24,592,697

See comment 2

(B) List gross U S exports in first 5 years which project will displace Then indicate extent of net displaced U S exports after netting out displacement due to non-U S alternatives to proposed U S investment

Gross U S Exports Displaced	$ -0-
Displacement Due to Non-U S Alternatives	-0-
Net U S Exports Displaced	$ -0-

(C) Determination of net project-connected U S exports

Net Project-Connected U S Exports (A - B)	$ 24,592,697

Determination of U S Indirect Exports 3/

Net annual host country foreign exchange earnings and savings during first 5 years is $_____ Using percentage figures for U S Share of LDC Imports, determine indirect effect on U S exports for first 5 years

$_____ x 0 x _____% = Increase in Indirect U S Exports First 5 Years

$ N/A

Determination of Total U S Export Effects

(A) Total U S export effects for first 5 years	$ 24,592,697
(B) Conversion of total U S export effects for first 5 years into man-years of U S employment 4/	
(i) Annual Average of Total U S Export Effects for First 5 Years	= $ 4,918,539
(ii) Average Value of U S Manufacturing Production Per Employee (SIC 3674)	= 47,246
(iii) Annual Average Man-Years of U S Employment from U S Exports (i) ÷ (ii)	= 104.1

1/ Based on information represented to OPIC in answer to Formal Application questions

2/ Unless otherwise indicated, information should relate to the effects caused by the new investment for which insurance is sought

3/ The indirect U S exports credit shall be taken only on investments to be located in countries with substantial and chronic foreign exchange deficits on current account

4/ Based on Department of Labor statistics of current average value of U S manufacturing production per employee

Addendum No 1 to Action Memorandum on Insurance Contract No _____

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2 U S Import Effects

(A) List project enterprise's likely sales to the U. S market over the first 5 years

Project-Connected U S Imports Estimated for First 5 Years $ 46,750,000

See comment 3

(B) List additional volume of like products which investor represents would otherwise have been sold by other foreign suppliers to the U S market in the absence of the proposed U S investment 5/

Non-Project-Connected U. S. Imports Estimated for First 5 Years $ 46,750,000

(C) Determination of net project-connected U S imports for first 5 years.

Total U S Import Effects for First 5 Years (A - B) $ -0-

(D) Conversion of total U S import effects for first 5 years into man-years of U. S employment 6/

(i) Annual Average of Total U S. Import Effects for First 5 Years = $ -0-

(ii) Average Value of U S Manufacturing Production Per Employee (SIC _____) = ---

(iii) Annual Average Man-Years of U S Employment Lost from U. S. Imports (i) ÷ (ii) = -0-

3 U S Financial Flows

(A) Total dollar capital investment by all U S investors in the project over the first 5 years.

By Insured Investor	$ 2,781,697
By Other U S Investor	-0-
Subtotal	$ 2,781,697
Less Offshore Funds	-0-
Total Direct U S Dollar Investment Outflow	$ 2,781,697

(B) Estimated return flows to the U S of funds from the project over the first 5 years

Interest and Principal Installments	$ -0-
Dividends	1,605,000
Royalties and Fees	-0-
Return of Capital	~~2,642,612~~ 0
	1,605,000
Total Financial Flows to U S	$ ~~4,247,612~~

See comment 4

(C) Determination of Net U S Financial Flow

See comment 5

Total Net U. S Financial Flow Over the First 5 Years (B - A) $ 1,465,915

5/ Verified by independent analysis where possible
6/ Based on Department of Labor statistics of current average value of U. S manufacturing production per employee

See comment 6

Addendum No 1 to Action Memorandum
on Insurance Contract No _____

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Page 3

4 Summary

EMPLOYMENT

(A) Annual U S Export Related Effects on Man-Years of U S Employment	104.1
Annual U S. Import Related Effects on Man-Years of U. S Employment	-0-
Net Total Effect on U S Employment Based on Annual Average of EXPORT-IMPORT Effects	104.1

BALANCE OF PAYMENTS

(B) Total U S Export Effects	$ 24,592,697
Total U S Import Effects	-0-
Net U S Financial Flows	1,465,915
Net Effect on U S Balance of Payments for First 5 Years	$ 26,058,612

5 Other Effects

Discuss significant, independent estimates of the effects of the project on the international competitive position of U S technology (if any) and on U S market prices (if any) of the product(s) concerned

Comments

The following are explanatory comments on OPIC's sample computation sheet.

1. This is an example of the computation sheet OPIC used to compute the effects on U.S. trade and employment of the projects covered in our review. This particular sheet is for the sample project discussed in chapter 3. OPIC recently informed us that it will not use a formal computation sheet in the future.

2. OPIC offsets U.S. exports displaced by the project with those of a hypothetical alternative.

3. OPIC offsets (i.e., mathematically cancels out) the potentially adverse U.S. import flows of the proposed project with those of a hypothetical alternative—a foreign supplier to the U.S. market—to the project.

4. Handwritten changes were made by OPIC.

5. OPIC made an arithmetic error here. Value should be $-1,176,697—not $1,465,915.

6. OPIC made an arithmetic error here. The last two values should be $-1,176,697 and $23,416,000, respectively.

Comments From the Overseas Private Investment Corporation

Note GAO comments supplementing those in the report text appear at the end of this appendix

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January 16, 1987

Mr. Joseph E. Kelley
Associate Director
U.S. General Accounting Office
National Security and
International Division
441 G Street, N.W., Room 4124
Washington, D.C. 20548

Dear Mr. Kelley:

Pursuant to our recent telephone conversation I am enclosing three copies of OPIC's final response to the draft GAO report "Foreign Aid: Impact of the Overseas Private Investment Corporation Activities on U.S. Employment" (GAO Assignment Code 472102).

I would like to reiterate what Craig Nalen, OPIC's President, stated in an earlier letter to GAO dated December 23, 1986. In our view the report in large measure is "premised on incorrect factual assumptions concerning the manner in which the Corporation analyzes projects and thereafter reports its conclusions to the Congress. Consequently, it is impossible for OPIC to agree, much less comply, with many of the recommendations contained in the report, since they are irrelevant to OPIC's actual mode of operation."

You will recall that during the course of our conversation I volunteered that if the GAO's final report should differ significantly from the draft of November 24, 1986, OPIC would be prepared to modify the enclosed response. I believe that it is very important for the Congress to have before it a report which includes not only the GAO's findings, but also OPIC's response. We believe that permitting OPIC to react to any major modifications to the November draft GAO report, and having its modified response formally incorporated into the final report, would best serve the interests of Congress.

Sincerely,

Gerald T. West
Vice President
Office of Development

INTRODUCTION

In December 1985, Congress directed the GAO to "conduct a study of the impact on employment in the United States" of OPIC's activities. The GAO was required to report its findings by December 1986, and to share with OPIC the raw data it obtained in carrying out its research. The auditors, none of whom had previously worked on OPIC matters, did not begin their field work until the late spring of 1986. Perhaps because of the time pressures involved and the staff's unfamiliarity with OPIC, the draft GAO report* evidences considerable misunderstanding of OPIC operations, and is not a particularly relevant or useful review of the Corporation's activities.

Now on pp 32 38
See pp 41 42

Much of the draft GAO report critiques a methodology for analyzing the U.S. effects of OPIC projects, which in fact OPIC does not use, except in relatively rare circumstances. The auditors then suggest a methodology of their own for analyzing the U.S. effects of OPIC projects which is totally inadequate. Furthermore, it appears that the authors of the draft report neither appreciated nor understood the significance of OPIC's sectoral analysis process. Instead, they focused on a worksheet used by insurance officers which provides initial estimates of the U.S. effects of a proposed project. That worksheet does not form the primary basis either for OPIC's judgment of whether to proceed with a project or for its reporting to Congress. It is merely part of the complex process carried out in the analysis of projects. Thus, the GAO findings and recommendations concerning OPIC's methodology are unfortunately of limited value.

Now on pp 16 19
Now on p 32
See p 41

Now on pp 45 46
See p 49.

The report errs further by assuming that any project which generates exports to the United States will, ipso facto, result in U.S. unemployment. It is too simplistic, however, to equate imports to the U.S. with U.S. unemployment. (For example, OPIC's assistance to a banana plantation in Central America which exports to the U.S. obviously does not cause U.S. unemployment.)

See pp 49 50

It is notable that the 1981 GAO study of OPIC, specifically addressing the U.S. effects of OPIC-assisted projects, found no direct relationship between OPIC-assisted projects and U.S. job loss. At that time the GAO acknowledged the complexity of trying to assess the effects of such projects on U.S. employment and stressed the importance of making "appropriate basic assumptions." However, the current report largely ignores these complexities and rests on inappropriate assumptions.

*These comments are based on the GAO draft report dated November 24, 1986, not this final GAO report.

See pp 41-42

In sum, OPIC cannot accept the major findings in the draft GAO report because they are based on fundamental misunderstandings of its sectoral analysis process, or they are founded on naive and inappropriate economic assumptions. Because Congress directed the GAO to share with OPIC the raw data it obtained, OPIC analysts have been able to retrace the GAO's steps and understand the empirical basis (or lack thereof) from which the drafters of the report derived their conclusions and recommendations. In addition to this commentary, we have conveyed extensive written remarks to the GAO on the particulars of the draft report. This commentary pertains only to the major concerns OPIC has with the draft GAO report.

See p 13

OPIC'S ANALYTIC METHODOLOGY

Now on pp 16-24

Evaluating the impact of overseas investments on U.S. employment is not an easy task. The GAO's draft report evidences a lack of understanding of the procedures and methodology that OPIC uses to screen out projects with the potential for significant adverse effects on U.S. employment. The authors of the report erroneously asserted that OPIC invariably uses a "worst case" alternative--i.e., that OPIC always assumes that in the absence of OPIC assistance to the U.S. investor, a non-U.S. competitor will undertake the proposed project, displace U.S. domestic production and foreign sales, and make no purchases from the U.S. Although OPIC does consider the possibility that an investment might be made by a foreign company, this alternative is in fact rarely invoked, and only when there is concrete evidence to support such an assumption.

Now on pp 32-33, 36-37
See pp 41-42

Now on pp 33-35
See comment 1

The report presents numerous graphs purporting to show how, in a case involving the importation of ferrite memory cores and computer terminals, OPIC supposedly calculated the direct employment effect of the project as being negative and offset this against the jobs that would hypothetically have been lost under a "worst case" scenario. In fact, this methodology was not utilized by OPIC analysts at all in that case. OPIC concluded that U.S. employment would not be affected because: 1) the cores were no longer assembled in this country, and 2) the small number of terminals imported could be easily absorbed by growing demand.

See p 41
See comment 2

An analysis of the 22 projects in import-sensitive industries studied by the GAO confirms that its assertion that OPIC always uses a worst case scenario is unfounded. In these cases, the alternative scenario was employed by OPIC only four times; in all four situations, there was convincing independent evidence that a non-U.S. investor would undertake the investment absent the OPIC-assisted U.S. investor. In the majority of the projects (13 of 22), OPIC determined that project imports would displace existing imports from other countries or producers, and thus would have no negative effect

- 3 -

on U.S. employment. In three cases, OPIC concluded that although the project created incremental imports, they would not affect U.S. employment, either because the industry did not exist in the U.S., or because of expected growth in demand. Lastly, two of the projects studied involved neither U.S. imports nor the potential displacement of U.S. exports. Clearly, these facts do not support the GAO's claim that OPIC always uses the alternative assumption that a foreign investor would be involved were OPIC not to assist the project. Indeed, they show that OPIC does not use this assumption where to do so would be inappropriate. Therefore, the report's recommendations concerning improved analytic methods and reporting techniques--all of which are based on this incorrect assertion--are not relevant.

Now on p 54
See p 55

Now on p 40
See pp 49-50

The GAO proposes measuring a project's U.S. economic impact by calculating the project's net trade flows, without adjusting for any "hypothetical trade flows [which would] offset those of the proposed project". This methodological approach is grievously incorrect because it assumes that all U.S. imports from OPIC-assisted projects are incremental, and that they result in a concomitant loss of jobs for U.S. workers. This supposition is contrary to the economic realities in which OPIC and investors operate. It is unrealistic to expect that all imports from OPIC-assisted projects will only add to U.S. trade flows, and to claim that such imports are the direct cause of U.S. job losses. (This fallacy is illustrated by the absence of negative U.S. employment effects of banana exports to the United States.) Two cases in the GAO study exemplify the flaws in this approach.

Now on pp 44-46
See pp 46-47

The draft report points to a net negative impact of $218.3 million on U.S. trade from the OPIC-assisted projects examined. However, it ignores the fact that one project in Central America, involving the storage and trans-shipment of crude Alaskan oil through a pipeline, accounts for the vast majority of the direct "sales" to the U.S. from the 57 projects analyzed. To conclude that the trans-shipment services which lead to U.S. "imports" have led to U.S. unemployment is clearly fallacious. On the contrary, the project indirectly stimulates employment in U.S. oil-related industries. Proper treatment of this one project alone would virtually wipe out the aggregate negative trade and employment effects reported in the GAO draft report.

See p 47

Another project which the GAO claims has a negative employment impact involves the manufacture of recording equipment in the Far East. The investor indicated that the project had exports to the U.S. The GAO translated this dollar figure directly into a negative U.S. employment effect. However, the standard practice in this industry is to perform assembly overseas. There are few, if any, U.S. workers who could potentially be displaced by such a project. The assumption that imports automatically translate into the displacement of U.S. workers is simply incorrect. In sum, we

See p 49

believe it is erroneous to try to determine the impact of OPIC projects on the U.S. economy by simply looking at what the GAO claims are "direct effects," without giving due consideration to the facts of the particular case in question.

Now on pp 20 22
See p 30

The GAO's assertion that OPIC failed to maintain constant contact with the Department of Labor's Office of Trade Adjustment Assistance (TAA), and that such failure resulted in the loss of jobs by employees of eight companies receiving OPIC assistance is not supported by an examination of the relevant cases and the TAA files. In two cases, the relevant OPIC-assisted projects did not export to the United States. Thus, layoffs due to import competition cannot be attributed to the OPIC-assisted investments. In three instances, the TAA certifications referred to by the GAO were for products expressly different from those produced by the OPIC-assisted projects. In the last three cases, information contained in TAA public files was insufficient to demonstrate whether or not the certification involved merchandise identical to that produced by the OPIC project. At the same time, even where a certification relates to the same product, it is not necessarily relevant to the project OPIC is considering. In one of these cases an investor's employees had a single petition certified involving a similar product. However, that certification was issued in 1976; the company sought OPIC assistance in 1982. OPIC assistance could not have been causally related to job losses six years earlier. Examination of the TAA data provides absolutely no evidence from which to conclude that OPIC-assisted projects have resulted in layoffs of U.S. employees. When screening projects, OPIC does consult TAA data and appropriately uses this information to determine the sensitivity of an industry to imports.

Now on pp 16 24

OPIC sectoral analyses (which form the bases for all judgments about the U.S. effects of projects and for the Corporation's reports to the Congress) involve a great deal more complexity than the draft GAO report ascribes to them. First, OPIC sectoral analyses are not purely qualitative in nature. As our files demonstrate, these documents quantify considerable amounts of industry, trade and project information to help OPIC determine the effect of a proposed project. Second, OPIC does not rely solely--or even largely--on investors' estimates or projections of future economic trends. We conduct an extensive and independent economic analysis to verify the information provided by the investor, and to arrive at an independent judgment as to the effect of a particular project on the U.S. economy.

OPIC'S REPORTING METHODOLOGY

Now on pp 35 36
See p 41

The draft GAO report claims that OPIC's annual report to the Congress provides a distorted picture of the effects of OPIC-assisted projects. This is based in large part on the assertion that OPIC utilizes the "worst case" alternative to

See p 41

disguise adverse effects its projects are having on the U.S. economy. However, since OPIC does not utilize this assumption except where justified, it follows that the Corporation's reports to Congress are not distorted.

Now on pp 38 39
See p 39

OPIC analyzes the effects of its projects for the first five years of their operation. The GAO contends that this presents a distorted picture of their effects because substantial initial procurement may be offset in later years by project exports to the United States. When appropriate, OPIC sectoral analyses do take into account the effects of projects beyond five years, for example, in long-term projects involving agricultural tree crops. However, for its reports to Congress, the Corporation has determined that a five-year horizon provides a reasonable and accurate picture of the effects of OPIC's projects on the U.S. economy. Projections beyond five years are likely to be speculative and thus serve no useful purpose. Moreover, many projects are terminated or do not seek insurance beyond this time period. Furthermore, OPIC has been reporting to Congress on this basis for at least ten years, and is not aware of any previous Congressional or GAO concern whatsoever on this point.

OPIC'S SCREENING PROCEDURES

Now on p 19
See p 28

OPIC has informal written guidelines which outline the steps involved in carrying out sectoral analyses. In all instances, these guidelines are supplemented by "hands-on" training provided by an Office Director who works closely with new employees and interns. This Director has always reviewed all sectoral analyses; his work in all sensitive cases is reviewed by another director or his supervisor(s). Because OPIC is a small organization it prefers to substitute personal guidance for cumbersome bureaucratic procedures. Given the complex nature of the analysis that must be performed for each unique project, OPIC believes this approach makes sense. The GAO audit, it is important to note, contains no evidence that a single sectoral analysis carried out by OPIC was inaccurate or resulted in a project which harmed the U.S. economy.

Now on p 20
See p 29

Contrary to another GAO contention, OPIC has in fact developed policies for sensitive sectors. OPIC's Board of Directors has established specific criteria for agricultural and textile projects. OPIC has not developed any industry-specific criteria for the electronics industry; nor does it believe that it would be useful to do so. This industry covers a wide range of products which are constantly changing, and any guidelines would very quickly become obsolete. OPIC prefers to carry out its analyses on a case-by-case basis as Congress intended.

See pp 9 10, 19 20
See p 29

Congress clearly gave the Corporation discretion in determining when the harm done by a project was "significant" enough to warrant its rejection. OPIC exercises this judgment

- 6 -

in good faith. Each year, OPIC turns down an average of 10 projects formally and rejects several times that many informally. There are vast differences among industries in terms of their sensitivity to imports. No definition of the word "significant" could cover all of the situations encountered in the course of OPIC's analyses. OPIC prefers to analyze each project on its merits. Unless there is a finding that the Corporation has abused the trust of Congress, which is not asserted in the GAO's draft report, there is no reason to propose--as the GAO has done--that a specific definition is necessary.

See comment 3

The GAO draft report asserts that OPIC ignores the cumulative effects of its projects, which could harm U.S. employment. This is simply not the case. The Corporation has been and is concerned with the cumulative effects of its projects, particularly in sensitive industries, as demonstrated by its refusal to assist an expansion of the project cited in the report involving cut flower imports because of the cumulative significant harm that would result. Records in OPIC's files document that OPIC has been and is concerned with the cumulative effects of its projects in other sensitive industries, including electronics, pineapples and shrimp.

Now on pp 20-23

The GAO draft report asserts that OPIC analysts only "occasionally" refer to consultant studies or industry experts. OPIC analysts routinely contact industry experts at the Departments of Labor, Commerce, Agriculture, the ITC and other relevant government organizations such as USTR. They regularly consult, when appropriate, with nongovernment agencies such as trade associations and labor unions. It is true that OPIC has made only occasional use of consultants, in order to conserve scarce financial resources. However, it is prepared to call on outside analytical assistance when appropriate.

OPIC PROJECT MONITORING

See comment 4

The GAO draft report quotes representatives of two OPIC-supported projects as saying that one project had replaced production previously performed by U.S. parent company employees, and that another project's parent firm planned to move all of its operations offshore. Close examination of the facts in these cases--which have been conveyed to the GAO--illustrates the importance of thorough research to avoid jumping to unfounded conclusions. In one case, the parent company's reduction in domestic employment resulted from a consolidation of operations, common to the industry as a whole due to a declining market. This consolidation affected workers connected with a particular product produced only in the United States--not with the product produced overseas.

See comment 4

In the other case, the OPIC-assisted investment was clearly not a runaway. The investor later shifted overseas its

- 7 -

production of a product line, different from the one which OPIC insured. However, OPIC was not associated with this subsequent investment. Thus, the report's intimation that OPIC projects have resulted in the loss of U.S. jobs in these cases is patently untrue. It can be demonstrated in both cases that the OPIC-supported project did not result in U.S. job displacement.

Now on p 27
See pp 30-31

As a general rule, OPIC believes that auditing of investors' records during field monitoring is unneccessary. The GAO audit discovered no instance in which project representatives misrepresented information which was later contradicted as the result of an inspection of the books. Since active misrepresentation by project investors has not been shown to be a problem, there is no reasonable basis for the GAO's recommendation that OPIC should undertake selective audits of investors' records. OPIC acknowledges that there may be situations requiring an audit, and we will not hesitate to do so in such cases.

Now on pp 56-58

The examples given to substantiate the GAO's contention that major differences arise between the application and actual project results are misleading at best. It appears that the GAO arrived at its conclusion by analyzing the seven electronics industry projects appearing in its sample. OPIC's own analysis of the same data shows, however, that the GAO has made some fundamental errors with respect to its calculations.

Now on p 56
See p 58

In one example the report asserts that an electronics project, whose exports to the United States were originally estimated to be $3 million annually, were in actuality $25 million in 1985. This example is fallacious for two reasons: (1) it incorrectly compares data based on two different accounting systems and (2) it drastically overstates the amount of foreign value-added contained in the U.S. imports from the project. First, putting all data on a consistent accounting basis, the project increased its exports to the United States from an original estimated $16.8 million to a monitored $25.3 million. Second, the GAO indicates that the project is exporting on average $22 million more annually to the United States than was originally anticipated. However, it ignores the fact that the project increased its procurement of production inputs from the U.S. commensurately. Taking these two adjustments into consideration, the net imports to the United States are in reality significantly smaller than indicated in the draft report, resulting in additional net U.S. imports of only $5 to $6 million annually.

Now on p 56
See p 58

In the second example given by the GAO, the import situation is reversed. The report states that the investor has dramatically reduced its procurement of production inputs from the U.S., implying that the net benefit to the nation is less than projected. But the report ignores another important fact--this time that the project did not sell to the United States any of the substantial amount of exports originally projected.

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See p 58

Using a consistent accounting system and the GAO's method of calculating percent change, in the aggregate, there has been a 95% decrease in the amount of gross electronic component imports into the United States from that which the investors originally anticipated. In short, the GAO's own data disprove its assertion that the U.S. economy was harmed by these electronic projects.

See pp 56 57 24 25

More generally, it should be noted that projects often change from the time of their inception to the time of their implementation. Monitoring takes place a few years later, and the project--because of economic, marketing or other factors--may have changed even further. OPIC anticipates that these changes will occur and seeks in every instance to account for and reconcile differences between the information provided in the application and what is discovered during site visits.

Now on pp 27 28
See p 31

The draft GAO report posits a hypothetical situation in which an investor goes overseas and produces greater quantities of goods than originally anticipated. The report further supposes that this incremental production turns out to be harmful to the United States. It is then asserted than in such a situation, OPIC cannot legally cancel an investor's contract. In OPIC's actual experience, few projects have ever been revealed to have made drastic changes in their product lines or methods of operation. Nor does the draft GAO report cite any verified instance where significant changes in product lines of OPIC-insured projects led to adverse U.S. economic effects. Nonetheless, all investors are contractually obligated to notify OPIC of any such changes, on penalty of losing insurance coverage or financing.

Now on pp 26 27
See pp 30 31

Because OPIC is a small organization with very limited manpower resources, it expects each of its professional staff members to be versatile. OPIC does not devote "too few" resources to monitoring, as in fact most professional staff members become involved in the process. These officers receive comprehensive instructions from the Office of Development in order to carry out their monitoring responsibilities correctly. OPIC management is convinced that permitting all staff officers to review completed projects improves the project design and approval process and allows for a cost-efficient use of OPIC's limited travel budget. The report has not cited a single instance in which the number or type of personnel involved in project monitoring caused OPIC to monitor its projects less than adequately.

MISCELLANEOUS

The GAO draft report states that OPIC-supported investment is small compared with total U.S. overseas investment, representing less than 5 percent. By OPIC's analysis, however, it appears that OPIC's participation in the

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See p 9

flow of U.S. investment to developing countries is closer to 20 percent. Assisting 20 percent of U.S. investment in the Third World is not inconsiderable, but this figure greatly understates OPIC's role in assisting investment eligible for its support. Much of U.S. investment abroad is ineligible for OPIC assistance, because of its location in an ineligible country, potential detrimental effects to the U.S. economy, or other factors rendering it ineligible, including OPIC's inability to assist existing investment, and the exclusion of certain specific types of investments from its programs. Lastly, the data relied on by GAO excludes information about small business investments. While statistically this group may be inconsequential, serving the needs of this group is an important OPIC mandate.

See p 59

The report also claims that other industrialized countries (mainly Japan and the European Community) benefit as much as or more than the U.S. from procurement resulting from OPIC-assisted projects. Longstanding OPIC policies prevent the Corporation from insuring projects when more than 75 percent of the initial procurement is in "rich" third countries, or when more than 50 percent of the insured U.S. investment is to be spent on procurement in such nations. This ensures that the projects OPIC supports will obtain a considerable proportion of their initial procurement from the developing world or the United States. Once a project is established, however, OPIC cannot control on an on-going basis where the production inputs are obtained. Often investors do source their materials from industrialized nations. However, it is frequently the case that these inputs are produced by American subsidiaries operating abroad (e.g., chemicals purchased in Europe), and are sourced overseas because of savings in transportation costs. For a variety of reasons, then, OPIC does not believe this GAO concern to be a significant problem.

OPIC Response to the Draft GAO Recommendations

Now on pp. 54 55
See p 55

OPIC believes that, by and large, the recommendations contained in the draft report are not relevant to its operations, given the methodological errors and misconceptions inherent in the GAO's analysis--some of which we have cited above. For reasons detailed above:

- OPIC does not believe that it is necessary to have new formal guidelines or policies for screening the U.S. economic effects of projects.

- OPIC's present methodology for screening projects accurately estimates the impact those projects will have on the U.S. economy. Indeed, the GAO's own data support this fact. OPIC does not use the alternative hypothesis attributed to it by the GAO to offset possible adverse effects unless fully justified by the facts of a particular case.

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- In carrying out its sectoral analyses, the Corporation considers, where appropriate, the long-term economic effects of operating procurement and project exports. In its report to Congress, OPIC uses five-year projections only, and utilizes overall labor output ratios. OPIC management is confident that these methods, which the GAO and Congress have scrutinized and approved before, have fairly conveyed to the Congress the effects of OPIC projects for at least a decade and need not be changed.

- OPIC has specific guidelines for the textile and agriculture sectors, and believes them both unnecessary and unworkable for other sensitive sectors.

- The Corporation does not believe that its discretion in the use of the term "significant" in analyzing U.S. effects should be circumscribed and will continue to analyze the effects of each project on a case-by-case basis.

OPIC looks forward to responding in detail to all of the recommendations contained in the final GAO report to Congress.

GAO Comments

OPIC's major comments have been incorporated in the text where appropriate. The following are our responses to other points made by OPIC. These responses are numbered and keyed to OPIC's specific comments.

1. We used this project to illustrate how OPIC calculates the effects on employment of its projects, and it is an accurate depiction of OPIC's use of a hypothetical alternative to offset direct effects, as presented in chapter 3.

Further, we question whether the two reasons cited by OPIC—that the ferrite memory cores were no longer assembled in the United States and that imported computer terminals could easily be absorbed by growing demand—are sufficient to totally offset the project's potentially adverse effect on U S. employment. Although the specific process (core assembly) may no longer be performed in this country, the product to be shipped to the United States may compete with U.S. products that are intended to perform the same functions—e.g , semiconductor memories. Secondly, the growing market argument does not address the question of what U S production and employment would be in this industry in the absence of this project, the displacement of possible U.S production in a growing market does not mean that there would be no adverse effects on employment. Furthermore, our review of current project documents and OPIC's sectoral analysis shows that, contrary to OPIC's characterization (in its official comments) of project imports as "small," computer terminal shipments to the United States from this project are rather large, about 40,000 per year.

Finally, we note that these reasons were cited by OPIC in its sectoral analysis to make the qualitative judgment that the project "does not appear to have the potential for a negative effect on the U.S. economy or employment." This sectoral analysis, as we note in our report, does not quantify the effects of the project on trade and employment, and there is evidence to suggest that these reasons given in the sectoral analysis were not the basis for the actual offsets used in the computation sheet. For example, even though the sectoral analysis did not justify offsetting the negative effect on trade, the project's estimated adverse effects on both employment and trade were offset in the computation sheet and subsequent report to the Congress.

2. We question the reasonableness of OPIC's assumption that in 13 of 22 projects, U.S. imports from an OPIC-assisted project would displace existing imports from other countries or producers and, thus, would have no negative effects on the U.S economy. OPIC assumes that the

about-to-be displaced foreign supplier will forgo for the next 5 years its corresponding U.S sales and markets. This scenario is possible but not likely. In our opinion, it is more likely that the OPIC-assisted project would be just another supplier competing in the U.S. market.

3. We have deleted our discussion of the need for cumulative effects studies because OPIC recently, in response to congressional concern, initiated a legislatively mandated study which may assess the overall long-term cumulative impact of OPIC assistance on key industries.

4. We deleted the particular statements attributed to company and project officials because the events in question are some years old and we could not verify further the information provided either by them or OPIC.

Suggested Format for OPIC in Reporting Economic Effects on the United States

Table IV.1 is a suggested reporting format, which incorporates our reporting recommendations. OPIC could use this format to report separately the aggregate direct effects of those projects having positive direct effects and those having negative direct effects on U.S. trade and employment. The top section—designated "A"—records the direct effects of the project, while the bottom half—designated "B"—separately reports the offsets. Lines A1 through A4 record figures on the four direct project trade flows for the first 5-year period of operations. Both trade flow values and employment equivalents are recorded. The five general categories that OPIC uses to offset adverse direct effects of projects are reported on lines B1 through B5. Two of these categories, B2 and B3, offset adverse effects on U.S. employment but not adverse effects on U.S. trade flows. Finally, the effects on trade and employment of initial procurement exports for project construction and start-up are reported separately.

Format for Reporting Effects of Projects on U.S. Trade and Employment (aggregate effects during initial 5-year period of operations)[a]

	Trade flows $	Employment (employee years)
Project Operations:		
Direct effects		
A1. U.S. operational exports to the project	_____	_____
A2. Less displaced U.S. exports	_____	_____
A3. Less U.S. direct project imports	_____	_____
A4. Less U.S. indirect project imports	_____	_____
A. Total direct effects	_____	_____
Offsets		
B1. Imports displace existing U.S. imports from third countries	_____	_____
B2. U.S. market will grow fast enough to absorb project sales	b	_____
B3. U.S. does not produce the specific project product	b	_____
B4. Shipments to the U.S. would have been made by non-U.S. investor in absence of OPIC-assisted project	_____	_____
B5. U.S. exports would have been displaced by non-U.S. investor in the absence of OPIC-assisted project	_____	_____
B. Total offsets	_____	_____
Project Initial Procurement:		
Effects	_____	_____

[a]One sheet for those projects having positive direct effects and one sheet for those projects having negative direct effects.

[b]Does not offset adverse U.S. trade flows.

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