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BY THE COMPTROLLER GENERAL

Report To The Congress OF THE UNITED STATES

10/3/79

Meeting U.S. Political Objectives Through Economic Aid In The Middle East And Southern Africa

One way the United States advances its foreign policy objectives is through what is presently called Economic Support Fund assistance. The Congress has appropriated over \$8 billion for this fund from fiscal years 1975 through 1979. In fiscal year 1978, the fund accounted for 40 percent of all U.S. bilateral economic aid.

Notwithstanding the political focus of the fund, the Congress has also stressed in recent years that the assistance should, to the extent possible, be responsive to the New Directions policy set forth in the Foreign Assistance Act of 1961, as amended. The importance of economic goals has also been emphasized. This report comments on how the fund is achieving these two broad objectives.



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WASHINGTON, D.C. 20548

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

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This report comments on how Economic Support Fund aid (also known as Security Supporting Assistance) is advancing economic development and addressing basic human needs. It also describes how the political framework has imparted certain unique characteristics to the program.

One of the important ways in which the United States furthers its security and political interests is through the Economic Support Fund. The Congress appropriated over \$8 billion for this fund from fiscal years 1975 through 1979. Notwithstanding the political focus of the fund, the Congress has emphasized that these funds should be used for economically sound purposes and when possible, should respond to the New Directions policy set forth in the Foreign Assistance Act of 1961, as amended.

We are sending copies of the report to the Director, Office of Management and Budget; the Secretary of State; the Administrator, Agency for International Development; and to cognizant congressional committees.

James D. Stacks

Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

MEETING U.S. POLITICAL
OBJECTIVES THROUGH ECO-
NOMIC AID IN THE MIDDLE
EAST AND SOUTHERN AFRICA

D I G E S T

*Der cover
Bell*

ESF

The Economic Support Fund (presently the Security Supporting Assistance Program) is intended to advance U.S. political interests and demonstrate the U.S. commitment to, and concern for, countries receiving such economic assistance. This report assesses selected Economic Support Fund programs, including their responsiveness to basic human needs.

The Congress has appropriated over \$8 billion for these purposes from fiscal years 1975 through 1979. In fiscal year 1978, the fund accounted for 40 percent of all U.S. bilateral economic aid.

Notwithstanding the political focus of the fund, the Congress has also stressed in recent years that the assistance should, to the extent possible, be responsive to the New Directions policy set forth in the Foreign Assistance Act of 1961, as amended. The importance of economic goals has also been emphasized.

ECONOMIC ACHIEVEMENTS

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Most economic achievements of the fund have resulted from program assistance--specifically, large disbursements made against cash transfers, budget support, and commodity-import forms of assistance. This fast-disbursing type of assistance has

- responded to urgent economic needs in Egypt and Zambia;
- financed development activities in Jordan and Botswana;
- helped Israel through its balance-of-payments crisis after the 1973 October

ID-79-23

War and, in recent years, helped improve its economic situation; and

--helped Syria, to some extent, raise the productive capacity of selected economic sectors. (See p. 15.)

Capital development projects aimed at promoting sustained long-term growth have had little economic impact on recipient countries thus far. These large civil works and industrial-type projects require lengthy implementation periods and the Agency for International Development has encountered difficulties in meeting project schedules. This has delayed project completions and has resulted in large amounts of unspent funds. By the close of fiscal year 1978, for example, the Agency had disbursed only \$128 million of the almost \$1.5 billion obligated for Middle East capital development projects during the fiscal year 1975-78 period. (See p. 22.)

AGENCY RESPONSE

Agency for International Development officials agreed that capital development projects in Egypt, and particularly in Syria, have encountered implementation difficulties that have set back project timetables. The officials stressed that projects, such as those in Egypt, normally develop slowly and are subject to delays--circumstances not particularly unique to Egypt. The Egyptian projects will still have the desired economic impact, though later than anticipated.

GAO believes the Agency and the recipient countries have learned from past projects and should now be able to devise more realistic project schedules. To improve the capital development process further, the Administrator, Agency for International Development, should

--continue to encourage other Egyptian assistance donors to prepare annual estimates of local currency expenditures in Egypt;

- decide whether increasing the commodity-import portion of the Syrian program would be appropriate if capital projects cannot be developed or implemented within a reasonable period; and
- report to the Congress in the fiscal year 1981 authorizing request for Syria on the progress made in funding some local costs for fiscal year 1979 capital development projects.

MEETING BASIC HUMAN NEEDS

GAO's review of progress in advancing New Directions development goals in the Middle East noted that there are opportunities for improving the focus of Egyptian and Syrian programs. To achieve this, the Administrator, Agency for International Development, should

- carry out plans to support training in skills which improve employment opportunities for Egypt's poor,
- initiate urban community-development activities which help Egypt's poor participate in the development process, and
- report in the fiscal year 1981 congressional authorization request on efforts to focus the Syrian program on rural development needs. (See p. 32.)

AGENCY RESPONSE

Agency officials are acting in line with GAO's recommendations. Officials indicated that the recommendations identified areas where more should be done in Egypt. They also outlined plans for three fiscal year 1979 rural-development projects for Syria which they believe will be prototypes for future projects.

POLITICAL FRAMEWORK

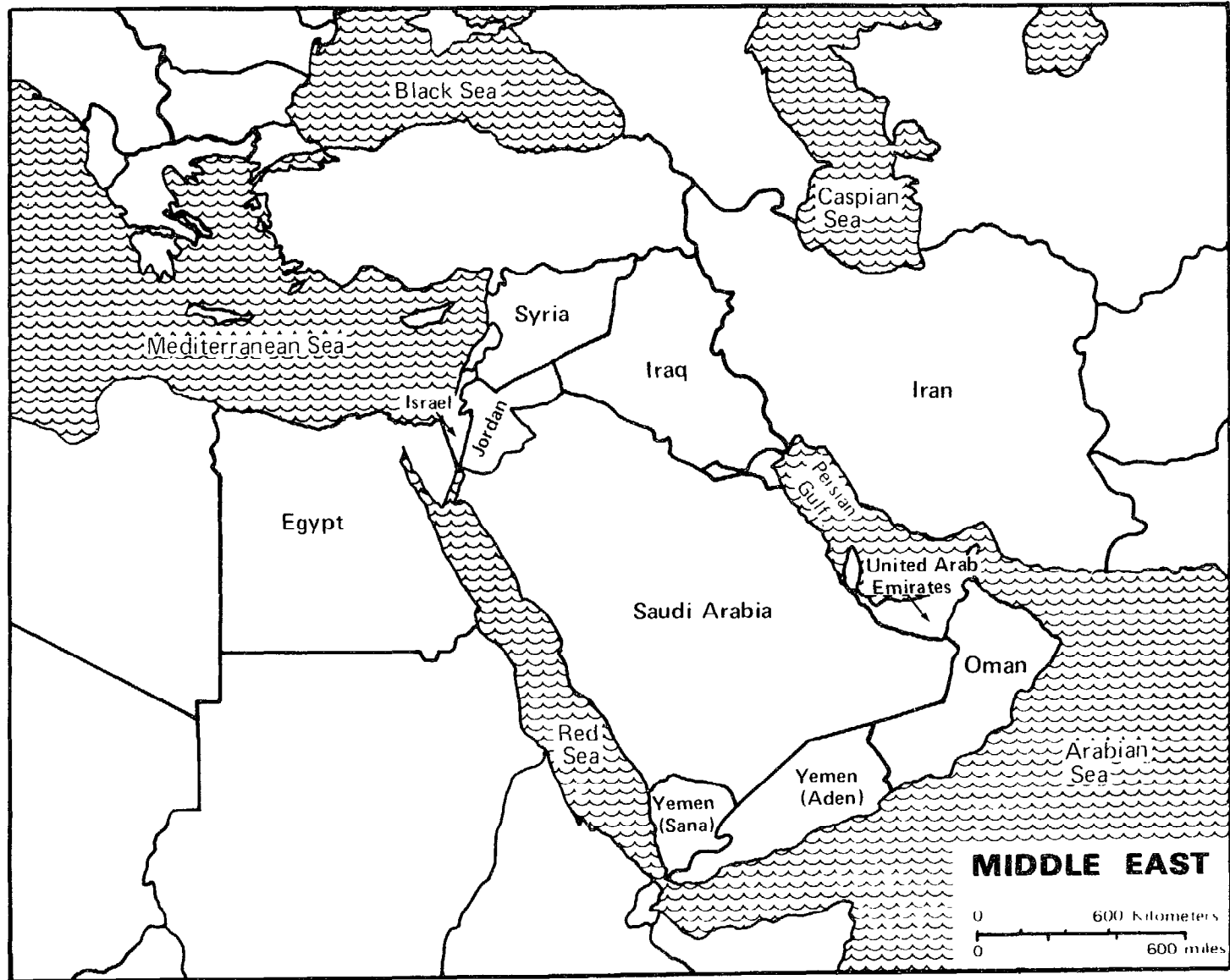
The political framework has given the program in the Middle East certain unique characteristics.

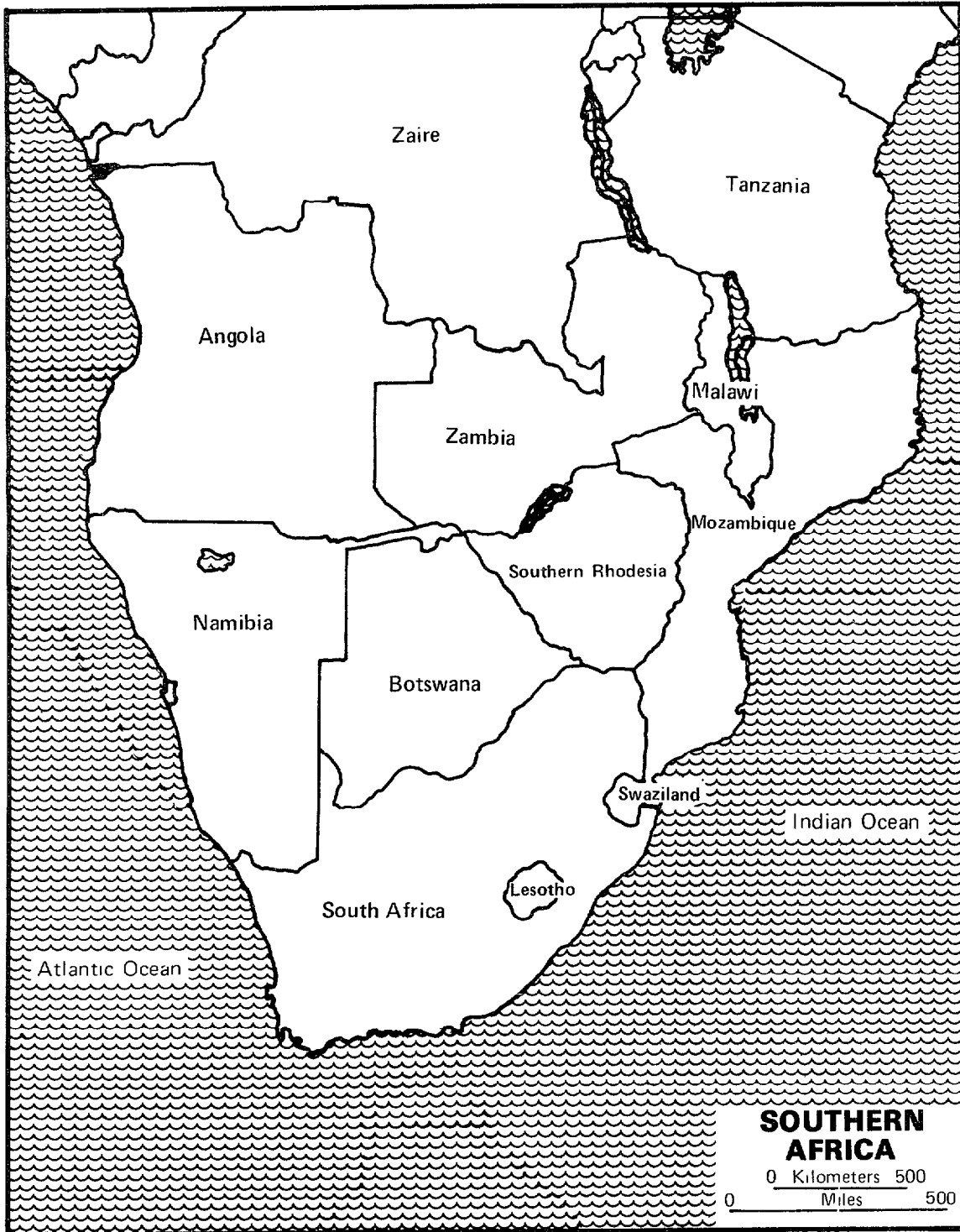
- Aid has become institutionalized. What started out in 1975 as an assistance program, at least partially directed toward short-term needs which resulted from the October 1973 War, has become a U.S. commitment to long-range economic development in support of peace.
- Extensive assistance for Middle East recipients has remained roughly the same over the past few years. The assistance became fixed because any decrease in U.S. assistance--either overall or to any one recipient--was considered a signal of waning U.S. concern or interest.
- Flexibility in setting Middle East assistance levels has been reduced by links between assistance levels for Egypt and Israel and for Jordan and Syria. The State Department says that this practice demonstrates U.S. even-handedness in dealings with Middle East countries. (See p. 5.)

PROGRAM CONSTRAINTS

Programs also have certain built-in constraints.

- High assistance levels set for political reasons can, in some instances, strain the abilities of the countries to effectively absorb the extensive project assistance.
- Programming of funds is influenced by the priorities of the recipients as well as by U.S. objectives. In some cases, this means the United States cannot carry out development goals it regards as important.
- In some countries, U.S. officials are sensitive about having large U.S. staffs working there. This strains field mission ability to monitor assistance programs. (See p. 10.)





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ABBREVIATIONS

AID	Agency for International Development
CIP	Commodity Import Program
ESF	Economic Support Fund
GAO	General Accounting Office

CHAPTER 1

INTRODUCTION

The Economic Support Fund (ESF), formerly designated Security Supporting Assistance, ^{1/} can be defined as economic assistance provided to certain countries or areas in support of U.S. security and political interests. ESF also represents a fusion of political and economic objectives. The influx of economic aid hopefully contributes to internal stability which in turn affects the political postures of the recipient governments. As a political signal per se, ESF demonstrates the U.S. commitment to and concern for the countries receiving funds.

The Foreign Assistance Act of 1961 provides the basis for ESF; subsequent amendments have further defined the Congress' intent with respect to the uses and limits of such assistance. In recent years the Congress has stressed that ESF funds be used, to the extent possible, in ways consistent with the New Directions policy set forth in the Foreign Assistance Act of 1961, as amended. The importance of the economic goals of ESF programs has also been emphasized.

ESF RECIPIENTS

From fiscal years 1975 through 1979, the United States appropriated over \$8 billion in ESF assistance. In fiscal year 1978 alone, ESF constituted 40 percent of all U.S. bilateral assistance.

The Middle East

The bulk of ESF monies has been concentrated in the Middle East over the past 5 fiscal years, earmarked for four countries as follows:

^{1/}The International Security Assistance Act of 1978 (P.L. 95-384, Sept. 26, 1978), replaced Security Supporting Assistance by establishing an Economic Support Fund.

	ESF aid (FY 1975-79) (millions)
Israel	\$3,404.5
Egypt	3,242.5
Jordan	476.1
Syria	<u>438.0</u>
Total	<u>\$7,561.1</u> (note a)

a/Includes funds from the Middle East Special Requirements Fund.

This considerable financial support reflects the high priority the President and the Congress have attached to bringing about a just and lasting peace in the Middle East.

Southern Africa

Mounting U.S. concern over the volatile situation in southern Africa has led to the provision of ESF monies to some of the majority ruled states in the region. U.S. programs there are aimed at alleviating the dislocations caused by political turbulence in Rhodesia, Namibia, and South Africa. In fiscal year 1977, \$34 million in ESF funds was provided for Botswana, Zambia, and regional projects; ^{1/} assistance increased sharply to over \$100 million in fiscal year 1978, and the program expanded to include Lesotho and Swaziland. An additional \$45 million was appropriated for southern Africa in fiscal year 1979.

Other recipients

In recent years other countries have also received ESF monies for a variety of political and economic reasons. Recipients have included Spain, Turkey, Malta, Lebanon, Cyprus, and Jamaica. A profile of ESF assistance by individual country is shown in appendix I.

PROGRAM COMPOSITION

A key advantage of ESF is its flexibility in financing many types of economic aid. The aid generally falls into two broad categories:

^{1/}In addition, \$20 million in ESF assistance was provided to Zaire in 1977.

--program aid which includes cash transfers,
and commodity-import financing; and

--project aid which consists of capital develop-
ment projects and technical assistance projects.

In some cases, these countries also receive other assistance,
such as military equipment, services, and training from non-
ESF sources.

GAO STUDIES OF SECURITY
SUPPORTING ASSISTANCE

We have given priority attention to ESF, both because
of the fund size and because of congressional concern about
its impact. Thus, this is a follow-up report to four pre-
vious reports on the program.

--"Issues and Observations on the Purposes of
Special Security Supporting Assistance Pro-
grams," ID-76-11, September 12, 1975.

--"Egypt's Capacity to Absorb and Use Eco-
nomic Assistance Effectively," ID-79-33,
September 15, 1977.

--"U.S. Economic Assistance for Israel,"
ID-78-31, August 18, 1978.

--"U.S. Economic Aid for the West Bank and Gaza--
A Positive Contribution," ID-78-35, July 5, 1978.

SCOPE OF REVIEW

Information for this report was obtained principally from
U.S. Government records and discussions with AID and Depart-
ment of State officials. In view of the concentration of ESF
monies in the Middle East and southern Africa, and our inter-
est in examining the use of ESF in a regional context, we
limited our review to an analysis of ESF programs in Israel,
Egypt, Jordan, Syria, Botswana, Zambia, and Lesotho. Our
review focused on the program assistance, capital development
project assistance, and basic human needs activities. We
selected the first two forms of assistance because (1) they
account for a large part of the total aid dollar value and
(2) prior reviews of programs in the Middle East have noted
undisbursed funds and implementation problems. We reviewed
basic human needs activities because of congressional interest.

In September and October 1978, we visited Egypt, Jordan, Syria, Botswana, and Lesotho to review the programs with U.S. officials. We also talked with local government officials and visited selected project activities. Our review in southern Africa was limited to transport, refugee, and program assistance components.

Our work was directed primarily toward (1) learning how the ESF program is planned and administered, (2) identifying the economic-development impact of the program, (3) examining AID efforts to carry out the congressional New Directions mandate, and (4) identifying problems and the constraints facing the success of these efforts.

CHAPTER 2

THE POLITICAL FRAMEWORK

ESF is conceptualized as a mechanism to promote the interests of the United States and the security and economic well-being of recipient countries. Although the aid itself is expressly economic, the primary reason for its use is political; economic development considerations per se remain secondary. In general terms, ESF monies have been extended to areas where it has been determined that the funds can usefully serve the cause of peace or can stave off serious economic or political crises.

AID TO THE MIDDLE EAST

The Sinai Accord concluded between Israel and Egypt following the October 1973 War provided the catalyst for an influx of U.S. economic assistance to the Middle East in support of peace efforts there. The administration's proposed aid program for fiscal year 1975 included economic assistance to Egypt, Jordan, and Israel; Syria received aid during that fiscal year through the Middle East Special Requirements Fund.

The overall objective of U.S. assistance is to create a more receptive climate for peace in the region. That goal has been translated into programs designed to foster internal political and economic stability, maintain moderate regimes, and strengthen U.S. bilateral relations with the Arab states. Assistance to Israel is viewed as a tangible and positive expression of the U.S. commitment to Israel's security and economic well-being.

Institutionalization of U.S. assistance

Initially, U.S. aid to the Middle East was at least partially aimed at addressing specific, short-term objectives. In the aftermath of the October 1973 War, aid was programed to help offset Israel's balance-of-payments difficulties and to support Egyptian reconstruction. According to the State Department, the programs were consistent with the concept of using ESF to deal with hopefully finite, temporary crises.

The U.S. commitment to the peace process led to an expansion of the assistance programs and buttressed the long-term nature of U.S. economic involvement in the area. In Egypt and Jordan, in particular, the United States is heavily committed to long-range development efforts, and large aid levels are now projected into the early 1980s.

ASSISTANCE TO SOUTHERN AFRICA

The allocation of ESF monies to countries in southern Africa is a relatively recent occurrence, predicated, according to AID officials, on the U.S. desire to evidence support for majority rule and to ameliorate the effects of the conflict there. The assistance reflects the desire of the U.S. Government to support moderate states committed to negotiated settlements. The authorizing legislation provides explicit language on the appropriate use of such assistance.

"* * * funds may be used to provide humanitarian assistance to African refugees and persons displaced by war and internal strife in southern Africa, to improve transportation links interrupted or jeopardized by regional political conflicts, and to provide economic support to countries in the region."

The Southern Africa Special Requirements Fund authorized by the Congress for fiscal year 1978, earmarked funds for Botswana, Lesotho, Swaziland, and regional programs. The legislation also provided that no aid be made available to Zambia unless the President determined that such assistance was in the foreign policy interests of the United States. The President did so determine, and \$30 million was allocated to Zambia in fiscal year 1978.

In its fiscal year 1979 budget, the administration proposed continued ESF funding for the Botswana transport sector, a commodity-import program (CIP) for Zambia, and regional programs for refugee assistance. Funding for small assistance programs in Lesotho and Swaziland was transferred to the AID general development assistance accounts. The administration proposal represented an attempt to distinguish important activities that could not normally be financed from the functional development assistance accounts.

SETTING THE ASSISTANCE LEVELS

The Department of State provides the political and security justification for extending ESF monies, and, consequently, bears responsibility for determining the aid levels necessary to satisfy those objectives. That responsibility is exercised in cooperation with AID, which administers the programs.

The zero-based budget process

AID field missions 1/ prepare annual budget submissions for consideration by AID/Washington and the State Department. Under zero-based budget techniques, a series of options are presented, each treating a specified assistance level with corresponding program components. In ESF countries, Ambassadors take commanding roles in recommending the proposed assistance levels.

AID/Washington then reviews the submissions, primarily on the basis of economic justifications, and its recommendations are represented within Department of State country decision packages. The next level of review takes place in the Security Assistance Program Review Working Group of the Arms Export Control Board, 2/ an advisory body established to counsel the Under Secretary of State for Security Assistance, Science and Technology, on security assistance matters. Following formal consideration by the Board and recommendations by the Under Secretary, the Secretary of State transmits his recommendations to the President through the Office of Management and Budget.

"Straight-lining" assistance levels to the Middle East

In theory, the zero-based budget process allows consideration of a number of options, but in practice, the ESF levels for the Middle East have remained relatively fixed over the past few years. "Straight-lining" advocates argued successfully that any diminution of U.S. aid--either across-the-board or to any one recipient--conveyed a negative signal that would adversely affect U.S. political objectives.

Thus, ESF assistance to Israel, for example, amounted to \$785 million in fiscal years 1978 and 1979, and the same amount is being requested by the administration for fiscal year 1980. Similarly, the level of aid to Egypt has been

1/There is no AID mission in Israel. The budget submission is prepared by the AID/Washington staff.

2/A group composed of representatives from the Departments of State, Defense, the Treasury, the Arms Control and Disarmament Agency, the National Security Council, the Office of Management and Budget, the Joint Chiefs of Staff, the Central Intelligence Agency, and the Agency for International Development.

set at \$750 million annually. In the case of Jordan, \$93 million in ESF funds was provided in each of fiscal years 1978 and 1979 for the country program. In fiscal year 1979, however, an additional \$50 million was allocated for the Maqarin Dam project. AID has stated that the decision to fund Maqarin as a separate line item in the budget was due to the project's size and planned multiyear funding commitment.

A significant departure from the "straight-lining" of aid levels occurred in the fiscal year 1980 budget request, when the administration proposed a funding level of only \$60 million each for Syria and Jordan. There was also a separate request of \$38 million for the Maqarin Dam project.

The proportionality concept

Flexibility in determining assistance for the Middle East has been further reduced by the application of the proportionality concept. Aid to Egypt in fiscal year 1976 was raised to \$750 million, an increase of \$500 million over the preceding year. The increase was justified primarily on the basis of demonstrating U.S. evenhandedness in the Middle East. Assistance to Egypt was made commensurate with the economic assistance to Israel. A similar link also exists between the Jordanian and Syrian assistance programs. State Department officials told us that the recipients themselves attach importance to these pairings.

POLITICAL INFLUENCE ON PROGRAM COMPOSITION

Given the inherently political character of ESF, it is not surprising that the actual composition of the programs as well as the aid levels, as such, reflect political and security objectives. This should not, however, obscure the fact that these programs have legitimate developmental objectives.

ESF provides the flexibility to use types of aid not ordinarily authorized under regular U.S. development assistance programs. Significant amounts of program and capital development aid have been and will continue to be programmed to meet the high politically set assistance levels. This includes cash grants and commodity-import financing as well as funding of large-scale infrastructure projects.

Program assistance

Program assistance has been provided under the ESF umbrella in the form of cash transfers to Israel, 1/ Jordan, and Botswana, and CIPs for Egypt, Syria, and Zambia. The compelling motivation for the continued provision of such assistance is the furtherance of U.S. security and political objectives. Internal stability is perceived as a means of providing Middle East leaders, such as President Sadat, with flexibility in pursuing peace. Cash transfers provide additional foreign exchange and budget resources and help relieve the burden of defense expenditures borne by recipient governments.

A key argument advanced for CIP use has been the need to temper internal political and economic instability through the influx of fast-disbursing assistance. The visibility of commodity imports also demonstrates U.S. involvement in and commitment to the economies of the region. The assistance program for Syria has also led to CIP use as a means of reaching the high level of assistance mandated for political reasons.

Project assistance

A wide selection of capital projects comprises the AID project portfolio. The high Middle East assistance levels require the inclusion of many large-scale projects to reach the authorized levels.

There are certain projects that offer perceived political as well as economic benefits. In Jordan, the United States has become the prime sponsor of the \$650 million Maqarin Dam project. Aside from any economic benefit calculations, U.S. participation is viewed as crucial to the project's success from the standpoint of attracting other donor support and resolving the water rights questions surrounding dam construction.

The impact of political factors on specific project selection is demonstrated in southern Africa. A key reason for U.S. funding of the Southern Perimeter Road in Lesotho, for example, was the desire to support the Lesotho policy for nonrecognition of the South African homeland of Transkei.

1/Israel also received CIP aid through FY 1978.

Indeed, the U.S. Ambassador to Lesotho enthusiastically supported the decision to fund a sizeable portion of the road, on its political merits, even before the economic feasibility was established. The anticipated funding of transport activities in Botswana is a similar instance.

Political considerations are also reflected in the desire to benefit certain target groups. In Jordan, U.S. assistance to the Jordan Valley accommodated Jordanian priorities as well as the less visible goal of providing productive employment for disadvantaged Palestinians. As a further example, in Egypt, AID involvement in the improvement of the Cairo telephone service is geared, in part, to affecting the Egyptian middle class whose support is necessary to President Sadat. AID officials pointed out that, aside from political considerations, the telephone project has economic development significance.

PROGRAM CONSTRAINTS

The attainment of political and economic stability objectives must be done through the effective use of assistance funds. The ability to do so is, to some extent, hindered by certain built-in program constraints.

Absorptive capacity

Assistance levels--set on the basis of political considerations rather than on the ability of recipients to absorb the assistance--can, in some instances, strain the AID and recipient-country ability to devise economically sound, implementable projects.

The United States has been channeling economic aid into Egypt for the last 4 years, currently at an annual rate of \$1 billion. That level requires substantial input--financial and managerial--from the Egyptians; consequently, AID bears the responsibility for monitoring Egypt's continued ability to provide such inputs.

In Syria, if assistance continues at projected levels and current AID plans for expanding rural services projects are not successful, there is a possibility that quality projects acceptable to AID will not be available for financing.

Recipient receptivity

The programing of ESF monies is also influenced by the priorities of the recipients and by U.S. objectives. Indeed,

we found in Egypt, Syria, and particularly in Jordan, that AID missions work closely with government officials to articulate areas of concern and ways in which AID can respond to those needs.

Nevertheless, the recipients have in some cases precluded AID from becoming involved in certain projects. AID sensitivity to the political objectives of the assistance programs has perhaps curtailed the leverage otherwise exercised in support of development objectives. In Jordan and Syria, for example, there has been a decided lack of interest in developing bilateral family-planning programs.

There is also the risk that activities may have a boomerang effect on program goals. Officials in both Jordan and Syria have complained that program documentation requirements for AID-sponsored projects are time-consuming, unnecessary, and denote a lack of trust. The AID mission staff in Jordan indicated that this negative perception becomes an impediment in dealing with the Jordanians and, consequently, results in politically undesirable side effects.

Staff levels

Because of managerial and security concerns, the size of AID mission staffs in Jordan, Syria, Botswana, and Lesotho has been limited by the U.S. Ambassadors for those countries. The validity of such concerns notwithstanding, staffing limitations strain the abilities of these missions to monitor aid programs--a problem that will become more acute as more projects move into the implementation phase.

ADDRESSING DISLOCATIONS IN SOUTHERN AFRICA

ESF was introduced to the countries of southern Africa in fiscal year 1977 to respond to the dislocations in the region caused by the movements toward majority rule. The effects of conflict and the continuing political uncertainties justified the use of ESF, which offered the flexibility to finance transport-sector activities, CIPs, and program grants.

The United States has also assisted most of these countries in addressing their long-term development needs in agriculture, health, and education. Such assistance has been funded at times under AID development assistance accounts and, at times, under ESF. For fiscal year 1980, the administration is requesting funds from the ESF account for Botswana, Lesotho, Malawi, Mozambique, Swaziland, Zambia, and regional projects.

The authorizing legislation specifically provides for the use of ESF funds where transport links are jeopardized by conflict and also for refugee assistance. Assistance for transport needs has been provided to Lesotho and is planned in Botswana.

AID is providing \$26 million 1/ for construction of the Southern Perimeter Road in Lesotho, to respond to disruptions caused by the Lesotho policy of nonrecognition of the Transkei homeland South Africa established. The road will permit Lesotho nationals in the eastern part of the country to reach western Lesotho without entering the Transkei homeland. The construction of the road will also support the achievement of some development objectives. It will facilitate the expansion of services to western Lesotho where 14 percent of the country's 1.2 million people live. The AID grant agreement includes a waiver, permitting the purchase of bulk materials in South Africa.

Funds were also allocated to the Botswana transport sector in fiscal year 1978 to assist in the anticipated Government takeover of the railroad. Eighty percent of Botswana exports and imports are carried on this north-south rail link which is owned and operated by Rhodesia. Botswana faces the possibility that service will be interrupted as a result of conflict in Rhodesia. A sustained interruption of service would have a devastating economic effect on Botswana and could require South African assistance to restore rail service. The project failed to materialize, and the fiscal year 1978 funds were reallocated for a program grant.

Although AID is no longer proposing assistance to the railroad, it is continuing to allocate funds to the transport sector. Only one road project under consideration will provide an alternate export route. This project, which will link population centers in eastern Botswana with Namibia, will not be in suitable form for funding before fiscal year 1980. Other projects under consideration will support the development of the transport system needed to address the needs of the rural poor and will facilitate the economic integration of remote areas into the rest of Botswana. These latter projects should be viewed against the appropriate ESF or development criteria.

ESF funds are also being used to ease the refugee situation. Through the United Nations High Commissioner for

1/Additional funds have been requested for fiscal year 1980 to upgrade Lesotho's national road maintenance capability.

Refugees and voluntary agencies, AID is assisting Botswana and Zambia in absorbing a rapidly escalating influx of Rhodesian refugees. Assistance has also been provided to expand educational opportunities for South African refugees in Botswana.

We discussed with AID officials the desirability of distinguishing projects which respond to the economic dislocations of regional conflict from AID activities which primarily address long-term development. The advantages of this dual approach would be to

- inhibit the institutionalization of assistance levels at heights inflated by the short-term, conflict-induced needs and
- facilitate project evaluation against the appropriate ESF or development-assistance criteria.

The distinction of AID activities by primary objective, for example, could be accomplished by (1) using a regional ESF allocation to fund conflict-related projects (as done in the case of the fiscal year 1978 Southern Perimeter Road project in Lesotho) while still funding country programs under ESF or (2) using ESF solely for conflict-related assistance and funding conventional aid activities from development-assistance accounts, as done in fiscal year 1979.

AID officials told us that this is not practical because conflict-related assistance and development assistance are not mutually exclusive. They said the basic rationale for ESF is normally the special U.S. political and economic interests to be served in specific countries or regions. Thus, the decision to use ESF should be made by country or region, rather than by project.

AID officials believe that a clear distinction must be maintained between the overall political or economic rationale for ESF funds and their ultimate utilization. In essence, every effort is made to direct these funds to development-assistance objectives, but political objectives are sometimes overriding.

OBSERVATIONS AND CONCLUSIONS

The administration has consistently and successfully argued that the high levels of assistance to Israel, Egypt, Jordan, and Syria, in and of themselves, convey a clear political signal of the continued U.S. commitment to the goals of peace and stability in the region. By the same token, any reduction of those levels would be perceived as an equally

clear signal of wavering U.S. support. The introduction of the proportionality concept--linking the aid levels to Israel and Egypt, and Jordan and Syria--has been used as a means of reinforcing the U.S. principle of evenhandedness in its dealings with the Middle East states.

Without challenging the validity of the political imperatives that led initially to the institutionalization of these high assistance levels, we believe that it is important to examine the justification for such levels in the context of the economic achievements the programs have already, or can reasonably be expected to achieve. (See chs. 3 and 4.) State Department and AID officials say that these achievements are reexamined annually during the budget-preparation process.

It is also important to recognize the limitations on the administration's ability to comply with the congressional mandate to use ESF, to the maximum extent feasible, to carry out the New Directions policy set forth in the Foreign Assistance Act of 1961, as amended. Such compliance will be limited by the need to program the high, politically set assistance levels. Thus, cash grants, CIPs, and large-scale capital development projects will continue to be important features of the Middle East programs in order that the assistance is absorbed.

For the recently initiated ESF programs in the countries of southern Africa, it would be helpful to distinguish between the funding of economic needs induced by conflict and long-range development needs. This could help avoid the institutionalization of assistance at extraordinary levels, while enhancing the capability to evaluate assistance activities against either ESF or development-assistance criteria. State Department and AID officials, however, indicated their preference for funding programs from a single account.

CHAPTER 3

ECONOMIC ACHIEVEMENTS: PROGRAM ASSISTANCE

ESF is intended to advance the development of recipient countries as a primary means of satisfying stated political objectives. Creation of a stable economic environment is the short-term economic goal of the assistance, and fast disbursing program assistance is the primary tool for its achievement. Over the longer term, the assistance is expected to provide the basis for equitable growth; project assistance is the primary means of realizing this objective.

To date, achievements of ESF have come largely from program assistance rather than project assistance. Most disbursements have been made against cash transfers, budget support, and commodity-import forms of program assistance.

The amounts of program assistance provided are shown here.

<u>Country</u>	<u>Type of assistance</u>	<u>Purpose</u>	<u>Total obligations FY 1975-78</u>	<u>Disbursements as of 9-30-78</u>	<u>FY 1979 planned obligations</u>
-----millions of U.S. dollars-----					
Israel	CIP, cash transfer	Balance-of-payments support	\$2,619.5	\$2,317.6	\$ 785
Egypt	CIP	Balance-of-payments support	1,205.0	662.6	250
Jordan	Cash transfer	Budget support	255.5	255.5	30
Syria	CIP	Balance-of-payments support	105.0	31.9	20
total Middle East			<u>\$4,185.0</u>	<u>\$3,267.6</u>	<u>\$1,085</u>
Zambia	CIP	Balance-of-payments support	50.0	35.7	20
Botswana	Cash transfer	Budget support	9.0	-	-
total Africa			<u>59.0</u>	<u>35.7</u>	<u>20</u>
Total			<u><u>\$4,244.0</u></u>	<u><u>\$3,303.3</u></u>	<u><u>\$1,105</u></u>

A substantial share of ESF funds--71 percent over fiscal years 1975-78--has been provided as program assistance. Use of program assistance is advocated when a shortfall in foreign exchange or budget resources jeopardizes performance of an economy.

We found that program assistance has indeed helped stabilize the economies of some recipients. Balance-of-payments support to Egypt is currently assisting that country in meeting its population's needs. Program assistance was instrumental in sustaining Israel's economy during the balance-of-payments crisis which followed the October 1973 War.

We also found that program assistance has been extended to countries that did not have critical balance-of-payments or budgetary problems. The provision of assistance to Israel in recent years--and to Jordan and Botswana--are cases in point. In these instances, the additional resources permitted the acceleration of development plans.

STABILIZING ECONOMIES FACING BALANCE-OF-PAYMENTS CRISES

Program assistance has been extended to Egypt, Israel, Syria, and Zambia to help overcome balance-of-payments difficulties. This assistance has generally been provided under CIPs, although assistance to Israel has, in part, been provided under cash transfers.

Egypt

Program assistance has been used to support economic stability in Egypt. Since 1973, Egypt has faced a critical balance-of-payments situation with its foreign exchange requirements far outstripping its ability to finance them through foreign exchange earnings. CIP has made possible the import of basic foodstuffs, consumer goods, inputs to keep industry operating, and capital equipment. CIP-financed imports totaled \$233 million in calendar year 1977 and \$413 million in 1978. In addition to ESF assistance, Egypt has been aided in meeting the food needs of its population by a massive P.L. 480 Title I program (Agricultural Trade Development and Assistance Act of 1954, as amended), totaling over \$641 million from 1975 to 1978.

Although CIP constitutes an important source of import financing, Arab donors have been the primary source of balance-of-payments support during the post-1973 period. Arab assistance of nearly \$1 billion was crucial to the financing of a \$1.1 billion current account deficit and about a \$1 billion debt-repayments bill in 1978.

The impact of a deteriorating economic situation on political stability is evidenced by the events of January 1977. During 1976, Egypt's available foreign exchange was insufficient to meet import needs and international obligations. The economic crisis culminated with rioting in the streets of Cairo in January 1977. The ostensible cause of the riots was an increase in the prices of selected subsidized goods. Some observers believe, however, that the instability reflected deep-seated concern about the deteriorating economic situation and dissatisfaction with the pace of development.

During 1976, the actual flow of goods under CIP was not significant enough to affect the overall supply of goods except in a marginal way. Although \$465 million had been obligated in fiscal years 1975 and 1976, disbursements against CIP totaled only \$91 million by the end of calendar year 1976. The low rate of disbursement reflected the time-consuming nature of the CIP procurement process, particularly as it applied to capital equipment. Concerned that the political impact of the program would be lost if there were not physical evidence of the U.S. assistance effort in the form of visible capital equipment, the U.S. Ambassador to Egypt limited the financing of consumables to roughly half the CIP.

U.S. policymakers reacted to the riots by altering the program to make it more responsive to Egypt's short-term needs. Funds were reallocated from project assistance to the CIP, increasing the CIP from \$250 million to \$440 million. The range of commodities eligible for CIP financing was expanded to include food items. At the same time, P.L. 480 assistance was increased.

Israel

U.S. program aid was also significant in alleviating a balance-of-payments crisis in Israel. Following the 1973 October War, Israel's import bill rose dramatically as a result of increases in import prices and military requirements. By 1975 Israel's trade deficit had reached \$4 billion, and economic growth had slowed drastically. Despite austerity policies designed to curb imports, a massive infusion of U.S. assistance was necessary to sustain the economy.

Balance-of-payments support has been provided through a CIP and cash grant. Under CIP, Israel has been reimbursed for nonmilitary imports from the United States. The cash grant was instituted to compensate Israel for the foreign exchange costs incurred as a result of the Sinai II

Agreement. A cash transfer replaced CIP in fiscal year 1979 due to problems in drawing down the CIP. 1/

Through 1979, assistance has continued to be justified on the basis of Israel's balance-of-payments needs, although the crisis of 1974-75 has largely passed. As a result of policies designed to restrain imports and expand exports, the deficit on goods and services was reduced from \$4.1 billion in 1975 to \$2.6 billion in 1977. The continued high level of assistance, in view of the improved balance-of-payments situation, has permitted Israel to (1) reduce debt, (2) increase foreign exchange reserves, and (3) pursue growth-oriented policies.

Zambia

A CIP was instituted in fiscal year 1977 to help Zambia overcome its balance-of-payments problems. The primary causes of Zambia's financial crisis are (1) the sharp decline in world copper prices and (2) problems in transporting the copper exports which account for over 90 percent of export earnings. The conflict in Rhodesia has burdened Zambia with a rapidly increasing refugee population and has necessitated the use of alternate transport routes.

CIP assistance of \$20 million in fiscal year 1977 and \$30 million in fiscal year 1978 and \$20 million in fiscal year 1979 is marginal in relation to Zambia's total needs. CIP has financed the import of a variety of equipment, although AID officials plan to concentrate future CIP assistance on agricultural needs. AID and State officials maintain that CIP will facilitate the diversification of the Zambian economy away from copper into agriculture. Although agreeing that improved performance in the agricultural sector is normally advanced through project assistance, officials maintain that there is a continued need for CIP financing of agricultural inputs such as fertilizer. Increased emphasis on project assistance is planned in the fiscal year 1980 program.

The International Monetary Fund has been the primary public source of short-term, balance-of-payments support. As of January 1979, \$164 million from a 1978 stabilization package had been drawn down. AID relies on the International Monetary Fund to institute policy measures that assure movement towards stabilization and development objectives. Zambia

1/See "U.S. Economic Assistance for Israel," ID-78-31, August 18, 1978.

is meeting International Monetary Fund conditions although a waiver of one performance criterion has been made in recognition of exceptional transport problems. In April 1979 the International Monetary Fund certified that Zambia was observing all performance criteria and thus was eligible to draw additional funds under the stabilization agreement.

Implementation of CIP has proceeded quickly. As of October 1978, 94 percent of the fiscal year 1977 and 58 percent of the 1978 program funds had been disbursed. Problems were encountered, however, in the transport of CIP-financed fertilizer during 1978. As a result of transport problems, the border with Rhodesia--which had been closed since 1973--was reopened, permitting timely delivery of fertilizer before the growing season started.

Syria

Although Syria has experienced balance-of-payments difficulties, commodity-import loans have played only a marginal role in alleviating this constraint. Disbursements against CIP totaled \$32 million from 1975 to 1978. During 1977 alone, Syria's import bill amounted to \$2.4 billion and its trade deficit exceeded \$1.4 billion.

CIP loans in Syria have been used to expand the productive capacity and economic development of selected sectors. When the program was initiated in 1975, AID officials intended that CIP be directed to the agricultural sector. Because of difficulties in implementing procurement actions for agricultural machinery, the loan was used to import heavy construction equipment, some of which was used in agriculture and some in other sectors. Commodity-import loans have also financed the import of other equipment, such as agricultural, surgical, and sanitation equipment.

ASSISTING COUNTRIES FACING BUDGETARY PROBLEMS

Assistance under the Economic Support Fund has also been used to provide budget support to Jordan and Botswana. Budget support can be effective in stabilizing an economy in which local currency receipts are insufficient to cover a desired expenditure level. The foreign exchange provided under budget support is intended to assist the government in mobilizing the domestic resources necessary to bridge the gap between budget receipts and expenditures.

Because adequate resources are available from domestic revenues and other donor assistance to cover recurring expenditures, neither Jordan nor Botswana faces a budgetary crisis.

In Botswana's case, the program grant of \$9 million has supplemented the development budget, making possible expenditures which otherwise would have been deferred. The additional resources were intended as a substitute for those domestic resources needed to finance defense expenditures.

Cash transfers to Jordan, amounting to about \$440 million from fiscal years 1970 to 1979, have similarly supplemented available budget resources--accounting for 5 percent of budget expenditures in 1977. In Jordan's case, however, the elimination of U.S. budget support would not necessarily require a reduction in expenditures. If reforms suggested by international economists were undertaken, the budget deficit could be financed by mobilizing resources through increased domestic borrowing. Moreover, Jordanian foreign exchange reserves, equal to about 7 months of imports in 1978, could also be substituted for AID-supplied foreign exchange.

Although U.S. budget support covers only a small portion of Jordan's expenditures, Jordan remains heavily dependent on continued budget support from Arab donors. Domestic revenues were expected to finance only 79 percent of recurring expenditures and 55 percent of total (recurring and development) expenditures in 1978. Thirty-one percent of total expenditures were to be covered by Arab budget support.

POLITICAL EVENTS WILL SHAPE FUTURE REQUIREMENTS

The continued provision of U.S. assistance in the form of cash transfers and budget support will also be affected by future political events. Both Egypt and Jordan, for example, are heavily dependent on Arab assistance. Remittances from workers employed in Arab oil countries constitute an important source of foreign exchange. Actions in the political arena may affect the flow of these resources. In Israel's case, the costs of the Sinai withdrawal, envisioned as part of the peace settlement, could strain the balance of payments; Israel estimates the foreign-exchange costs at \$3 billion.

In southern Africa, an escalation of the conflict in Rhodesia could lead to (1) the closure of export routes, (2) an accelerated inflow of refugees, or (3) increased defense expenditures. Such events would have a critical effect on Botswana's short-term prospects and would add to Zambia's economic difficulties. The scale and form of the U.S. response would of course be governed by political parameters.

CONCLUSIONS

Substantial sums have been provided to ESF countries through various forms of program assistance to promote economic stability as well as advance political objectives and absorb high aid levels. The assistance has been instrumental in promoting a stable economic environment in Egypt and in Israel immediately after the 1973 October War. However, the provision of assistance cannot, in several cases, be rationalized on balance-of-payments or budgetary grounds. The economic impact of this assistance in Jordan, Botswana, and in recent years, Israel, has been to facilitate the acceleration of development plans. For Syria and Zambia, program assistance has helped increase the productive capacity of selective sectors, a development goal normally advanced by project assistance. The continued need for high levels of program assistance will have to be based on an assessment of whether it is the appropriate tool for furthering particular economic and political objectives.

CHAPTER 4

ECONOMIC ACHIEVEMENTS: CAPITAL PROJECTS

The large amounts of program assistance discussed in the preceding chapter have been paralleled by a corresponding large influx of capital project assistance to selected Middle East countries. These projects are designed to support the ESF long-term objective of sustained economic growth and have ranged from road and power plant construction to the upgrading of water and sewage facilities. This assistance has been substantial; project assistance to Egypt, Jordan, and Syria in fiscal years 1975-78 has amounted to approximately \$1.4 billion--or 45 percent of the total ESF monies provided to those countries. The amounts of project assistance provided (by country) are summarized below.

<u>Country</u>	<u>FY 1975-78</u>		<u>FY 1979 planned obligations</u>
	<u>Project obligations</u>	<u>Disbursements</u>	
	------(millions)-----		
Egypt	\$1,116.2	\$ 87.1	\$328.0
Jordan	106.7	40.1	58.0
Syria	<u>220.7</u>	<u>.8</u>	<u>54.4</u>
Total	<u>\$1,443.6</u>	<u>\$128.0</u>	<u>\$440.4</u>

To date, the projects have had little impact on the economies of Syria and Egypt. The large projects that make up the AID portfolio in these countries necessarily require lengthy implementation. The difficulties AID has encountered in meeting original project schedules have, in some cases, already postponed completion 18 to 24 months. The situation in Jordan is better; projects obligated in 1975 and 1976 are moving ahead fairly well.

PIPELINE OF UNSPENT FUNDS

With the resumption of assistance programs in Egypt and Syria in fiscal year 1975, AID faced serious problems in devising and implementing its large-scale capital development projects. Actual project disbursements have not kept pace with AID estimates of expected expenditures, and there now exists a large pipeline of funds obligated but unspent. In its 1979 congressional presentation, for example, AID predicted that in 1978, disbursements of over \$123 million

would be made against 19 Egyptian capital projects obligated during the 1975-77 period. Actual expenditures for 1978 have totaled only about \$53.4 million. (See app. II.) Expenditures in Syria have also lagged. Estimated disbursements during 1978 for five AID 1975-77 projects totaled \$13.8 million; actual disbursements amounted to \$660,000. (See app. III.) Again, the Jordan program reflects a better rate of progress. As of September 30, 1978, close to 62 percent of funds obligated for fiscal year 1975-77 projects had been disbursed.

PROJECT STATUS: EGYPT

The majority of U.S. project assistance to the Middle East goes to Egypt, which received over \$1 billion in such assistance during the fiscal year 1975-78 period. The program has had considerable delays and the large-scale infrastructure projects obligated in the early years are only just now moving into the construction phase.

Capital projects have been concentrated in power, transportation, telecommunications, and water and sewage areas. AID has also ventured into the industrial sector with, for example, financing of cement and textile plants. Project selection has considered Egyptian Government preferences for addressing capital development needs. Another factor has been the AID perception of which projects the Egyptian ministries or agencies concerned can most readily implement from a managerial standpoint.

Measurements of progress

Since our September 1977 report 1/ on U.S. economic assistance to Egypt, AID and the Egyptian Government have progressed to the point of satisfying the preconditions for disbursement on most project loans and grants. Contracts for architectural and engineering services have been let for most projects, and construction contracts awarded for, among others, the Grain Storage I and Talkha-Helwan plant projects.

Many projects have, nevertheless, already suffered appreciable slippages in scheduled completion dates. Delays have been attributed to (1) initial problems in establishing a working relationship with Egyptian ministries, (2) problems in negotiating architectural and engineering contracts, and

1/"Egypt's Capacity to Absorb and Use Economic Assistance Effectively," (ID-77-33, September 15, 1977.)

(3) the time-consuming contract approval process by the Egyptian Government. AID officials commented that the original tight schedules were established to give an incentive in meeting project deadlines to the Government of Egypt.

The following examples illustrate some of the problems and delays encountered in the implementation of Egyptian capital development projects. The 1975 ^{1/} Grain Storage project has encountered problems, ranging from protracted contract negotiations to customs delays, and is now at least 18 months behind schedule. Of the fiscal year 1976 projects, the PVC Pipe Drainage project and Ismailia power plant projects are 22 and 18 months behind original schedules, respectively. In the case of Ismailia, the delays reflect the subsequent change in bidding documents and the fact that the initial schedule did not provide for the necessary time to hire a consulting engineer. The National Energy Control Center project has suffered delays because of problems in selecting a general contractor. A lesser delay, in the range of 7 to 8 months, has been experienced on the Talkha-Helwan gas turbine plant.

On the credit side, no major problems with the Mahalla textile plant have been recorded, nor did the AID mission staff project any delay on the Alexandria Port equipment project. Funds for fiscal year 1977 projects had been obligated for approximately 1 year at the time of our in-country review in Egypt. At that time, the projects were then recorded an average of 5 months behind schedule.

AID officials acknowledged the schedule slippages, but emphasized that the lengthy time required for project implementation and the numerous problems are normal for capital development projects, and are by no means unique to Egypt. AID officials also stressed that these capital development projects will still have the desired economic impact, though later than anticipated.

Required future inputs

Since AID-financed capital projects are still in pre- or early implementation phases, existing schedules do not

^{1/}The other two projects for which funds were obligated in FY 1975 involved supplies of road and electrical equipment and, consequently, fit the definition of commodity imports more than capital projects.

reflect the possibility of further delays during actual construction. The availability of local financial and construction support for AID projects represents, potentially, the most serious impediment to timely project completion.

As of September 1978, the Egyptian Government had met the local financing requirements on AID-financed projects. Local requirements will increase markedly, however, as projects move into construction phases. AID has thus far pursued two strategies in attempting to insure that sufficient local funds will be available for current projects. In the case of certain projects--those in the energy sector--the Egyptian Electricity Authority, the implementing agency, has been required to establish irrevocable letters of credit on consultant and construction contracts. This procedure places necessary funds in accounts for draw-down by the contractors.

In other instances, AID has preferred to obtain written assurances from the Egyptian ministry or agency concerned that necessary funds have been budgeted and will be available. This procedure has the advantage of encouraging the Government of Egypt to take the lead in mobilizing domestic resources in support of its development programs.

These approaches demonstrate the dilemma AID faces in balancing the need to insure the completion of AID projects, on one hand, and on the other, the desirability of assuring that noninflationary resources are made available through sound budgetary practices.

AID has provided the Egyptian Government with annual estimates of local currency requirements, and the United States has encouraged other assistance donors to do the same. As of March 1979, other donors had not provided these estimates, but AID officials told us that continued efforts are being made through the Egypt Consultative Group to get such estimates.

The availability of local construction support is equally important. AID-financed projects in industrial and other sectors rely on construction services and supplies obtainable locally. For example, the extension of Quay 85 at the Alexandria Port, to be done by an Egyptian construction firm, is a critical component of the U.S. Grain Storage I project. The U.S. architectural and engineering contractor for the project informed us, however, that the work is behind schedule, which could delay completion of the entire project.

The AID mission staff believes that if problems in obtaining local support become acute, more work may have to be contracted to U.S. companies, and consideration may be given to going outside Egypt for supply procurement.

PROJECT STATUS: JORDAN

Implementation of capital projects in Jordan has proceeded at a relatively smooth pace. AID officials attribute this largely to a long and cooperative U.S.-Jordanian assistance relationship and to the compatibility of AID and Jordanian development objectives.

Program compactness also contributes to AID effectiveness in monitoring and implementing projects. Much U.S. assistance to date has been directed to the Jordan Valley, ranging from road construction to the building of schools and irrigation systems. That assistance will continue with the U.S. anticipated contribution to the Maqarin Dam and Jordan Valley Irrigation System. In its fiscal year 1979 and proposed fiscal year 1980 programs, however, AID has given greater emphasis to Jordan's urban centers, with planned water and sewage projects in Aqaba, Irbid, and Zarka.

Procedural flexibility

The Jordan assistance program contains some distinctive features not shared by the other Middle East programs. It has become a standard practice for AID to absorb a portion of local currency costs associated with AID-funded capital projects, the actual amount dependent on the nature of the project. Such financing, definable as an additional, though less-visible source of budget support, helps absorb the ESF level to Jordan and has not, in the opinion of AID, diminished the Jordanian commitment to project execution.

With some exceptions, competition for services and supply contracts has been expanded to permit participation by firms from developing countries. South Korean construction companies have been awarded some contracts, resulting in lower project costs.

Key projects: potash plant and Maqarin Dam

AID has programmed loans of \$33 million and \$50 million in fiscal year 1979 towards construction of the Jordan potash plant and Maqarin Dam projects, respectively. The projects, both multidonor efforts, are technically ambitious and AID has already funded feasibility and design studies for both. U.S. backing is considered crucial to the success of the politically sensitive Maqarin project, which involves the issue of equitable apportionment of Jordan River waters among the bordering states of Israel, Syria, and Jordan. The Congress has stipulated that no U.S. funds can be obligated for either

project until firm financial commitments have been obtained from other donors.

The 1.2 million ton per year potash plant, a future source of needed foreign exchange, will be constructed near the Dead Sea, almost directly opposite a similar Israeli operation. According to AID officials, firm financial commitments have now been received from all donors, and, consequently, the AID funds were recently obligated.

The success of Maqarin is far more tenuous. Technical as well as water rights issues still have to be resolved, and AID will be hard pressed to meet the conditions for loan obligation by the end of fiscal year 1979.

Future program direction

AID initially focused on projects in the Jordan Valley, a priority concern of the Jordanian Government, but has now begun to expand its efforts to encompass the needs of the urban centers. In fiscal year 1978, AID funded the Amman Water and Sewage project, which will involve the upgrading and expansion of existing facilities. Also under consideration for future funding are sewage projects in Aqaba and Irbid.

AID participation in both Jordan Valley irrigation and urban water projects postulates an AID role in resolving the issue of equitable distribution in the face of Jordan's potentially acute water shortages and the consequent competing demand for resources. We believe AID can and should encourage the Jordan Government to devise and implement a national water policy to deal with the questions of allocation, urban tariff rate structures, etc.

PROJECT STATUS: SYRIA

During fiscal years 1975-78, AID obligated \$220.7 million for six capital development projects in Syria. The AID portfolio is comprised of the Damascus Water Supply I and II, Euphrates Basin Irrigation Maintenance, Rural Electrification, Damascus-Dera'a and Lattakia-Tartous highways projects. Three additional projects--Rural Schools, Rural Roads, and Provincial Water Supplies--have been tentatively programmed for fiscal year 1979. The bulk of AID's \$220.7 million investment remains unspent: all projects are still in the preequipment-award or preconstruction stage, and disbursements have been nominal.

Program implementation

AID problems, in part, stem from the hasty institution of a large assistance program for Syria in fiscal year 1975, which left AID with little time to develop either a planning base or needed expertise in the procedures and operations of the Syrian Government. A limited AID staff had to establish a working relationship with the Syrians after a long hiatus in U.S.-Syrian relations and was forced to rely on outside feasibility studies in selecting projects.

AID activities in Syria have been conditioned by the political realities of operating in a socialist-oriented economy where U.S. bilateral relations have not been historically strong. Indeed, the AID staff regards Syria as really a matter of doing the possible, given the constraints under which it must operate.

Recurring problems

Identifying appropriate projects for funding has plagued AID from the start of the program. Projects AID considered early in the budget process invariably fall out and must be replaced. This identification problem is likely to remain acute over the next few years if the U.S. assistance program to Syria continues at high levels. With the exception of an irrigation project in the Akkar plain--itself still tentative--AID may have to rely on agricultural and transport-sector surveys barely underway to identify future projects. AID has pointed out, however, that the problem may be ameliorated as a result of the proposed fiscal year 1979 rural projects. If successful, those projects could serve as prototypes for subsequent similar undertakings, according to AID.

AID has also faced recurring problems that have slowed project implementation and contributed to the buildup of undisbursed funds. The contracting process represents the single largest source of delays to date. Lengthy contract negotiations between Syrian agencies and prospective U.S. contractors have been attributed to the incompatibility of Syrian and AID regulations as well as Syrian dissatisfaction with quoted U.S. prices.

To cite an extreme case, the Syrians began negotiations in May 1977 with a U.S. firm for architectural and engineering services in connection with the AID-financed Damascus-Dera'a highway. Although the terms of a contract were agreed on by September, a high-level Syria Government review resulted in a contract rejection because of unacceptably high costs. A contract subsequently negotiated with a second U.S. firm was

not formally approved by the Syrians until May 1978. The protracted negotiations delayed project implementation and resulted in an AID-estimated cost escalation of \$6 to \$7 million.

The incompatibility of Syrian and AID contracting methods and procedures has required a time-consuming educating process on both sides and some significant AID accommodations. AID, for example, although traditionally favoring a cost-plus-fixed-fee contract, has yielded to Syrian insistence that contracts be negotiated on a time-rate basis.

OBSERVATIONS AND CONCLUSIONS

The expenditure of large amounts of economic assistance to support political objectives has necessitated large U.S. involvement in Middle East capital projects, an investment likely to continue if current assistance levels hold steady. Such projects necessarily incur a lengthy implementation period, and measurable progress has been slow in Egypt and Syria as a result of contracting and other problems.

The hasty resumption of large aid programs in Egypt and Syria in fiscal year 1975 placed AID in the position of selecting projects and predicting implementation schedules based on very little experience. Indeed, some projects obligated during the first years of the programs are among those encountering the severest delays when reflected against the early, optimistic AID timetables. We believe that AID should now be in a position to more accurately estimate the actual time required for project completion.

Nevertheless, AID's annual predictions of project expenditures have consistently exceeded actual disbursements by significant margins. We believe that these optimistic estimates of expenditures create unnecessarily high expectations on the part of the Congress, and may obscure the problems AID is encountering in implementing capital projects.

Rates of progress

AID has come some distance in implementing its large-scale capital projects, particularly in Jordan, where a long-standing relationship exists, and to a much lesser extent in Egypt, where project completion dates are still admittedly distant. Syria suffers by comparison; all projects there are far behind schedule, and it is difficult to be optimistic about future rates of progress.

AID difficulties in Syria have been compounded by the basic incompatibility of AID and Syrian contracting procedures and regulations, and protracted contract price negotiations. Those problems are not susceptible to easy resolution, making rapid progress on current or future Syrian capital projects unlikely.

AID problems with its Syria program have increased because of the difficulties in locating and developing quality projects sufficient to absorb the continued high assistance levels. AID is hopeful that the success of proposed fiscal year 1979 projects will provide the basis for future projects. A real possibility remains, however, that beyond fiscal year 1979, AID will face problems in developing viable projects for funding. If so, that fact--coupled with the consistent problems AID has faced in project implementation--argues the need for careful consideration of the components of the Syria assistance programs in succeeding years, in the context of the political objectives being served and the most appropriate uses of aid monies.

Local cost financing

The timely and sufficient availability of local resources will be a key factor in the successful implementation of AID capital projects in Egypt. Because AID projects are primarily still in early implementation stages, Egypt's ability to provide those resources has not been substantively tested.

The AID mission in Cairo is aware of the critical importance of sufficient local inputs and has provided the Egyptian Government with annual estimates of required Egyptian fund expenditures. We support AID's intention to monitor the availability of local resources to support its projects, and we believe other donors should provide similar estimates.

These actions should not, however, minimize the very real difficulties Egypt faces in mobilizing domestic resources to support its development programs. We recommended in September 1977 that the Congress and AID consider the merits of providing hard currency financing for the local costs of selected U.S. projects. AID has begun financing some local costs incurred for New Directions-oriented projects, but has thus far not encouraged local cost financing of capital projects.

There may be a special advantage in considering a similar approach in Syria, particularly in view of the recurring difficulties AID has encountered in obligating \$90 million annually in ESF assistance to Syria. Financing a portion of local

currency expenditures for AID projects would help absorb a portion of the large assistance level. AID has indicated that the rural projects that now tentatively comprise the AID portfolio in fiscal year 1979 will include funding of some local costs.

X RECOMMENDATIONS

In support of the foregoing observations and conclusions, we believe the AID Administrator should, with respect to the Syrian aid program,

--report to the Congress in the fiscal year 1981 authorizing request, on the progress made in funding some local costs incurred for fiscal year 1979 capital development projects; and

--decide whether it would be appropriate to increase the commodity-import portion of assistance if capital projects cannot be developed or implemented within a reasonable period.

With respect to the Egypt aid program, we believe the AID Administrator should

--continue efforts to encourage the submission of annual estimates of local currency expenditures by other Egyptian assistance donors.

CHAPTER 5

MEETING BASIC HUMAN NEEDS

The International Security Assistance Act of 1977 required that, when possible, ESF monies be used to achieve the objectives of the AID New Directions mandate. The political framework of ESF affects the extent to which ESF programs in the Middle East can be brought in line with the New Directions mandate:

- The preferences of recipient governments are of paramount importance in shaping how pre-determined assistance levels can be spent. If the governments are not receptive to assistance in AID's primary areas of concern, funds cannot be reduced but must instead be directed to projects which the recipient governments prefer.
- The politically set levels of assistance are not geared to the absorptive capacity of countries, much less to the availability of projects meeting basic human needs.
- The advancement of certain political objectives, such as reducing foreign exchange gaps of countries, may dictate the funding of projects which develop export potential, but lie outside the mandate.

In our review of the extent to which ESF programs in Egypt, Syria, and Jordan are advancing New Directions objectives, 1/ we found that the AID program has become increasingly responsive to New Directions concerns, particularly in Egypt and Jordan. We believe, however, that there are additional basic human needs opportunities in the Egypt and Syria programs.

THE NEW DIRECTIONS MANDATE

The Foreign Assistance Act of 1973 provided that conventional AID programs be directed to meeting the basic needs of the poor majority in developing countries. The New Directions

1/We did not review how the southern Africa programs are advancing New Directions objectives.

mandate, as it came to be known, focused assistance efforts on the critical problems affecting the quality of life of the poor majority--that is, on agricultural and rural development, population growth, health, and education. The legislation also provided that AID programs support the integration of women into the economic life of developing countries.

A March 1978 AID policy paper provides further insights into the objective of a basic needs-oriented assistance strategy. It states that the major elements of the strategy are

- to assist the poor in increasing their incomes-- by raising their productivity and access to productive resources as well as expanding their opportunities for productive employment; and
- to increase the availability of, and access to, those goods and services required to meet basic human needs.

Legislation and the AID policy paper both encourage involvement in the development process through popular participation in local institutions. According to the policy paper, "without such participation there is a strong possibility the poor will not benefit, that their basic needs will not be met." The success of the programs in Egypt, Syria, and Jordan in advancing these goals is discussed below.

EGYPT

The size of the assistance program has led to broad AID involvement in Egyptian economic life. This involvement, coupled with the commitment of the Egyptian Government to meeting the needs of its 40 million people, requires that the program be responsive to the advancement of equitable growth.

Since fiscal year 1977, AID has emphasized the areas of concern outlined in the New Directions mandate. Projects have been initiated to upgrade and expand Egypt's network of social services and to assist the poor in raising their incomes.

Expanding the availability of services

Progress in centering the Egypt program on New Directions concerns has been most pronounced with respect to improving the delivery of goods and services to the poor. Projects have been initiated in family planning, delivery of urban and rural health services, and in training rural social service

workers. Considerable investments have been made in water and sewage projects, which will increase the availability of clean water supplies to urban households. Access to low-cost housing will also be expanded in urban areas, where 44 percent of Egypt's population lives.

The rural poor are being encouraged to participate in defining and meeting their own needs. Such support of local community initiatives is particularly appropriate in the Egyptian setting. Traditionally, the Egyptian approach to development is "top-down"--decisionmaking is highly centralized in Cairo. This "top-down" approach is the antithesis of the New Directions approach, emphasizing the participation of the poor in the development process. Development efforts without such participation can be counterproductive; unrealistic expectations of what the Government can do may emerge, while an appreciation of what can be accomplished through community and private initiatives is not created.

AID is encouraging community participation and is supporting Egyptian decentralization policies through its rural development program. As part of development decentralization, resources will be made available to elected rural village councils to develop local services and infrastructure. No comparable effort is being made, however, to encourage popular participation of the urban poor in the development process. Such urban community development activities could provide appropriate opportunities for expanded voluntary agency involvement in the AID program. U.S. voluntary agencies are active in Egypt, and their utilization is encouraged by the Congress.

AID officials agreed that increasing their involvement in urban community development would be beneficial. They pointed out that, although there have been no major initiatives in this area, participatory elements are included in urban health and housing projects. AID officials indicated that a planned addition of an urban affairs advisor to the Egypt mission staff will give them the capability of exploring opportunities for participatory activities that reinforce the Government decentralization commitment.

Assisting the poor to increase their incomes

The AID program also includes projects intended to increase the income earning capacity of Egypt's poor. Projects have been initiated to develop improved technology and methods of agricultural production. A high proportion of Egypt's small farmers are expected to benefit from, for example, activities in water management and rice, wheat, and maize production.

Agricultural activities will also address the need for off-farm employment opportunities according to AID officials. These projects are expected to generate employment in marketing, transport, machinery repair, and production of agricultural inputs. Attention to the availability of employment opportunities is appropriate. Nearly half Egypt's rural population own no land, and planned investments in agricultural mechanization will reduce opportunities for farm employment.

The availability of employment opportunities is of concern in both urban and rural areas. By 1990, Egypt's labor force is expected to increase by about 50 percent. Moreover, the number of opportunities generated by industry has until now been inflated by the Government's guaranteed employment policies and overstaffing practices. Improvement of economic efficiency counsels against the hiring of surplus workers.

The AID program is having some impact on the availability of employment opportunities to Egypt's urban poor. CIP finances the import of inputs needed to maintain industrial production and thus employment. Considerable investments have also been made in industry and the infrastructure to support industrial expansion although the capital-intensive nature of these investments suggests only limited opportunity for widespread participation in project benefits. AID officials expect, however, that activities supporting development of the private sector will have important employment effects.

Expansion of employment opportunities needs to be accompanied by efforts to provide the poor with the necessary skills to take advantage of employment opportunities. There is currently a shortage of workers skilled in certain trades. Through fiscal year 1978, AID had not initiated training in the skills which improve access to job opportunities. A vocational training project has not gone forward as planned due, in part, to insufficient mission staff resources in this area. Moreover, although 57 percent of Egypt's adult population is illiterate, AID has not undertaken any projects in basic education.

Agency officials indicated that they will be undertaking activities in vocational training and education. Two vocational training projects are planned, one of which is with the ministry responsible for almost half of the public sector industrial labor force. AID is also planning to undertake a study of the education sector to define an appropriate AID role.

SYRIA

Limited progress has been achieved in making the Syrian program responsive to basic human-needs objectives. Two technical assistance projects have been initiated in the health sector; one in health planning and one in upgrading the delivery of health services. Funds have also been obligated to expand the availability of water supplies in Damascus. Through fiscal year 1978, however, projects had not been initiated to increase the income-earning capacity of Syria's urban and rural poor. And an electrification project is the sole undertaking focused on increasing the availability of services in rural areas where half of Syria's 8 million people reside.

AID mission officials indicated their desire to focus the program on (1) increasing incomes in agriculture, (2) expanding rural services, and (3) upgrading health services. Agency officials are hopeful that the fiscal year 1979 program will include provincial water, rural schools, and rural roads projects.

Constraints on increasing the New Directions focus

The AID ability to respond to rural-development needs and other New Directions concerns has been constrained by Syrian Government resistance. The Syrians are firmly opposed to AID interest in undertaking bilateral family planning activities. Lack of Government interest has also prevented AID from undertaking a health-sector assessment.

AID officials share our belief in the desirability of focusing the program on rural-development needs. The pace at which the program can be made more responsive will, however, be determined by Syrian priorities and preferences.

JORDAN

Efforts to bring ESF programs in line with the New Directions mandate have been most successful in Jordan. This success reflects strong Jordanian interest in projects which are consistent with the AID mandate.

Considerable resources are being directed to development of the Jordan Valley--\$60 million through fiscal year 1977 with an additional \$158 million planned. 1/ Increased production of fruits and vegetables made possible by Jordan Valley

1/Includes \$150 million programed for the Maqarin Dam.

development will help satisfy domestic food needs and provide a source of foreign exchange.

In addition to developing irrigation systems and financing the construction of roads, housing, health clinics, and other projects, the AID program has exhibited appropriate concern in insuring the equitable participation of tenant farmers in Jordan Valley development. Future assistance will need to be directed to providing farmers with the technical services necessary to fully realize the potential benefits of these investments.

A strategy for meeting basic human needs in Jordan must also respond to the needs of those outside the Valley. Only about 90,000 of Jordan's 2.2 million people live in the Valley, and nearly three-fourths of the population resides in urban centers.

Since fiscal year 1976, attention has been given to increasing the availability of services outside the Valley. AID has financed water and sewage systems expansion, school construction, and health service improvements.

Assistance has not been directed at increasing the income-earning capacity of the poor outside the Jordan Valley. The general availability of employment opportunities and a shortage of skilled workers suggest the need to provide the poor, including women, with the training necessary to take advantage of existing opportunities. AID officials indicated that they plan to initiate a vocational-education project in fiscal year 1979.

The ability to respond to needs is sometimes limited, as in Syria, by Jordanian resistance to AID involvement. Thus, although AID officials agree on the desirability of expanding family-planning services and of helping dryland farmers, the Jordanians have not been receptive to such assistance. Jordan's dryland farmers, who comprise 60 percent of the agricultural labor force, are among the poorest groups.

The scope for completely focusing the program on New Directions objectives is limited by the need to advance other politically determined goals. U.S. policymakers attach great importance to reducing Jordan's reliance on outside assistance. As a result, AID is financing activities, such as potash production, which will generate export earnings and public revenues.

CONCLUSIONS AND RECOMMENDATIONS

AC Although progress has been made, program orientation can be expanded to meet basic human needs. In Syria, for example, an increased focus on agriculture and rural-development needs is desirable, but political constraints may affect the pace at which this can be achieved. In Egypt, AID has emphasized New Directions areas of concern but there are opportunities for greater involvement. ~~We believe~~ ^{Expanded efforts should} be made to (1) facilitate participation of the urban poor in the development process and (2) assist the poor in increasing their incomes through expanded training opportunities.

Therefore, we recommend that the Administrator, AID

- X* --carry out plans to support training in the skills which improve the access of Egypt's poor to employment opportunities;
- initiate community-development activities which facilitate participation of Egypt's urban poor in the development process, utilizing U.S. voluntary agencies where possible; and
- report to the Congress in the fiscal year 1981 authorization request, on efforts to focus the Syria program on rural-development needs.

AID officials agreed with our recommendations. AID officials outlined plans to implement the recommendations for Egypt and, in the case of Syria, they expect to initiate three rural-development projects in 1979, which will provide the basis for future years.

PROFILE OF ESF PROGRAMS
a/
FY 1978 AND FY 1979

<u>Recipient/ program</u>	<u>Funding</u>		<u>Types of programs</u>	<u>Program justification</u>
	<u>FY 1978 (actual)</u>	<u>FY 1979 (estimated)</u>		
	<u>---(\$ millions)---</u>			
Israel	\$785.0	\$785.0	CIP, <u>b/</u> cash transfer	support of Middle East peace
Egypt	750.8	750.0	CIP, development projects	support of Middle East peace
Jordan	93.0	93.0	cash transfer, development projects	support of Middle East peace
Syria	90.0	90.0	CIP, development projects	support of Middle East peace
Maqarin Dam	-	45.0	development project	support of Middle East peace
Middle East regional cooperation	-	5.0	regional projects	support of Middle East peace
Sinai Support	11.7	11.7 <u>c/</u>	early warning system	part of Israeli-Egyptian disengagement arrangements
Middle East special requirements	11.5	11.8 <u>c/</u>	fund to support unanticipated special needs	support of Middle East peace
Lebanon	20.0	-	relief and reconstruction projects	alleviate problems caused by Lebanese conflict
Cyprus	15.0	15.0	refugee relief and rehabilitation	promote settlement between Greek and Turkish Cypriots
Malta	9.5	-	cash transfer	U.S. share of NATO payments

a/FY 1978 programs authorized under the heading of Security Supporting Assistance.

b/CIP component phased out in FY 1979 program.

c/Funding classed in FY 1979 under heading Peacekeeping Operations.

Recipient/ program	Funding		Types of programs	Program justification
	FY 1978 (actual) ----(\$ millions)-----	FY 1979 (estimated)		
Portugal	\$300.0	\$ -	cash transfer	support for Portuguese economic stability and growth
Spain	7.0	7.0 <u>c/</u>	educational, cultural, scientific and technological cooperative projects	treaty obligations in exchange for base rights
Turkey	-	50.0	cash transfer	support for Turkish economic stabilization
U.N. Forces in Cyprus	9.1	8.7 <u>c/</u>	U.S. contribution to operating costs	support for U.N. peacekeeping force
Jamaica	11.0	-	CIP	support for Jamaican economic and social stability
Botswana	15.1	11.0	cash transfer, development projects	aid transition to majority rule in southern Africa
Lesotho	5.3	- <u>d/</u>	development projects	aid transition to majority rule in southern Africa
Swaziland	12.7	- <u>d/</u>	development projects	aid transition to majority rule in southern Africa
Zaire	10.0	-	development projects	assist Zaire economic stability
Zambia	30.0	20.0	CIP	assist Zambian economic recovery
Southern Africa regional cooperation	37.6	14.0	private voluntary organization grants, refugee assistance	assistance to African refugees

c/Funding classed in FY 1979 under heading Peacekeeping Operations.

d/Funded from development assistance in FY 1979.

EGYPT

EXPENDITURES FOR CAPITAL PROJECTS OBLIGATED IN FY 1975-77

<u>Project</u>	<u>Funds obligated</u>	<u>FY 1975-77</u>	<u>FY 1978</u>	
		<u>Actual expenditures</u>	<u>Estimated expenditures</u>	<u>Actual expenditures</u>
----- (millions) -----				
Electric Distribution	\$ 30.0	\$25.3	\$ 4.7	\$ 3.6
Road Equipment	14.0	6.6	7.4	7.3
Ismailia Power Plant	141.0	.2	2.0	.5
Suez Cement Plant	90.0	.6	10.0	9.6
Hydrographic Survey	8.0	-	4.5	5.3
Port Said Salines	13.0	-	1.2	-
Talkha-Helwan Generators	69.0	.2	12.8	19.6
Mahalla Textile	96.0	.3	20.4	.4
Cargo Equipment	31.0	-	6.2	.3
Development Industrial Bank	32.0	-	9.0	.3
PVC Pipe Drainage	31.0	-	7.0	-
National Energy Control Center	24.0	-	6.4 <u>1/</u>	2.1
Grain Storage I	44.3	.4	2.8	2.1
Urban Electric Distribution	17.0	-	3.4 <u>1/</u>	-
Canal Dredging Equipment	26.0	-	8.5	-
Grain Storage II	42.0	-	7.2	.1
Irrigation Pumps	11.0	-	0.4	-
Alexandria Sewage	15.0	-	2.2	1.1
Cairo Water Supply	<u>30.0</u>	<u>-</u>	<u>7.5</u>	<u>1.1</u>
Total	<u>\$764.3</u>	<u>\$33.6</u>	<u>\$123.6</u>	<u>\$53.4</u>

1/Additional funds were obligated in FY 1978.

SYRIAEXPENDITURES FOR CAPITAL PROJECTS OBLIGATED IN FY 1975-77

<u>Project</u>	<u>Funds obligated</u>	<u>FY 1975-77</u>	<u>FY 1978</u>	
		<u>Actual expenditures</u>	<u>Estimated expenditures</u>	<u>Actual expenditures</u>
----- (millions) -----				
Damascus Water I	\$ 48.0	\$0.1	\$ 6.5	\$0.2
Damascus Water II	14.5	-	0.3	-
Euphrates Basin Irrigation Maintenance	17.6	-	5.5	0.3
Damascus-Dera'a Highway	45.9	-	1.5	0.2
Rural Electrifi- cation I	<u>34.7</u>	<u>-</u>	<u>0.1</u>	<u>-</u>
Total	<u>\$160.7</u>	<u>\$0.1</u>	<u>\$13.9</u>	<u>\$0.7</u>

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