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INTERNATIONAL FOOD ASSISTANCE

Local and Regional Procurement Provides Opportunities to Enhance U.S. Food Aid, but Challenges May Constrain Its Implementation

Statement of Thomas Melito, Director
International Affairs and Trade Team

June 4, 2009

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here to discuss how local and regional procurement (LRP)[1] can provide opportunities to enhance U.S. food aid, though challenges can constrain its implementation. This hearing is of particular importance given today's environment of increasing emergencies and growing global food insecurity,[2] in which the United States and other donors face intense pressures to feed the world's expanding undernourished population. In September 2008, the United Nations (UN) Food and Agriculture Organization (FAO) reported that high food prices had resulted in the number of undernourished people reaching a record 963 million.[3]

LRP has increasingly become a key element in the multilateral food aid response over the past decade. Most bilateral donors of food aid have switched from commodity-based in-kind food aid to a cash-based food assistance program in recent years. As the largest international food aid donor, contributing over half of all food aid supplies to alleviate hunger and support development, the United States plays an important role in responding to emergency food assistance needs and ensuring global food security. The large majority of U.S. food assistance is for U.S.-grown commodities purchased competitively in the United States and shipped to recipient countries on U.S.-flag carriers.

[1]We define local and regional procurement (LRP) as the purchase of food aid by donors in countries affected by disasters and food crises or in a different country within the same region. Procurements of food aid can be categorized geographically as (1) *international:* donor-financed purchases of food aid in world markets, which may include both developed and developing countries; (2) *regional:* donor-financed purchases of food aid in a different country in the same region; or (3) *local:* donor-financed purchases of food aid in countries affected by disasters and food crises.

[2]Food insecurity is the lack of access of all people at all times to sufficient, nutritionally adequate, and safe food, without undue risk of losing such access. The Food and Agriculture Organization (FAO) of the United Nations defines the elements of food security to include (1) food availability, (2) access, and (3) utilization.

[3]GAO, *International Food Security: Insufficient Efforts by Host Governments and Donors Threaten Progress to Halve Hunger in Sub-Saharan Africa by 2015*, GAO-08-680 (Washington, D.C.: May 29, 2008). In this report, we cited FAO estimates that indicate that sub-Saharan Africa is the region with the highest prevalence of food insecurity; one out of every three people there are considered undernourished.

My testimony is based on our May 2009 report, which we publicly released today.[4] I will focus on four topics. First, I will discuss the impact of LRP on the efficiency[5] of food aid delivery. Second, I will discuss the impact of LRP on economies where food is procured. Third, I will discuss U.S. legal requirements that could affect U.S. agencies' use of LRP. Finally, I will summarize our recommendations regarding improvements to U.S. agencies' use of LRP.

In preparing this testimony, we largely relied on our May 2009 report. To address our objectives, we compared the cost of LRP food with in-kind food aid from the United States by analyzing the per ton cost of similar commodities for the same recipient countries in the same quarter of a given year for the World Food Program (WFP) and U.S. Agency for International Development (USAID), respectively. We also examined WFP data that compared the delivery time[6] of LRP with in-kind food aid for 10 countries in sub-Saharan Africa for 2004 through 2008. We conducted fieldwork in four selected African countries—South Africa, Kenya, Uganda, and Burkina Faso. In Washington, D.C., we interviewed officials from U.S. agencies, including USAID, USDA, State, Department of Transportation (DOT), and the Treasury; and the Millennium Challenge Corporation (MCC). In addition, we met with the Rome-based UN food and agriculture agencies, the U.S. Mission to the UN, and several bilateral donors. We conducted semi-structured interviews with 11 WFP procurement officers based in Africa and Asia. Finally, we convened a roundtable of 10 experts and practitioners to discuss key issues and challenges to the implementation of LRP. For a full description of our scope and methodology, see GAO-09-570.

We conducted this performance audit from June 2008 to May 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient,

[4]GAO, *International Food Assistance: Local and Regional Procurement Can Enhance the Efficiency of U.S. Food Aid, but Challenges May Constrain Its Implementation*, GAO-09-570 (Washington, D.C.: May 29, 2009).

[5]We define "efficiency" as the extent to which a program is acquiring, protecting, and using its resources in the most productive manner in terms of cost, delivery time, and appropriateness of food aid.

[6]In this testimony, we use the term "delivery time" to refer to the number of days that elapses from the purchase order date to the date WFP takes possession of the food in the recipient country (also referred to as "lead time"). Additional time is required for the food to reach intended beneficiaries.

appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

LRP of Food Aid Can Improve Efficiency, but Challenges Remain

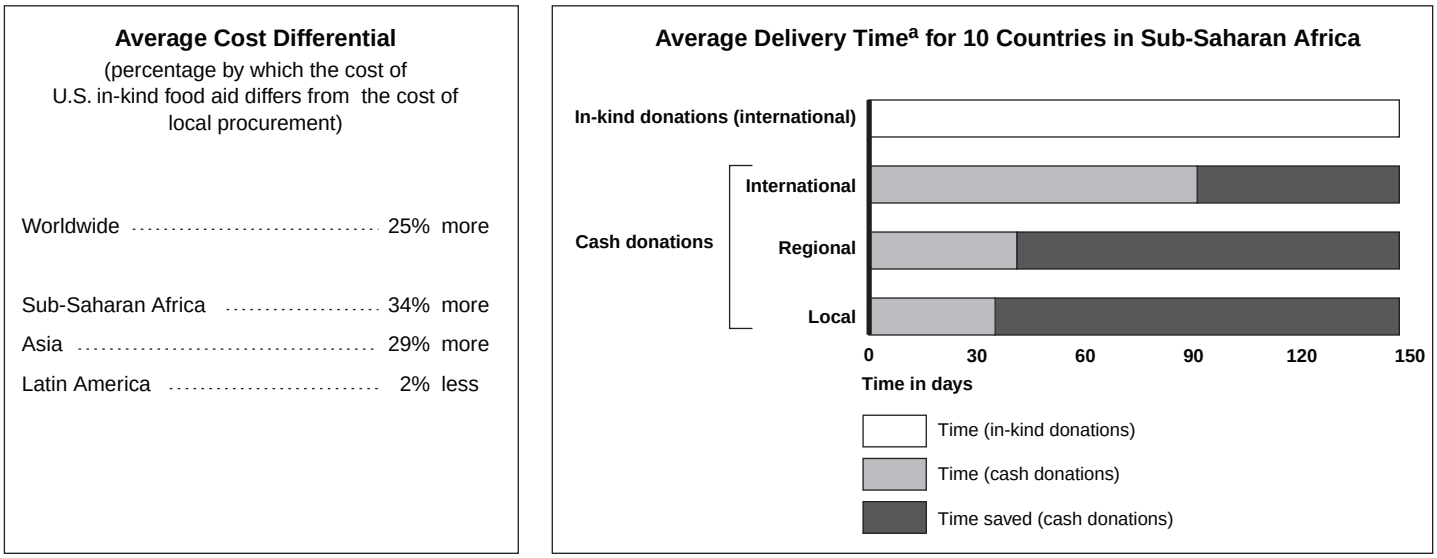
We found that locally and regionally procured food costs considerably less than U.S. in-kind food aid for sub-Saharan Africa and Asia, though the costs are comparable for Latin America. We compared the cost per ton of eight similar commodities[7] for the same recipient countries in the same quarter of a given year and found that the average cost of WFP's local procurements in sub-Saharan Africa and Asia was 34 percent and 29 percent lower, respectively, than the cost of food aid shipped from the United States.[8] (See fig. 1.) Additionally, about 95 percent of WFP local procurements in sub-Saharan Africa and 96 percent in Asia cost less than corresponding U.S. in-kind food aid. However, the average cost of WFP local procurements in Latin America was 2 percent higher than that of U.S. food aid, and the number of WFP's transactions with a lower cost than U.S. food aid was close to the number of transactions with a higher cost.

According to WFP data, LRPs in sub-Saharan Africa generally have a shorter delivery time than food aid procured internationally. We compared the median delivery time for LRP to the median delivery time for food aid either procured or donated internationally for 10 sub-Saharan countries. We selected these countries because they had received both LRP and international food aid. We found that international in-kind donation took the longest, averaging 147 days. Local and regional procurements took on average 35 and 41 days, shortening the delivery time from international donations by 112 days and 106 days, respectively.

[7]The eight commodities were beans, corn soy blend (CSB), maize, maize meal, rice, sorghum/millet, vegetable oil, and wheat, which represent the majority of food aid that WFP and USAID provided.

[8]The cost comparison demonstrates the difference in cost of delivering similar food products in a similar time frame to the same countries. It does not suggest that if the United States had purchased the same amount of food through LRP, it would have cost the same because additional demand in the market could have driven up the prices and there might not have been enough food available for purchase. However, LRP could have offered the United States the flexibility to explore other potential cost-saving opportunities in the region.

Figure 1: Comparison of Cost and Time in Food Aid Delivery



Source: GAO analysis of USAID and WFP data.

[a]Time elapsed between the purchase order date and the date WFP takes possession of the food in the recipient country. Additional time is required for the food to reach intended beneficiaries.

Despite potential benefits, factors such as a lack of reliable suppliers, limited logistical capacity, weak legal systems, and donor funding restrictions have limited the efficiency of LRP. Of the 11 WFP procurement officers we interviewed, 9 identified finding reliable suppliers and preventing supplier default as a challenge to implementing LRP. In addition, limited infrastructure and logistical capacity could delay delivery. For example, according to some WFP officials and private traders we met with, South Africa's rail system and ports are underinvested and have limited capacity to handle food aid during peak seasons. Furthermore, a weak legal system could limit buyers' ability to enforce contracts. WFP generally requires suppliers to purchase bonds, which they will lose if they do not fulfill their obligations under the contracts. However, this requirement is not always feasible to implement, especially when procuring from small suppliers.

Local and regional procurement can provide food that is more acceptable to the dietary needs and preferences of beneficiaries in recipient countries. Experts and practitioners have mixed views on how LRP affects donors' ability to adhere to product specifications and quality standards—such as moisture content and the level of broken and foreign matter—which ensure food safety and nutritional content. However, donors have

yet to systematically collect evidence that demonstrates whether food procured in different locations varies significantly in meeting product specifications and quality.

LRP of Food Aid Has Potential for Adverse Market Impacts That Can Be Mitigated by Better Market Intelligence

LRP can make food more costly to consumers by increasing demand and driving up prices.[9] Although most of the WFP procurement officers we interviewed stated that local procurements of food aid generally do not affect market prices, our review of the literature and interviews during fieldwork show that there have been instances where LRP contributed to price hikes and price volatility in markets from which food is procured. Despite these concerns, almost all of the WFP procurement officers we interviewed stated that they supported the idea of the United States increasing its funding for LRP. However, WFP procurement officers we spoke to, NGO officials in countries we visited, and other experts we met with agreed that increased use of LRP should be done incrementally and that significant challenges remain to expanding market capacity in many countries, particularly in sub-Saharan Africa.

The most significant challenge to avoiding potential adverse market impacts when conducting LRP is unreliable market intelligence. While WFP and other food aid providers rely on market intelligence to understand market conditions, a number of WFP studies, NGO evaluations, and donor assessments show that some pre-purchase market analyses have been incomplete and inaccurate—contributing to unintended consequences such as price hikes and reduced access to food. For example, in 2007, the government of Malawi decided to export 400,000 metric tons of maize to Zimbabwe.[10] In the same year, WFP also procured 48,445 metric tons of food aid from Malawi to support its operations in other countries. USAID Food for Peace, Famine Early Warning Systems Network (FEWS NET), and other private-sector officials working in southern Africa told us that Malawi's decision to export to Zimbabwe and sell to WFP was based on inaccurate production estimates. A few months later, Malawi experienced higher food prices and food shortages. WFP has significantly increased its mandate and ability to collect and analyze local and regional market information in the last decade, but WFP analyses and

[9]Transoceanic shipments of in-kind food aid, if not carefully targeted, can have the opposite but also detrimental market impact of depressing market prices by rapidly increasing the supply of food in markets.

[10]Not all of it was ultimately delivered.

procurement officers confirmed that WFP's market intelligence, while improved, is often inaccurate or incomplete. In many low-income countries, national market intelligence systems are weak and unreliable, and timely data are not always available, which may limit the effectiveness of WFP's market intelligence efforts, according to a WFP report.[11]

In an effort to significantly reduce the risk of contributing to price hikes and long-term food price inflation, WFP uses import parity pricing. In addition to serving as a measure for cost-efficiency, comparing local prices with import parity prices helps those involved in local procurement to determine whether a local procurement will "do no harm" to local markets and consumers by not making local procurements when local prices are higher than international prices.

While the primary purpose of LRP is to provide food assistance in humanitarian emergencies in a timely and efficient manner, a potential secondary benefit is contributing to the development of the local economies from which food is purchased. The development benefits to local economies from LRP are secondary because in almost all cases WFP and NGO purchases are not large enough or reliable enough to sustain increased demand over time. Only recently has WFP acknowledged that LRP can contribute to local development. In several of the countries we visited, we observed WFP LRP initiatives under way that might support local economies in the long term and connect LRP to other food security initiatives. However, many of them are new and limited in scale.

[11]*Food Procurement in Developing Countries*, World Food Program, Executive Board First Regular Session (Rome: February 2006).

Legal Requirements for U.S. Food Aid May Constrain U.S. Agencies' Use of LRP

Legal Requirement to Purchase U.S.-Grown Food Limits Funding for Foreign-Grown Food

Most funding for U.S. food aid is authorized under the Food for Peace Act[12] and cannot be used to purchase foreign-grown food. Funding under the act, approximately $2 billion per year, is restricted to the purchase of U.S.-grown agricultural commodities. However, a limited amount of U.S. funding has been authorized through the 2008 Farm Bill, the Foreign Assistance Act, 2008/2009 bridge supplemental, and the 2009 Omnibus Appropriations.[13]

Uncertainty Regarding Cargo Preference Could Constrain Agencies' Implementation of LRP

Because the leading U.S. food assistance agencies and DOT disagree on how to implement the Cargo Preference Act, their use of LRP could be constrained. The Cargo Preference Act, as amended, requires that up to 75 percent of the gross tonnage of agricultural foreign assistance cargo be transported on U.S.-flag vessels. DOT issues and administers regulations necessary to enforce cargo preference. Among other things, the department has the authority to require the transportation on U.S.-flag vessels of cargo shipments not otherwise subject to cargo preference (hereafter referred to as "make-up requirements") when it determines that an agency has failed to sufficiently utilize U.S.-flag vessels.

Table 1 summarizes differences in agency officials' interpretations of cargo preference requirements.

[12]The 2008 Farm Bill changed the title of the underlying legislation from the Agricultural Trade Development and Assistance Act of 1954, also known as P.L. 480, to the Food for Peace Act.

[13]Since July 2008, Congress has appropriated $50 million to USAID that can be used for LRP in addition to $75 million that the Administration allocated for LRP in International Disaster Assistance funding. The 2009 Omnibus Appropriations Act provided another $75 million to USAID for global food security, including LRP and distribution of food.

Table 1: U.S. Agencies' Interpretations of Cargo Preference Requirements as They Pertain to Implementation of LRP

Requirements	Agency interpretations		
	DOT	**USAID**	**USDA**
1. Agency responsible for determining availability of U.S.-flag vessels	DOT is the sole determining agency for U.S.-flag vessel availability.	USAID is the determining agency for U.S.-flag vessel availability based on USAID program needs. However, USAID seeks DOT concurrence.	USDA is the determining agency for U.S.-flag vessel availability based on USDA program needs. DOT is not permitted to provide input into a determination of programmatic need.
2. Make-up requirements when U.S.-flag vessels are unavailable or an agency uses notwithstanding authority	Tonnage shipped on foreign-flag vessels when U.S.-flag vessels are unavailable or under USAID's notwithstanding authority is counted toward the maximum tonnage allowed on foreign-flag vessels. Any foreign-flag tonnage exceeding the maximum must be made up.	When U.S.-flag vessels are unavailable or when USAID uses notwithstanding authority, tonnage shipped on foreign-flag vessels should not be counted toward the maximum tonnage allowed.	Tonnage shipped on foreign-flag vessels is counted toward the maximum tonnage allowed on foreign-flag vessels. USDA does not have notwithstanding authority since it does not implement emergency programs.
3. Applicability of cargo preference requirements to public international organizations	The grants to international organizations are governed by regulations and guidance issued by DOT.	Cargo preference regulations apply when the authority for LRP is Food for Peace. However, the regulations do not apply when LRP is carried out under authority of the Foreign Assistance Act.	Cargo preference applies to international organizations.
4. Reimbursement methodology	DOT reimburses food aid agencies for a portion of the ocean freight and transportation costs that exceed 20 percent of total program costs.	DOT reimbursement methodology is not specified for all possible scenarios.	DOT reimbursement methodology is not specified for all possible scenarios.

Source: DOT, USAID, and USDA.

The lack of clarity on how to interpret and implement cargo preference regulations may constrain agencies' ability to utilize LRP. For example, USAID's and USDA's LRP pilot programs could be hindered if U.S.-flag vessels are unavailable. USAID officials indicated that, given the limited volume of regional shipments relative to regular Title II shipments, the agency would probably not be able to meet the U.S.-flag compliance threshold if even one shipment could not be transported on a U.S.-flag vessel. According to a USDA official, countries chosen for its LRP pilot field-based projects will likely receive food shipments only once in a fiscal year. If U.S.-flag vessels are unavailable for service at that time, it is unclear how USDA will make up tonnage by country and program the following year since the pilot is of limited duration.

The memorandum of understanding (MOU) that outlines the manner in which USAID, USDA, and DOT coordinate the administration of cargo preference requirements was last updated in 1987 and does not reflect modern transportation practices or the areas of ambiguity related to LRP. In our 2007 review of U.S. food aid,[14] we found that cargo preference can increase delivery costs and time frames, with program impacts dependent on the sufficiency of DOT reimbursements. Therefore, we recommended that USAID, USDA, and DOT seek to minimize the cost impact of cargo preference regulations by updating implementation and reimbursement methodologies of cargo preference as it applies to U.S. food aid. Since 2007, USAID and USDA have proposed a working group with DOT to renegotiate the MOU. To date, however, there have been few meetings and no agreement has been reached between the agencies.

Implementation of Recommendations Could Help Enhance U.S. Food Aid

To address the concerns I have just summarized, we recommend in the report we publicly released today that the Administrator of the U.S. Agency for International Development and the Secretary of Agriculture

- systematically collect evidence on LRP's adherence to quality standards and product specifications to ensure food safety and nutritional content;
- work with implementing partners to improve the reliability and utility of market intelligence in areas where U.S.-funded LRP occurs, thereby ensuring that U.S.-funded LRP practices minimize adverse impacts and maximize potential benefits; and
- work with the Secretary of Transportation and relevant parties to expedite updating the MOU between U.S. food assistance agencies and the Department of Transportation, consistent with our 2007 recommendation, to minimize the cost impact of cargo preference regulations on food aid transportation expenditures and to resolve uncertainties associated with the application of cargo preference to regional procurement.

USAID generally concurred with our recommendations. USDA generally concurred but noted that aggregating some of the products into commodity groups caused a loss of precision in our methodology. In conducting our overall analysis, we worked to ensure that we included the largest number of procurement transactions over the longest possible time period for which we had data, so some aggregation was required. DOT

[14]GAO, *Foreign Assistance: Various Challenges Impede the Efficiency and Effectiveness of U.S. Food Aid*, GAO-07-560 (Washington, D.C.: Apr. 13, 2007).

noted that it implements its mandate through regulation, not the MOU. Nevertheless, the regulations contain ambiguities and we believe these ambiguities can be resolved by updating the MOU. WFP welcomed our timely examination of LRP but noted the lack of evidence showing that LRP introduces quality challenges that are not already challenges to internationally procured and donor provided food aid.

In summary, the timely provision of food aid is critical in responding to humanitarian emergencies and food crises, and LRP has the potential to better meet the needs of hungry people by providing food aid in both a more timely and less costly manner. To fully realize this potential, however, challenges to its effective implementation must be addressed.

Mr. Chairman, this concludes my statement. I would be pleased to respond to any questions you or other Members of the Subcommittee may have.

Contacts and Acknowledgments

For questions about this statement, please contact Thomas Melito at (202) 512-9601 or melitot@gao.gov. Individuals who made key contributions to this testimony include Phillip Thomas (Assistant Director), Sada Aksartova, Kathryn Bernet, Carol Bray, Ming Chen, Debbie Chung, Lynn Cothern, Martin De Alteriis, Mark Dowling, Etana Finkler, Katrina Greaves, Kendall Helm, Joy Labez, Andrea Miller, Julia A. Roberts, Jerry Sandau, and David Schneider.

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