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MEMORANDUM FOR THE RECORD

SUBJECT: Minutes of CIEP Executive Committee Meeting, April 12, 1974 in the Roosevelt Room

ATTENDEES: List Attached

The meeting, chaired by Secretary Shultz and attended by the persons listed at Annex A considered issues relating to international investment, foreign banking activities in the U.S. and assistance to the LDCs to meet the balance of payments problems created by rising import costs for oil and other commodities. The item relating to DISC which was on the agenda was not considered.

1. International Investment

Mr. Flanigan opened the discussion by referring to the paper which had been distributed and indicated that a similar paper had been prepared with respect to overall policy in connection with trade and monetary matters. He pointed out that those aspects of our effort to reform the international economic system relating to investment were lagging. While there was work going on in the XCSS, he felt that the focus was not broad enough and that there was no broad U.S. policy to guide our overall actions. He pointed out that there was a possible hiatus in progress on international economic reform due to potential delays in the trade and monetary field and that it would be desirable to have investment as another area for continuing the discussion of an open world economy with our foreign partners.

He proposed that we use the OECD ministerial meeting to give new impetus to investment work in the XCSS, which in his opinion, had slowed down. Mr. Flanigan felt that if the paper under consideration correctly stated the Administration position he would suggest that it should serve as the basis of the statement at the May ministerial meeting to stepup the pace of investment activities in connection with reform of the international economic system which we had proposed. He suggested that the meeting consider (1) the substance of the paper and (2) the desirability and content of a U.S. statement at the OECD ministerial meeting.

a. Substance

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Mr. Burns asked whether the statement took account of Congressional concern over investment in strategic industries. Mr. Flanigan pointed out that the Administration had testified before committees in both houses and pointed out that there was adequate protection available under existing laws. In addition, the policy statement recognizes certain critical sectors as appropriate exceptions to the overall policy. Mr. Flanigan indicated that Chairman Burns was right in referring to Congressional concern (especially in light of recent bills that have been introduced by Representative Roe) but that he felt that the only serious bills were those designed to get more information about foreign investment and not to restrict it.

Mr. Burns asked if the CIEP had made a list of existing constraints on foreign investment. Mr. Flanigan indicated that such a list had been prepared and that it would be circulated to the Executive Committee members.

Mr. Rush indicated that the statement was a good one but expressed concern that the U.S. was one of the major culprits when it came to government interference. He referred to the Jackson/Vanik amendment with respect to MFN, the extraterritorial problem with respect to application of the Trading with the Enemy Act in Argentina and antitrust problems similar to those faced by ICI whose sales office in New York gave the Justice Department jurisdiction to seek data with respect to its worldwide operations. He said in his opinion our antitrust laws are the most flagrant example of the extraterritorial application of laws in the investment field.

Mr. Flanigan pointed out that while it was true that we sinned in the investment area most other nations (with the possible exception of the Federal Republic of Germany) were far worse sinners than the U.S. Chairman Shultz did note, however, that if we pushed the investment issue then we would be sure to get the areas where we were vulnerable raised by other nations. Mr. Flanigan noted that we must accept the fact that nations will be reluctant to accept the kind of policies we have outlined and that we may need to grandfather certain practices. What we are trying to do with the policy statement is to set forth a general framework and to begin work on removing the existing restrictions.

Mr. Eberle endorsed the principle of the grandfathering concept of extraterritorialling as expressed in Item III(2) and also endorsed the proposal in Item III(3) where we would seek to negotiate procedures for handling conflicts caused by extraterritorial application of laws. He also pointed out that Item I(3)(a) dealing with investment incentives that distort trade patterns could create a problem for the U.S. with respect to state laws and that we might need to grandfather some of our state practices.

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In addition, he raised the question of whether it would be possible to totally eliminate or harmonize investment incentives, and suggested we revise our statement on the purpose of our work on incentives to bring it in line with what we are seeking in the OECD Trade Committee and GATT.

Mr. Volcker felt that the major issues with respect to the investment statement were those of tactics and priorities. He felt that it was a good statement of our position and that he had no problem with it as such except to note that it would be extremely difficult to negotiate and that some of its provisions would hit the U.S. as well as other nations.

After Messrs. Volcker, Rush and Tabor had agreed that the statement was a generally acceptable statement of our overall aims, Mr. Shultz suggested that the statement be reviewed in light of the previous discussion and that any specific comments be given promptly to Mr. Flanigan.

b. Tactics

The meeting then considered the question of tactics. Mr. Volcker expressed a strong view that it would not be useful to "throw a big stone" into the OECD Ministerial Meeting on the basis of the draft statement of policy. He believed that we should continue to proceed in those areas where progress seems most feasible and that the best course of action would be to proceed in the same manner as we had over the past year. He felt that any new statement from such a sweeping document could raise questions and could set the OECD work back by creating suspicions in the minds of other nations (e.g. that we were changing our mind by starting the investment exercise anew). In short, he felt that we should continue to push along in the XCSS and that no new initiative was required.

Mr. Casey felt that there should be a new thrust at the ministerial meeting but that we would need to be careful as to how we presented our position. He noted that there was not much enthusiasm in the OECD for the investment exercise and that it was only U.S. efforts which had kept it alive. Even now there were only two areas in which work is seriously proceeding-- national treatment and investment distortions -- and that all that was likely to result from the negotiations in these areas was some general principle with respect to consultation. He felt that the U.S. should continue to push to get something more favorable and suggested that there may be some pressures to this end from Congress resulting from the UN effort (in this regard he cited his recent letter from Rep. Gonzales with respect to a new investment forum and greater involvement of the LDCs). In short, Mr. Casey felt that a worthwhile initiative could be taken by the U.S. at the ministerial meeting.

Mr. Eberle supported Mr. Casey's view and indicated that we needed to move in a firm positive way in the OECD. If we didn't, OECD activities are apt to be concentrated on MNCs and results might be negative. He felt that we should take the initiative, that we could gain from such an initiative and that we would, at least, prevent any negative results.

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Mr. Rush agreed with Mr. Volcker and indicated that it was his impression that a number of matters in the investment field were moving well in the OECD. If we came forth now with broad proposals, we could be counter-productive by upsetting existing work and perhaps accelerating work on the MNC issue. While he felt it to be a good statement of our broad objectives, he felt that we should not toss out a big bomb at the ministerial meeting.

Mr. Flanigan pointed out that there was apparently a different perception as to how investment matters were moving in the OECD as some felt that the investment exercise needed a major infusion to keep it moving. He pointed out that he did not feel that a statement at this time would represent a new initiative or any change in U.S. position. He pointed out that we did not have to use this statement in its entirety but could refer to the work that was going on and then suggest areas for further work so that there would be no winding down of the current limited efforts in investment. Rather, we would attempt to broaden the OECD efforts with respect to investment to complement our reform movements in the trade and monetary field.

Mr. Volcker agreed that there was no major progress in the investment field in the OECD and there were real pockets of opposition and restraint. However, he pointed out that the XCSS was set up largely to handle investment matters and that it was in our interest to keep the investment exercise moving. He had no great disagreement in seeing something done at the ministerial meeting but pointed out that if we take a new hard approach we might force others to back off from their even limited cooperation. In short, he felt we should push only where progress seemed possible.

Mr. Rush added that if we were making a new initiative we should consult with our partners before hand.

Mr. Stein felt that this was not a major new initiative. In fact, it was a course of action which we had agreed upon two years ago and had dribbled along in a generally unproductive way since then.

Mr. Shultz then summarized the discussion on investment as follows:

1. There was general agreement on the policy paper which had been circulated but there were a few problems which had been raised which should be taken care of. Comments should be given to Mr. Flanigan and the CIEP staff, and the revised paper circulated for internal use as an internal policy guideline for administration officials;

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2. There was general agreement that the U.S. should keep the investment issue alive in the OECD and use the ministerial meeting, to the extent possible, to do so. The best way to provide continued emphasis was essentially tactical but the general consensus of the meeting was that the U.S. should not come on strong with a major new initiative. He felt that a group was needed to consider what our tactics should be for the ministerial meeting and what document we would need to do this. He suggested that the State Department take the lead and chair a small working group with representatives of CIEP, Treasury and other interested agencies, to decide on the best way to use the OECD, and in particular the ministerial meeting, to keep the investment issue moving.

3. It was agreed that we would need to consult with our major trading partners prior to the ministerial meeting.

2. International Capital Markets

a. National Treatment for Foreign Banks

Mr. Flanigan began the discussion by saying that this issue had been discussed before at the January CIEP Executive Committee Meeting, and that in principle the Council had agreed that principle of non-discrimination should apply to foreign bank regulation in the United States. Because of disagreements among departments regarding the Federal Reserve's draft legislation designed to bring foreign bank regulation in line with the principle of national treatment, Mr. Flanigan felt that it was necessary to re-raise the issue before the Council.

Governor Mitchell then reviewed the status of the Fed's proposal. He indicated that the objectives of the legislation were to bring foreign bank regulations in line with the principle of national treatment, to subject foreign banks to controls for monetary policy purposes, and to provide a Federal option for U.S. entry by foreign banks. During the past year, Governor Mitchell had extensive discussions with foreign central bankers, and generally the principle of nondiscrimination was acceptable. Further discussions with foreign central banks are being carried on. Foreign commercial banks are concerned about what the reserve requirements of the Federal Reserve will cost them, and are concerned about their existing activities in the U.S. Governor Mitchell indicated that required Fed membership for foreign banks was technically not national treatment, but since major U.S. competitors of foreign banks are members of the Fed, in practice, it is nondiscriminatory treatment. He also indicated that all foreign banks derive some type of grandfathering procedure for multi-state activities as well as for their non-banking activities in the underwriting and brokerage areas. Governor Mitchell felt that it was important to move ahead quickly with legislation because of the rapid expansion of foreign bank activities in the United States. Postponement of action will make grandfathering more difficult. Since grandfathering is a way of reducing the likelihood of foreign retaliation, it is better to take action now when it is easier to grandfather the existing activities than to wait until the level of foreign bank activity is even greater. If U.S. banks want to continue to expand abroad in the future, it is important to get this issue settled now in a satisfactory way.

Governor Burns stated that if we wait, the problems will become more acute and we may get restrictive legislation in the future. He indicated that U.S. banks would prefer no action at the moment, because they fear retaliation. But if we proceed with generous grandfathering provisions, the fear of foreign bank retaliation will decline. He indicated that he would be opposed to permanent grandfathering even for branching. Practically, he did not think that there was a great difference between

15 year grandfathering and permanent grandfathering since many of the activities that would be grandfathered will probably be allowed to all U.S. banks, foreign and domestic-owned banks, sometime within the next 10 to 15 years.

Mr. Rush indicated that the State Department was studying our treaties to determine if there would be major problems with various grandfathering procedures. So far, none appear to have emerged.

Mr. Volcker indicated that there were contrasting views within the Treasury Department. For some, the present circumstances are not bad and put desirable pressure on the U.S. banking system, especially in the area of multi-state branching. Actions along the lines of the Fed bill would tend to freeze the U.S. banking system at its present form. Since there is no possibility that legislation could be passed this year, we should wait and see how things develop and possibly prepare legislation that would include changes in the U.S. banking system. He indicated that while grandfathering procedures may protect existing U.S. banks abroad, future American banking growth abroad may be subject to restrictions.

Chairman Burns stated that he did not think the Fed proposals would freeze the U.S. banking system since the Fed proposal simply brought the regulation of foreign banks in line with the regulations of U.S. banks, but did not prevent overall changes in the U.S. banking system.

Governor Mitchell indicated that if foreign countries did retaliate by restricting future American bank growth, we could vigorously protest such actions on the basis that such actions would be nondiscriminatory treatment.

Mr. Volcker indicated that national treatment can be subject to many interpretations. For example, if we override the principle of state's rights, which is an important principle in our banking system, we could be accused of not applying national treatment. Mr. Volcker felt that it was not undesirable to have some fluidity in the system. In addition, he was concerned that the legislation proposed by the Fed might come out of Congress even more restrictive because it will serve as a vehicle for discriminatory amendments.

Mr. Eberle felt that it was important to set a grandfathering date in some way as soon as possible.

Chairman Burns stated that Mr. Volcker was right that there would be no legislation this year, but that there is a process - a period of education - which will have to take place if concrete legislation is to be carried forward at some time. Proposing new legislation now would enable us to set a grandfathering date and would provide a specific concrete set of proposals for everyone to discuss.

Secretary Shultz concluded the discussion by stating that he thought it was the consensus of the group that it was important to propose a piece of legislation to Congress and establish a grandfathering date. In addition, he stated that it was important to proceed with consultations with foreign governments and foreign banks so that it will be made clear that our intention is to avoid discriminatory treatment. Continued Administration support for the Federal Reserve draft legislation would be contingent on that legislation remaining consistent with the principle of nondiscrimination.

b. The Foreign Window Proposal

Chairman Burns stated that the Fed would have a paper on the foreign window proposal, but at the present time, thinking is running against the proposal.

Governor Mitchell indicated that the basic problem is how to build a fence around the foreign window in order to protect domestic monetary policy. Establishing the foreign windows would create channels for U.S. and domestic residents to avoid interest rates and reserve requirement restrictions. The foreign window raises other questions, of a more technical nature: for example, how deposits held in the foreign windows should be melded into U.S. domestic money supply. The work within the Fed today indicates that there is a hazard that there would be leakages from the foreign window or into the U.S. domestic monetary market. In addition, Governor Mitchell indicated that U.S. banks have not been that receptive to the proposal since U.S. banks believe that it is necessary to maintain a full service capability abroad in any case.

Chairman Burns also stated that he saw no serious interest on the part of American banks in having this foreign window and the existence of the foreign window would raise hazards for the credit and money policy. He indicated, however, that work within the Federal Reserve on the proposal would continue and that in addition the Fed will consider an option which would allow a U.S. bank to accept foreign currency deposits.

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3. U.S. Policy Towards Financial Proposals to Assist LDCs to meet oil and other import problems

Mr. Volcker lead off the discussion on the Treasury Department paper by pointing out that the only agreement so far was the universal recognition of the problem and many suggestions for its solution. With respect to procedural aspects of the problem, he raised the question of whether the U.S. could contribute anything by suggesting a forum for discussion to sort out the various proposals. With respect to our substantive position, he said we needed to decide what contribution the U.S. could make and what our overall attitude toward the effort will be. He concluded by noting that if we had no U.S. position then Secretary Kissinger should finesse the question during his upcoming UN speech.

Secretary Shultz indicated that we did have a position -- i.e. holding our level of support to the levels projected in the budget. He felt that we would be doing extremely well if we got the amounts for aid that we had requested and that we could not make further commitments because of the Congressional problem.

Mr. Cooper pointed out that it might be somewhat premature to discuss magnitudes of overall aid to the LDCs because of questions as to the magnitude of the impact of the oil price rise and also as to the precise timing of this impact. Mr. Flanigan noted that what was needed was careful country studies to assess the size and timing of the impact.

Mr. Volcker raised the question of whether the U.S. should accept a position of no additional aid. Mr. Eberle said in his opinion we should not lock the door on the possibility of additional aid but that we should not adopt a position that accepts the continuance of the current oil price. Mr. Flanigan noted that, on the basis of what was said so far, he would feel that it would be inappropriate to bring the issue forward in an international forum like the UN before we know our own position.

Mr. Cooper indicated that informal discussions were now underway and oil producers' indecision gave the U.S. some time to decide on its ultimate position. In his opinion what was needed was a better picture of the timing of the problem. Mr. Volcker expressed his uneasiness with respect to this kind of informal approach and Mr. Flanigan added that the U.S. would not exercise the appropriate leadership if it merely determined the parameters of the problem and waited for others to advance proposals or to take action.

The committee agreed to Mr. Flanigan's proposal that a working group under Mr. Cooper's chairmanship should be convened to examine the extent of the problem and timing issues and suggest options for U.S. policy.

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MEMORANDUM

THE WHITE HOUSE

WASHINGTON

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May 14, 1974

MEMORANDUM FOR:

SECRETARY OF STATE
SECRETARY OF THE TREASURY
SECRETARY OF AGRICULTURE
SECRETARY OF COMMERCE
SECRETARY OF LABOR
DIRECTOR OF THE OFFICE OF MANAGEMENT AND BUDGET
CHAIRMAN OF THE COUNCIL OF ECONOMIC ADVISORS
THE SPECIAL REPRESENTATIVE FOR TRADE NEGOTIATIONS
ASSISTANT TO THE PRESIDENT FOR NATIONAL SECURITY AFFAIRS
ADMINISTRATOR AGENCY FOR INTERNATIONAL DEVELOPMENT

FROM: PETER M. FLANIGAN

PMF

SUBJECT: Meeting of the Executive Committee of the Council on International Economic Policy, Friday, May 17, 1974, 3:00 p.m., Roosevelt Room, The White House

Agenda

I. World Food Policy - CIEPSM 30 presents options for U.S. policy on national and international stocks of food in preparation for the World Food Conference later this year. CIEPSM 31 proposes alternative positions for USG food aid programs. (TABS A-D)

II. International Investment - Report on Mr. Flanigan's consultations with Europeans regarding possible U.S. proposals to the OECD. (NO PAPER DISTRIBUTED)

III. DISC - The paper attached at Tab E reviews the current status of the DISC program and presents options for the future of the program. (TAB E)

Please confirm your attendance to the CIEP Secretariat, 456-2937.

Attachments (As stated)

cc: NSC - General Scowcroft

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SUMMARY

A-D

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COUNCIL ON INTERNATIONAL ECONOMIC POLICY

WASHINGTON, D.C. 20500

U.S. POLICY ON NATIONAL AND INTERNATIONAL STOCKS OF AGRICULTURAL COMMODITIES (CIEPSM 30) AND FOOD AID (CIEPSM 31)

I. INTRODUCTION

The attached papers outline options for U.S. policy on national and international stocks of agricultural commodities (TABS A & B) and food aid (TABS C & D). This summary paper highlights the issues and the options and sets out the key considerations for these policy areas.

A U.S. policy position is required for the upcoming deliberations and negotiations in the World Food Conference, the FAO, and the MTN.

II. SUMMARY OF THE PROBLEM, THE ISSUES, AND THE OPTIONS

A. STOCKPILING

1. The Problem

World grain stocks have rapidly fallen to very low levels. If the world does not rebuild these stocks to adequate levels, future shortfalls in world grain production will result in unacceptable price rises in the U.S. and/or in an unacceptable degree of malnutrition and starvation in LDCs.

2. The Issues

The key issues in determining the U.S. policy position for stockpiling are:

a. Will other countries in the world, especially the Central Plan countries and major developed country importers, hold more grain stocks than they have in the past?

b. If other countries in the world will hold more grain stocks, What positive strategy can the U.S. Government pursue to to assure that they do hold more stocks?

c. If other countries will not hold more stocks, or other countries will not increase their stocks enough, Will the Governments of the U.S. and other major grain exporters hold the additional necessary amount of stocks?

d. If the Governments of the U.S. and other major grain exporters will not hold these additional stocks, Will the U.S. allow the Central Plan and major developed importers to have unlimited access to its markets during world grain shortages at the expense of the LDCs and U.S. consumers?

e. If the U.S. will not allow unlimited access to its markets when world stocks are inadequate and world production shortfalls occur, How will the market access mechanism used affect U.S. consumers, commercial trading partners, and LDCs?

3. The Options

The options, as set out in the papers at TABS A and B, all lend themselves to a multilateral approach in which the U.S. would seek to have other nations carry more stocks, to further open their markets and to keep them open, to exchange information about production levels and import requirements, and to consult on production policies (other possible approaches are discussed in Part III). The options are:

OPTION A: No U.S. Government held stocks (all stocks held by private traders and others); food reserves the responsibility of individual countries; open market purchase of food aid; present domestic farm program (price supports, loan rates, land set-aside).

OPTION B: U.S. Government accumulate stocks when required by domestic farm price program only for emergency food aid on a grant basis.

OPTION C: U.S. Government accumulate stocks sufficient for general food aid needs, including concessional sales.

OPTION D: U. S. Government accumulate non-designated stocks according to international guidelines (or, without such guidelines, on its own) for use in covering commercial and food aid requirements. Some portion of carrying costs would be recovered when the stocks were released.

OPTION E: U.S. Government participation in an internationally controlled stockpile in which accumulation and maintenance of stocks would be jointly financed by exporters and importers.

B. FOOD AID

1. The Problem

Food aid has been used by the U.S. to attain a variety of objectives abroad, particularly: disaster relief, helping to fill balance of payment and budget gaps in security related situations, raising nutritional levels, promoting economic development, meeting broad political objectives, and developing new commercial markets. In the overall food shortage situation of the past 18 months, these objectives came into sharp conflict between themselves and with domestic food and agricultural objectives. Moreover, the U.S. suggestion of a World Food Conference to review the world food situation has focused attention on possible mechanisms, including food aid, for helping developing nations to meet their food needs. These factors, plus the growing importance of food in the changing foreign policy environment, necessitate an analysis of the effectiveness and desired role of food aid in comparison with other forms of aid in attaining U.S. objectives, both at home and aboard.

2. The Issues

The key issues in determining the U.S. policy position for food aid are:

a. What objectives does the U.S. want to achieve with its food aid program?

b. Will food aid be the major U.S. contribution to world food security, or will it be a relatively minor part of a U.S. stocks policy and related policies designed to assure a high degree of domestic and world food security in a more open world economy?

c. What degree of burden is the U.S. willing to bear to achieve its food aid objectives?

d. Is the U.S. willing to guarantee stability of supply for food aid?

e. What related financial aid is required to make food aid most effective?

3. The Options

The options, as set out in the food aid study at TABS C & D, are:

OPTION I: Phase down ongoing food aid and provide food only in emergency and disaster situations.

OPTION II: Provide food only for disaster relief, highest priority security assistance requirements, and high nutritional impact activities.

OPTION III. Continue the present multi-purpose program (disaster relief, security/short-term political, nutritional, and development assistance).

OPTION IV. Provide food and dollar aid in a major long term effort to underwrite per capita consumption and production levels in LDCs.

III. DISCUSSION

The major objective of U.S. policies for stocks and food aid is, in conjunction with the related policies of other nations, to provide an acceptable degree of domestic and world food security. The working definition for food security that was agreed to by most of the agencies involved in these studies is:

> "That condition in which food production and reserves are adequate to protect normal consumption requirements (measured either in terms of aggregate demand trends or in terms of per capita needs based on a moving average) against year-to-year variations in production within an acceptable range of price fluctuation."

Major policies that contribute to domestic and world food security, as defined, include stockpiling of agricultural commodities, food aid, and devices to allocate available supplies (e.g., export controls). Mechanisms that support these policies and the attainment of world food security include, on the supply side, agricultural and economic development assistance to less developed countries, more open world trade, consistent domestic agriculture programs, and on the demand side, expanded population control programs and, in developed countries, a reduction in protein consumption.

The attached studies allude to some of these supporting mechanisms but for the most part, they deal with only two pieces of the policy matrix that helps provide world food security, namely stockpiling and food aid.

There is a high degree of interaction between stockpiling, food aid, and financial aid policies. Food aid commitments can be made without the backup support of a stockpile, but after a certain food aid commitment level is reached, a stockpile, perhaps only of the size necessary to support the food aid commitment, is appropriate. Stockpiling levels can also be designed to primarily sustain living standards, or, they can be designed to sustain living standards and provide support for a specific level of food aid.

In the long run, as is noted more fully later, there can be no world food security unless trends in production growth keep up with trends in population growth. Consequently, financial aid aimed at balancing food demand and supply in LDCs is a significant part of any policy mix for attaining domestic and world food security in a more open world market and thus, for enabling the U.S. to achieve its domestic and international objectives.

A. FOOD SECURITY

A high degree of U.S. domestic food security (minimal price fluctuation) during world grain production shortfalls depends on:

1. The existence of an adequate level of grain stocks in the world, or

2. The use of export controls

Without one of these factors being present, U.S. food prices will rise to unacceptable levels during world grain production shortfalls.

A high degree of world food security can only be assured by the existence of an adequate level of grain stocks in the world to buffer against world grain production shortfalls. However, a minimal degree of world food security (avoidance of large scale starvation) could be attained without adequate world grain stocks if an appropriate level of food aid could be provided to those in need when world production shortfalls occur.

In that the U.S. seeks a more open world economy in which market forces are allowed to operate more freely, an adequate degree of domestic and world food security depends largely upon the existence of a satisfactory amount of grain stocks in the world at all times. Food aid programs serve as a supplement to the food security provided by this level of world grain stocks for those consumers with particular needs.

An adequate world stockpile of grains can contribute to the attainment of numerous objectives. These include:

- Providing food supply and price stability.
- Providing support for food aid programs
- Protecting consumers, especially against upside price swings.
- Protecting meat producers against upside price swings for grain.

- Protecting grain producers against wide price fluctuations, especially downside price swings.
- Protecting consumption levels in LDCs.
- Protecting commercial international trade levels and flows.
- Providing a base to undertake and maintain trade initiatives with new trade partners (e.g., Central Plan countries for the U.S.).
- Providing a means for export development.
- Retaining open world markets and better access to supplies.

However, even the past relatively high levels of grain stocks were shown to be inadequate to achieve these objectives, both for the U.S. and for other countries during the past two years. In 1972-73 world grain stocks were drawn down from 144 to 100 million MT. Except for the estimated 25 million MT surplus accumulated by the USSR due to their record 1973-74 grain crop (a surplus that cannot be counted on with certainty from year to year), stocks would have been drawn down even more in 1973-74. In the major grain exporting countries, stocks were not only drawn down significantly in 1972-73 (43 million MT), but are likely to be drawn down by an additional 14 million MT during 1973-74. At the same time, the acreage reserve in the U.S. was being exhausted. The result was strong upward price pressures in the U.S. and elsewhere and food shortages in many parts of the world.

It is questionable whether even these inadequate past world stock levels will be rebuilt unless government policies are deliberately designed to do so. If they are not rebuilt, not only will the above objectives be unattainable, but the next serious shortfall in world grain production will have much more significant impacts on world food availabilities and prices than were experienced in the past two years, not only because of the lower stock levels to begin with, but also because of increasing affluence and population growth. For example, a crop failure in the upcoming 1974/75 crop year that resulted in a stocks drawdown similar to that in 1972-73 would reduce 1975-76 beginning world grain stocks below 96 million MT (even when the questionable estimate of 25 million MT of stocks held in the USSR is included in total world grain stocks).

Thus, for the U.S. to attain its own domestic and international objectives in this area, an adequate level of world stocks must be rebuilt. One way to accomplish this is for countries other than the U.S. to hold more stocks than they have in the past. However, the attached studies do not estimate the quantity of stocks that will be held by other countries and the U.S., the degree of price fluctuation that will result when world grain production falls short, nor the cost to the U.S. Government under each combination of options. Nevertheless, if U.S. stockpiling and food aid options are to be dependent on this approach, the extent to which other countries will carry additional stocks and contribute more food aid is critical because it will determine the degree of U.S. domestic and world food security that will accrue as a result of these U.S. policies. Furthermore, a positive U.S. strategy for assuring that other countries will hold more stocks than they have in the past must be developed and implemented.

In the recent past, the source of a large portion of year-to-year variations in the world grain production has been the Central Plan countries (the USSR, the PRC, and Eastern Europe). India had significant production shortfalls in the mid-1960s, but then achieved some stability until the shortfalls of the last two years. (It should be noted that the U.S., which has experienced yield shortfalls for wheat as high as 6.2 percent due purely to weather, achieved nearly full production in the recent years when the largest shortfalls in production occurred abroad.)

Thus, the Central Plan countries should be convinced to produce or buy adequate stockpiles of grain, or to tighten their belts substantially when they have crop shortfalls. If they cannot be convinced, a stockpiling and food aid mechanism must be designed to buffer the U.S. and other countries, including the LDCs, from the impact of crop shortfalls in these countries. If such a buffer is not created, the U.S. and other countries will be subject to substantial price increases from surges in import demand by these countries (unless export controls are used), and LDCs will be subject to food shortages (whether or not export controls are used). In such cases, a food aid program of some magnitude would be in order. However, it would be difficult to provide adequate levels of food aid in such circumstances, even if the U.S. and other developed countries guaranteed stability for their food aid programs.

B. THE ROLE OF GOVERNMENT

The central issue here is the extent to which action by the U.S. Government is necessary to provide the desired degree of domestic and world food security. Thus, should the role of the U.S. Government be:

1. To assure that the action of the U.S. Government does not unduly interfere with the operation of world market forces in determining production, stocks, resource allocation, and prices of food and feed grains, or

2. To seek to assure by its stockpiling, food aid, and related policies that world food production plus reserves are adequate to protect normal consumption requirements against year-to-year variations in production within an acceptable range of price fluctuation.

This issue is a particularly acute one if other countries cannot be convinced to hold that level of stocks which will enable the U.S. to attain its domestic and foreign objectives in this area. If other countries will not hold the necessary level of stocks , is the U.S. Government, perhaps along with the governments of other major grain exporters, willing to hold the additional amount of stocks, including stocks required for food aid programs, necessary to assure an adequate degree of domestic and world food security in a more open world economy?

It should be noted here that even if it is decided that the role of the U.S. Government is to assure the desired degree of domestic and world food security, it does not follow that the U.S. Government will have to hold large stocks. If other countries can be convinced to increase the level of their stocks and their food aid commitments and they are assisted in doing so, the U.S. burden may be lightened. Under this approach, however, if there is a shortfall in the level of world stocks carried by other countries and private U.S. sources, the U.S. Government would carry enough reserves to bring total world stocks up to the desired level.

C. DOMESTIC ASPECTS

Congress and the American public do not want domestic and world food security to fall below some critical minimum level. Put another way, in considering different stockpiling and food aid policies, the likely response of other countries to them and to strategies for implementing them, the Administration is also deciding what degree of world food security will reduce the risk of potentially unpalatable national choices during future world grain production shortfalls to an acceptable level.

In that the Central Plan countries tend to account for much of the variation in world grain production, the level of world stocks held under each combination of stockpiling and food aid options will determine the degree to which grain production shortfalls in these countries will affect the U.S. economy. If U.S. policies are such that grain production shortfalls in these countries and subsequent large U.S. and world grain purchases by them result in significantly higher U.S. food prices and less than sufficient grain availabilities for the poorest nations, the reaction of Congress and the public to these policies is likely to be a strongly negative one. To the extent that this public reaction results in limiting the access of other countries to the U.S. grain market, the impact of an export control mechanism on U.S. consumers, new and traditional trading partners, and the LDCs would be a problem of significant magnitude, especially if world grain supplies were particularly short.

These factors, in turn, need to be related to the costs of more U.S. Government intervention in the marketplace and of the U.S. Government holding larger stocks than would be held by U.S. private traders and others. That is, although the U.S. Government may add to U.S. and world price stability by its stocks policy (by acquiring stocks in times of surplus so as to hold prices up and releasing them during production shortfalls so as to hold prices down), there are other factors such as associated storage costs and the degree of compatibility between domestic farm policy and stockpiling and food aid policy that should be considered, too.

D. INTERNATIONAL ASPECTS

The degree of world food security the U.S. chooses as its objective and the consequences flowing from the strategy and policies it selects to achieve it will influence world grain price stability, the impact of world product shortfalls on developed countries and especially on LDCs, and the extent to which nations will depend upon allocation mechanisms to control domestic and international movements of food in the future. To some extent these policies will also determine the flexibility that the U.S. will have in attaining the cooperation of many nations in meeting other U.S. objectives. In addition, they will help determine the credibility of the U.S. as a dependable supplier of agricultural commodities as we seek more open trade. These policies will also influence our ability to negotiate effectively in the World Food Conference, the FAO, and the MTN.

A final point as to the international implications of these two policy areas deserves mention. As indicated earlier, stockpiling and food aid are only two elements of the policy matrix that facilitates attaining a sufficient degree of domestic and world food security. They speak to the short run; to assuring that year-to-year variations in food supplies do not result in unacceptable price rises in the U.S. and in undue hardship for other nations.

In the intermediate and long run other elements of the policy matrix are critical. World population is expected to reach at least 10 billion near the end of the 21st century (the lowest U.N. projection). At best, food production in the least developed countries has barely kept up with population growth in the recent past, and there are cases in which it has not kept up. Moreover, rising affluence has grown to be a formidable competitor for available food supplies. Stockpiling and food aid are not designed to deal with this long term problem. However, the financial aid category included in the food aid options could be directed at slowing population growth, increasing production, and at other needs in the LDCs. Such efforts would focus on this longer range problem. To this degree, the food aid options include the potential for a broader set of U.S. programs designed to more effectively contribute to the easing of the food problem in the LDCs over the longer run.

E. INTERNATIONAL APPROACHES

There are three basic approaches that the U.S. can take in dealing with these stockpiling and food aid issues. A unilateral approach could be used in which the U.S. would develop its own policy in these areas, leaving others to adapt to that policy in whatever manner they choose.

Another approach would be for the U.S. to negotiate bilateral agreements on stockpile and food aid policies with other major grain exporters, leaving major importers and others to adapt in whatever way they choose. This approach was not considered in the stockpiling study because of the orientation of U.S. policy toward multilateral solutions and U.S. antipathy to producer cartels. However, failing to attain a multilateral solution, this approach may be desirable as a fallback position.

The multilateral approach would be for the U.S. to negotiate stockpile and food aid policies with major grain exporters and importers and others. The options in the stockpiling paper, in varying degrees, lend themselves to a multilateral approach in that they are intended to include efforts to get other countries to carry more stocks and to contribute more food aid to further open their markets and to keep them open, and features such as international exchanges of information, and consultative procedures for production policies.

IV. CONCLUSION

The attached studies include numerous combinations of stockpiling, food aid and financial aid options that can be adopted as the U.S. policy position. The basic combinations, which are presented in Figure 1, each contribute to the attainment of such U.S. domestic and international objectives as price stability, more open trade, and adequate food supplies for the poorest countries to a different degree. One of the combinations of options needs to be selected as the U.S. policy position for the upcoming deliberations and negotiations in the World Food Conference, the FAO, and the MTN.

It should be noted that the degree of domestic and world food security resulting from this choice will depend on the extent to which other countries will increase their stockpiling and food aid burdens over past levels. Thus, although there are risks in such an approach, the U.S. can choose a policy position for the World Food Conference and other international forums that will put substantial pressure on other countries to share more of the total burden of stockpiling, food and financial aid. Then, if other countries do not assume an adequate portion of this burden, the U.S. could fall back on a different combination of options, perhaps in conjunction with a shift to a bilateral or unilateral approach achieving its objectives.

FIGURE 1: Combinations of Stockpiling and Food Aid Options

STOCKPILING OPTIONS

FOOD AID OPTIONS	Option A No US Held Stocks; Stocks held by Private Sources	Option B US Held Stocks for emergency food aid	Option C US Held Stocks for general food aid	Option D US Held Stocks for commercial and food aid needs	Option E US Held Stocks under international control
Option I Disaster relief only; increased dollar aid					
Option II Disaster relief, high priority security assistance, high nutritional impact; some dollar aid					
Option III Continue present multi-purpose program; some dollar aid					
Option IV Food and dollar aid to upgrade per capita consumption and production in LDCs					

Consequences and Degree of Contribution to the Attainment of U.S. Domestic and International Objectives of Each Combination of Options

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U.S. POLICY ON NATIONAL AND INTERNATIONAL STOCKS OF AGRICULTURAL COMMODITIES

A Summary of CIEP/SM 30

The United States and the international community have economic, political, and humanitarian interests in world food security. World food security is defined as that condition in which world production plus reserves are adequate to protect normal consumption requirements (measured either in terms of aggregate demand trends or in terms of per capita needs based on a moving average) against year-to-year variations in production. This definition implies minimal price fluctuations.

World food security, and how to provide for it, raises a number of policy issues, not all of which can be answered in a discussion of stocks policy. For example, it must be recognized that over the long-run there will be no world food security unless trends in production keep pace with trends in population growth. World food security, therefore, has implications for domestic farm policy and for foreign assistance programs which are not touched upon in this paper. This paper also has not dealt with the problem of assuring appropriate distribution of available world supplies -- a particular problem when supplies are short and governments want to ensure that the food requirements of the most needy groups will continue to be met.

Thus reserve stocks are only one aspect of world food security. They are suited to dealing with the problem of aggregate year-to-year supply variations. Therefore, the basic issue that stocks policy must address is how best to provide against the next bad crop year.

This study includes a preliminary effort to quantify stock levels required to meet varying degrees of world food security. The selection of a US stock policy, and the accompanying degree of world food security which it implies, will be influenced by other U.S. policy objectives such as:

1. Minimum government intervention in grain markets;

2. Increased U.S. foreign exchange earnings from agricultural exports;

3. Avoidance of export controls;

4. Avoidance of extreme price fluctuations for both consumers and producers;

5. Avoidance of excessive budgetary costs for the U.S.;

6. Equitable sharing of the costs of world food reserves;

7. Assuring a U.S. ability to respond to humanitarian needs and foreign policy requirements.

One approach open to the US would be to return to the unilateral stocks policy of the 1950s and 1960s. This approach proved very costly and we have deliberately moved away from it. A second approach would be to negotiate bilateral agreements with other grain exporters to develop stock and export policies in concert. We did not examine this approach in detail because of our present policy orientation toward multilateralism and our antipathy to producer cartels.

Five options which would lend themselves in varying degrees to a multilateral approach were explored -- one involving no USG-held stocks, three requiring USG stocks, and one calling for internationally-held stocks.

Option A would make world food reserves the primary responsibility of individual importing countries, with a variety of techniques available to the U.S. to enable developing countries to participate fully in the system. U.S. food aid commitments would be met by open market purchases. Production would be controlled in the U.S. by acreage reduction, either because of falling prices if surpluses built up, or by Government action to set aside farm land.

Under Option B, the primary responsibility for food reserves would still rest with importing countries but, the USG would hold stocks for emergency food aid to be provided on a grant basis only. These stocks would be acculumated only as required by the domestic farm price program. Under Option C, USG stocks would be larger and would be available to meet general food aid needs, including on a concessional sale basis. Importing countries would still bear a substantial responsibility for holding their own reserve stocks.

Option D provides for non-designated U.S. stocks which would be built up according to internationally-agreed guidelines for use in covering commercial shortfalls as well as food aid requirements. (Failing agreement on guidelines the USG could build up such non-designated stocks on its own.)

This option would provide for recovery of some portion of the carrying costs when the stocks were sold.

Option E proposes an approach in which an international body would acquire and dispose of stocks on the basis of long-range trends in consumption and supply. Accumulation and maintenance of stocks would be jointly financed by exporters and importers.

In discussing negotiating considerations, the paper points out that most importing countries would favor some form of international supply management approach to world food security, but that exporting countries in the past have not. It also calls attention to the importance the U.S. has attached to negotiating market access along with supply access in the GATT.

The paper further notes that the options are not mutually exclusive, and that several of them contain elements which could be combined in ways other than those suggested.

The extent to which the objective of world food security would be met varies from one option to another:

-- Option A -- Degree of world food reserves build-up cannot be predicted, since it depends entirely on decisions of importing countries;

-- Option B -- Build-up of world food reserves to cover emergency needs would be assured. Beyond this it depends on decisions of importing countries;

-- Option C -- Build-up of world food reserves to cover emergency needs plus U.S. share of other food aid needs would be assured. Beyond this it depends on decisions of importing countries;

-- Option D -- Would probably assure the build-up of world food reserves to cover a substantial portion of likely production shortfalls, based on historical trends;

-- Option E -- Would probably assure build-up of world food reserves to cover a substantial portion of likely production shortfalls, based on historical trends.

As for other U.S. policy objectives, in some cases there is very little difference between the options. Some important differences should be noted however.

-- Regarding the objective of minimizing government intervention in grain markets, Option A would not involve USG intervention in grain markets, since there would be no acquisition or disposal of stocks. The other options would involve some degree of government intervention, the extent of which would vary depending on the size of the stockpile to be accumulated.

-- Regarding the objective of avoiding extreme price fluctuations, Option A would provide no assurance that extreme price fluctuation would be avoided; Option B and C would help to moderate but would not eliminate price fluctuations; Options D and E would tend to minimize price fluctuations.

-- Regarding the objective of responding to humanitarian needs and foreign policy requirements, under Option A only the most compelling needs would be likely to be met in periods of short supply and high prices; under Options B, C, and D there would be greater assurance of U.S. ability to meet humanitarian needs and foreign policy requirements; under Option E, U.S. ability to respond to these needs would be determined by its international undertakings.

Further technical work needs to be done before we can make an assessment of the effect of each of the options for certain other U.S. policy objectives: how burden-sharing is to be implemented; what the cost implications would be of various stocks policy options; and the implications of non-cooperation by the USSR and the PRC, particularly for the use of export controls and licensing.

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U.S. POLICY ON NATIONAL AND INTERNATIONAL STOCKS OF AGRICULTURAL COMMODITIES

CIEP/SM 30

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I. INTRODUCTION

There are a number of purposes for which a U.S. policy on national and international stocks may be needed. These include domestic farm program objectives, domestic consumer interests, food aid and humanitarian obligations, international economic considerations, foreign policy goals, and perhaps others as well. This paper addresses itself primarily to the objective of world food security, although other U.S. policy objectives are also taken into account.

The United States and the international community have economic, political and humanitarian interests in world food security. World food security is defined as that condition in which world production plus reserves are adequate to protect normal consumption requirements (measured either in terms of aggregate demand trends or in terms of per capita needs based on a moving average) against year-to-year variations in production.

Reserve stocks are an important aspect of world food security. They are suited to dealing with the problem of aggregate year-to-year supply variations. Therefore, the basic issue that stocks policy must address is how best to provide against the next bad crop year.

But world food security, and how to provide for it, raises a number of other policy issues, not all of which can be answered in a discussion of U.S. stocks policy. The following are some of the more important related factors the world community must take into account if it is to construct an effective system of minimum world food security for the future.

Changing Purposes of U.S. Stockpiling Policy in Light of World Food Demand Trends

The U.S. approach to world stockpiling requirements will be different in the future from what it has been in the past. Although the United States expects to continue as a major commercial exporter of wheat and feedgrains, it does not intend to accumulate again the enormous surpluses it held in other years. There are several reasons why this is so.

World demand for grain continues to strengthen. Increased national incomes have placed new commercial demands on world production. Over the past several years until 1972, nations have been able to move away from their dependence on food aid as they generate foreign exchange to meet food import requirements--requirements stimulated by personal income growth in developing as well as in industrialized countries. The increased personal incomes have allowed more of the world's people to shift their consumption away from cereal grains and toward animal proteins--beef, pork, poultry, and dairy and poultry products. Production of proteins calls for very heavy use of grain.

Growing worldwide demand for grain has, in turn, prompted a number of basic changes in domestic farm policy, many of the changes being incorporated in the Agricultural Act of 1970. Growing world demand for grain is now making it possible for U.S. farmers to secure more of their income from the market place instead of through Government price support programs. One consequence has been the release of American agriculture from all production restraints, at least for the time being. Another consequence, in this time of high maket prices, has been to free the Government from the need to acquire and hold large commodity inventories, which are the inevitable "by-product of support operations. These new realities are reflected in the Agriculture and Consumer Protection Act of 1973 which moved even further to return decision-making back to the farmers and allow producers to obtain their income from the marketplace.

The huge stocks of other years have been marketed. And under the new laws, the U.S. Government has other options available besides stock-rebuilding to meet domestic farm program objectives. From now on, the principal concern of U.S. farm policy will be to adjust production patterns to meet anticipated U.S. and world needs. Rebuilding of large Government reserves as a consequence of domestic policy requirements is neither desired nor anticipated.

Need for Sharing the Cost of Carrying Grain Reserves

Today the United States believes that the burden of carrying reserves of wheat and feedgrains must be shared among both importing and exporting countries. "Burden sharing" implies that major importing countries wishing to assure themselves of adequate commercial supplies should take certain essential steps either through self-generated or internationally-aided efforts to stock the needed commodities physically, make forward contracts, enter into multi-year supply commitments, or any mix of such programs deemed best suited to their particular needs which would constitute a national stocks policy providing the desired level of national food security.

Insistence on burden sharing is a natural policy objective for the U.S., given the rapid changes in the character of U.S. and world food supply and demand factors described above. For four decades, the United States held most of the reserve wheat and feedgrain supplies required for the world's food system. Sotckholding was a function that served other U.S. farm policy objectives. U.S. domestic price support programs dating back to 1933 were designed principally to maintain farm income while guaranteeing adequate food supplies to U.S. consumers. These price programs stimulated production, which necessitated a dual reserve system--commodity reserves acquired by the Commodity Credit Corporation through its support operations, and the accumulation of excess production capacity in the form of acreage idled under "land bank" programs.

As the size of grain reserve increased, it became apparent that U.S. agriculture's productivity was growing so fast that the release of CCC-held stocks into the domestic market would rarely be necessary. The Congress, therefore, in an effort to reduce the cost of the grain storage program, approved legislation providing for both export promotion of U.S. farm products, and export subsidy payments that would allow U.S. grains to compete in the lower-price world market.

Grain importers, looking at world production prospects, found that world prices reflected the ready availability of U.S. surpluses plus the idled but potential production capacity on U.S. farms. Thus, in effect, U.S. domestic policies aimed at protecting farm income also became instruments for stabilizing world food prices at relatively low levels and for providing a cushion against growing world demand.

Foreign countries benefited from U.S. stockpiling policies. In the mid-Sixties, the United States demonstrated that it richly deserved its reputation as a "reliable supplier" by meeting India's huge emergency requirements for grain. The United States passed an even more severe test in recent months by filling shortfalls in world grain production far larger than those of the mid-Sixties.

But there is no reason from now on why the United States and other grain-producing countries should carry commercial reserves for all the world's potential paying customers. A better approach to world food security will be one in which importing countries themselves take the necessary steps to assure that supplies will be adequate in short crop years. For LDCs, special assistance may be needed to enable them to do this.

Need for Improving Marketing and Information Systems

Any international consideration of world food security requirements should focus as much on distribution and marketing problems as on the absolute quantities of stocks needed. In considering such problems, it should be recognized that the U.S. economic system is based on prices and that the delivery system we have developed is uniquely adapted to function in this economic environment. Our delivery system does not impede the price setting process--it reacts to it, and does so with a high degree of flexibility. Any improvements in the international distribution system should therefore be designed so as to enhance rather than hamper the ability of our delivery system to perform well under constantly changing market conditions.

Finally, an effective world food security system will require a full and free flow of information about supply and demand prospects if destabilizing market fluctuations are to be avoided. No matter how secure a stock cushion is built up, the sudden entry or exit of one or two large purchasers into the market can touch off speculative price swings, impede national production policy development and lead to unsettled trading conditions. Only an effectively operating information system can prevent this problem from developing.

Agreement among nations of the world along the lines indicated above would imply a far-reaching extension of international cooperation. It would place additional, but shared responsibilities, on grain exporting and importing countries alike. It would require procedures for consultation and joint action considerably more elaborate than those we now have.

Need for Price Responsive Production Policies

Any system, to operate properly, must be responsive to changes in supply/demand relationships. The best indication of change is price fluctuation. Price fluctuations are the most prompt and reliable indicators of supply requirements. The existence of large surplus stocks can have a price dampening effect, with the consequence that price is no longer as reliable an indicator of change as it would be without surplus. With the role of price moderated, the production response is likely to be slower and may not adjust to the extent required.

National production policy reaction to changing market conditions is then both more timely and based upon true market and demand situations.

The cornerstone of future policy, therefore, should be production adjustments dictated by anticipated market needs. Market needs can and do include amounts used for nearby consumption, plus any purchased to build up stocks.

There is considerable current debate over whether the role of government, at least of the U.S. Government, should be one of non-interference in the market or one of supply management. The U.S. in particular and some other agricultural exporters to a lesser extent have generally preferred to emphasize the role of the free market in determining how agricultural resources are to be allocated. As efficient producers, they do this largely in their own self-interest, although in times of competitive prices, this has at times in the past put the U.S. in the position of residual supplier. In times of scarcities, competition lessens and sometimes disappears, but efficient producers nevertheless benefit by higher margins of profit and--in cases such as the U.S. where production can be controlled--by increased sales measured on a quantity basis. This had led, in the case of the U.S., to a position which generally does not favor active intervention of the government in the market.

Even for efficient producers, however, the picture is not entirely one-sided. An active government role in agriculture--including participation in an international world food security agreement involving reserves--is favored by some producers in order to guard against the danger of unreasonably low prices to farmers in times of surpluses, and by some consumers in order to guard against unreasonably high prices in times of scarcity. These governments are aware that agriculture is only one part of the entire economy and that domestic consumers and producers of food may put strong pressure on governments to take measures to influence food prices through direct intervention on the market. Also, to the extent that food aid and disaster relief require an active government role, there are pressures from groups motivated by humanitarian considerations to encourage government stockpiling efforts (although it should be noted that depending upon the amounts involved, this could be handled by government purchases in the market rather than government acquisition of reserves). Finally, there are elements in many exporting countries who favor government intervention because the stability which they believe will accompany it will better achieve the goals agreed on by all--increased exports, farm income and investment.

The need for price-responsive production policies would seem to point to a market-oriented stocks policy. If there is a felt need by countries to carry larger stocks, this need will be reflected in market demand for commodities until such time as countries are satisfied with the level of their stocks. Under this approach, there would be no need to establish stock targets independently of what the market showed the stock requirement to be in any given year. Nor would there be any need for the U.S. Government to hold stocks at all, since users--both domestic and foreign--would build up and carry stocks at whatever level they determined necessary to secure themselves against short crop years.

But a supply management approach would give the government greater control over whatever stocks were built up, and could therefore be used as a more effective instrument for cushioning/temporarily the domestic and international price effects of short crop years than the free market. It is also an approach which might have appeal if the government wished to use stocks for foreign policy reasons.

It is the conclusion of this paper that both approaches could serve the broad purpose of world food security effectively, but that the balance of merits and demerits in relation to other purposes of a U.S. stocks policy will differ, depending on which is selected.

Public and Congressional Attitudes on Stockpiling

As the tight supply situation in food began to become evident in late 1972, supporters of stockpiling began increasing, particularly those who favored action on the international side. Thus Lester Brown and others predicting serious food shortages during the coming decade urged and continue to urge the creation of a World Food Bank. Senator Humphrey (on behalf of himself and eight other Senators) has also re-introduced legislation in the current session of Congress which would require the CCC to establish a domestic reserve of major food- and feedgrains.

As long as domestic grain and soybean prices remain high, however, there will continue to be substantial opposition from most domestic farm groups to the establishment of a domestic stockpile; their reasoning is that such a policy of accumulating U.S. Government stocks would have a depressing effect on prices received by farmers. However, these same interests would probably favor reserves accumulation if surpluses built up and prices fell.

A current reading of the prospects for passage by the Congress of the Humphrey proposal or something similar suggests that they are unlikely at this time. Most of the members of the Senate Agriculture Committee are opposed to the concept of stockpiling, and the mood in the Senate and the House as a whole seems not to have changed substantially since last year when Humphrey's proposal was defeated on the floor by a vote on the proportion of 3 to 1.

Some opposition to the Humphrey proposal comes from U.S. consumer representatives who are concerned that building of stockpiles might force food prices even further upward in the short term. However, other consumer groups, and certain urban congressmen attuned to them, nevertheless have favored the establishment of a stockpiling policy including the gradual accumulation of reserves to be used later in times of shortages to keep prices from increasing too rapidly. There are also members of the Congress and public opinion groups which have traditionally favored international programs by the U.S. for humanitarian purposes, and many of these are on record as favoring U.S. contributions to an international food aid reserve.

Since the prospects for action by the Congress on stockpiling legislation are small, the Administration probably can chart its own course on the issue of U.S. stockpiling, despite the mixed public reaction.

II. WORLD STOCKPILING REQUIREMENTS

World stockpiling requirements are determined by two factors

(1) variations in production and

(2) the extent to which these variations are covered by imports.

Production

Most of the recent severe fluctuations in production shortfalls have come in centrally planned countries. (See figure 1). Grain production in the Soviet Union has been very erratic, with sizeable shortfalls occuring in 1963, 1965, and 1972. The deviations from trend for Soviet grain production are shown in Table 1.

Table 1--Soviet grain production

Year	Actual production	Trend 1960-1972	Deviation from trend
	Million metric tons		
1960	125.5	120.8	+ 4.7
1961	130.8	125.8	+ 5.0
1962	140.2	130.9	+ 9.3
1963	107.5	135.9	-28.4
1964	152.1	140.9	+11.2
1965	121.1	146.0	-24.9
1966	171.2	151.1	+20.1
1967	147.9	156.1	- 8.2
1968	169.5	161.2	+ 8.3
1969	162.4	166.3	- 3.9
1970	186.8	171.3	+15.5
1971	181.2	176.4	+ 4.8
1972	168.0	181.4	-13.4

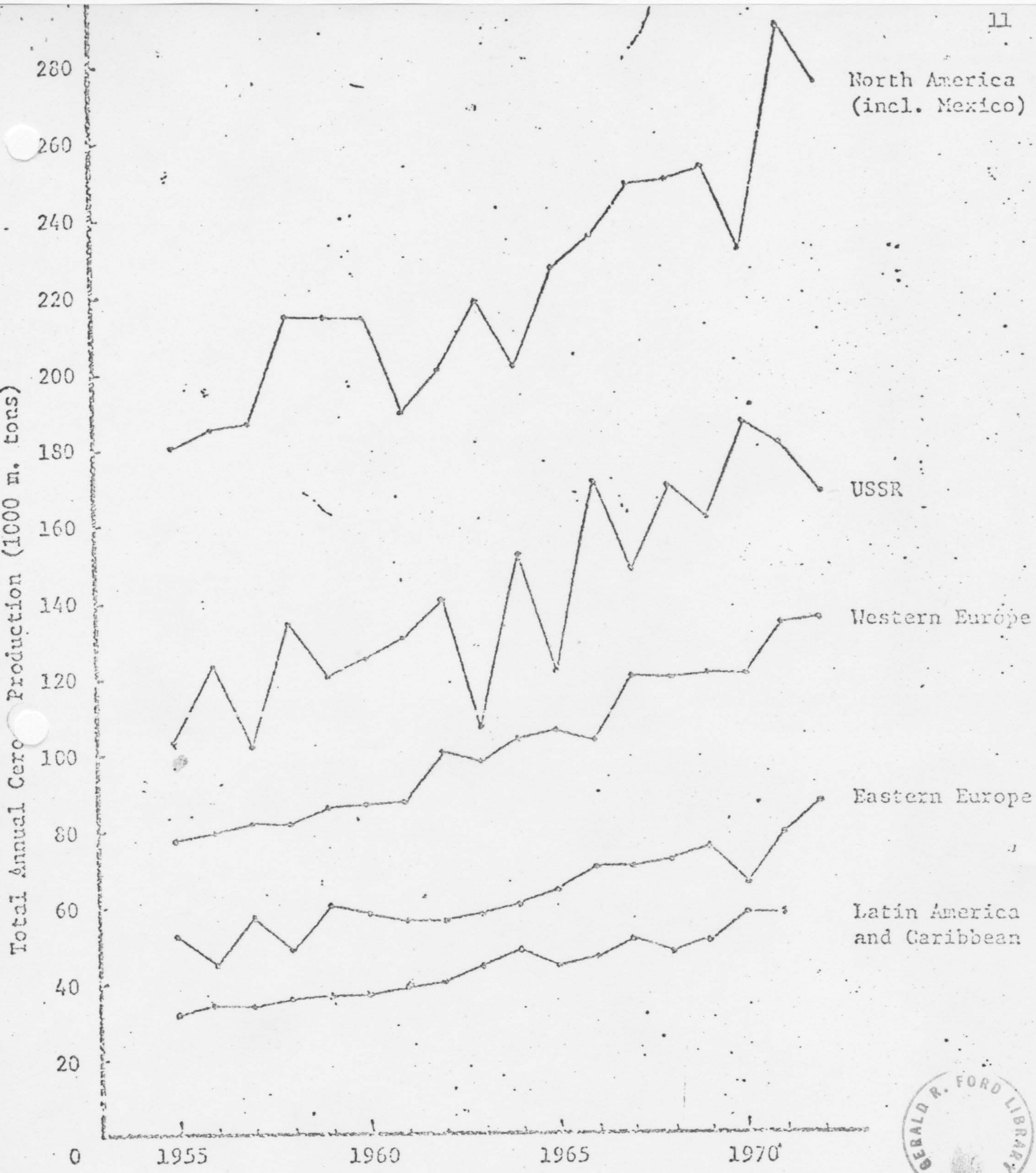

Figure 1. Cereal Production in Major Regions of the World, 1955 to 1972.

Source: Martin E. Abel, "World Food Distribution Policies," paper presented at the seminar on World Food Perspectives, Rockfeller and Ford Foundations, New York, December 1973.

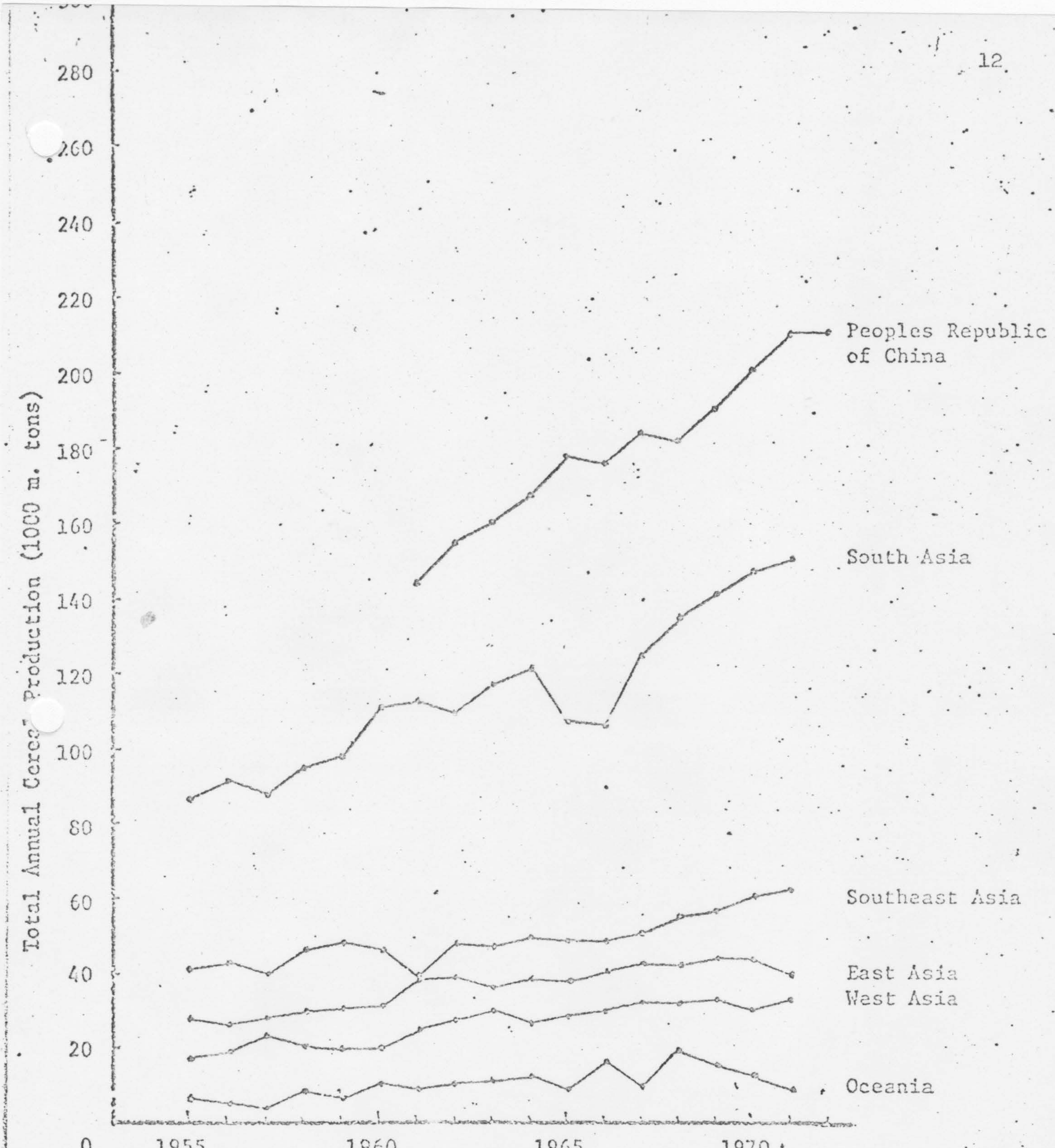

Figure 1. (continued)

India in the mid-Sixties also experienced a severe shortfall in production, although it subsequently achieved some stability until the 1972 shortfall in production.

North America has experienced rather dramatic fluctuations in total production. Part of the variation is due to weather, however, it is mainly a result of governmental planning, particularly production adjustments to meet developments in export markets. An analysis of the variation in wheat yields in the U.S. since 1950 indicates a maximum yield shortfall of 6.2 percent from trend attributable purely to weather.

In some instances the shortfalls in other countries have coincided with shortfalls in the U.S. But in 1963, 1965, and 1972 the years of the largest shortfalls abroad, the U.S. had nearly full production.

Imports

An examination of world import demand by regions reveals that about one-third of world import demand for wheat is accounted for by Western Europe and Japan and about one-half by the less developed countries. U.S. production has in the past met its share of these requirements with few problems. However, when the sporadic needs of the Central Plan countries are aggregated into total world demand, supply shortfalls have occured. Therefore, in terms of world stockpiling requirements, three categories of demand must be accounted for:

(a) Regular or commercial purchases by developed countries

(b) Regular or commercial purchases and emergency relief for less developed countries, and

(c) Occasional commercial purchases by centrally planned countries.

The regular commercial customers of the U.S. -- essentially the developed world -- do not vary greatly in the year-to-year import demands upon the United States. Their imports of U.S. wheat shows an absence of fluctuations and a slow but steady growth in demand.

The less developed countries, South Asia excluded, have exhibited a more rapid growth trend in import demand, primarily because of the higher income elasticity of demand but also a noticeable fluctuation in demand around the long term.

In contrast to the other LDC's as a group, South Asia has exhibited little or no trend growth in demand despite the large imports in 1965-68 resulting from extensive and prolonged droughts and the subsequent reduction in imports because of the Green Revolution. Like South Asia, the People's Republic of China and Eastern Europe have exhibited zero or negative growth trends but definite year-to-year fluctuations in import demand. As for the USSR, its import demand consists primarily of large fluctuations in imports in 1964,1966, and 1973, years of crop shortfalls.

The regions contributing most of the 1963-1974 growth in world wheat imports were the developed countries (36 percent) and the less developed countries (64 percent). On the other hand, the Central Plan countries contributed practically nothing to the trend growth. The question arises about their contribution to the fluctuations in import demand.

Preliminary analysis indicates that over 90 percent of the deviation from trend in world import demand for wheat since fiscal year 1963 can be attributed to the changing imports of the Soviet Union, Eastern Europe, and the People's Republic of China. (Figure 2 shows how production shortfalls are translated into the world wheat market).

Grain Equivalents: Fiscal Years
1963 thru 1974

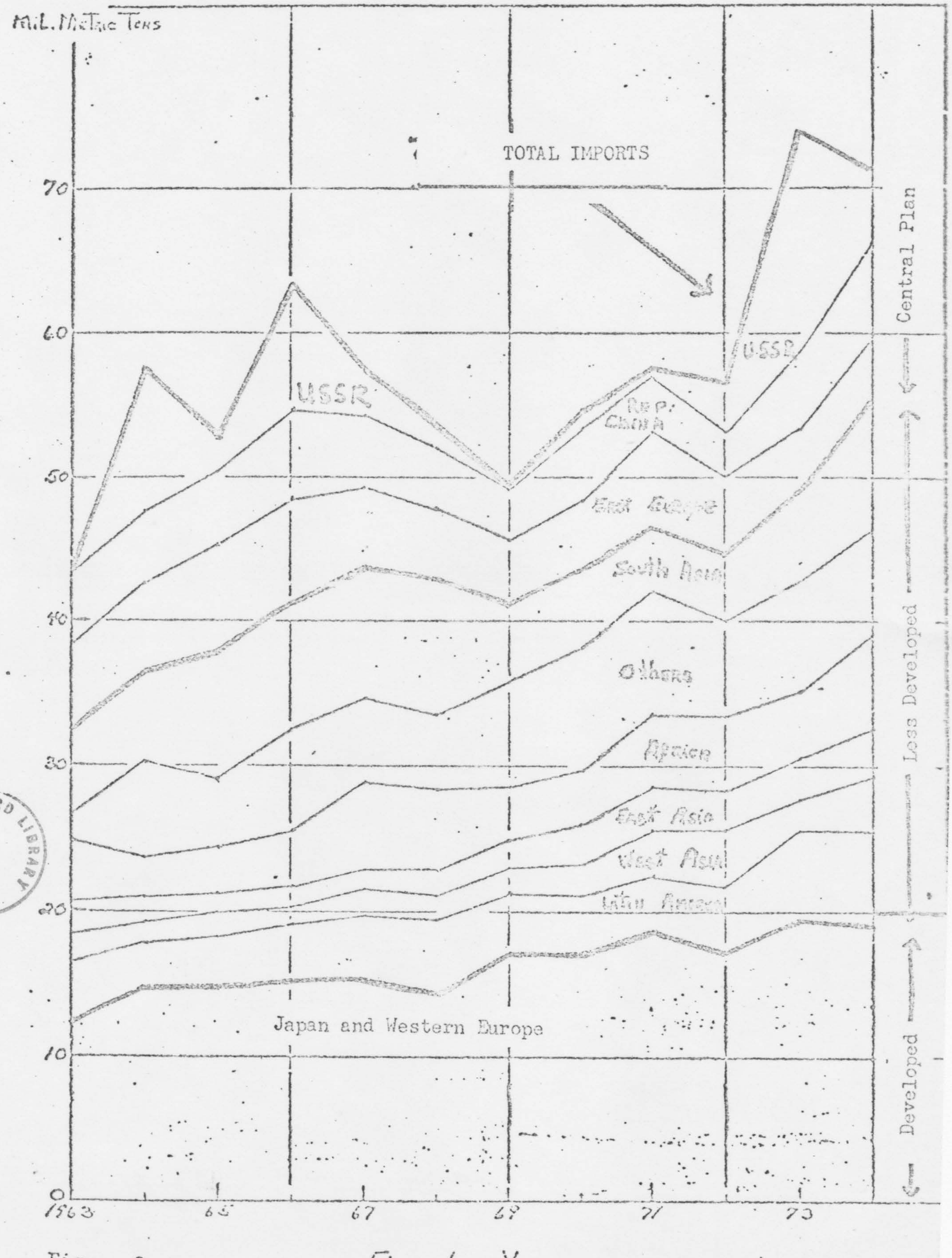

Figure 2

The impact of this fluctuating import demand upon wheat exports of world exporters, especially the U.S. and Canada, has accounted for a major proportion of the fluctuations in world wheat exports since FY-1963, primarily because they carried over large grain stocks. These fluctuations in exports were directly related to the fluctuations in import demand that resulted from shortfalls in grain production in the Soviet Union, East Europe, People's Republic of China, and India.

The Central Plan countries were responsible for 93 percent of the deviation about the trend of world wheat imports between 1963-1974. The USSR alone was responsible for 80 percent of the fluctuation in world wheat imports during this period. It is clear from this analysis that the world market for wheat would be a rather stable and slowly growing one if the import demand of the Central Plan countries were excluded. While somewhat erratic, the individual and combined exports of West Europe, East Europe, USSR, Argentina, and Australia have tended upwards in response to this steadily increasing demand. However, the United States and Canada account for most of the fluctuation in world wheat exports since 1963, primarily because of their reserve grain stocks.

The fluctuation in U.S. exports accounts for 83 percent of the fluctuation in world exports. Canada and the U.S. together accounted for 92 percent. These fluctuations in exports were directly related to the fluctuations in import demand that grew out of crop shortfalls in USSR, China, East Europe, and South Asia. In other words, the U.S. and Canada have supplied largely from their reserve stocks, most of the increased requirements resulting from crop shortfalls in these areas.

These analyses suggest that the major factors affecting the price of wheat have been: (1) the level of stocks in the U.S. and Canada and

(2) fluctuation of supplies and consequently of import demand in the rest of the world, especially the Central Plan countries.

In summary, these data suggest both a trend growth in world import demand for wheat, attributable to income growth, and a large fluctuation in import demand, attributable to fluctuations in supply, i.e. a large residual demand component centered especially in the Central Plan or Communist countries.

Stock Levels

We have attempted to ascertain how much of the "world" (excluding the U.S.) and the U.S. net shortfalls in grain production could be met by various levels of grain reserve stocks. A shortfall is defined as the amount by which production for the year is below trend. Data are for the 1950-69 period. We assume that world deviations on the plus side would be consumed in place and not used to offset a U.S. shortfall nor stored and carried over. The deviations in total grain production from trend in million metric tons were as follows:

Year	World	U.S.	Year	World	U.S.
1950	- 7.4	8.2	1960	2.2	16.6
1951	- 2.6	- 4.0	1961	-11.1	- 7.0
1952	17.2	6.2	1962	- 1.3	-10.5
1953	10.9	- 3.7	1963	-21.0	- 2.2
1954	- 8.6	- 7.0	1964	2.7	-20.2
1955	1.0	- 6.3	1965	-30.8	- 2.0
1956	11.5	-10.2	1966	6.9	- 5.9
1957	- 8.9	- 2.7	1967	- 6.0	12.7
1958	9.8	16.8	1968	7.4	4.1
1959	.5	8.4	1969	6.5	1.9

In 7 of the 20 years, total grain production was below trend in both the world (excluding the U.S.) and the U.S. In 6 years, grain production was above trend in both the world and the U.S. In 5 years, production was above trend in the world, but below trend in the U.S.

The sum of the negative deviations in the above data are 179.4 million tons, of which 97.7 million are world, and 81.7 million are U.S., the latter due chiefly to adjustments in production.

A world grain reserve equivalent to 8 percent of U.S. grain production would have met 142.5 million tons of the total 179.4 million ton shortfall over the period. The shortfall tonnage not met would have been in the years 1957, 1963, 1964, and 1975. A world grain reserve equivalent to 10 percent of U.S. grain production would have met 162.4 million tons of the 179.4 million ton shortfall. A world grain reserve equivalent to 12 percent of U.S. grain production would have met 170.4 million tons of the 179.4 million ton shortfall. The shortfall tonnage not fully met would have occurred in 1963 and 1965.

A world grain reserve equal to about 15 percent production of U.S. grain would have met most, but not all of the production shortfalls over the period. Based on the 1973/74 marketing year, such a formula would call for a reserve of about 300 million bushels of wheat and nearly 1,200 million bushels of feedgrains.

Reserves of this size compare with U.S. carry-in stocks (Government-owned inventories plus "free" stocks) on June 30, 1972 of 863 million bushels of wheat and 1,984 million bushels of feedgrains. However, average "free" stock carry-out in the U.S. for the five-year period from 1967-68 through 1971-72 totaled only 175 million bushels of wheat and 719 million bushels of feedgrains. If the U.S. were to hold all of the world's reserve requirements at a 15% target level an additional 125 million bushels of wheat and 481 million bushels of feedgrains on average would have to be carried. At 1973 values, CCC interest costs, storage, and other charges--not including acquisition--would be about $223 million annually.

It would have required a world grain reserve equivalent to about 17 percent of U.S. grain production to have met the total shortfall of 32.8 million tons in 1965. In other words, the reserve would have had to be nearly 50 percent larger than the 12 percent level and at a considerable increase in cost to meet the contingency of the one most extreme year in 20.

A reserve stock level sufficient to meet (say) three-fourths of the expected annual world shortfalls in their entirety, would also meet a substantial portion of the shortfall tonnage of the larger, less frequent shortfalls in production. At such times, some grain users would have to get along with somewhat less grain than they would like to have. Nevertheless, the reserve stock would reduce the severity of the reduction in supplies and soften the rise in market prices.

Expressed in terms of historical global import demand for wheat, the maximum variation in a given year has been 15 million metric tons. A stock level equivalent to this variation would have been sufficient to meet 100 percent of above trend demand resulting from production shortfalls.

On a regional basis, the maximum variation in any given year has been 2 million metric tons in the developed countries, 9 million metric tons in the less developed countries, and 15 million metric tons in the central plan countries.

Aggregating the regional totals gives a figure in excess of the historical global import demand maximum, since the shortfalls have not occurred at the same time or to the same extent around the world. Therefore, a global stock level of 26 million metric tons, equivalent to the sum of the regional above trend variations, would not be needed unless each region were to attempt to cover the entirety of its own potential shortfall. Assuming (a) that all regions were participating fully in an international stockpiling program, (b) that each region bore a responsibility proportionate to its probable call on total reserves over time, and (c) that all reserves wherever held were fully available to whatever region was experiencing above trend demand in a given year, the stock burden by region would be 1.14 million metric tons for the developed countries, 5.1 million metric tons for the less developed countries, and 9.0 million metric tons for the central plan countries.

Recognizing that under such a system the cost of burden sharing for LDCs would be greater than they could bear without aid, and that the sum total of reserves to be carried by the LDCs would be larger if each country covered its own weather risks in entirety than if the exporters covered the risks of the LDCs as a group, some adjustment mechanism would have to be developed. Various possibilities addressed to the issue of stock carrying mechanisms are outlined in the options which follow.

III. STOCKPILING OPTIONS

Two basic considerations for a U.S. approach to world food security are whether that approach should be unilateral, bilateral, or multilateral, and whether or not the approach should involve U.S. Government stocks. Stocks may or may not be a feature depending upon the objectives and contingencies to be insured against, the extent to which variation in demand can be met by production adjustments and the manner in which each of the three regional demand categories is to be handled.

Unilateral Stocks Policy

A unilateral stocks policy without USG stocks would have many of the same features as Option A (see below). The United States would unilaterally examine the trends and variability in world grain production; assess on its own the production, stockpile, and food aid policies of major importing and exporting countries; and decide for itself what policies to adopt and what commitments to undertake.

A unilateral stocks policy with U.S. Government stocks would involve a return to the kind of stockpiling system the world has relied on for the past 25 years, wherein the United States and Canada have carried the bulk of the world's grain reserves through the operation of their domestic price support programs. For the United States, a return to this system would entail returning to a policy of CCC-stock acquisition for resale on the commercial market when needed. Acquisition of these stocks would be dictated by the needs of domestic support programs. This could entail either open market purchases by the CCC or acquisition of stocks through the loan program, depending on cost factors.

A unilateral USG stocks policy need not lead to the sizeable reserves build-up of past years, however. The U.S. could unilaterally decide what its objectives and commitments are and set a target level of reserves that would meet only these commitments. Surplus stocks would not have to be built up. The requirement that the U.S. maintain a grain reserve of up to 75 million bushels to meet domestic emergency requirements represents one such target already contained in the law.

The United States would have to run its program primarily on the basis of domestic policy considerations, although account would be taken of the probable level of worldwide commercial and food aid requirements in arriving at production and support policy decisions. P.L. 480 programs could continue to be operated much as they have been in the past, with sales and grants being made contingent largely on the availability of supplies. In addition, there would be nothing to prevent the United States from making expanded commitments to existing international food aid programs.

There have been a number of legislative proposals for the creation of domestic food reserves which would be compatible with a unilateral stocks policy. However, such an approach would clearly entail export licensing and export controls whenever supplies were short.

<u>Pros</u>

1. Does not depend on negotiations or cumbersome agreements to put into effect.
2. Would not require international regulations which could curb the market.
3. Should maximize USG and private grain trade discretion in the world market.
4. Could be managed so as to give the Government another tool in addition to set-asides to keep prices above support levels.

5. Could be managed so as to provide immediate access to large reserves in case extraordinary needs developed, as in 1972 and 1973.

Cons

1. Without stocks, would interfere with commercial market operations if export licensing and/or export controls became necessary.
2. With stocks, would make the farmer reliant on the Government as buyer of last resort, thereby reducing the responsiveness of the production system to world demand.
3. Without international cooperation could result either in inadequate production and insufficient global stocks build-up to cover short crop years; or in very heavy costs for the U.S. to carry sufficient reserve stocks for the entire world.

Bilateral or Limited Multilateral Stocks Agreement

A bilateral approach to world food security could take two different forms. One would involve agreement among major exporters to consult and exchange information so as to avoid being played off against each other by a single large purchaser such as the USSR entering the market unexpectedly. Additionally, they might want to consider agreeing on the rate at which each would reduce its stocks during a marketing year. However, this would require export licensing.

The other form would involve bilateral arrangements between the U.S. and major importing countries, including stockpile commitments, food aid commitments, multi-year purchase commitments, and other similar mechanisms designed to fix the level of import demand with more certainty and permit production to be adjusted accordingly.

Under this approach it would be assumed that a fully effective international information system could not be achieved and that countries would not be able to act cooperatively to assure global world food security at any given target level. The U.S. would follow one of the two types of unilateral policies discussed above, modified as necessary to fit its bilateral commitments.

Pros

1. In absence of full international agreement would increase ability to manage demand through bilateral agreements among major trading partners.
2. Would reduce the market uncertainty stemming from lack of production and import requirement information.
3. Could reduce the size of reserves to be held in the U.S.
4. Could limit the cost of a stockpiling program to the USG.

Cons

1. Could be viewed as a producers cartel.
2. Could lead to a proliferation of criss-crossing bilateral arrangements, contrary to general thrust of U.S. trade policy.
3. Would necessitate some type of USG presence in the grain trade in order to faciltate agreements, which action would reverse the present direction of Administration policy.
4. Would be difficult to find agreement on unified policy among exporting countries.
5. Would require permanent export licensing system which would be incompatible with USG policy.

Multilateral/International Stocks Agreement

With No USG-Held Stocks: The objectives of an international approach to stockpiling which did not entail USG stocks would include: world food security; sharing of the burden of carrying commercial reserves; improvement in marketing and distribution techniques; an effective information system; and production adjustments based on market needs as reflected by prices and forward contracts.

There are two major routes open to accomplish these broad objectives. (1) One is based upon no set-aside or production restraints and no extended loan program. Production adjustments would be determined largely by market forces, although target price guarantees might provide a degree of incentive that lessens production response dictated by market prices. (2) The other is based upon USDA exercising production restraints through operation of set-aside during periods when likely production will exceed that which the world's buyers are likely to take.

Option A - Alternative 1: Free Market Approach

1. No government program to regulate production.
2. Open production.
3. Private U.S. stocks, rather than Commodity Credit Corporation inventories.
4. Forward contracting.
5. National stocks in importing countries.
6. International food aid commitments met through open market purchases.

The cornerstone of this option is that producers would make the decision as to what and how much to plant. No acreage set-aside would be implemented. In time of excess productive capacity in the world, the disincentive of lower market prices would act as a restraint on how much acreage would be planted to any individual commodity. While producing for market, income protection would be provided by target price guarantees and non-recourse loans. Users throughout the world would have to provide, primarily through price, an incentive great enough to attract needed production. The absence of extended loans would act as a further disincentive to production in excess of what the market is willing to buy.

Pros

1. Consistent with a truly market-oriented approach.
2. Minimizes governmental interference in the decision-making process.
3. Enables farmers to derive their income from the market.
4. Would encourage importing countries to formulate and implement positive stock policies.
5. Is less expensive than programs which emphasize build up of Government stocks.

Cons

1. Would subject producers and consumers to price uncertainty.
2. No real policy option to deal with countries not implementing a national stocks policy.
3. Increased cost for food aid in times of short supply, or risk of inadequate supplies to meet production shortfalls.
4. Could lead to large surpluses and political pressure for Government stockpiling.
5. Income deficiency payments could be costly.

Option A - Alternative 2: Supply Management Approach

1. Open production for the time being, with implementation of planting restrictions in the form of set-aside whenever supply availability in exporting countries is clearly going to exceed projected needs.
2. Reliance on firm commitments by users (forward contracts, multi-year commitments, etc.) plus forward prices as indicators of projected needs.
3. Consultations with buyers before implementation of set-aside.
4. Private U.S. stocks, supplemented by modified extended loan program.
5. International food aid commitments met through open market purchases.

Private stocks in the U.S. can go far toward meeting the quantities necessary to cover the commercial requirements of domestic consumers and importing nations. The United States can and does, through the private trade and the extended loan program, hold stocks in excess of quantities needed to fill normal pipeline requirements. The Government would in addition, continue to maintain a 75 million bushel emergency stockpile.

If additional supply stability in the United States is deemed necessary, expanded stock-carrying capacity can be obtained through modification of the extended loan (reseal) program to increase its attractiveness to farmers. As the program has been administered in recent years, CCC makes storage payments to farmers who are not yet ready to market their products. The program tends to concentrate stocks in the hands of producers who have the option of repaying the loan at any time and selling to meet market demand.

This program could be modified, however, to provide a premium to producers electing to reseal stocks for a fixed minimum period. Producers would forego the right of redemption within that period unless the Government decides that conditions warrant an early redemption opportunity. This reseal alternative is similar to the certificates of deposit issued by banks that pay the highest interest rates on deposits committed for a relatively long period. It has two attractive features for national stockpiling policy. First, it offers farmers a financial incentive to continue carrying stocks during a period of falling prices when they might otherwise be tempted to sell. Second, it gives Government a degree of control over the release of "resealed" stocks which would otherwise be absent from the system.

Under this alternative every importing country would be free to decide for itself whether it wanted to keep stocks at, above, or below the target level necessary for its own food security. Each country would decide for itself the form in which reserves would be carried -- forward contracts or nationally owned stocks. But, in the absence of U.S.-held stocks on which they have relied as a cushion in the past, many importing countries would undoubtedly see the wisdom of adopting national stockpiling policies.

Long-term supply contracts for more than one marketing year ahead could play a significant role in assuring increased burden sharing by importing countries. Forward contracts of private U.S. companies could, if used extensively, make for improved production planning and lead to increased market stability.

The forward contract would likely contain two essential components: (1) maximum/minimum quantity figures, with the absolute quantity within the range up to the buyer; and (2) a deferred price-fixing procedure, probably keyed to annual futures prices, and sufficiently well-defined to make the agreement a binding contract. The deferred price feature would be aimed at overcoming the reluctance of either buyers or sellers to gamble by forward contracting at fixed prices.

Pros

1. Would be market-oriented, maintaining income guarantee features through operation of set-aside.
2. Would encourage formation of private stocks through the use of the extended loan program.
3. Would provide for coordination with importing countries, yet allow them to decide what stock levels they should carry and in what form (forward contracts or nationally owned stocks).
4. Would eliminate the necessity of fixing quantitiative stock targets.

Cons

1. Risk of having insufficient reserves to meet all contingencies.
2. International coordination and cooperation will be difficult.
3. Government control of production policy might not be sufficient to prevent surpluses and price declines below target levels.

With USG-Held Stocks:

A second class of options for an international food reserve system would include some level of USG stocks, in addition, to or in combination with, private stocks. While sharing the same food security objectives as a system not incorporating USG stocks, such a system would require that the exporting countries assume a greater share of the burden of carrying reserves for emergency or other purposes. There are several variants of this class of options. They differ primarily in the level of the USG stock commitment and its relation to global food reserve requirements, and secondarily in the degree to which international commitments would dictate national stocks programs.

Option B: Emergency Food Aid Stocks

1. Open production (production at full capacity), at least for the time being.
2. Private U.S. commercial stocks, rather than Commodity Credit Corporation inventories, to meet commercial needs.
3. Moderate CCC stocks, accumulated by the CCC should grain prices approach support levels, for use only in meeting emergency food aid needs on a donation basis.
4. Forward contracting.
5. National stocks in importing countries.

An international approach incorporating USG stocks could be formulated in a manner identical with Option A, except for the accumulation of moderate CCC stocks to meet emergency food aid requirements.

Under this option the U.S. could make an emergency stock commitment in one of two ways. The U.S. could agree simply that if Option A were tried and if set-aside and/or price disincentives were not enough to prevent prices from falling to loan levels, any stocks acquired by the CCC would be designated for emergency food aid use only, with cash sale release prohibited.

Alternatively, the U.S. could agree to build up an emergency stock which, in combination with emergency stock commitments by other exporting countries, would be sufficient to cover the emergency portion of the developing countries' reserves requirement. Acquisition would begin when prices fell near enough toward farm income support targets that set-aside had to be considered. Acquisition would be limited primarily to wheat. However, some open-market purchases of fortified and blended foods and of rice and corn would also be needed for infant feeding and for non-wheat-eating peoples. This option assumes that importing countries (including centrally-planned economies) would take the responsibility for carrying their own commercial reserves, and that special credits would be made available to developing countries to enable them to develop their own stocks programs to cover non-emergency food needs from year to year. U.S. food aid commitments of a non-emergency nature would continue to be met by open market purchases as needed.

Stocks accumulated by the United States under such a program would be designated for disposal only to meet emergency food aid needs and would thus not be available for eventual release in the commercial market. CCC could further be required to make open market purchases in preference to using stocks to meet emergency food aid commitments except when world price levels and carryover indicated that supplies were scarce.

Under certain conditions, the acquisition of moderate commodity stocks could serve the useful function of "buying time" for policy makers. (Such a situation might prevail should forward prices fall to a point justifying acreage set-asides, a program that cannot be implemented speedily.)

Pros

1. Would establish a contingency stock specifically designated for emergency food aid.
2. Would limit government management of production to set-aside and CCC emergency reserve, thereby leaving producers largely reliant on market for income.
3. Would give the United States more lead time to introduce effective production control measures if other countries fail to build up commercial stockpiles, or engage in forward contracting, and prices begin to fall toward target levels.
4. Would provide for the acquisition of emergency stocks as a first priority as soon as market conditions warranted the rebuilding of wheat reserves.
5. Acquisition of commodities -- <u>but only for emergency food aid requirements</u> -- could well cushion the effects of a price decline without undue disturbance to the <u>commercial</u> system.

Cons

1. Would not be true international food aid commitment since program would operate only as a consequence of domestic production policy, though emergency food aid requirements could be included in production policy.
2. Would not necessarily cover all world food security requirements in short crop years.

3. Would not provide for acquisition of surpluses if they built up beyond level designated as U.S. emergency food aid commitment.
4. Could result in stocks being held even in times of high prices because no true emergency situation developed.

Option C: General Food Aid Stocks

1. Open production (production at full capacity), at least for the time being.
2. Private U.S. commercial stocks, rather than Commodity Credit Corporation inventories, to meet commercial needs.
3. CCC stocks at a level sufficient to meet all U.S. food aid commitments even in bad crop years.
4. National stocks in importing countries.
5. International food aid commitment made on an annual crop basis.

This option would entail a potentially larger USG stockpile than option B (how much larger would depend on the extent to which other countries also held stocks to cover fluctuations in developing country demands). It would involve disposal of stocks through concessional sale to developing countries who might not otherwise make the purchases at all, as well as food aid grants.

Under this option, the U.S. would make a stock commitment bearing a relation to internationally-determined feed aid target levels. The commitment to build up and maintain stocks to cover LDC food aid requirements would be carried out by CCC purchases whenever the U.S. concluded that market conditions were right. Similarly, stocks would be released into the market whenever price increases indicated that the demand pressures for which stocks were created required it.

Pros

1. Would enable U.S. to cover annual food aid commitments at a consistent level from year to year.
2. Would probably increase LDC import demand thus ensuring greater U.S. export market.

3. Through larger U.S. export markets would permit continued maximum U.S. production.

Cons

1. Requirement that stocks be used only for emergency food aid grants and concessional sales to developing countries would be difficult to maintain and administer and might require an export licensing system.
2. If there were an increase in developing country import demand for food because of production shortfalls in a given year, not all the short fall would be met by concessional sales out of stocks, and there would still be upward pressure on prices.
3. If concessional food aid were consistently available, a good many developing countries might fail to take the measures necessary to assure their own food security over time.
4. Unless there were international agreement among all countries holding food aid stocks, the release policies pursued by some could thwart legitimate domestic farm policy objectives of others.

Option D: Non-designated Stocks--Alternative 1: Target-Level Stocks Agreement

1. International agreement on quantitative national stock targets for all participating countries.
2. One production (production at full capacity), at least for the time being.
3. Forward contracting.

4. CCC-held stocks in the United States, but limited to quantities necessary to bring total U.S. reserves up to an internationally-agreed target.
5. Nationally-owned stocks in other countries in accordance with internationally-agreed targets.
6. Sales to importing countries from CCC stocks at prices that would recapture the cost of carrying the reserves.

Farmers would produce, at least for the time being, at full capacity to meet expanding world needs.

Forward contracting would be encouraged.

Private U.S. stocks would be supplemented by moderate "export reserves" accumulated by the CCC should prices approach the support level. Accumulation at such junctures would give the Government some lead time to introduce production controls before prices fell all the way to the loan rates.

Accumulation of such reserves would not be, per se, for purposes of price stabilization. Accumulation--not through the takeover of loan collateral but through open market purchases when prices are falling rather than rising--would enable the Government to build its export reserves to desired levels at relatively moderate cost. But such purchases, of course, would have the incidental but important effect of stabilizing prices to a degree.

A world food reserves target would be agreed internationally by producing and consuming countries together. National stock targets would be determined first by assessing the desirable reserve level for each country and then by determining how much of that could feasibly be carried by the country itself. Stock targets for producing countries such as the U.S., Canada, and Australia would be set so as to help cover the difference between what is desirable and what is feasible for countries with high reserve requirements and low capacity such as India and Sahel. In combination, the national stock targets would be fixed so as to equal the global target. The quantities held by CCC would supplement private stocks by a volume necessary to bring total U.S. reserves to the agreed target level.

Except for those required to meet food aid commitments, sales from CCC stocks would be made at prices that would recapture from foreign buyers the cost of acquiring the grain, plus storage and other carrying charges. Initiation of such a pricing policy on reserve stocks could well encourage decisions by importing countries to build up their own national reserves.

Pros

1. Would provide USG with capacity to respond flexibly to extraordinary export requirements.
2. The existence of stocks in other countries would also help moderate extreme price fluctuations and assure stability of supply in short crop years.
3. Would enable U.S. to recapture some of the costs of carrying reserves.

Cons

1. Would be difficult to provide for efficient distribution of stocks if stocks were widely dispersed.
2. Global reserve level might have to be higher if stocks were widely dispersed.
3. Large global stocks could be price-depressing, particularly as their wide depersal would increase danger of premature release.
4. Could be costly.

Option D: Non-Designated Stocks -- Alternative 2: Target-Price Acquisition/Release Agreement

1. International agreement on when and how to acquire and dispose of stocks.
2. Open production (production at full capacity), at least for the time being.
3. Forward contracting.
4. CCC-held stocks in the United States, acquired and released according to internationally-agreed guidelines.
5. Nationally-owned stocks in other countries in accordance with internationally-agreed guidelines.
6. Sales to importing countries from CCC stocks at prices that would recapture the cost of carrying the reserves.

Instead of being linked to domestic farm program considerations, or to internationally-agreed stock target levels, CCC stock acquisition under this option would occur according to a set of internationally-agreed guidelines, probably expressed in terms of prices. The principal difference between this alternative and alternative 1 would be that international agreement on quantitative stock target levels would be downplayed while international guidelines as to when and how to acquire and dispose of stocks would be emphasized.

The price mechanism could be fine tuned so as to respond to price trends in the U.S. futures market, rather than being fixed absolutely. International consultations would be needed in order to harmonize actions, depending on the general assessment of the situation. If price ranges were used, they would have to be adjusted periodically to reflect inflation, exchange rate changes and other factors.

Pros

1. Such an agreement would help encourage consumer countries to increase stocks as prices fall and thus help support U.S. farm incomes and our balance of payments when most needed.
2. International guidelines would encourage reduction of consumer stocks in times of high prices, thereby helping to moderate the increase in prices, including prices to U.S. consumers.
3. Such an agreement would provide U.S. farmers we well as farmers in other countries with some guidance for long-term planning decisions. At the same time the wide ranges and the substantial flexibility in individual government (and private) hands would allow market forces considerable freedome with a minimum of government intervention.
4. The requirement that sales from CCC stocks be made at prices that would recapture from foreign buyers the cost of acquiring the grain, plus storage and other carrying charges, would also make this option operate compatibly with the market system. Food aid commitments would be exempt from this requirement.

5. Set price range would provide greater stability than other options and therefore, be preferable from standpoint of importers and domestic consumers.

6. Such a program would provide the USG with another tool besides set-aside to keep prices above target levels if surpluses build up.

Cons

1. The principal problem with this option is whether realistic price ranges could be negotiated and renegotiated when necessary, and whether countries would actually act in keeping with the guidelines when the going got tough. If not, the U.S. could find itself once again holding most of the world's stocks and playing once more the role of residual supplier.

2. In general this alternative is less market-oriented then other options since it introduces greater government intervention into marketing and decision-making.

3. The build up of government-owned stocks overhanging the market could be price depressing.

4. As with most international commodity agreements, the necessary pricing mechanism is not likely to be effective.

With Internationally-Held Stocks: Option E: World Food Bank/International Reserves

1. Stocks in the U.S. would be privately held.
2. There would be full international information exchange regarding stock levels and expected production, consumption, imports, and exports.
3. An international grain reserve stock financed jointly by consumers and producers would be established to insure adequate availability of grains in times of world wide production shortfalls.
4. Explicit guidelines on acquisition and disposal of the international stocks.

Under Option E, the U.S. Government would not hold grain stocks as part of its national agricultural policies. Domestic production plans would be formulated in light of the signals (price movements) coming from the market place.

A fairly detailed information exchange system, enabling a free flow of production and consumption forecasts among participating countries, coupled with information about national and private stockpile activities would be essential to efficient international reserve stock management and to domestic production planning. Hence, reporting requirements are a vital part of the reserve stock plan.

The international grain reserve would aim for quantity stability and would operate to supplement private and national stocks as additional insurance against shortage. Stocks would be built up to a determined level gradually over time, during periods when world production exceeds the "equilibrium" level (the long-run trend in world consumption). Compulsory sales from the reserve would then occur only in times of evident shortage--when supplies forthcoming to the market (new production plus national and commercial stockpiles) fall short of projected demand by some fixed percentage. In times of world-wide surplus, there would be buying from the world market only to replenish the stockpile, so that the reserve stock would not become a vent for surplus or an incentive to over-production. In normal years once the stock has reached its established level, there would be no reason for the reserve to operate in the international market.

The size of the reserve stock would presumably be some function of the variance of supply about the long-run trend in consumption. No floor price support provision would be included, and the reserve would act only indirectly to prevent excessive price increases to the extent that the stock is permitted to be reduced in any given season.

The reserve would be financed jointly by consumers and producers. Provision for a famine relief fund could be grafted onto the reserve stock scheme as a "set-aside" reserve to be carried at all times for emergency assistance in times of widespread drought or famine in developing countries. The fund could release grain to or provide financing for grain purchases by specific countries, whereas the general reserve would release grain into the market regardless of destination.

Pros

1. Would relieve the United States of its past role as residual supplier of grain in times of world production shortfalls;
2. Wouldprovide additional supply reliability to buttress the case for moving toward freer trade in agriculture;
3. Would be more consistent with a multilateral trading framework than the current tendency toward bilateral supply guarantees;

4. U.S. would continue to maintain control over domestic production policies within the framework of international consultation.
5. Would act as a potential dampener of excessive price increases that in part result in financial hardship for developing countries; and
6. Would continue to rely on the international market place's ability to serve as an impersonal allocator of supplies among the various consuming countries.

Cons

1. Could result in a high degree of international control over domestic production policies.
2. Could distort the price signals which the market should be giving to producers.
3. Could result in pressures on the international bureaucracy to act in ways not consistent with U.S. interest.
4. In addition to cost of carrying stocks, there would be a cost for maintaining an international bureaucracy. This, however, would be shared internationally.

IV. NEGOTIATING CONSIDERATIONS

As noted earlier, the U.S. has preferred to emphasize the role of the free market in determining how agricultural resources are to be allocated.

Other producer nations such as Canada and Australia have generally supported the U.S., but nevertheless have government-controlled wheat boards which regulate export sales and have on occasion expressed interest, and in the case of Australia even enthusiasm, about the idea of international arrangements to "manage" if not control international trade in certain key agricultural products.

Food importers and those exporters with no comparative advantage in agriculture tend to take a different view. Importers (many of them developing countries) see themselves overly dependent upon foreign sources of supply; they are anxious to ensure that their farmers are not subject to more efficient foreign competition, both because they wish to maintain (and if possible increase) their own self-sufficiency in food, as well as to ensure adequate incomes to their farmers. To the extent that these countries are not self-sufficient, they wish to ensure that adequate supplies of food will be available from exporters, and that the use of export controls is effectively limited. (The U.S., it should be noted, is not alone in applying export controls; other countries have adopted similar measures, and the Canadians through their Wheat Board have effectively limited sales of wheat during the past year.) In addition, in times of scarcity, importers seek to assure prices at "reasonable" levels, i.e., levels below what the current market situation would dictate. Negotiations on stockpiling may thus bring about an alliance between developed and developing importing countries on this issue.

Since the grain importing countries greatly outnumber the exporting countries (although the latter will of course have an influence far out of proportion to their numbers), it is fair to say that a majority--probably an overwhelming majority--of countries favor international action by governments to regulate trade in grains, including stockpiling measures. As we have indicated earlier, Australia and Canada (and probably Argentina as well, although we have no firm reading of that country's views) among the exporters also have stated both privately and publicly their willingness to cooperate in international governmental measures--possibly even including commodity agreements--on grains.

Whatever option is chosen, account must be taken of various international negotiations on trade and food problems now underway. The multilateral negotiations on trade matters under the auspices of the GATT began last September and are now in their initial preparatory phase, although final decisions on actual concessions on tariffs and non-tariff barriers are still several years away. Should the U.S. be willing to enter into international arrangements on food aid and/or stockpiling, our positions on these matters will obviously have an important bearing on our negotiating posture on trade matters and on the attitude of our negotiating partners as well. If, for example, the U.S. were willing to enter into commitments on stockpiling and food aid (which presumably means a guarantee of assurance of supply), these could be valuable tools in our efforts to convince other nations that improved market access is a necessary accompanying step to any U.S. action on stocks.

Another forum in which stockpiling will be under active discussion during the coming year is the FAO. In June 1973, FAO Director General Boerma proposed that FAO members (which do not include the Soviet Union) agree on voluntary guidelines to establish a minimum level of international reserves, with each country to carry its own stocks and to determine for itself the level of reserves it considers as appropriate for its contribution to overall world food security. The proposal provides a guide as to what kind of world food security system may be negotiable internationally. It would involve an effort to develop an improved information system, including the Soviet Union; a review of national stock policies which, in combination, maintain at least a minimum safe level of basic food stocks for the world as a whole; a review of national stock targets or objectives with the aim of maintaining national stocks at least at the levels regarded as necessary for ensuring continuity of supplies to meet domestic and where appropriate export requirements, including a security margin for contingencies or emergency needs in case of crop failure or natural disaster; and a commitment by countries to take measures to ensure that national stocks are replenished whenever they have been drawn down below such minimum levels to meet food shortages.

Of the options presented in this paper, the variations of option D are most clearly compatible with the Boerma world food reserve proposal.

Option D meets Boerma's criteria since it is linked to the target concept yet retains national sovereignty over stocks. Nevertheless, the Boerma proposal is phrased in such general terms that depending on how they are developed, any of the multilateral approaches to stocks policies may be compatible.

The U.S. agreed in principle to the Boerma proposal at the FAO Conference last November, since it is potentially compatible with all of the options discussed above. Nevertheless, should the Boerma proposal become more specific in terms of the overall level of stocks to be held and the responsibilities of individual countries, as well as the degree of commitment involved, the U.S. will have to assess its position on the Boerma proposal in the light of whatever decision is made on the options on stockpiling contained in this paper and in the light of progress toward trade liberalization in the MTN.

It is also possible that the World Food Conference to be held in November of this year may provide an international arena in which the U.S. may wish to advance its position on the stockpiling issue. It is the current U.S. position, however, that the overall results of the Conference should be focussed on attaining agreement on general concepts rather than on the negotiation of specific commitments. As NSSM 187 states, the purpose of the Conference is to "establish a broad policy framework for dealing with the world's food problems." If a decision is made in favor of one of the options on stockpiling listed above, the U.S. might be able to encourage agreement by the WFC on a "principle" which would anticipate the particular stockpiling option we favor. Negotiation of specific commitments might then take place in the MTN.

V. Conclusions

In NSSM 187, it was noted (page 37) that a successful negotiation leading to better international cooperation in agriculture should take account of--if not necessarily specifically include--four basic elements: market access, supply assurances, food aid, and farm income maintenance. Thus, all of the stockpiling options listed above should be considered in tandem with U.S. efforts to liberalize existing barriers against trade in agricultural products, commitments on food aid which might exist outside the framework of any stockpiling arrangements, and the need for each nation to maintain adequate income for its agricultural sector.

Given these objectives, the options listed should not be considered as being mutually exclusive. In fact, a U.S. reserves policy taking into account all of the above considerations would probably reflect some elements of several options, given that a reserves policy can be a mix of physical stocks, forward contracts, or multi-year supply commitments.

Neither is a multilateral approach a direct substitute for the unilateral and bilateral approaches previously discussed. Instead it constitutes a "build on" to the other approaches to a system of grain reserves. The exact structure of a reserves program blending one or more of the options depends on the extent to which each of the considerations involved is addressed.

A policy incorporating elements of options A and B and addressing itself to the issues of food aid, supply assurance, farm income, and national stocks may be developed out of the two variants of Option A.

From a practical standpoint, a policy under the free market alternative of Option A will probably, at some point in time, result in a carryover greater than the private sector is willing to carry. It is also quite possible that the same condition could exist even if the set-aside alternative is followed. By that time, production adjustment measures should have been implemented, but the question of surplus would still remain.

In such a situation the first priority for stock acquired by CCC may be designated as emergency relief throughout the world as in Option B. A quantitative determination could be made, and release of these stocks would be limited to emergency relief. This stock could constitute the U.S. commitment to LDC's for emergencies. Ideally, this commitment would only be a part of an emergency reserve established by all of the world's developed countries. One advantage of such a reserve is that emergency needs can be met in periods of relatively tight supplies without exerting further pressure on prices.

Unless and until emergency stocks were built up through operation of the loan program, U.S. food aid policy could entail quantitative commitments to be met through open market purchases, as suggested in Option A. If the quantitative limit for an emergency reserve were filled, and a further surplus still existed then the government would again be faced with carrying stocks for commercial purposes.

In the event of such surplus developing, a greatly modified approach to disposition than has existed in the past could be proposed. Resale prices of CCC-owned grain could no longer be geared to loan levels, but instead, reflect the cost of acquisition and cumulative costs of storage and interest. Some ceiling price might have to be incorporated because a succession of relatively price stable years could escalate the resale price to such a high level that only in time of extreme shortage and very high prices would stocks be available to the market.

Domestic price consideration may be better served by an earlier release of stocks to hopefully mitigate against further price escalation. This modification would not impair the goal of cost recovery. Equally as important, buyers in most instances would have to continue to look to the marketplace for their needs, not CCC inventory. This notion is introduced in Option D, and would be particularly suited to the target price-release alternative.

Such a modification would achieve the desired insulation of stocks from the marketplace so as to prevent an overhang leading to a price depression and production cutbacks.

In this regard Option C would not be feasible since it would neither insulate stocks nor make commercial sale of stocks on the same basis as private commercial sales.

Regardless of which option or combination of options is developed into a stockpiling policy, account will need to be taken of the financial and technical requirements of the LDC's to enable them to develop adequate national food security programs. Technical assistance could involve counselling and advising them with respect to grain marketing and distribution problems, including forward buying; helping them develop appropriate domestic storage programs; and offering production development assistance. In addition, special credits could be given to less developed countries to acquire stocks and, in selected cases, to develop storage capacity as well. The effect would be to strengthen the world market and raise world stocks to a level greater than would result without such credits. Such a plan would increase Option A's ability to meet emergency needs. In addition, it would delay or decrease the need for planting restrictions in the short run.

Control of these credits could follow either a unilateral or multilateral approach. The United States would have greater control under a unilateral approach; U.S. costs would be less, though control would be decreased, under a multilateral approach.

Because international coordination and cooperation are difficult under the best of circumstances, the United States would need to consult frequently with importing countries.

Above all, under any of the options there would have to be cooperation with respect to obtaining a free flow of information about supply and demand prospects if de-stabilizing market fluctuations are to be avoided. No matter how secure a stock cushion is built up, the sudden entry to or exist from the the market by one or two large purchasers can touch off speculative price swings that could impede the development of a global stockpiling policy.