ASSESSMENT OF THE EFFECTS OF BARTER AND COUNTERTRADE TRANSACTIONS ON U.S. INDUSTRIES

Report on Investigation No. 332-185 Under Section 332 of the Tariff Act of 1930

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Preface

On June 11, 1984, on its own motion and in accordance with section 332(b) of the Tariff Act of 1930 (19 U.S.C. 1332(b)), the United States International Trade Commission instituted investigation No. 332-185, Assessment of the Effects of Barter and Countertrade Transactions on U.S. Industries. The study examines (1) the effects of the growing involvement of U.S. companies in international countertrade transactions as well as offset arrangements whether or not related to foreign military export sales and (2) the economic conditions that have created the demand for such trade. Notice of the investigation was given by posting copies of the notice of investigation at the Office of the Secretary, U.S. International Trade Commission, Washington, DC, and by publishing the notice in the Federal Register (49 F.R. 25316, June 20, 1984) (app. A). 1/

Concurrent with the Commission's investigation, Congress enacted the Defense Production Act Amendments of 1984 (Public Law 98-265, approved Apr. 17, 1984), which amended the Defense Production Act of 1950 (50 U.S.C. App. 2061) (app. B). The 1984 law added section 309 to the Defense Production Act. Section 309 requires the President, not later than 18 months after the date of enactment, to submit to the Committee on Banking, Finance, and Urban Affairs of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate a report on the impact of offsets on the defense preparedness, industrial competitiveness, employment, and trade of the United States. The President directed the Office of Management and Budget (OMB) to coordinate preparation of the section 309 study of the impact of offsets.

Both the OMB and the Commission intended to survey U.S. corporations on the effects of offset arrangements in the respective investigations. On August 6, 1985, the Commission submitted a questionnaire to the OMB for approval. Citing the burden on U.S. corporations of completing two similar questionnaires under the two investigations, the OMB requested that the Commission alone gather the necessary information for both investigations and provide the OMB certain information pertaining to offsets associated with military related exports. The Commission agreed to the OMB's request and in turn solicited U.S. corporations' responses to a questionnaire jointly developed by the Commission and the OMB (49 F.R. 47440, Dec. 4, 1984) (app. A). Information from the questionnaire was provided to the OMB on July 22, 1985, at the direction of the OMB pursuant to authority delegated to the OMB by the President under the Defense Production Act (see Executive Order No. 12521 of June 24, 1985 (50 F.R. 26335)).

In the course of its investigation, the Commission collected questionnaire data from 154 firms having offset obligations resulting from military-related export sales (including firms which were subcontractors for firms having such offset obligations) and 369 major U.S. export firms engaged in countertrade transactions.

1/ Various other Federal Register notices concerning the study questionnaire and public hearings are also contained in app. A.

A public hearing was held on May 30, 1985 (49 F.R. 50317, Dec. 27, 1984, and 50 F.R. 12090, Mar. 27, 1985) (app. A)), in the Commission's hearing room in Washington, DC, and testimony was received from several representatives of trade associations, multinational corporations, and consultants involved with or concerned about international countertrade transactions (app. C). Additionally, information was obtained from published sources, from interviews with corporate executives representing U.S. firms with offset or countertrade interests, from the Commission's files, and from other sources.

The information and analysis in this report are for the purpose of this report only. Nothing in this report should be construed to indicate how the Commission would find in an investigation conducted under other statutory authority covering the same or similar matter.

CONTENTS

CONTENTS

Figures

Tables

CONTENTS

Executive Summary

During 1980-84, international trade has seen a marked increase in the number of countries and intensity of efforts involved in actively promoting barter and countertrade as a means of conducting international exchanges of goods and services.

This study identified as many as 61 governments with policies which encourage such techniques to some degree. A growing number of governments have become direct, active participants in countertrade transactions and still others have levied requirements for countertrade on some aspects of privately conducted trade.

Estimates of the overall importance of countertrade 1/ vary widely. Few governments collect or publish data specifically to identify such transactions. A 1985 study of the 25-member Organization for Economic Cooperation and Development, based in Paris, concluded that countertrade transactions are a relatively marginal practice, accounting for less than 5 percent of world exports, excluding trade among Eastern European nations.

It is widely agreed, however, that in 1980-84 the world has seen a marked increase in efforts to promote and expand countertrade in various forms. A great variety of nations use countertrade including oil-poor developing nations (e.g., Israel, Jamaica, and Turkey), oil-rich developing nations (Indonesia, Malaysia, Mexico, and Saudi Arabia), newly industrialized nations (Korea and Singapore), and such traditional users as the Eastern Europeans (East Germany, the Soviet Union, Poland, etc.). Even developed market economies such as Australia, Belgium, Canada, and Japan have become important actors. In an unusual case, a U.S. company has requested a countertrade commitment as part of a major purchase from one newly industrialized nation.

Reasons given for the expanding international emphasis on countertrade include: (1) the international debt and balance of payments problems of many nations, forcing upon them the need to find non-hard-currency ways of paying for important imports; (2) national budget problems which dictate a need to economize on and even recoup the costs of major military import purchases; and (3) political pressures to maintain economic development and employment-expansion programs despite budget and payments deficits and intensifying competition in export markets.

During 1980-84, the average current account deficit of all non-oil-producing developing countries averaged $65 billion annually, whereas that for industrialized countries collectively averaged $36 billion (see table 14, page 39). In these circumstances, international commercial lending to many of the more indebted countries was curtailed. Additionally, many debtor nations are under obligations to the International Monetary Fund (IMF) to conserve foreign exchange and reduce high debt levels. Many debtor countries,

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1/ For purposes of this report, the term "countertrade" refers to all forms of reciprocal or "tied" international contractual or "best effort" commitments. Such forms of countertrade include offsets (whether or not linked to military-related export sales), barter, compensation, counterpurchase, and blocked currency countertrade (see pp. 1-8 for specific definitions).

especially those heavily dependent upon imported resources, have resorted to countertrade as a means of conserving foreign exchange. Many countries have undertaken import reduction programs. As a result, exporting companies must compete more vigorously for diminished export demand and are therefore more vulnerable to countertrade demands. With respect to U.S. firms, this trend can be seen by the dramatic rise in countertrade obligations during 1980-84.

The purpose of this study is to determine the extent of U.S. involvement in countertrade and its impact on U.S. trade and domestic economic interests. Understanding this involvement also requires knowledge of the policies and practices of the countries that have stimulated these techniques.

Countertrade transactions consist of three major elements: the export sales agreement; the obligation agreements (there may be more than one obligation agreement associated with a sales agreement); and the fulfillment, or implementation, of the obligations. The obligation agreements are not necessarily entered into at the same time that the original sales agreement is signed. Often, final agreement on the obligations lags behind the sales agreement by 6 months or more. Final fulfillment of the obligations, the third element in a countertrade transaction, may take as many as 10 years or more to complete.

The information presented in this report is based principally on responses to the Commission's questionnaires from more than 500 U.S. corporations. The respondents accounted for approximately $2 trillion in total sales in 1984, including export sales of $127 billion. (Total U.S. merchandise exports in 1984 were $212 billion.)

Two types of corporations were surveyed by Commission questionnaires in the course of this investigation--those substantially involved with military-related export sales having associated offset obligations and those corporations with foreign sales involving other types of countertrade. Because the offset obligations associated with foreign military sales are generally fulfilled differently from other types of countertrade obligations, and because detailed data on such offset obligations were gathered in a separate Commission questionnaire, these types of obligations are frequently discussed separately in this report. Direct comparisons of nonmilitary countertrade and countertrade associated with military offsets are made to the extent that the two data bases are similar in scope.

The major findings of this study of U.S. involvement in countertrade are as follows:

- Of $127 billion of 1984 U.S. export sales surveyed, $7.1 billion or 5.6 percent involved countertrade obligations. The total value of associated U.S. countertrade obligations peaked in 1983 at $3.5 billion, declining to $2.8 billion in 1984, equivalent to just more than 2 percent of exports.

According to questionnaire responses, the ratio of total countertrade obligations (including offsets) to associated export sales agreements fluctuated dramatically from year to year, but it generally exhibited an increasing trend. The ratio ran as high as 66 percent in 1983 and as low as 10 percent in 1980. In 1984 the ratio was 39 percent. The average for the 1980-1984 period as a whole was 39 percent.

A summary of the value of U.S. sales agreements involving countertrade and associated obligations in 1980, 1982, and 1984, for both military and nonmilitary related transactions, is shown below (in millions of dollars):

Item	1980	1982	1984
Sales agreements involving countertrade:			
Military related (offsets)-----	6,568	732	5,890
Nonmilitary--------------------	1,846	983	1,249
Total--------------------------	8,414	1,715	7,139
Countertrade obligations:			
Military related (offsets)-----	414	439	2,182
Nonmilitary--------------------	467	479	580
Total--------------------------	881	918	2,762

- o <u>Almost $5.5 billion in total U.S. exports resulted from countertrade (excluding offsets) agreements during 1980-84, and approximately 4.6 billion dollars worth of goods and services are currently planned for export during 1985-2000</u>.

U.S. exports associated with nonoffset countertrade increased by almost fourfold, from $285 million in 1980 to $1.4 billion in 1984. From 1980 through 1984, they represented 84 percent of the total exports committed under sales agreements signed during the 1980-84 period. In most major export sales contracts, the actual time of delivery of the export product ranged from several months to several years after the contract signing, and delivery may have been spread out over several years. Current contracts call for exports targeted during 1985-2000 to exceed $4.6 billion.

- o <u>Imports from nonoffset countertrade totaled $1.8 billion during the same period. U.S. imports resulting from countertrade (including military offsets) transactions accounted for an insignificant share of total U.S. imports</u>.

The $525 million peak in 1984 in U.S. imports under countertrade transactions, including offsets, accounted for just over 0.1 percent of total U.S. imports of goods and services that year. Imports associated with nonmilitary-related countertrade accounted for virtually all of countertrade imports in 1980 and for about 80 percent ($420 million) of the total in 1984; U.S. imports received in such countertrade fluctuated annually between $323 million and $420 million and totaled $1.8 billion during 1980-84.

Countertrade imports in 1984 accounted for only 19 percent of total obligations that year. Additional goods and services received in countertrade in 1984 were either sold abroad, absorbed by foreign affiliates of U.S.

companies, or sold to a trading company, while any remaining difference is due to the multiyear period over which countertrade transactions can be implemented.

- o The total value of U.S. exports obtained under nonmilitary countertrade exceeded that of U.S. imports. 1/

During 1980-84, U.S. exports resulting from countertrade (excluding offsets) agreements exceeded countertrade imports in each year except 1980. In 1980, countertrade imports were valued at $323 million, whereas exports were valued at $285 million, representing a trade deficit of $38 million in goods and services associated with nonmilitary countertrade. 2/ Since 1980, however, the United States has experienced annual trade surpluses in nonmilitary countertrade, increasing from $538 million in 1981 to $1.5 billion in 1983 before declining to $940 million in 1984. It should be noted that annual trade surpluses are expected in countertrade transactions, because most countertrade agreements permit associated purchase obligations to be less than the full value of the export contract, to be carried out over several years, and to involve arrangements other than imports into the exporting country. As a result, U.S. imports against U.S. countertrade obligations are generally much less than the associated exports and lag well behind obligation values.

- o Military offset arrangements accounted for 80 percent of all U.S. counterpurchase obligations in 1980-84, and for most of their increase in the period.

Offset obligations fluctuated dramatically from lows of more than $400 million in 1980 and 1982, to a peak of $3.2 billion in 1983. From 1980 to 1984, their value increased more than fivefold and their percentage of total countertrade from 47 percent to 79 percent. Military offset obligations resulted primarily from foreign purchases of major weapons systems made in the United States. The record high levels in 1983-84 reflect major arms updates mainly by NATO nations and increased weapon systems procurements by other U.S. trade partners.

- o For 1980-84, an average of 39 percent of U.S. military exports had associated offset obligations. The value of total obligations were equivalent to about 18 percent of those export sales.

During the period, U.S. military export sales increased steadily, nearly doubling between 1980 and 1984, to more than $11.2 billion. The ratio of

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1/ Because the reported obligation agreements may have been signed in 1 or more years subsequent to the year the actual signing of the export sales contract took place, the values of the obligations in a particular year will not correspond directly to the value of that year's export sales agreements.

2/ Frequently the flow of imports associated with a particular sale may span as much as a ten-year period, whereas U.S. products under the agreement typically are exported during a shorter timeframe. Therefore, the annual flows will not necessarily reflect the actual long-term balance of trade under countertrade.

obligations associated with sales was highly volatile from year to year, from a high of 94 percent to a low of 7 percent. In 1983 and 1984, the ratio was 42 percent and 53 percent, respectively. The study found that military-related export sales are much more likely to include a countertrade obligation than are nonmilitary transactions.

Sources responding to Commission questionnaires and interviews believe it is likely that a decline in foreign purchasing power associated with the high U.S. dollar between 1982 and 1984 has accelerated foreign government demands for offsets. Another factor is increased emphasis on development of domestic arms industries through various means that offset agreements can provide, including technology transfer, coproduction, joint venture, and counterpurchase arrangements.

- U.S. nonmilitary countertrade commitment accounted for only 20 percent of total U.S. countertrade obligation for the period 1980-84.

Nonmilitary countertrade obligations in 1980 totaled $467 million, and rose 24 percent to $580 million in 1984. However, their share of total U.S. countertrade obligations fell from 53 percent in 1980 to 21 percent in 1984. Over the period, these obligations varied in a narrow range of plus or minus 30 percent, around an average of $440 million per year, from a low of $320 million in 1981 to the 1984 high of $579 million.

In this period, world demands for countertrade grew markedly in the face of multiple economic problems, including recession, international debt crises, and domestic budget stringencies. Developed nations were among the most numerous to resort to countertrade techniques. Nevertheless increases in U.S. nonmilitary countertrade and in countertrade with developing nations generally were small compared to levels and increases of military offset obligations. Replies to Commission questionnaires indicate that the high value of the U.S. dollar tended to limit the scope of countertrade for U.S. products where the United States has strong technological leadership and competitive advantage.

- The value of U.S. companies' countertrade (including offsets) obligations with Europe grew by more than fourfold during 1980-84, and such obligations with Asia more than tripled. 1/

Latin American countries, which were among the most active in attempting to expand their countertrade, were a minor element in the expansion of U.S. countertrade involvement. By contrast, countertrade obligations entered into by U.S. companies with European entities registered a fourfold increase, reaching almost $1.4 billion in 1984 compared with $285 million in 1980. Europe's share of total U.S. countertrade obligations rose from 32 percent in 1980 to 50 percent in 1984. Much of the increase in obligations with Europe

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1/ Asia as defined in this study encompasses Middle Eastern countries from Asia Minor eastward, as well as South Asia, Southeast Asia and East Asia, including China and Korea.

results from increases in military sales to NATO member countries. NATO countries in Europe accounted for 44 percent of total U.S. countertrade obligations during 1980-84.

U.S. companies' countertrade obligations with Asia climbed by 223 percent during the period, from $295 million in 1980 to $953 million in 1984. Asia's share of total U.S. countertrade obligations increased slightly from 34 to 35 percent over the period. Most of the increased obligations resulted from offsets associated with military-related export sales. The largest increases, in 1981 and 1984, were related to large U.S. military sales to Israel. Saudi Arabia is becoming a major player. A number of other Middle Eastern countries have engaged in countertrade transactions with the United States. In nonmilitary countertrade transactions with Asia, China's foreign trade liberalization, Indonesia's new countertrade requirements, and Philippine foreign debt and exchange reserve problems have stimulated countertrade transaction increases.

Of sales agreements between the United States and all European entities during 1980-84, most (representing 85 percent of all sales agreements) were associated with military-related exports and involved offset requirements. Similarly, sales contracts representing 81 percent of the face value of total sales agreements with Asia involved military-related offsets. Sales contracts with offsets between the U.S. and all other regions of the world accounted for 68 percent of the total face value of all sales contracts.

Europe accounted for a much higher ratio of obligation to sales than did other world regions. Increased U.S. competition for military sales to Europe is the primary force for driving up the share of obligations to sales. A summary of the face value of sales agreements with associated countertrade (including offsets) obligations and the value of such obligations in 1980, 1982, and 1984 are as follows (in millions of dollars):

Item	1980	1982	1984 1/
Sales agreements involving countertrade (including offsets):			
Europe	2,959	483	1,848
Asia	1,654	556	4,807
All other	3,801	676	484
Total	8,414	1,715	7,139
Countertrade obligations (including offsets):			
Europe	285	201	1,378
Asia	295	235	953
All other	301	482	431
Total	881	918	2,762

1/ Because of rounding, figures may not add to the totals shown.

o The single most important product grouping associated with export sales contracts involving all countertrade during 1980-84 was aerospace products. Other sectors with large countertrade involvement are communications and electronics and defense products.

Sales contracts for aerospace products by U.S. companies that included countertrade obligations were valued at $20.2 billion, equivalent to 70 percent of all export sales agreements involving countertrade (including offsets). In contrast, countertrade (including offsets) obligations to be fulfilled by contracting abroad for aerospace products were valued at 20 billion, or 7.6 percent of the total countertrade obligations.

For 1980-1984, 25 percent of the $79.8 billion in U.S. aerospace exports (including both military and nonmilitary) had associated countertrade obligations. This high concentration is attributed, in part, to the U.S. technology edge in these products and, in part, to the great size and foreign exchange cost of aerospace purchases. Other export sectors in which countertrade was important were defense products, communications and electronics, construction projects, minerals, and chemicals.

o Sales agreements with counterpurchase-type 1/ obligations account for most of the sales agreements associated with nonmilitary countertrade obligations.

Sales agreements with counterpurchase obligations accounted for $5.7 billion, or 91 percent of all sales agreements in which a nonmilitary countertrade was negotiated during 1980-84. Compensation-related sales agreements accounted for $298.7 million, or 5 percent of the total, and barter-related sales agreements accounted for $115.4 million, or less than 2 percent.

o Half of all U.S. imports resulting from nonmilitary countertrade was accounted for by Eastern Europe.

Imports from Eastern Europe accounted for 70 percent of total nonmilitary countertrade imports in 1980. During 1981-84, the Eastern European share fell to 33 percent in 1982 before climbing to 50 percent in 1984. Imports from Asia represented 5 percent of the total in 1984 compared with 1 percent in 1980. The share of total nonmilitary countertrade imports accounted for by Latin America grew from zero in 1980 to 36 percent of the total in 1982 before declining to 12 percent in 1984.

1/ A counterpurchase transaction obligates the seller in an export sales contract to purchase some specified value of products from the buyer in a separate transaction. In a compensation transaction, usually involving the sale of plant, equipment, or technology, the seller agrees to take in payment some portion of the output resulting from the sale of plant, equipment, or technology. A barter is an equal trade of goods and services and is accomplished in one transaction. (See the "Elements of Countertrade" section of this report.)

o <u>Almost one-half of the goods and services imported under nonmilitary countertrade were used internally by U.S. companies that were parties to the countertrade sales agreements</u>.

Of the $1.8 billion in imports making up nonmilitary countertrade during 1980-84, 46 percent were absorbed inhouse for use by the U.S. companies involved in the countertrade agreements. In 1980, inhouse use of countertrade imports accounted for 33 percent of the total nonmilitary countertrade imports. Inhouse use of countertrade imports grew to 64 percent of total nonmilitary countertrade imports in 1982 before declining to 44 percent in 1984. The growth of inhouse use of products received in countertrade is a reflection of the trend toward importing more sophisticated, and therefore more usable products into the United States.

o <u>During 1980-84, the total military offset obligation was divided almost equally between direct and indirect offsets</u>.

Direct offset obligations (those that involve subcontractor production, coproduction, and the licensed production of products that are dedicated to the product being sold, e.g., avionics for aircraft) were valued at $4.8 billion during 1980-84 compared with indirect offset obligations of $3.6 billion. Most (61 percent) of the direct offset obligations will be satisfied through subcontractor production in foreign countries. For example, the production of the avionics for a particular aircraft involved in an offset agreement may be shifted to the country buying the aircraft. Of the more than $2.7 billion in offset obligations fulfilled during 1980-84, $1.5 billion, or 56 percent of the total, has been fulfilled through direct offset arrangements. Fulfillment of indirect offsets during 1980-84 was valued at $1.2 billion, or 44 percent of the total obligations fulfilled during this period. The planned fulfillment of much (74 percent) of the indirect offset 1/ obligation was unspecified by respondents, whereas most of the remainder of the indirect offset will be satisfied through some form of countertrade.

o <u>During 1980-84, subcontractors to U.S. prime contractors involved in military offsets assumed almost $1 billion of the offset obligations of the prime contractor.</u>

Subcontractors assumed $977 million of their prime contractors' offset obligations during 1980-84. More than one-half ($507 million) of these obligations were or will be fulfilled through indirect offset arrangements. Assumption of a portion of the prime's obligation may be completed in one of two ways: (1) the subcontractor may be asked to join in a predetermined commitment, such as participation in disposing of or using inhouse products that the prime has already agreed to accept from the buying country; or (2) the subcontractor may be given the opportunity to negotiate its own obligation agreement with the buying government, which would be done on behalf of the prime contractor.

1/ Indirect offsets are those that are not related to the product being sold. For example, the seller of aircraft may provide the buying country with technology to produce electronic components that are not designed to be incorporated into the aircraft sold.

- <u>Respondents reported positive countertrade benefits overall, from increased employment, sales, and production efficiencies despite some lost sales</u>.

The majority of respondents engaging in countertrade and military offsets indicated that they have been able to maintain or increase existing levels of employment and plant capacity because of new business generated by such sales agreements. Other benefits that companies have derived from countertrade agreements include larger and more efficient production runs, lower unit costs, increased capital formation, and the development of new technology. According to information gathered during this investigation, countertrade has not adversely affected the competitiveness of the U.S. companies surveyed, both those engaging in countertrade and those that are not. However, some U.S. firms expressed concern over the potential impact on their business because of competition emerging from countertrade transactions, as a result of requirements for technology transfer, local procurement conditions enhancing the strength of local suppliers, and deals that put new players into marketing counterpurchase imports, in one type cited, of tourism services.

U.S. companies reported that 31 contracts, totaling $1 billion, were lost during 1980-84 because of countertrade requirements. The primary reason for this loss of sales was that individual corporate policies prohibit or discourage the use of countertrade. To a lesser extent, sales were lost to foreign competitors that offered more competitive countertrade proposals.

Elements of Countertrade 1/

Countertrade is made up of several forms of reciprocal trade. The most basic forms of countertrade agreements are counterpurchase, compensation, and barter. "Offset" and "switch trade" are terms used to describe unique types of countertrade often encompassing one or more of the above forms.

Counterpurchase

Companies in the industrialized countries seeking to sell their products in many nonmarket economy countries (NME's) and less developed countries (LDC's) often discover that the LDC's or NME's will not agree to purchase contracts, unless the companies agree to buy or market products of the LDC or NME that are valued at less than those products in the original Western purchase contract. If the products offered by NME's or LDC's are unrelated to the products being sold by the company seeking to export (i.e., they do not result from the Western export of plant, equipment, technology, or products), the agreement is referred to as a "counterpurchase" arrangement. As a general rule, such arrangements contain the following characteristics:

- o The period for fulfilling the counterpurchase obligation is rather short term--1 to 5 years.
- o The value of goods offered by the foreign government or company is usually less than 100 percent of the original sales contract value.
- o The counterpurchase requirement is contractually agreed upon, either in the original sales contract or as a separate, parallel contract.

In a typical counterpurchase contract, the company is required to fulfill its contract within a specified period or face some agreed-upon penalty. Usually, the penalty is an outright hard-currency payment equal to some percentage of the original contract commitment. Penalties usually range from 5 to 25 percent of the value of the company's counterpurchase obligation. Also, the other contracting party is expected to fulfill its part of the agreement, i.e., to purchase the specified product during a finite period or, in the case of default, pay an agreed-upon hard-currency penalty.

In instances where counterpurchases are required by an Eastern European country or an LDC, a contracting company is frequently offered a limited list of products from which it can select. Corporate executives in the United States report that such lists typically include products that are in oversupply in the country of origin or that are not readily marketable in industrialized countries. Usually, companies agree to buy these products only if sizable discounts are given. For this reason, counterpurchase arrangements are reluctantly entered into by many companies in industrialized countries.

1/ A discussion of the economic and other reasons for the worldwide growth of countertrade is presented later in this report.

To overcome the problems associated with counterpurchase requirements, many companies have resorted to "evidence accounts." 1/ By means of evidence accounts, which are usually opened with the foreign trade bank or a private bank of the importing organization, a company's purchases are automatically credited against its current or future counterpurchase obligations in that country so that further counterpurchase obligations can be satisfied by past purchases. Evidence accounts can also be established with one or more foreign trade organizations (FTO's) 2/ in most of the Eastern bloc countries. Instead of facing an immediate and uncertain counterpurchase demand at the signing of a sales contract, the exporting firm can, through the evidence account, have time to preselect products that can be marketed back home. Furthermore, the exporting firm can spend more time assisting the foreign party in the development of new or redesigned products that will find receptive markets. 3/

Although the actual wording of an evidence account contract varies from one country to another, in most cases the contract stipulates the value of sales and purchases by the contracting company and the magnitude of purchases that must offset the sale. The evidence account mechanism also permits the contracting company to negotiate a number of sales contracts without having to fulfill a particular counterpurchase obligation for each contract. Evidence accounts are not required to be in equilibrium each year; however, such agreements often require a company's counterpurchase to reach as much as 80 percent of sales value. Should the contracting firm not fulfill the stipulated volume of its annual purchase requirement, the unfulfilled portion is added to the following year's purchase obligation.

Companies dealing in raw materials, chemicals, and other basic commodities are more likely to engage in evidence accounts, since product demand and sales of such goods are more easily projected for several years. Companies willing to enter into long-term evidence agreements are usually viewed favorably by the host government. However, once a company enters into an evidence agreement, it is expected to fulfill its portion of the commitment. Furthermore, a company generally is restricted under evidence accounts from transferring its counterpurchase obligation to a third party, such as an independent trading house. Notwithstanding the restrictions associated with evidence accounts, most trade experts agree that such transactions are likely to increase.

Compensation

Sometimes referred to as "buy-backs," compensation agreements entail the sale of plant, equipment, and/or technology in return for resultant products

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1/ Evidence accounts result from an agreement whereby, for example, a Western firm undertakes to buy and sell goods from an LDC over a given period. Such sales and purchases are recorded in evidence accounts maintained by banks in both countries. These accounts are used because individual countertrade transactions do not necessarily balance. Thus, if the LDC sells more to the Western firm than it purchases from it, it receives credit at the Western firm's bank in hard currency. In the reverse case, the Western firm receives credit at the LDC firm's bank in local currency.

2/ FTO's perform most trade functions in many NME's.

3/ "Using Evidence Accounts to Rationalize Countertrade," Business Eastern Europe, Nov. 16, 1979.

once the facilities become functional. These types of arrangements, frequently involving the sale of a "turn key" facility, became popular in the mid-1960's. Most early compensation deals involved the sale of technology and machinery for large-scale petrochemical facilities and mining operations.

Characteristics of compensation transactions are as follows:

- o The average value of transactions is usually much higher compared with those of other forms of countertrade, with the exception of offsets.
- o The typical period of product take-back is relatively long--5 to 20 years.
- o The value of product take-back during the contract period usually equals the aggregate value of the plant, technology, and/or equipment, plus compensation for interest expense incurred during the period of take-back.

Compensation arrangements have been used by Eastern European countries, the U.S.S.R., China, and several less developed countries to obtain sophisticated foreign technology without depleting scarce hard-currency reserves. Such agreements provide the country receiving the plant, technology, and/or equipment with a supply of much needed production capacity and guaranteed exports. In addition to limiting the burdens associated with large capital investments, compensation agreements allow the host country to take advantage of the foreign firm's marketing expertise to dispose of the resultant products. The foreign partner benefits because it receives a guaranteed supply of products for a specified period of time. More importantly, compensation arrangements provide the supplier of the plant, equipment, and/or technology with entry into a market not otherwise accessible.

In a typical compensation agreement, project financing is arranged either through a Western bank, a foreign State bank, or a combination of the two. Once production begins, the exporting firm takes title to the agreed-upon portion of the plant's output for either captive use or to sell in world markets on its own account.

Barter

Barter is the contractual direct exchange of goods or services between two principals without the use of currencies. In this type of arrangement, the two contracting parties decide the value of the products (or services) to be exchanged. For example, if a sugar manufacturer seeks frozen orange juice concentrate at the world price of $1.30 per pound and in exchange is willing to offer its sugar at $0.13 per pound, then the agreed-upon exchange ratio would be 10:1, or 10 pounds of sugar for 1 pound of concentrate. When the volume of the exchange and delivery dates are agreed upon, each side fulfills its obligation and the deal is completed.

Barter agreements are frequently consummated over a short period of time, usually less than 1 year, so that world price fluctuations do not generally favor either side. Deals requiring longer periods usually include provisions for adjusting the exchange ratios by taking into account world price fluctuations. Another feature of barter is that the transfer of goods is usually accomplished through a single contract. Further, third parties are rarely involved in marketing the products, since most barter is done government to government.

Barter became popular during World War II, when international financial systems were in disarray. Since World War II, transactions of this sort have been common in trade within the Communist bloc, between LDC's, or between LDC's and the Communist bloc. According to trade press reports, in recent years, oil barter has become a method for several Organization of Petroleum Exporting Countries (OPEC) countries to finance military hardware purchases, large commercial purchases, and infrastructure development programs. 1/

Barter transactions between governments are often accomplished by the use of "clearing agreements," wherein two countries decide on the type and quantity of goods they wish to trade. The clearing agreement specifies the goods to be exchanged, the ratio of exchange, and the period for effecting the exchange. The goods are offered at an agreed-upon ratio similar to that previously described in barter transactions. During the period covered by the clearing agreement, each country arranges to receive some portion of the goods offered by the other, and at the end of the period (usually 1 year), reconciliation is made. Any imbalances are settled in several ways, e.g., a hard-currency payment or the issuance of a credit against the next year's clearing account, assuming one is negotiated. Such agreements are often renewed on an annual basis.

If market conditions change and the imported product cannot be absorbed in the home market, the importing country has two options--it may suspend the importation of the product, risking an imbalanced account, or it may sell its purchase option to a third party. The purchase option is usually offered at a substantial discount and sold for hard currency. The third party, however, may have to forfeit part of the discount in order to sell the product internationally for hard currency. The products are often turned over to international trade specialists called switch traders; switching operations and switch traders are described in the following section.

Switch

Switch trading, typically associated with East-West countertrade, occurs after counterdeliveries of products begin. If the recipient of the countertrade products cannot dispose of the goods, the products are turned over to a Western trading house specializing in switch trade. A switch operation frequently involves a series of complicated transactions before a hard-currency buyer is found. Also, discounts of up to 40 percent are sometimes given to sell the products to the trading house. Trading house experts, or switch traders, maintain a self-developed network of companies and individuals that offer ready markets for discounted countertrade products. For example, in a switch transaction a switch trader is offered products at a

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1/ "Reasonable Price and Oil Barter possible," Financial Times, Apr. 22, 1985, p. 5.

substantial discount. The switch trader may find a buyer in a soft-currency country 1/ or in a country in which the central government has imposed hard-currency transfer restrictions. If the potential buyer is unable to pay for the goods with hard currency, the seller may be offered payment in goods produced in the buyer's home country. If the terms are agreeable to both sides, an exchange is made. Since the products received in payment may not be marketable in a country with surplus hard currency, the switch trader may have to repeat the above scenario several times until goods that the trader obtains can be sold for hard currency. In each step of the transaction, the switch trade usually offers a portion of the original discount in order to make the deal more attractive. The difference between the final hard-currency payment and the cost of the original goods represents the profit margin for the switch trade. These deals often take over 1 year to complete. Most of the switch trading organizations are located in Western Europe (especially in Vienna, Amsterdam, London, and Hamburg) and deal primarily in Eastern European goods.

There are advantages and disadvantages in dealing with switch traders. The obvious advantages, reported by U.S. corporate executives, are that companies committed to a counterpurchase can easily dispose of countertrade obligations to a switch-trading house. Furthermore, by releasing the goods, a company can relieve its own staff from the time-consuming tasks of marketing goods received in countertrade. The disadvantages are that a company transferring its obligation to a trading house is often looked upon unfavorably by the country supplying the countertraded goods because such an action is seen as an insincere attempt to establish a long-term trade commitment. This is especially a problem when switching houses dispose of products in markets traditionally served by the supplying country at prices significantly below those charged by the supplying country. Eastern European foreign trade organizations prefer a Western company that uses countertrade goods either for internal consumption or as transfer shipments to its subsidiaries or its suppliers. In certain instances, Eastern European foreign trading companies have broken off negotiations with a Western firm if they find the Western firm plans to turn over its countertrade commitment to a switch-trading house.

Offset

A final type of countertrade, the offset agreement, is mainly used for defense-related sales, sales of commercial aircraft, and other "large ticket" items considered a priority by the purchasing organization--usually a government or a state enterprise. Frequently, an offset arrangement takes place between a firm in an industrialized country and a foreign government. Generally, offsets help recover the hard currency drain resulting from the purchase and, more importantly, provide desired transfer of technology and local employment.

Since the 1950's, offsets have increasingly become a normal business practice for arms transfers, with U.S. firms competing among themselves and with foreign firms for foreign military sales. Although aircraft sales

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1/ Soft-currency countries are those with currencies not readily convertible into dollars.

usually constitute the largest volume in offsets, they are by no means the only type of military equipment that involve offset obligations. Communications equipment, electronic components and accessories, and guided missiles and spare parts are also frequently involved in offset agreements.

The industrial and commercial compensation practices required to offset the purchase of military-related exports generally include five types, 1/ as follows:

- Co-production: Overseas production based upon a government-to-government agreement that permits a foreign government or producer to acquire the technical information to manufacture all or part of a U.S.-origin defense article. It includes government-to-government licensed production and excludes licensed production based upon direct commercial arrangements by U.S. manufacturers.

- Licensed production: Overseas production of a U.S.-origin defense article based upon transfer of technical information under direct commercial arrangements between a U.S. manufacturer and a foreign government or producer.

- Subcontractor production: Overseas production of a part or component of a U.S.-origin defense article. The subcontract does not necessarily involve license of technological information and is usually a direct commercial arrangement between the U.S. manufacturer and a foreign producer.

- Overseas investment: Investment arising from the offset agreement, usually taking the form of capital invested to establish or expand a subsidiary or joint venture in the foreign country.

- Technology transfer: As a result of an offset agreement, research and development may be conducted abroad; technical assistance may be provided to the subsidiary or the joint venture partner; or other activities under direct commercial arrangement between the U.S. manufacturer and the foreign entity may be entered into.

1/ U.S. Department of the Treasury, Survey of Offset/Coproduction Requirements, Dec. 27, 1982, pp. 5-6.

In addition, a company entering into an offset may satisfy all or some portion of that offset through the use of any of the previously mentioned forms of countertrade.

Offset arrangements can generally be classified into one of three categories:

1. Direct offsets include any business that relates directly to the product being sold; generally, the foreign vendor seeks local contractors to joint venture or coproduce certain parts;

2. Indirect offsets include all business unrelated to the product being sold; generally the vendor is asked to buy a country's goods or invest in an unrelated business; or

3. A combination of direct and indirect offsets. 1/

In offset transactions, the selling company is normally aware of a required offset prior to negotiations. Generally, the only variables in the sales contract to be negotiated are the share of the offset of the total contract price, the specific products to be included, scheduling of delivery, and the overall time period to be covered. If the seller does not accept the terms of the proposed offsets, the sale may go to a competitor. 2/

According to industry sources, offsets do not result in artificial pricing, because companies do not view offsets as a subsidy or financial loss, but rather as a means of incorporating a completed product or investment into their operation. Companies consulted noted they would not accept offset requirements that are not competitive internationally. However, extra costs associated with offset arrangements do result in lower profit margins. 3/

Information provided by U.S. companies involved in offsets indicates that a typical agreement requests that 20 to 100 percent of the invoice value of the original product be offset, and competition may cause the offset offer to be higher than 100 percent of the sale. 4/ For example, in one agreement reported by corporate officials, Ghana received Government assistance in selling manganese, timber, and bauxite to offset the purchase of Western-made aircraft. In a similar case, Yugoslavia also received assistance in finding buyers for its hams, transmission towers, iron castings, and rubber bumper guards for motor vehicles also to offset its purchase of Western-made aircraft.

The implementation of an offset is difficult and time consuming, sometimes taking up to 20 years to complete. Frequently, "offsetters" try to use the products themselves; if they cannot, they seek third parties, such as

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1/ Interviews with industry officials.
2/ Ibid.
3/ Ibid.
4/ Ibid.

a trading company, to dispose of the products, or they try to network 1/ so they can exchange or share the offset credits with other companies. 2/

Magnitude of U.S. Countertrade

In the course of this investigation, data regarding countertrade (including military offsets) transactions were received from 523 U.S. corporations representing approximately $2 trillion in total 1984 sales, including export sales of $127 billion. Of the $127 billion in their total export sales (both military and nonmilitary) in 1984, only 5.6 percent, or $7.1 billion, involved sales contracts with an associated countertrade.

The Commission's questionnaires requested that respondents classify their countertrade data into three categories: nonmilitary countertrade, military-related sales with offset obligations of $2 million or less, and military-related sales with offset obligations of more than $2 million. These three categories are discussed both collectively and separately in this report.

During 1980-84, the total face value of all contracts associated with countertrade (including military offsets) decreased by 16 percent, from $8.4 billion in 1980 to $7.1 billion in 1984, as shown in figure 1. Total countertrade sales contracts ($28.8 billion during the period for 1980-84) 3/ consisted of nonmilitary countertrade (valued at $6.3 billion), military sales contracts with offset obligations of more than $2 million (valued at $21.9 billion), and military sales contracts with offset obligations of $2 million or less (valued at $562 million).

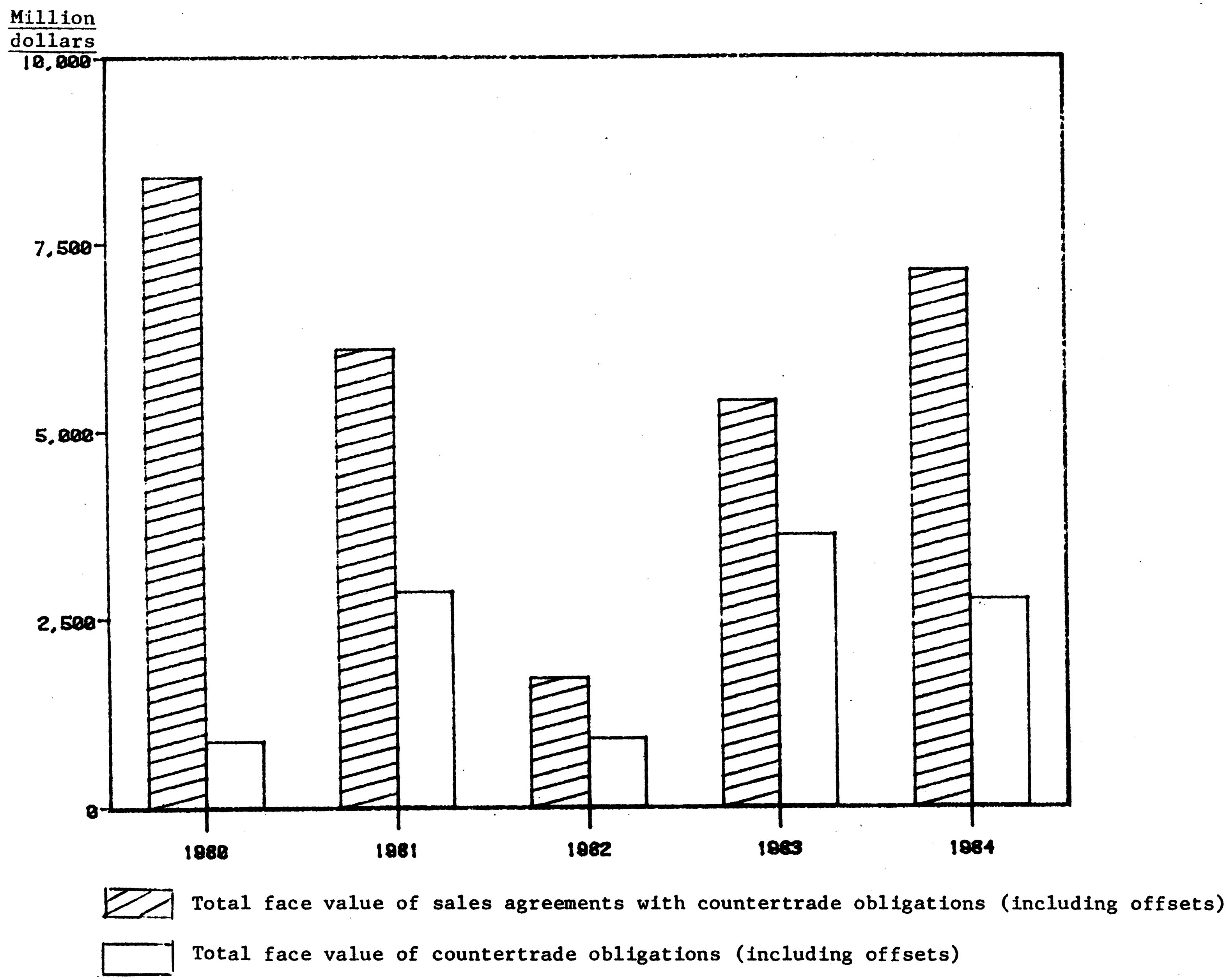
Although countertrade has long been a phenomenon in East-West trade, in recent years, as a result of the oil shocks, worldwide recession, and national debt crises, the use of countertrade has spread to more countries, both developed and developing. The North Altantic Treaty Organization (NATO) countries of Europe accounted for most of the sales agreements with U.S. companies during 1980-84 in which a countertrade (including military offset) was negotiated. Countertrade sales (valued at $8.9 billion) (table 1) to NATO countries were weighted heavily toward military offset sales reflecting the commonality of weapon systems within NATO. Sales agreements involving countertrade with Asia grew at a greater rate than those with the NATO countries of Europe, climbing from $1.7 billion in 1980 (or 20 percent of that year's total countertrade sales agreements) to $4.8 billion (or 67 percent of the total) in 1984 and totaled $9.0 billion during 1980-84. Sales agreements during 1980-84 with all other countries, principally Canada and Australia, accounted for $8.8 billion, or 31 percent of all countertrade sales agreements during the period. (For more detailed analyses, see section entitled "U.S. Regional Countertrade," page 46.)

1/ To "network" in this context means the sharing of information on investment, sales, purchases and trade opportunities related to countertrade (including military offsets) and offset export credits. For further information on the term "network," see John Naisbitt, Megatrends, New York, NY, 1982, pp. 193-205.

2/ Interviews with industry officials.

3/ Because of rounding, the figures do not add to the total $28.8 billion.

Figure 1.--Countertrade: Total face value of sales agreements with countertrade obligations and total face value of obligations (including military obligations), 1980-84.



Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 1.--Total face value of countertrade sales agreements (including military offsets) by regions, 1980-84

(In millions of dollars)

Region	1980	Percent of total	1984	Percent of total	1980-84	Percent of total
Europe:						
NATO countries 1/	2,752	33	1,516	21	8,893	31
Non-NATO countries 2/	191	2	277	5	1,280	4
Eastern bloc 3/	16	4/	55	4/	198	4/
Asia 5/	1,654	20	4,807	67	8,974	31
Latin America 6/	145	2	50	4/	652	2
All other 7/	3,656	43	434	6	8,771	31
Total	8,414	100	7,139	100	28,768	100

1/ Belgium, Denmark, Greece, Netherlands, Norway, Portugal, Spain, the United Kingdom, and West Germany.
2/ Austria, Finland, Sweden, Switzerland, and Yugoslavia.
3/ Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and the Soviet Union.
4/ Less than 0.5 percent.
5/ China, India, Indonesia, Israel, Japan, Lebanon, Pakistan, Philippines, Republic of Korea, Saudi Arabia, Singapore, Taiwan, and Turkey.
6/ Brazil, Colombia, Jamaica, and Mexico.
7/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

Data submitted also show that aerospace products 1/ were the single largest group of products involved in export sales agreements associated with countertrade (including military offsets), accounting for 70 percent ($20.2 billion) of all reported countertrade sales agreements negotiated during 1980-84. It is estimated that during the period investigated, U.S. export sales agreements associated with countertrade (including military offsets) for aerospace products 2/ were valued at 25.3 percent of the total

1/ According to the Aerospace Industries Association of America Inc., aerospace products include Standard Industrial Classification (SIC) codes 366, 372, 376, 381, and 382.
2/ The data for the sales agreements associated with countertrade represent intended exports; it is expected that most of the exports resulting from these sales agreements were exported during 1980-84.

U.S. aerospace export shipments of $79.8 billion. 1/ (See section entitled "Impact of Countertrade on U.S. Companies.")

Total sales involving countertrade (including offsets) declined during the period. Associated countertrade (including offset) obligation of U.S. companies fluctuated widely from lows of roughly $900 million in 1980 and 1982 to peaks of $3.6 billion and $2.8 billion in 1983 and 1984, respectively (fig. 2).

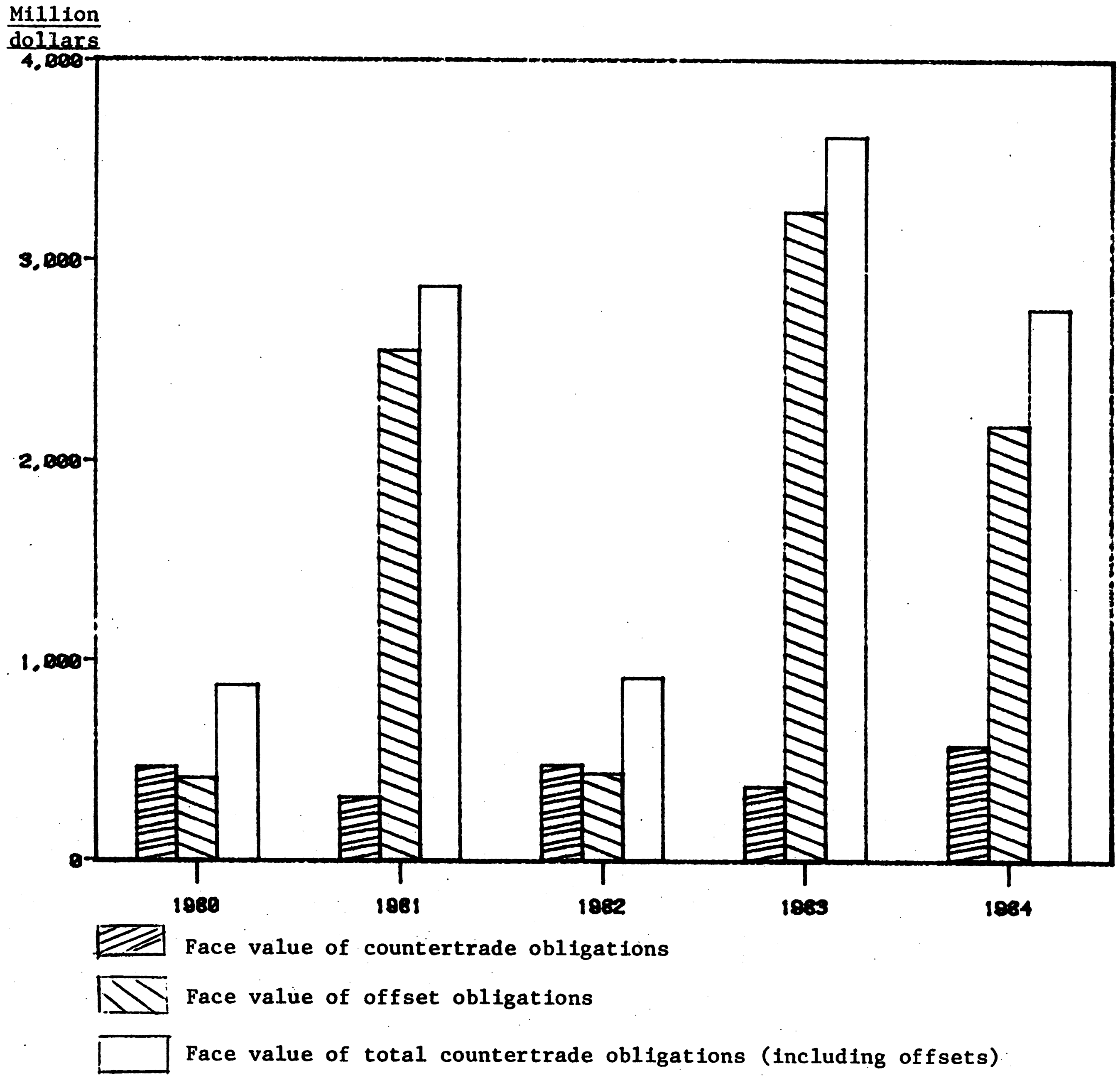
The total countertrade obligations as a share of the total export sales agreements involving countertrade (including offsets) rose from 11 percent in 1980 to more than 39 percent in 1984. The increase in the ratio of the obligation to the sales agreement reflects, in part, the increased competition for international sales among U.S. and foreign companies as well as increased countertrade demands on the part of foreign governments, according to industry sources. 2/

The value of nonmilitary countertrade obligations was greater than that of military obligations in 1980 and 1982. In all other years during 1980-84, military obligations far exceeded nonmilitary obligations. Military offset sales were especially prominent with "all other" countries (principally Australia and Canada) in 1981, and with Europe in 1983 and 1984 (see table 2). These peaks in military obligations coincide with the signing of large military contracts in these years.

1/ Aerospace Industries Association of America, Inc., Aerospace Facts and Figures, 1984/85, Washington, DC, p. 127. The 1984 value of exports, $15 billion, included in the total, was supplied by the Aerospace Industries Association. The value of actual U.S. shipments of aerospace products for exports approximate the value of sales agreements over a 1-year period; however, there may be some lag in actual export performance.

2/ Commission staff interviews with industry sources and statements made by industry officials at the hearing held before the U.S. International Trade Commission, May 30, 1985.

Figure 2.--Countertrade: Face value of countertrade obligations, offset obligations, and total obligations (including military offsets), 1980-84



Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 2.--Total face value of countertrade obligations (including military offsets) by regions, 1980-84

(In millions of dollars)

Region	1980	1981	1982	1983	1984
Nonmilitary:					
Europe	126	144	43	119	157
Asia	59	48	137	85	154
Latin America	70	30	288	58	43
All other	212	98	11	112	226
Subtotal	468	320	479	374	579
Military:					
Europe	159	575	158	3,064	1,221
Asia	236	553	98	160	799
All other	19	1,423	183	20	162
Subtotal	413	2,551	440	3,244	2,182
Nonmilitary and military:					
Europe	285	719	201	3,183	1,378
Asia	295	601	235	245	953
Latin America	70	30	288	58	43
All other	231	1,521	194	132	388
Grand total	881	2,871	919	3,618	2,761

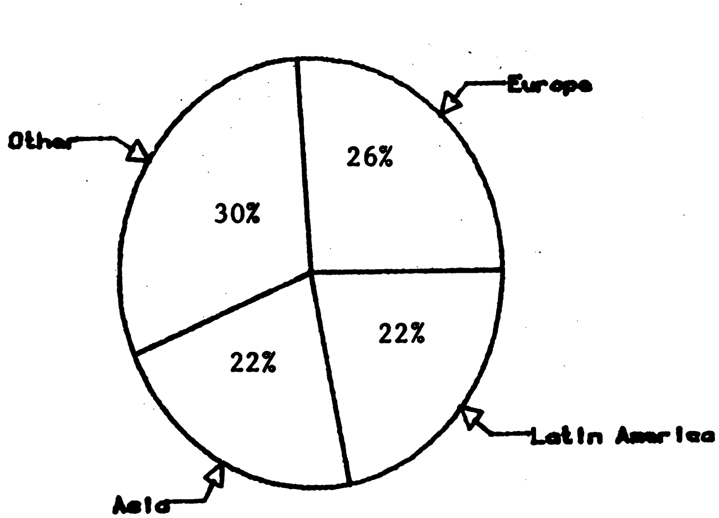
Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

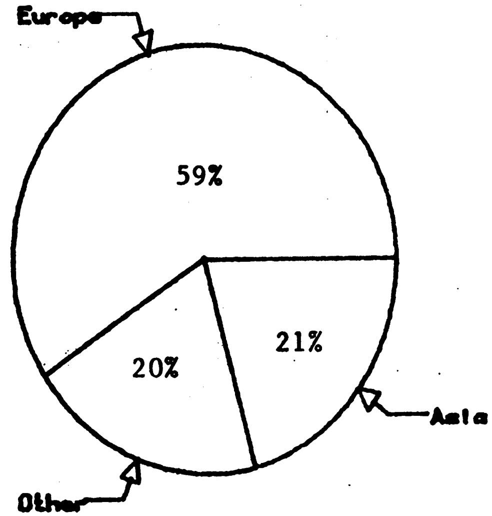
During 1980-84, the total countertrade obligation of $11.0 billion consisted of $2.2 billion for countertrade (excluding offsets) obligations, $8.7 billion for offset obligations of more than $2 million, and $108 million for offset obligations of $2 million or less. Europe accounted for both the largest share of U.S. countertrade obligations, with 52 percent ($5.8 billion) of the total obligation (fig. 3), and the largest share (36 percent) of total sales agreements involving countertrade.

NATO countries in Europe accounted for $4.8 billion in countertrade obligations with the United States during 1980-84, or 44 percent of total obligations. Virtually all of NATO obligations involved offsets associated with military related exports. Military offsets also made up a substantial portion of the obligations of non-NATO Europe, Asia, and all other countries, as shown in table 3. Offsets with NATO countries in Europe increased from 18 percent of 1980's total obligations to 41 percent of the total in 1984.

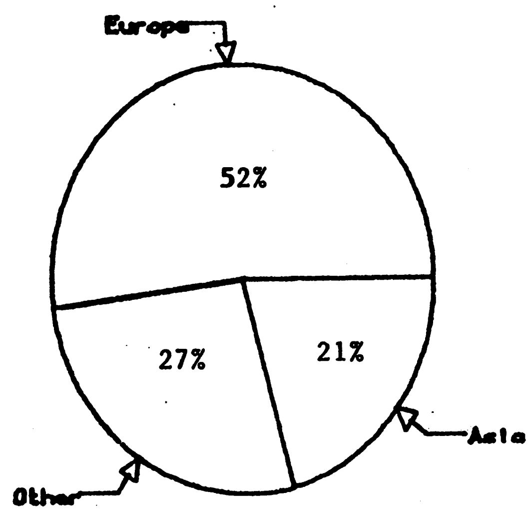
Figure 3.--Percentage of total countertrade obligations, by regions, 1980-84.



Total countertrade (excluding offset) obligations ($2.2 billion)



Total offset obligations ($8.8 billion)



Total countertrade obligations (including offsets) ($11.0 billion)

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 3.--Total face value of countertrade obligations (including military offsets) by regions, 1980-84

(In millions of dollars)

Region	1980	Percent of total	1984	Percent of total	1980-84	Percent of total
Europe:						
NATO countries: 1/						
Total----------	257	29	1,150	42	4,836	44
Offsets--------	159	18	1,128	41	4,638	42
Non-NATO countries: 2/						
Total----------	10	1	179	6	726	7
Offsets--------	-	-	93	3	539	5
Eastern bloc 3/--	18	2	49	2	204	2
Asia: 4/						
Total------------	295	34	953	35	2,329	21
Offsets----------	236	27	799	29	1,846	17
Latin America 5/---	70	8	43	2	489	4
All other: 6/						
Total------------	231	26	388	14	2,466	22
Offsets----------	19	3	162	6	1,807	16

1/ Belgium, Denmark, Greece, Italy, Netherlands, Norway, Portugal, Spain, the United Kingdom, and West Germany.

2/ Austria, Finland, Sweden, Switzerland, and Yugoslavia.

3/ Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and the Soviet Union.

4/ China, India, Indonesia, Israel, Japan, Lebanon, Pakistan, Philippines, Republic of Korea, Saudi Arabia, Singapore, Taiwan, and Turkey.

5/ Brazil, Colombia, Jamaica, and Mexico.

6/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

The large volume of associated countertrade obligations (especially military offsets) with Europe is, in part, attributable to the U.S. policy of enhancing the rationalization, standardization, and interoperability of weapons systems and equipment with NATO members and the U.S.-NATO joint commitment to the concept of a "Two-Way Street" in military trade. 1/

The value of countertrade obligations accounted for by Asian countries during 1980-84 was $2.3 billion, or about 21 percent of total countertrade obligations. Countertrade obligations with all other countries, mainly

1/ Office of the Secretary of Defense, International Coproduction/Industrial Participation Agreements, Report of the Department of Defense Task Group, Washington, DC, Aug. 15, 1983, pp. 3-5. See also Countertrade and Offsets In Search of a National Policy, Machinery and Allied Products Institute, Washington, DC, 1985, p. 35.

Australia and Canada, totaled almost 27 percent ($2.9 billion) of total obligations (fig. 3).

In contrast to the high percentage of aerospace products associated with countertrade (including military offsets) sales agreements, aerospace products represented only 20 percent of the total countertrade obligations. The data indicate that respondents involved in countertrade sales agreements tended to commit themselves to products other than aerospace products, such as agricultural chemicals, miscellaneous fabricated metal products, and petroleum and petroleum products. (See app. D, table D-1 and also the section entitled "Impact of Countertrade on U.S. Companies.")

During 1980-84, fulfillment of countertrade obligations (including military offsets) was valued at $4.7 billion, 1/ or 43 percent of the total obligation of $11.0 billion, rising irregularly from $682 million in 1980 to almost $1.5 billion in 1984 (see table 4). As with the countertrade obligation (including military offsets), the largest portion of fulfillment of the obligation was with Europe, which accounted for $2.2 billion, or 47 percent, of total fulfillment, followed closely by "all other" countries, mainly Australia and Canada, with $2.0 billion, or 43 percent of total fulfillment. The NATO countries in Europe accounted for the majority of total Western European fulfillment. As mentioned earlier, this is a result, in part, of the United States and NATO commitment to the concept of two way military trade. The value of fulfillment of countertrade obligations with Asian countries was only $547 million, or 12 percent, of total fulfillment.

1/ Data for the value of the fulfillment of the offset obligation of $2 million or less were not requested from respondents to the Commission's questionnaire; however, such data would not have changed the totals significantly because it is less than 0.1 percent.

Table 4.--Total face value of countertrade obligations fulfilled (including military offsets), by regions and years signed, 1980-84

(In millions of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	62	185	174	214	388
Non-NATO countries 2/	-	10	36	60	74
Subtotal	62	195	210	274	462
Eastern bloc 3/	237	201	122	150	249
Asia 4/	52	34	52	99	310
Latin America 5/	-	10	134	110	59
All other 6/	332	388	233	282	405
Total	682	827	750	914	1,484

1/ Belgium, Italy, Netherlands, Portugal, Spain, and West Germany.
2/ Austria, Finland, Sweden, and Yugoslavia.
3/ Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and Soviet Union.
4/ China, India, Indonesia, Israel, Japan, Lebanon, Pakistan, Philippines, Republic of Korea, and Turkey.
5/ Brazil, Colombia, Jamaica, and Mexico.
6/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the United States International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

Aerospace products were the major products involved in fulfilling countertrade obligations, accounting for $2 billion, or 43 percent, of the total $4.7 billion fulfilled during 1980-84. In terms of the countertrade obligation, this represents 63 percent of the total reported aerospace product obligation having been fulfilled during 1980-84. The large percentage of the aerospace product obligation fulfilled is, in part, attributable to the fact that during the early period of the timeframe investigated, the obligations were heavily weighted toward aerospace products. In later years, aerospace products became less prominent. In addition, the earlier obligations were signed with countries that had aerospace capabilities. Obligations signed later were with countries that had somewhat less aerospace capabilities. (See section entitled "Impact of Countertrade on U.S. Companies.")

Countertrade (excluding military offsets)

U.S. firms involved in countertrade reported nonmilitary countertrade sales agreements of $6.3 billion during 1980-84. The reported total face value of the sales agreements decreased by 33 percent, from $1.8 billion in

1980 to $1.2 billion in 1984, and was as low as $982 million in 1982, as indicated in the following tabulation (in millions of dollars): 1/

Year	Sales agreement value	Average face value
1980	$1,846	$102.6
1981	1,176	53.4
1982	983	41.0
1983	1,029	23.9
1984	1,248	26.5
Total or average	6,282	49.5

This overall decline in the face value of sales agreements involving nonmilitary countertrade reflects the worldwide recession and the strength of the U.S. dollar, making U.S. exports less price competitive. During this period, the annual average face value of the sales agreements also decreased steadily from $103 million per contract to $27 million in 1984. This decline was primarily due to a greater number of small- and medium-sized firms entering into countertrade agreements. In addition, it reflects an increase in international competition and a catchup process whereby smaller companies began to develop a countertrade capability.

The largest concentration (27 percent) of nonmilitary countertrade sales agreements were with Asian countries, followed by Europe, with 24 percent. The shares held by Western Europe and Eastern Europe were 21 and 3 percent, respectively, as shown in the following tabulation: 2/

Region	Total value sales agreements, 1980-84 (million dollars)	Share of total value of sales agreements (percent) 1/
Asia	$1,720	27
Europe:		
NATO countries	636	10
Non-NATO countries	685	11
Eastern bloc	198	3
Latin America	652	10
All other	2,391	38
Total	6,282	100

1/ Because of rounding, figures may not add to the totals shown.

During 1980-84, sales agreements involving counterpurchase 3/ were by far the most frequently mentioned type of nonmilitary countertrade. They accounted for 91 percent, or $5.7 billion, of total nonmilitary countertrade sales agreements. Although counterpurchase agreements are sometimes difficult

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1/ See also app. E, table E-1.
2/ Table E-1.
3/ See section of this report on "Elements of Countertrade" for a definition of counterpurchase, compensation, and barter.

to negotiate and complete, they have become more prevalent because they usually require less time and effort on the part of the Western firm than other types of reciprocal trade sales agreements.

Annual counterpurchase sales export agreements (excluding military sales agreements) declined steadily from a high of $1.7 billion in 1980 to a low of $844 million in 1982 and increased slightly to $1.2 billion in 1984. This represented a 31-percent decline over the 5-year period (table E-2). Compensation and barter sales agreements accounted for 5 and 2 percent, respectively, of the value of total sales agreements involving U.S. nonmilitary countertrade.

Aircraft and parts and other aerospace products were the main products involved in nonmilitary countertrade export sales contracts, accounting for 65 percent of the total reported value of such sales agreements. This large concentration of aerospace products is attributable, in part, to the fact that such products constitute a major portion of U.S. exports and to the fact that the United States generally has a leading edge in technology in aerospace products. In addition, in order to meet foreign competition in this area, U.S. companies have had to accept offsets in these products.

After the sales agreement has been negotiated and signed, the firm must then negotiate the countertrade obligation. The countertrade obligation is a commitment to perform some reciprocal trade transaction, e.g., buy and/or market the foreign country's goods and services, transfer technology, or take back a resultant product.

The total face value of countertrade obligations reported rose irregularly from $468 million in 1980 to $579 million in 1984, or by 24 percent (table 5). The share of obligations with Asia rose from 13 percent of the total face value of total nonmilitary countertrade obligations in 1980 to 27 percent in 1984. This increase from $59 million in 1980 to $154 million in 1984 represents over a 100-percent increase in the obligation. This trend is, in part, attributable to China's opening its door to foreign trade, Indonesia's 100 percent countertrade requirement, and the lack of Philippines hard-currency reserves.

Countertrade obligations with Latin America declined by 39 percent, from $70 million in 1980 to $43 million in 1984, peaking at $288 million in 1982. This increase in 1982 was, in part, due to Mexico's currency devaluation with its related import and export restrictions and blocked currency.

Table 5.--Total face value of countertrade obligations (excluding military offsets), by regions and years signed, 1980-84

(In thousands of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	98	47	31	-	22
Non-NATO countries 2/	10	50	9	32	86
Subtotal	108	97	40	32	108
Eastern bloc 3/	18	47	3	87	49
Asia 4/	59	48	137	85	154
Latin America 5/	70	30	288	58	43
All other 6/	212	98	11	112	226
Total	468	320	479	374	579

1/ Belgium, Italy, Netherlands, Portugal, Spain, and West Germany.
2/ Austria, Finland, Sweden, and Yugoslavia.
3/ Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and Soviet Union.
4/ China, India, Indonesia, Israel, Japan, Lebanon, Pakistan, Philippines, Republic of Korea, and Turkey.
5/ Brazil, Colombia, Jamaica, and Mexico.
6/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

As with the sales agreement, counterpurchase obligations 1/ were by far the most frequently mentioned type of nonmilitary countertrade obligation, accounting for 84 percent of the total obligation during 1980-84 (table 6). With some fluctuations, the annual counterpurchase obligation increased from $432 million in 1980 to $506 million in 1984. Counterpurchase obligations are more prevalent, because they generally require less participation by the Western firm than other types of countertrade obligations.

Like the sales agreement, the largest product category involved in a nonmilitary countertrade obligation was aircraft and parts. Obligations in this category declined from a high of $185 million in 1980 to $59 million in 1984 and totaled $574 million during 1980-84.

1/ See section of this report entitled "Elements of Countertrade" for a definition of counterpurchase, compensation, and barter.

Table 6.--Total face value of countertrade obligations (excluding military offsets), by types of countertrade and years signed, 1980-84

(In thousands of dollars)

Type of countertrade	1980	1981	1982	1983	1984
Barter	2,292	12,677	10,523	65,415	28,452
Compensation (including coproduction, technology transfer, and subcontractor production)	22,900	2,000	129,595	12,536	23,000
Counterpurchase	432,441	305,644	333,429	292,099	506,331
Blocked currency:					
Barter	-	-	5,100	60	-
Unspecified	-	-	-	3,301	-
Best efforts (unspecified countertrade)	10,000	-	-	-	15,000
Unspecified	-	-	-	-	6,420
Total	467,633	320,322	478,647	373,411	579,203

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

During 1980-84, the ratio of countertrade obligations to sales agreement ranged from a low of 45 percent in 1980 to a high of 127 percent in 1981, as shown in the following tabulation:

Year	Ratio 1/ of countertrade (excluding offset) obligation to sales agreement	Ratio 2/ of total annual (excluding offset) countertrade obligations to total annual sales agreements
1980	45	25.3
1981	127	27.2
1982	94	48.7
1983	100	36.2
1984	92	46.4

1/ The ratio of countertrade obligation to sales agreement was calculated for each contract and then all ratios of such transactions for a given year were averaged to yield an average of those ratios.

2/ Total face value of countertrade obligation divided by total face value of sales agreement.

Between 1982 and 1984, the average ratio (see col. 1 of the preceding tabulation) was over 90 percent. These ratios reflect a trend towards smaller, more numerous contracts in which the countertrade obligation constituted a significant portion of the sales agreement. The ratio of the total annual countertrade obligations to the total annual sales agreements (see col. 2 of the preceding tabulation) was 25.3 percent in 1980 and increased to a high of 48.7 percent in 1982. In 1983, this ratio declined to 36.2 percent and rose again in 1984 to 46.4 percent. The increase in the ratio over the 5-year period reflects a higher countertrade obligation because of increased demand and international competition willing to countertrade. In this investigation, it was found that there were numerous contracts with Eastern Europe in which the total value of the sales agreement was small but the ratio of the countertrade obligation to the sales agreement approached 100 percent, and, in other instances, was significantly greater.

The third element associated with a sales agreement involving countertrade is the fulfillment of the obligation. Total fulfillment of the countertrade obligation (excluding military offsets) rose from $325 million in 1980 to $474 million in 1984, or by 46 percent (table 7). As with the countertrade obligation (excluding military offsets), the largest portion of fulfillment was with Europe, which accounted for $1.1 billion, or 57 percent of total fulfillment. The majority of European fulfillment was with Eastern Europe, which reflects, in part, the longstanding experience Eastern Europeans have with countertrade.

Table 7.--Total face value of countertrade obligations fulfilled (excluding military offsets), by regions and years signed, 1980-84

(In millions of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	2/	22	22	9	7
Non-NATO countries 3/	-	8	13	30	20
Subtotal	2/	30	35	39	27
Eastern bloc 4/	237	201	122	150	249
Asia 5/	3	3	7	19	48
Latin America 6/	-	10	134	110	59
All other 7/	86	122	75	57	92
Total	325	366	372	374	474

1/ Belgium, Italy, Netherlands, Portugal, Spain, and West Germany.
2/ Less than $0.5 million.
3/ Austria, Finland, Sweden, and Yugoslavia.
4/ Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and Soviet Union.
5/ China, India, Indonesia, Israel, Japan, Lebanon, Pakistan, Philippines, Republic of Korea, and Turkey.
6/ Brazil, Colombia, Jamaica, and Mexico.
7/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

The largest product category involved in fulfillment of the nonmilitary countertrade obligation was aircraft and parts, accounting for 15 percent of total fulfillment. Aircraft and parts accounted for 48 percent of total fulfillment of the nonmilitary obligation during the 5-year period.

On the basis of current reported contracts, total U.S. nonmilitary countertrade commitments are expected to reach $575 million in 1985, and it is estimated that during 1989-2000, such commitments will total $2.3 billion This includes only those contracts currently reported.

Offsets

Offset data based on sales agreements with associated offset obligations of $2 million or less and those of more than $2 million were requested from respondents. Submitted offset data reveal that contracts with offset obligations of $2 million or less (accounting for 1 percent of total sales agreements involving offsets) during 1980-84 have been associated primarily with sales of U.S. components for weapons systems developed by foreign industries. Those contracts associated with offset obligations of more than $2 million (accounting for 98 percent of total offset sales agreements) were primarily for major weapons systems that were made in the United States and sold overseas.

During 1980-84, U.S. military export sales increased steadily from $7.0 billion (1980) to $11.2 billion (1984), or by 61 percent. Nonetheless, the value of the reported export sales agreements associated with an offset obligation fluctuated from a peak of $6.6 billion in 1980 to a low of $732 million in 1982, but declined overall by 10 percent during 1980-84, as shown in the following tabulation:

Year	Collective U.S.military export sales (million dollars)	Collective face value of sales contracts associated with a military related sale involving offsets (million dollars)	Ratio of sales contract with a military related export sale to total U.S. military export sales (percent)
1980	6,964	6,568	94
1981	8,907	4,919	55
1982	10,315	732	7
1983	10,428	4,377	42
1984	11,222	5,890	52
Total or average	47,835	22,486	47

The severe annual fluctuations in the value of reported military related export sales is a result of the sporadic flow of major weapon system purchases by foreign governments. This is due to the fact many foreign governments purchase a new major weapons system only once in a decade. Consequently, a large annual value of U.S. military related reported export sales contracts with associated offsets by U.S. defense system manufacturers is a reflection of several major foreign purchases in that particular year. The converse is also true in years where only a few major weapon systems export sales with offsets were reported. In 1980, 94 percent of total value of U.S. military export sales had some type of associated offset obligation (as shown in the previous tabulation), but, the offset obligation represented only 6 percent of the value of the total export sales contracts as shown in the following tabulation:

Year	Collective offset obligation associated with a military export sale (million dollars)	Ratio of offset obligation of sales contract associated with a military export sale (percent)
1980----------------	413	6
1981----------------	2,551	52
1982----------------	440	60
1983----------------	3,244	74
1984----------------	2,182	37
Total or average------	8,830	39

By 1984, the value of sales contracts with offsets dropped to 52 percent of total U.S. military export sales, but the offset obligation rose slightly to 37 percent. In 1982, there was a notable decrease in the value of exports sales contracts and associated offset obligations that paralleled the worldwide recession. 1/ According to industry sources, it is likely that the decline in foreign purchasing power associated with the high value of the dollar from 1982 to 1984 accelerated the need and corresponding governments' demand for offsets. Offset demands increased, in part, in order to help purchasing countries balance deteriorating current accounts and check the outflow of foreign exchange. Other reasons for increased offset demands include the desire for economic development through technology transfer and the desire for development of an industrial base.

After the sales agreement and the obligation, the third element of an offset transaction is fulfillment of the obligation. During 1980-84, reported military-related offset fulfillment reached $2.7 billion. 2/ The total offset obligation was reported at $8.8 billion. 3/ Thus, $6.1 billion remains to be fulfilled.

1/ Most countries experienced a recession during 1982. The aggregate output of the industrialized countries declined in 1982 for the first time since 1975 and unemployment rose to the highest levels since before World War II. World trade decreased by 2.5 percent in 1982. See International Monetary Fund Annual Report, 1983, ch. I.

2/ Fulfillment data were not requested from respondents that had sales contracts with offset obligations of $2 million or less. Therefore, there are no data included for these contracts.

3/ The $108 million required to satisfy offset obligations of $2 million or less is not included in this figure, because respondents were not requested to give data on the fulfillment of this obligation. Addition of this amount would make the unfilled portion of the obligation slightly higher.

The average period allowed for fulfillment of offsets associated with military sales tended to vary in proportion to the value of the offset obligation, that is, the higher the offset obligation the longer the period allowed for fulfillment. The average fulfillment period for offset obligations of $2 million or less was 45 months, and for offsets of more than $100 million, (unweighted) fulfillment averaged 158 months (fig. 4). The average fulfillment time allowed for all offset obligations was 61 months.

Sales contracts involving offset obligations of $2 million or less. 1/--Approximately 25 percent of the respondents to the Commission's questionnaire had export sales contracts that involved offset obligations of $2 million or less. During 1980-84, the face value of sales agreements associated with the offset obligations of $2 million or less increased overall by more than 100 percent. The total annual value fluctuated irregularly during the 5-year period as a result of the uneven flow of military purchases, rising from $78 million in 1980 to $101 million in 1981 before dropping by 30 percent, to $70 million, in 1982. The reported value then increased to a high of $160 million in 1983, or by 129 percent over the value of the previous year, and dropped slightly in 1984, as shown in the following tabulation:

Year	Total face value of sales agreements with offset of $2 million or less (million dollars)
1980	$78
1981	101
1982	70
1983	160
1984	156

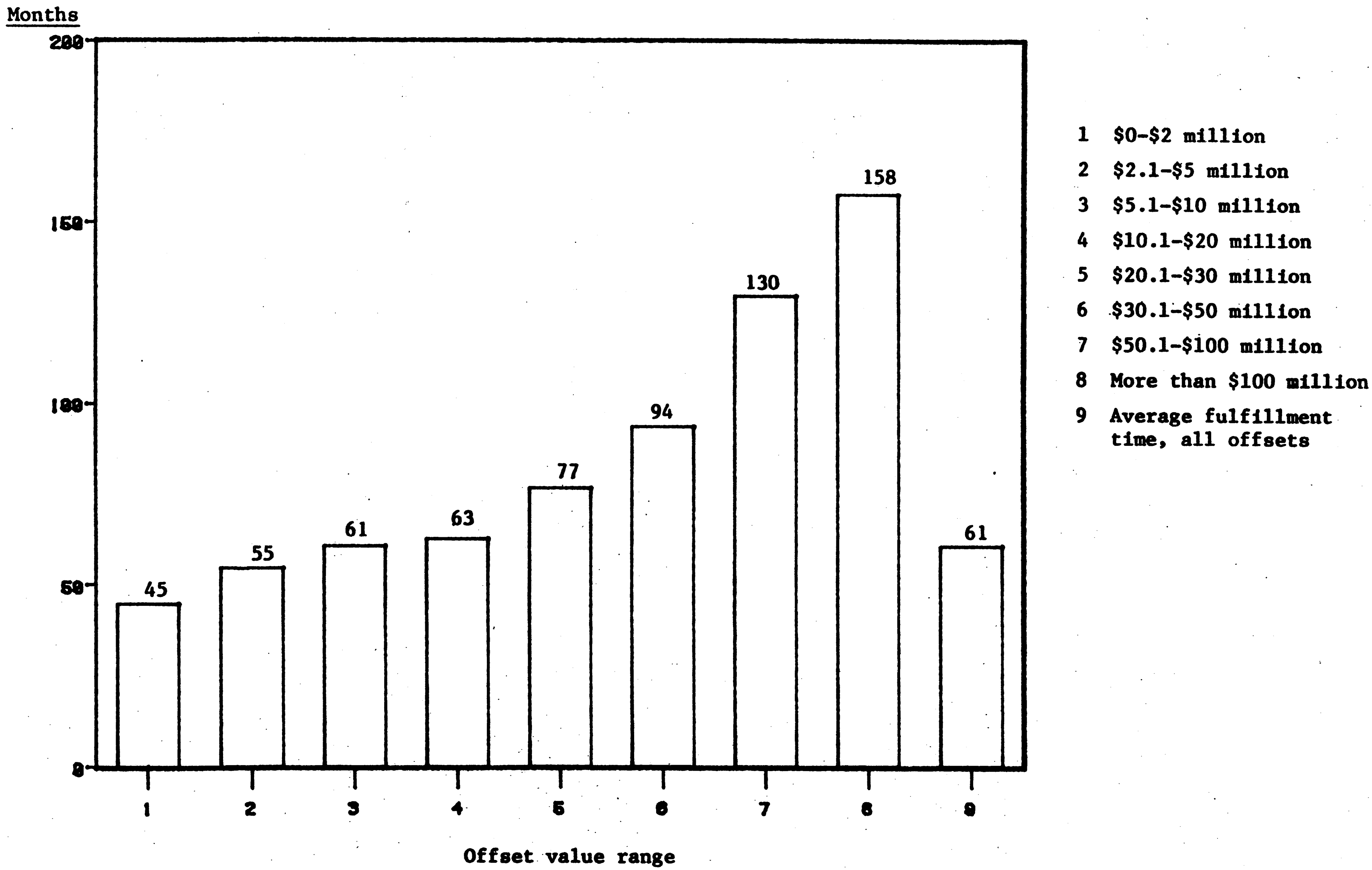
The increase of more than 100 percent in the total face value of the sales contracts during 1980-84 reflects increased sales by United States arms manufacturers of the components and services used for weapons systems developed by foreign industries, particularly, the established arms industries in Europe and the newer arms-exporting nations in Asia.

In addition, industry sources indicated that there is a trend for virtually all new export sales agreements to contain some type of offset requirement, which subsequently is subject to negotiation between the U.S. firm and the host country organization. As a practical matter, the offset requirement will either be negotiated to extend over a longer implementation period or subsequently be negotiated out of the sales agreement.

As with the nonmilitary sales agreements, the average annual face value of reported sales agreements associated with offset obligations of $2 million

1/ In the Commission's questionnaire, data for offset obligations of $2 million or less were gathered separately from larger offset obligations. The larger offset obligations will be presented in a separate section.

Figure 4.--Average number of months allowed for fulfillment of offset obligations, by ranges of offset commitment value, 1980-84.



Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

or less, per sales contract, declined steadily from $3.4 million in 1980 to $2.1 million in 1984, or by 38 percent, as shown in the following tabulation:

Year	Average total face value (million dollars)
1980	$3.4
1981	2.7
1982	2.2
1983	2.6
1984	2.1

Sales agreements associated with offset obligations of $2 million or less, highlight the fact that such trade is being carried out by industrialized and newly industrialized countries, particularly in Asia (table 8). During 1980-84, 56 percent of the value of sales contracts associated with offset obligations of $2 million or less were with Asian countries. Nonetheless, U.S. sales agreements with Europe increased 174 percent during the same 5-year period from $12 million in 1980 to $33 million in 1984.

Table 8.--Total face value of sales agreements with offset obligations of $2 million or less, by regions and years signed, 1980-84

(In millions of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	12	43	21	17	16
Non-NATO countries 2/	-	-	9	3/	17
Subtotal	12	43	30	17	33
Asia 4/	42	41	28	140	64
All other 5/	24	17	11	3	58
Total	78	101	70	160	156

1/ Denmark, Greece, Netherlands, Norway, Spain, and the United Kingdom.
2/ Sweden and Switzerland.
3/ Less than $0.5 million.
4/ India, Israel, Japan, Republic of Korea, Saudi Arabia, and Taiwan.
5/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

Communications equipment (aerospace products) accounted for the largest category of products involved in sales agreements associated with offset obligations of $2 million or less. As shown in the following tabulation, as well as table D-1, communications equipment sales ranged from 71 percent of total sales ($78 million) in 1980, or $55 million, to 50 percent of total sales ($156 million) in 1984, or $78 million:

Year	Sales agreements' face value for communications equipment for offset obligations of $2 million or less (million dollars)
1980	55
1981	57
1982	29
1983	70
1984	78

The offset obligations of $2 million or less more than doubled in value from 1980 to 1984 (table 9). The majority of the offset obligations of U.S. firms were with Asian countries, accounting for 58 percent of the total offset obligation of $108 million for the 5-year period.

Table 9.--Total face value of offset obligations of $2 million or less, by regions and years signed, 1980-84

(In millions of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	2	4	3	4	4
Non-NATO countries 2/	-	-	1	3/	10
Subtotal	2	4	4	4	14
Asia 4/	9	6	7	24	17
All others 5/	4	3	3	1	7
Total	14	13	14	29	38

1/ Denmark, Greece, Netherlands, Norway, Spain, and the United Kingdom.
2/ Sweden and Switzerland.
3/ Less than $0.5 million.
4/ India, Israel, Japan, Republic of Korea, Saudi Arabia and Taiwan.
5/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

As shown in the following tabulation, the average ratio of offset obligations of $2 million or less to the sales agreement increased steadily during of 1980-84, from 21.9 percent in 1980 to 35.6 percent in 1984:

Year	Average of ratio 1/ of offset obligations of $2 million or less to sales agreement (percent)
1980	21.9
1981	21.9
1982	24.1
1983	25.6
1984	35.6

1/ The ratio of offset obligations of $2 million or less to sales agreement was calculated for each contract, and then all ratios of such transactions for a given year were averaged to yield an average of those ratios.

The data indicate that more U.S. firms were accepting larger obligations in the face of increased international competition for military-related export sales.

Sales contracts involving offset obligations of more than $2 million.--During 1980-84, two distinct trends occurred in total sales with offset obligations of more than $2 million. Such sales declined by 90 percent, from a high of $6.5 billion in 1980 to a low of $663 million in 1982. The total value then increased in 1983 to $4.2 billion and again to $5.7 billion in 1984, (table 10). The substantial increase in sales agreements during 1982-84 reflects foreign governments' major arms updates, increased weapons systems procurement, and support of local arms industries.

Table 10.--Total value of goods and services to be supplied in sales agreements in which offsets of more than $2 million were negotiated by regions, and years contracts signed, 1980-84

(In millions of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	2,422	831	191	3,322	1,382
Non-NATO countries 2/	158	328	31	52	-
Subtotal	2,580	1,159	222	3,374	1,382
Asia 3/	1,293	796	35	578	4,237
All others 4/	2,617	2,863	406	266	116
Total	6,490	4,818	663	4,218	5,735

1/ Belgium, Denmark, Greece, Netherlands, Norway, Spain, and the United Kingdom.
2/ Sweden, Switzerland, and Yugoslavia.
3/ Israel, Japan, Philippines, Republic of Korea, Singapore, and Turkey.
4/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission, except as noted.

Note.--Because of rounding, figures may not add to the totals shown.

During 1980-84, Europe accounted for 40 percent ($8.7 billion) of total sales agreements associated with offset obligations of more than $2 million; those with Asia and all other countries accounted for 32 and 29 percent ($6.9 billion and $6.3 billion), respectively (table 10). Annual sales agreement fluctuations are, in part, a result of periodic sales of major weapons systems and updates. The sharp decrease in sales to Europe in 1984, for instance, can be explained by the strong U.S. dollar and a growing preference among Europeans for European weapon systems. 1/ European domestic arms production and cooperation arrangements among European producers have increased, resulting in fewer sales opportunities for U.S. systems in Europe. 2/ European cooperation stems in part from (1) a "mismatch of European and U.S. industrial capability and scale," (2) differences in government policy roles and their relationship to national industries, and (3) a perception by some Europeans that state-of-the-art technology transfer from the United States has been inhibited as a result of U.S. firms' desire to maintain a competitive advantage. 3/

Asian sales agreements with offset obligations of more than $2 million increased from $1.3 million in 1980 to $4.2 million in 1984, or by 228 percent. This increase reflects, in part, the spreading use of offsets in the area, the difficulty of paying for imports through conventional means, external debt problems, and a desire for transfer of technology.

The most significant portion of sales agreements associated with offsets of more than $2 million involved the sale of aircraft and parts. In 1980, sales of aircraft and parts accounted for 84 percent, or $5.4 billion, of the total $6.5 billion in sales agreements. During 1981-84, the value declined irregularly, reaching $1.7 billion, or 37 percent of the total sales agreement face value ($5.7 billion) in 1984 (see pages 58 and 59 for total aircraft and parts sales, SIC code 372).

Sales agreements with total offset obligations of more than $2 million involved in satisfying the sales agreements ranged from $399 million in 1980 to $2.1 billion in 1984. As shown in table 11, the face value of offset obligations with countries in Asia amounted to $227 million in 1980, or 57 percent, of the total obligation in that year. Obligations with Europe accounted for only $157 million, or 39 percent, of the total value in 1980. By 1984, however, Europe's share of the total value had increased to 56 percent, or $1,207 million, whereas Asia's share had declined to 36 percent of the total.

Aircraft, guided missiles and space vehicles and parts were the category of products most likely to be involved in the offset obligation, just as they accounted for the greatest portion of the face value of sales agreement. Although the signed offset obligations of these products were concentrated in 1981 and 1984, the implementation of these obligations were reported to be spread out over several years. In 1984, this category of products accounted for 25 percent of the total value of all goods and services involved in

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1/ "U.S. Military Continues Push for NATO Armaments Cooperation," Aviation Week & Space Technology, June 3, 1985, pp. 240-242.

2/ Ibid.

3/ Ibid.

Table 11.--Collective value of offset obligations 1/ of more than $2 million, by regions and years offset agreements were entered into, 1980-84

(In millions of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 2/	157	271	49	3,020	1,124
Non-NATO countries 3/	-	300	105	40	83
Subtotal	157	571	154	3,060	1,207
Asia 4/	227	547	91	136	782
All others 5/	15	1,420	180	19	155
Total	399	2,538	426	3,215	2,144

1/ Reported offset obligations signed prior to or after the reporting period of 1980-84 are not included in this data even though they may have been credited to a sales agreement that was signed during 1980-84.

2/ Belgium, Denmark, Greece, Netherlands, Norway, Spain, and the United Kingdom.

3/ Sweden, Switzerland, and Yugoslavia.

4/ Israel, Japan, Philippines, Republic of Korea, Singapore, and Turkey.

5/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

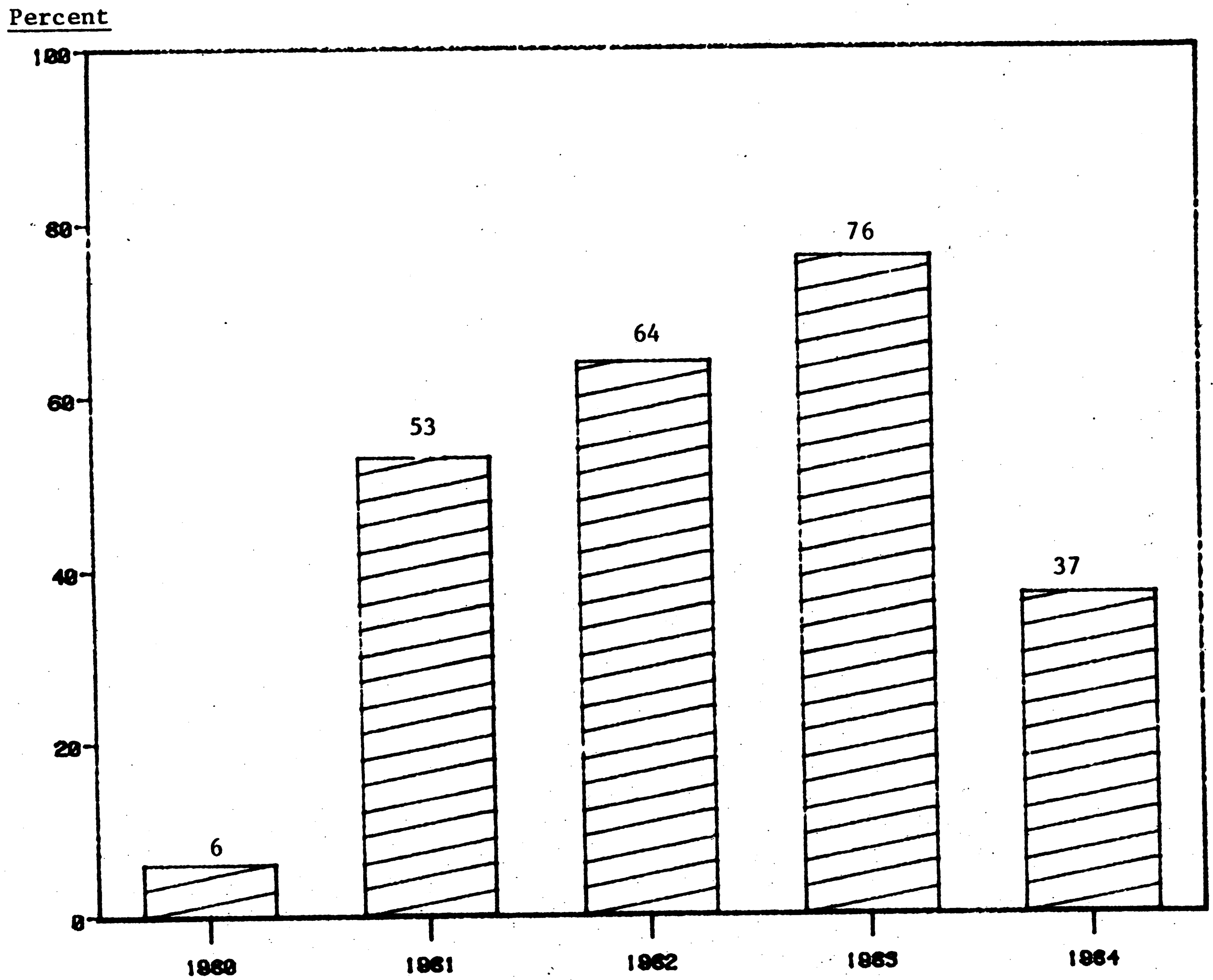
satisfying offset obligations of more than $2 million, as shown in the following tabulation:

Year	Face value of offset obligations of more than $2 million for aircraft and parts, guided missiles and space vehicle and parts (million dollars)
1980	286
1981	1,261
1982	52
1983	39
1984	785

The extreme fluctuations of the face value of offset obligations of more than $2 million for aircraft and parts are attributable, in part, to the signing of several major offset agreements for weapon systems beginning in 1981 and 1984.

The average ratio of the offset obligations of more than $2 million to the sales agreement increased steadily from 6 percent in 1980 to a high of 76 percent in 1983 and then declined to 37 percent in 1984 (fig. 5). Submitted

Figure 5.--Countertrade: Average ratio of offset obligations of more than $2 million to sales agreement, by year sales agreements were signed, 1980-84.



Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

data reveal that during 1980-83, U.S. firms were accepting larger offset obligations in the face of increased international competition for military-related export sales. The decline in the obligation in 1984 was not an indication of a declining obligation trend, but rather a reflection that obligations associated with sales in 1984 had not been signed.

During 1980-84, direct offset obligations were valued at $4.8 billion, and indirect offset obligations were valued at $3.6 billion. 1/ Subcontractor production accounted for 61 percent of the direct offset obligations, followed by coproduction commitments, which accounted for 32 percent. In 1980, subcontractor production commitments amounted to $338 million, or 91 percent, of the total direct offset obligation in that year. During 1981-84, subcontractor production fluctuated between extremes of $1.3 billion (1981) and $116 million (1982) (table 12). During 1980-84, coproduction commitments fluctuated between extremes of $29 million in 1980 and $770 million in 1984. According to industry sources, this increase in overseas production is attributable, in part, to U.S. manufacturers' attempts to upgrade the quality of goods to be produced under offset obligations. The increase is also related to the growing demand of many foreign aerospace industries for state-of-the-art production.

1/ See page 7 for an explanation of direct and indirect offsets.

Table 12.--Face value of goods and services that were obliged in satisfying offsets, by types of offset and years offset agreements were entered into, 1980-84

(In millions of dollars)

Type of offset	1980	1981	1982	1983	1984
Direct:					
Coproduction	29	532	141	45	770
Licensed production	-	-	-	16	50
Licensed production and co-production	-	-	-	-	-
Subcontractor production	338	1,271	116	640	521
Subcontractor production and technology transfer	1	3	-	-	-
Technology transfer	-	1/	3	6	8
Technology transfer and licensed production	5	-	-	-	-
Direct offsets but not yet specified	-	184	3	-	81
Total	373	1,990	263	707	1,430
Indirect:					
Foreign investment	-	-	-	5	32
Technology transfer	-	-	5	6	1/
Countertrade	14	302	73	39	383
Indirect offsets but not yet specified	-	161	1/	2,448	159
Total	14	463	78	2,498	574
Not yet specified:					
Contractually bound to not disclose details other than actual amount	-	75	-	-	-
Combination of direct and indirect offsets	-	-	80	7	4
Combination of direct and indirect offsets, not yet specified	12	3	-	3	45
Other	-	6	3	-	92
Total	12	84	83	10	141
Grand total	399	2,538	426	3,215	2,144

1/ Less than $0.5 million.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

The third phase in an offset agreement after the signing of the initial export sales contract and agreeing to an offset obligation is the fulfillment of the obligation. Reported fulfillment of offset obligations negotiated during 1980-84 rose from $357 million (1980) to $1.0 billion (1984), or by 183 percent (table 13). The majority of the fulfillment of the obligation was with Europe, which accounted for $1.1 billion, or 39 percent, of total fulfillment. As previously mentioned, the large European fulfillment reflects, in part, the U.S.-NATO joint commitment to the concept of a "Two Way Street" in military trade. During 1980-84, Asian fulfillment rose steadily from $49 million in 1980 to $262 million, or by over 400 percent. This increase is attributable to the expansion in the use of offsets in this region, the difficulty of paying for imports through conventional means, and the desire for transfer of technology.

Table 13.--Total face value of offset obligations of more than $2 million fulfilled, by regions and years contracts signed, 1980-84

(In millions of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	62	163	152	205	381
Non-NATO countries 2/	-	2	23	30	54
Subtotal	62	165	175	235	435
Asia 3/	49	31	45	80	262
All others 4/	246	266	158	225	313
Total	357	461	378	540	1,010

1/ Belgium, Denmark, Greece, Netherlands, Norway, Spain, and the United Kingdom.
2/ Sweden, Switzerland, and Yugoslavia.
3/ Israel, Japan, Philippines, Singapore, Republic of Korea, and Turkey.
4/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note: Because of rounding, figures may not add to the totals shown.

Aircraft and parts accounted for the single largest product involved in offset fulfillment, increasing from $277 million in 1980 to $441 million in 1984, as shown in the following tabulation:

Year	Fulfillment of the offset obligation of $2 million or more for aircraft and parts (million dollars)
1980	277
1981	303
1982	136
1983	249
1984	441

Of the more than $2.7 billion in offset obligations fulfilled during 1980-84, $1.5 billion, or 56 percent, of the total was fulfilled through direct offset arrangement, and the remainder ($1.2 billion) was fulfilled through indirect offsets (table E-3). Most of direct offset fulfillment (61 percent) was accounted for by subcontractor production in foreign countries; and about one-third was accomplished through coproduction arrangements with foreign-based entities.

Although most of the offset obligations are assumed by the prime contractors, in many instances, the major subcontractors for a particular system will be asked to share some portion of the burden of the prime offset obligation. This shared arrangement is often advantageous for both the prime and the subcontractor, since both have much to gain if the prime is awarded the export sales contract. The subcontractor may often negotiate an offset obligation directly with the buyer on behalf of the prime.

During 1980-84, the value of offset obligations of more than $2 million that was assumed by subcontractors to companies that were parties to the original sales' agreements totaled $977 million, as shown in the following tabulation:

Type of offset	Value of offsets assumed by subcontractors (million dollars)
Direct:	
Coproduction	131.0
Subcontractor production	331.0
Overseas investment	-
Technology transfer	-
Direct offsets but not yet specified	3.2
Indirect:	
Foreign investment	-
Technology transfer	-
Countertrade	207.7
Indirect offsets but not yet specified	299.3
Other:	
Indirect, but not known	5.0
Total	977.2

Of that total, 34 percent will be fulfilled by foreign subcontractor production. Countertrade obligations will fulfill $208 million, or 21 percent, of the total subcontractor obligations. Subcontractors' coproduction will account for $131 million, or 13 percent, of the total. Of U.S. prime contractors' offset obligations, $259 million was awarded to foreign subcontractors during 1980-84. U.S. firms also reported that foreign subcontractors would be assuming part of the offset obligation, but no specific value was given.

As a result of offset fulfillments during 1980-84, several respondents to the Commission's questionnaire indicated that new or enhanced foreign sources of products were generated. The largest number of new or enhanced sources of non-defense-related goods and services occurred in the area of electronic components and accessories, where seven new sources emerged (table E-4), mainly in Australia, Israel, and the Republic of Korea. For defense-related goods and services, new or enhanced sources emerged mainly in the manufacture of aircraft and parts, electronic components and accessories, and turbines and engines (table E-5). Australia and Israel together accounted for many of the new sources, followed by Denmark, Norway, and the United Kingdom. The fulfillment of offset obligations resulted in 26 new or expanded competitors to subcontractors and 32 new or expanded markets, mainly in the aircraft and parts industry.

Offsets associated with military-related export sales

Offsets are increasingly being required by both industrialized and developing countries in all areas of international trade, but especially as a prerequisite for purchasing major defense equipment. Offset deals create new business activity where it otherwise might not exist and also create new trading partners. Even though offsets are imposed on private-sector companies by governments, companies accept offset arrangements to enhance their business activities in general, to gain market share and/or access to markets, generate greater profits, and/or improve operating efficiencies by enlarging production runs. 1/ The enhanced business activity leads, in turn, to lower costs of those goods purchased by the U.S. Government, increased employment, and a better balance of payments. 2/ Military sales play an important role in increasing private-sector employment throughout the economy, especially in manufacturing. 3/ Offsets also increase tax revenues, since foreign military exports are treated as sales to foreign customers. 4/

Offsets and national security.--Proponents of offsets claim that such activities can benefit U.S. security interests through commonality of weapons systems and improved relations with the coproducing nations. Coproduction agreements serve to assist allies in improving their nonmilitary-related industrial capability and, therefore, their overall defense posture as well. Other benefits of coproduction include standardization of military hardware, especially among NATO countries, establishment of second sources for potential use for followup logistical support, and after-sales service. Other positive effects include increased sales of U.S. defense systems leading to lower unit costs through economies of scale, thereby creating new jobs. 5/

Offsets and the purchasing economy.--Purchasing governments are turning to offsets to reduce the impact of military equipment purchases on their

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1/ Statement of James P. Moore, Deputy Assistance Secretary for Trade Information and Analysis, Department of Commerce, before the House Committee on Banking, Finance, and Urban Affairs, May 22, 1984.

2/ Peter Harben, ed., "Offset Overview," Countertrade and Barter Quarterly, Autumn 1984.

3/ USAF, FY/84 Production Base Analysis, February 1984, p. 82.

4/ U.S. General Accounting Office, Trade Offsets in Foreign Military Sales, Apr. 13, 1984.

5/ Trade Offsets in Foreign Military Sales, General Accounting Office, Apr. 15, 1984.

domestic budgets and trade accounts. Purchasing countries view offsets as a means of revitalizing their economy and building up their defense capabilities while limiting the outflow of scarce foreign exchange. Offset arrangements allow LDC's to purchase military equipment that they could otherwise not afford. These countries hope to expand employment and increase the competitiveness of local industry by acquiring technology through offset agreements. The purchasing country can continue to utilize the technology and manufacture components even after offset obligations are fulfilled. In addition, they can force other countries to make investments in their economy that would not normally occur and receive assistance in the marketing of their exports. 1/

One drawback that offsets may present to the purchasing country is that the price of exports may have to be reduced in order to compensate the U.S. producer for the risks and inconvenience associated with the offset obligation. Another is that offset goods may displace sales in traditional, nonrestricted markets and may not lead to a net increase in earnings from trade.

Economic and Other Reasons for the Worldwide Growth of Countertrade

Nonmilitary countertrade

The severe lack of foreign exchange that developed in non-oil-producing LDC's and in some Eastern European NME's 2/ during 1973-80 represents the underlying cause for the growth in the worldwide volume and relative importance of nonmilitary countertrade since 1980. 3/ Since 1980, large current account deficits, particularly of non-oil-producing LDC's, caused multinational organizations to pressure the governments in these countries for economic policy reform, structural adjustments, and an expeditious eradication of their debts. 4/ Commercial credit for financing trade in debtor countries became scarce.

1/ Peter Harben, ed., "Offset Overview," Countertrade and Barter Quarterly, Autumn 1984.

2/ For the list of countries included in the non-oil-producing LDC, and Eastern European NME categories, see footnotes in table 14 on "current account balances."

3/ The expression "countertrade" is intended to cover all forms of domestic resource transfer by a buyer country as a condition of purchase. (See "Elements of Countertrade" section.) Thus, it fuses the traditional forms of countertrade with all the newly emerging forms of local-content, licensing, and service requirements. The term "compensatory trade" is being increasingly used for the same purpose. (See Thaddeus C. Kopinski, Threats and Opportunities of Global Countertrade, Business International Corporation, 1984.) The economic reasons that caused the growth of the traditional and new forms of countertrade practices do not essentially differ.

4/ This was confirmed by officials of eight countries interviewed in the course of this investigation (Bolivia, Colombia, Ecuador, Indonesia, Jamaica, Malaysia, Mexico, and Uruguay). The existence of legislation on countertrade in these countries, the relative prominence of these trading practices in their foreign trade at the time of the survey, and the consequent expertise of their commercial officials on the subject were the criteria that determined their selection for the survey.

Table 14.--Current account balances of industrial, non-oil-developing and Eastern European nonmarket economy countries, 1973-84

(In billions of dollars)

Item	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984
Industrial countries 1/	13.0	-22.9	8.8	-10.1	-15.4	17.8	-24.6	-59.6	-18.0	-22.9	-19.4	-58.3
Non oil developing countries 2/	-6.6	-30.0	-38.4	-24.9	-23.9	-33.2	-49.5	-72.1	-92.8	-69.4	-52.1	-37.9
Eastern European non-market economy countries 3/	-2.3	-5.0	-5.8	-5.8	-5.5	-6.2	-7.6	-7.0	-5.6	-.4	2.0	2.3

1/ United States, Canada, Australia, Japan, New Zealand, Austria, Belgium, Denmark, Finland, France, West Germany, Iceland, Ireland, Italy, Netherlands, Norway, Spain, Sweden, Switzerland, United Kingdom.

2/ All developing countries except Algeria, Indonesia, Iran, Iraq, Kuwait, Libya, Nigeria, Oman, Qatar, Saudi Arabia, United Arab Emirates, Venezuela.

3/ Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania.

Source: Data on industrial countries and non oil developing countries, calculated from information provided by the Current Publications Division of the External Relations Department, International Monetary Fund. Data on non market economies, compiled from Wharton Econometric Forecasting Associates (1973-1979 data are based on Wharton's unpublished estimates).

In 1979 and 1980, the heavily indebted countries embarked on comprehensive adjustment programs aimed at redressing their trade problems. They adopted austerity measures to improve their payments balances in the short run and to reallocate resources to economic sectors that could help cut their import dependence and increase their export potential in the long run. The composite effect of many countries trying to reduce their imports and increase their exports contributed to the adverse conditions of the world economy and trade during 1980-83. 1/

The economic and political difficulties that arose in many debtor countries as a result of trade problems and efforts to correct them led many debtor-country governments to make use of the leverage they had as importers. By insisting on countertrade, debtor-country governments, and in some instances private LDC firms, channeled back the pressure that their creditors imposed on them through the system of multilateral settlements. Many debtor-country governments saw countertrade as an opportunity to halt the deterioration of their current account deficits by balancing every transaction and assuring imports vital for the functioning of their economies regardless of costs. Sometimes, import restrictions imposed by these governments inadvertently created incentives for their domestic producers to seek alternatives to currency-based trade, i.e., countertrade.

Western firms were compelled to comply with countertrade demands of LDC governments for fear of losing their share of the shrinking non-oil-producing LDC and NME markets after 1979. Competition among Western multi-national firms and the ability of these companies to adjust to new situations and absorb inefficiencies helped proliferate international countertrade.

This study identifies six specific factors that, in addition to non-oil-producing LDC and NME government policies to increase the role of countertrade in national trade, may have contributed to the growth of these trade practices during the 1980-83 world recession. These factors 2/ are: (1) conditions attached to International Monetary Fund (IMF) assistance; (2) commercial bank lending restrictions; (3) LDC import restrictions through exchange-rate policies and restrictions on hard-currency repatriation; (4) export promotion by Western governments; (5) competition among Western firms and absorption of countertrade into corporate business practices; and (6) growth in commodity movements traditionally not accompanied by monetary transactions. These six factors (discussed in more detail in the following sections of this report) are not independent from one another, nor are they independent from the underlying cause of foreign-exchange shortages in non-oil-producing LDC's and Eastern European NME's. (See also app. F for a discussion of non-oil-producing LDC, NME, and Western Government involvement in countertrade.)

1/ The volume of world trade declined for 3 consecutive years. See IMF Survey, July 16, 1984, p. 221.

2/ The acquisition of illegitimate gains by private firms (e.g., import duty, corporate tax evasion, dumping) was not investigated as a possible reason for the increase of countertrade. For some thoughts on this subject see Douglas L. Adkins, U.S. Congress, Office of Technology Assessment, paper presented at Allied Social Science Association Meetings, San Francisco, Dec. 29, 1983, p. 10.

The major qualitative change that occurred in the worldwide use of countertrade during the 1980-83 world recession was that many LDC's that previously had not relied heavily on these trading methods began to do so. The NME's had always sought bilateral arrangements leading to countertrade in their foreign commercial relations. Their effort to sustain the flow of Western imports since 1980 further increased their interest in countertrade.

Even if economic conditions had not been as severe during 1973-83, NME trade and worldwide industrial cooperation in general would have spurred the spread of countertrade. But it is unlikely that these factors alone would have increased the relative importance of these trade practices in international commerce. The 1980-83 recession 1/ that handicapped the restoration of external equilibriums of debtor nations reinforced incentives for, and commitments of, debtor countries to rely on countertrade. Despite the recovery of the world economy and a noticeable improvement in the current account deficits of non-oil-producing LDC's and NME's in 1983 and 1984, the use of countertrade adopted during the recession continues to spread. In addition to the factors identified by the study as likely causes of the growth of countertrade since 1980, the present worldwide protectionism pressures may also have contributed to this growth. 2/

The capital movements that resulted in large-scale external debts during the period 1973-80 had two major directions: from the non-oil-producing to the oil-producing nations following the 1973-74 energy crisis and from the West to non-oil-producing LDC's and Eastern European NME's later during the 1970's.

The extent of worldwide payment problems of the decade 1973-83 may be best demonstrated by the current account balances of the three major groups of net oil-importing countries: industrialized countries, net oil-importing LDC's and Eastern European NME's (table 14). To a considerable extent, the industrial countries were able to finance their post-oil shock deficits by attracting direct inflows of OPEC funds and by borrowing in the international bond markets. Non-oil-producing LDC's and NME's began to build up their foreign debts by borrowing from Euromarkets, Western official lenders, and international organizations, creating the second major source of imbalance in the global flows of capital. Although these countries borrowed both to finance short-term current account deficits and structural adjustments initiated by the industrialized countries, much of their borrowing served only to finance balance-of-payments without capital formation. 3/

1/ The World Bank's "World Development Report 1984" defined 1980-83 as the period for the recent world economic recession See Bank For International Settlements (BIS) Press Review, No. 153, Aug. 8, 1984, p. 3.

2/ International Monetary Fund, Exchange Arrangements and Exchange Restrictions Annual Report, 1984, p. 17.

3/ Serious doubts have been raised whether--even without the global downturn of the world economy and trade in 1980-83--the total capital borrowed by these countries could have possibly resulted in a sufficient flow of hard-currency export revenues for the maintenance of their import levels and eventual eradication of their debts. For a survey of economic literature on analyzing the borrowing capacity of developing nations, see Donogh C. McDonald, "Debt Capacity and Developing Country Borrowing: A Survey of the Literature," International Monetary Fund Staff Papers, December 1982, pp. 603-646.

Contributing factors to the current account deterioration of non-oil-producing LDC's and Eastern European NME's

The lack of foreign exchange associated with the deterioration of current account balances of non-oil-producing LDC's and NME's was the probable underlying cause that led to the proliferation of international countertrade. The following factors were crucial in the current account balance deterioration of non-oil-producing LDC's and Eastern European NME's during 1973-80: 1/

- o Deterioration in the overall terms of trade for non-oil-producing LDC's and Eastern European NME's.
- o Moderation in the growth of industrialized nations.
- o Increases in the costs of financing from international capital markets.
- o Domestic factors in non-oil-producing LDC's and Eastern European NME's that contrained external adjustment policies.

For a further discussion of these factors, see app. G.

Factors that may have contributed to the growth of international countertrade

IMF conditions.--Several debtor nations are under obligation to the IMF to conserve their foreign-exchange reserves for the purpose of reducing their payments arrears. Such an obligation adds an incentive for debtor nations to shift from currency-based trade to countertrade. By increasing both exports and imports through countertrade at the expense of currency-based trade, a debtor country maintains its use of foreign resources while requesting debt rescheduling. If a given debtor country's economy is heavily dependent on imported resources, countertrade helps to maintain its level of domestic production and employment. 2/ An increase in the share of debtor-country obligations to commercial banks from obligations to official lenders creates the opposite incentive of increasing monetary export revenues at the expense of countertrade.

The improvement of trade balances is one of the IMF's conditions for supporting stabilization programs in debtor nations. (The IMF currently

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1/ For the data used in this section illustrating the factors that contributed to the current account deficits of non-oil-producing LDC's, see Moshin S. Khan and Malcolm D. Knight, "Determinants of Current Account Balances of Non-Oil Developing Countries in the 1970's," International Monetary Fund Staff Papers, December 1983, pp. 819-842.

2/ This was the opinion of senior officials in a number of Latin American countries according to a recent survey by Business International. (See Thaddeus C. Kopinski, Business International Corp., Threats and Opportunities of Global Countertrade, 1984, pt. II/C). Although exports and imports are balanced through international prices in a countertrade deal, thus seemingly leaving the trade balance unchanged, Western capital goods imported by a developing nation may be valued more in terms of domestic resources than their international price. If the capital goods acquired through countertrade play a crucial role in a developing country's export development program, countertrade may indeed help in improving the country's trade balance.

supports about 40 such stabilization programs.) Intentions by debtor nations to comply with these requirements for fear of losing the IMF's support have allegedly contributed to the spread of countertrade in international commerce. 1/

Commercial bank lending restrictions.--The debt crisis reduced funds available for financing North-South and East-West trade from Western commercial banks. This reduction was the result of the commercial banks' perception of risks associated with the acquisition of short-term, customarily high-interest-bearing assets from countries in financial crisis. But regulatory measures by some Western governments may have also played a part in this reduction. Lending restrictions by Western commercial banks acted as an incentive for traders to engage in countertrade, since these trading methods allowed the stretching of funds available for trade financing. For example, trading houses may assume part of the loan needed for the transaction or, by depositing in escrow the proceeds from an advance sale of bartered and countertraded goods for the Western seller, the LDC or NME partner may have a positive balance in a Western commercial bank. This helps an LDC or NME firm to retain its hard-currency earnings in addition to facilitating future commercial loans. 2/ The high real rates of interest caused by a relatively low supply of funds have also contributed (and continue to contribute) to the spread of international countertrade.

LDC import restrictions through exchange-rate policies and hard-currency repatriation.--Import restrictions through exchange-rate policies have been an integral part of efforts by debtor nations to correct their external imbalance. The curtailment of imports has taken place through periodic devaluation of the local currencies in most Latin American debtor nations. If the currency is devalued below its market value, a strong incentive is created for domestic users of imported goods to engage in countertrade in order to avoid cost increases. If LDC importers succeed in getting better deals through countertrade than they would by importing with expensive foreign currency, they may, in fact, be selectively revaluing their country's currency. To the extent countertraders get better deals than they would by importing with currency, they create their own import subsidy program.

Many LDC's, however, have been reluctant to fully devalue their currencies and allow the free operation of market forces to correct deficits in their balance of payments. Devaluation was feared as an accelerator of inflation in many debtor countries where expenditure-increasing policies (i.e., expansionary fiscal and monetary policies) were used to bring the domestic economies out of the recession in the early 1980's.

An overvalued national currency in an LDC increases the country's imports in the absence of foreign-exchange controls. Therefore, overvaluation and exchange controls create the need for a rationing of the country's sparse foreign-exchange reserves. Government authorization of exchange incidental to a regime of controls occurs according to some announced menu of priorities or on a case-by-case basis. Setting a higher official rate of exchange than the

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1/ Ibid.

2/ Briefing on countertrade at the American Managers Association, New York, NY, September 1983.

prevalent one for domestic importers is an alternative method of rationing. Although foreign-exchange policies are part of a large variety of import-restricting systems, any potentially effective system creates an incentive for private LDC and Western firms to circumvent it through countertrade.

Obstacles to hard-currency repatriation by certain LDC governments have led Western firms to engage in countertrade deals. Blocked currency reserves are spent by Western firms to acquire goods from the local market for resale on world markets or in the home-country market. 1/

Export promotion by Western governments.--Western governments often compete through offering concessionary financing for the implementation of foreign development projects in order to assist their exporters in world markets. If the borrowing foreign government also happens to have a policy of linking import and export transactions, the Western supplier will face countertrade requirements as a precondition for any sale. 2/ A Western government's assistance to its exporters facing countertrade demands is forthcoming if the goods to be acquired through such deals are also vital for the country's economy. Development for Import (DFI) programs may be a convenient countertrade arrangement to secure supplies from another country. 3/ In a typical DFI deal a Western firm obtains a low-cost loan from its own government for the development of raw or intermediary material sources in a foreign country.

The availability of inexpensive government credit to the Western supplier of a foreign development project may itself be an incentive to a Western firm to accept countertrade demands from foreign partners. Western governments may also be forced to accommodate the countertrade demands their exporters face in LDC's, because NME's generate competition for them through efforts to develop long-term bilateral relations with these countries. By catering to the countertrade demands of LDC's, Western governments attempt to create a favorable commercial climate for their firms. 4/

Competition among Western firms and absorption of countertrade into corporate business practices.--Western competition contributes to the increase of countertrade. In order to shore up their competitive positions, multinationals have engaged in a competitive acceptance of countertrade demands by LDC's and NME's. As a result, some Western firms may transfer some of their most advanced technology through buy-back agreements to these countries. 5/

1/ For a description of methods used by Western firms to repatriate blocked currencies from some Third World countries, see Thaddeus C. Kopinski, Business International Corp., Threats and Opportunities of Global Countertrade, 1984.

2/ The U.S. Eximbank prefers loan applications that do not involve countertrade. It admits, however, that for competitive reasons it cannot completely rule out the financing of foreign development projects that might result in countertrade for a U.S. firm. Interview with Eximbank official.

3/ For example, France, Japan, and West Germany have DFI programs.

4/ Interview with Business International Corp.

5/ Interview with Dr. Douglas L. Adkins, U.S. Congress, Office of Technology Assessment.

Many large, successful Western firms have integrated countertrade into their business routine. Some of them openly use countertrade as a marketing tool and allegedly use some of the acquired commodities as a hedge against instability in financial markets. Some Western firms have also found that countertrade reduces their risks of nonpayment by importers, especially in the case of heavily indebted countries. 1/ The relatively high costs of countertrade transactions compared with currency-based trade has created a profit incentive in Western corporate business life to improve the efficiency of these trading methods. Innovative new schemes, such as the London-based countertrade data center or the creation of International Trading Certificates (ITC's), tend to make countertrade multilateral. 2/

The increasing expertise and expanding contacts of countertraders (i.e., trading houses specializing in countertrade, and the inhouse countertrade units of multinational corporations) may themselves have become a factor contributing to the growth of international countertrade.

Growth in commodity movements traditionally not accompanied by monetary transactions.--Long before the onset of the current worldwide growth of countertrade, a distinct opportunity to obviate monetary transactions had been recognized in two areas: (1) inter-firm production cooperation and (2) the transportation of homogeneous goods. Under bilateral (or multilateral) industrial cooperation arrangements, firms from different countries may at least partially assume the role of industrial plants under unified management. Since deliveries under such cooperation agreements will be similar to deliveries within an industrial firm, the role of monetary transactions will be relegated to settling balances at the end of stipulated periods. The growing number and variety of international microeconomic links create opportunities for economizing on monetary transactions. Growth in output produced under such cooperation agreements also means growth in countertrade.

Barter arrangements among suppliers of homogeneous goods (e.g., crude oil, metals, chemicals, and agricultural products) to save transportation costs are called "swaps." The worldwide flow of such goods, whether they are sold under long-term contracts or on spot markets, are ideally suited to be rationalized through barter in order to save transportation costs. A recent example of a swap is the arrangement involving Soviet oil shipments to Cuba. Since Mexico sells oil to Western Europeans, the swapping of Soviet oil to Cuba for Mexican oil bound for Europe reduced shipping costs for both suppliers.

Efforts to restrain the growth of countertrade.--Efforts to restrain the growth of countertrade have taken place in the context of the OECD where a consensus of members has been sought on limiting use of these techniques. This effort has been supported by the United States. The issue of countertrade has also been raised by the United States in the GATT (see appendix H).

1/ Interview with Business International Corp.

2/ For a report on the countertrade data center, see Counter Trade Data Centre Established in London, Financial Times, Oct. 24, 1984, p. 8. For a description of International Trading Certificates, see Business Eastern Europe, July 6, 1984, pp. 209-210.

U.S. Regional Countertrade

During 1980-84, the number of countries either (1) requiring countertrade (including military offsets) for both the private and public sectors of their economies, (2) pursuing countertrade on a bilateral basis, or (3) establishing bilateral payment agreements has grown dramatically.

U.S. companies indicated that nonmilitary countertrade was required by 61 countries during 1980-85, as shown below: 1/

Albania	Guatemala	Norway
Algeria	Honduras	Pakistan
Argentina	Hungary	Peru
Bangladesh	India	Philippines
Belgium	Iran	Portugal
Bolivia	Iraq	Poland
Brazil	Israel	Romania
Bulgaria	Ivory Coast	South Korea
Burma	Indonesia	Spain
Canada	Jamaica	Switzerland
Chile	Kenya	Syria
China	Lebanon	Soviet Union
Colombia	Liberia	Thailand
Costa Rica	Libya	Tunisia
Czechoslovakia	Malaysia	Turkey
Dominican Republic	Mexico	Uganda
Ecuador	Morocco	Uruguay
Egypt	Netherlands	Venezuela
East Germany	New Zealand	Yugoslavia
Greece	Nicaragua	Zaire
		Zimbabwe

Only 23 countries, shown below, were involved in offset obligations associated with military-related export sales.

Australia	New Zealand
Belgium	Norway
Canada	Saudi Arabia
Denmark	Singapore
Egypt	South Korea
Greece	Spain
India	Sweden
Israel	Switzerland
Italy	Taiwan
Japan	Turkey
Netherlands	United Kingdom
	Yugoslavia

1/ An analysis of the official policies of selected countries requiring countertrade is provided in app. I. See submission to the Commission by Univex Corporation, Nov. 9, 1984, p. 13. According to a survey undertaken by the Foreign Trade Council, 88 countries were cited as particularly active in countertrade. For a list of selected foreign organizations involved in negotiating countertrade and offset arrangements, see app. J.

On balance, these offset countries tended to be more industrialized and more closely allied to the U.S. Government in terms of military cooperation.

U.S. firms reported that they engaged in nonmilitary countertrade and military offsets primarily because it was required by a foreign government. In addition, such agreements were entered into because they provided a competitive advantage to the firm's exports or they helped maintain foreign market share, as shown below (see also table E-6 for more detail concerning military offsets):

Reasons	Number of reported occurrences: Nonmilitary countertrade	Number of reported occurrences: Military offsets
Required by foreign government------	113	109
Provided a competitive advantage to firm's exports-------------------	29	20
To maintain foreign-market share----	24	29
Used to help finance firm's exports-------------------------	10	-
Helps repatriate blocked currency---	6	-
All other---------------------------	8	27

The following list, compiled from data submitted in response to Commission questionnaires, shows reasons provided by U.S. companies for engaging in countertrade during 1980-84:

Reasons	Country		
Required by foreign government----	Australia	India	Poland
	Austria	Indonesia	Portugal
	Belgium	Israel	Romania
	Brazil	Italy	South Korea
	Bulgaria	Jamaica	Soviet Union
	Canada	Japan	Sweden
	China	Lebanon	Turkey
	West Germany	Mexico	Yugoslavia
	East Germany	Netherlands	Zimbabwe
	Hungary	Philippines	
Provided competitive advantage----	Brazil	Israel	Republic of Korea
	China	Mexico	
	East Germany	Netherlands	Soviet Union
	Hungary	Poland	Spain
	Indonesia	Romania	Sweden
			Yugoslavia
To maintain foreign-market share--	Austria	Finland	Netherlands
	Brazil	Hungary	Poland
	China	India	Romania
	Colombia	Indonesia	South Korea
			Yugoslavia

Reasons--Continued	Country--Continued		
Used to help finance firms exports.	Bulgaria China East Germany Hungary	Poland Romania Yugoslavia	
Helps repatriate blocked currency.	Mexico	Romania	Zambia
All other	Italy Mexico	New Zealand Pakistan	Poland Soviet Union

The absence of Latin American countries in many categories reflects their governments' late entry into mandated countertrade.

As mentioned earlier in this report, the total countertrade (including offset) obligation during 1980-84 amounted to $11.0 billion. During 1980-84, total U.S. countertrade obligations including those associated with military offsets with Europe were reported to be just under $5.8 billion, or 52 percent of total obligation, as shown in table 15. Total U.S. countertrade obligations with Asian countries were reported to be $2.3 billion, or 21 percent of the total, and those obligations with all other countries were $2.9 billion, or 27 percent. A discussion of the regional patterns of U.S. countertrade appears in the following sections of this report.

Table 15.--Total U.S. countertrade obligations, 1980-84

(In millions of dollars)

Year	Sales	Countertrade (military and nonmilitary) obligations
		Europe
1980	2,959	285
1981	1,520	719
1982	483	201
1983	3,561	3,183
1984	1,848	1,378
Total	10,371	5,766
		Asia
1980	1,654	295
1981	1,088	601
1982	556	235
1983	869	245
1984	4,807	953
Total	8,974	2,329

Table 15.--Total U.S. countertrade obligations, 1980-84--Continued

(In millions of dollars)

Year	Sales	Countertrade (military and nonmilitary obligations)
		Other
1980	3,801	301
1981	3,486	1,551
1982	676	482
1983	976	190
1984	484	431
Total	9,423	2,955

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

United States-Europe

During 1980-84, U.S. nonmilitary and military countertrade obligations with Europe increased erratically from $285 million to almost $1.4 billion in 1984, as shown in the following tabulation:

(In millions of dollars)

Item	1980	1981	1982	1983	1984
Nonmilitary countertrade:					
Western Europe:					
NATO countries	98	47	31	-	22
Non-NATO countries	10	50	9	32	86
Subtotal	108	97	40	32	108
Eastern bloc	18	47	3	87	49
Total	126	144	43	119	157
Military offsets:					
NATO countries	159	275	52	3,024	1,128
Non-NATO countries	-	300	106	40	93
Total	159	575	158	3,064	1,221
Grand total	285	719	201	3,183	1,378

1/ Excludes Yugoslavia, which is included in Western Europe for this study.

In 1983, there was a significant increase in such obligations to almost $3.2 billion from $201 million in the previous year. Most of this rise was due to an increase in military offsets with NATO countries, which accounted for the greatest share of total countertrade obligations during the period. The decrease in the value of the total countertrade obligations including military offset obligations in 1982 was attributable in part to the decline in the general world economy. Nonmilitary countertrade involving United States and Eastern Europe 1/ was lower than that reported between the United States and Western Europe during 1980-84. According to questionnaire responses and industry sources, countertrade agreements with Eastern Europe have been more difficult to negotiate, in part because of the lack of acceptable goods to take in return and the lack of major capital projects especially in 1982.

United States-Western Europe.--United States-Western European nonmilitary countertrade and military offset obligations increased from $285 million in 1980 to slightly more than $3.1 billion in 1983 before dropping to $1.3 billion in 1984. Non-military countertrade with NATO countries decreased by 78 percent between 1980 and 1984 while such trade with non-NATO countries increased from $10 million in 1980 to $86 million in 1984. Military offsets accounted for as little as 56 percent of this trade in 1980 and as much as 96 percent of the total in 1983. U.S. countertrade including offsets occurred with most European countries except France. 2/ According to the Department of Defense (DOD), most cooperative efforts (i.e., coproduction) and direct offsets occur within NATO-member countries and other Western European nations, which have the infrastructure to absorb offsets, but most indirect offsets occur with non-NATO countries. 3/ The framework for a substantial portion of the military offset obligations with Western Europe was established through a number of Memoranda of Understanding between the United States and its Western European allies. 4/ As an example of such offsets, one U.S. aircraft manufacturer in a deal with Spain will offset a portion of the costs of the aircraft purchase (up to $1.8 billion). The fulfillment of the offset obligation will occur during 1984-93. The obligation covers coproduction of aircraft parts, the transfer of aerospace and other high technology to industries in Spain, the promotion of Spanish exports and foreign investment, as well as increasing tourism to that country. 5/ According to public testimony before the Commission, several countries (e.g., Spain, Greece, Finland, and Yugoslavia) have demanded fulfillment of offset obligations with tourism (an indirect offset), in contrast to large capital projects and high-technology offsets associated with the remaining Western Europe countries. 6/

United States-Eastern Europe.--During 1980-84, United States-Eastern Europe nonmilitary countertrade obligations fluctuated from a low of $3 million in 1982 to as much as $87 million in 1983 (see table 15 on page 48). Respondents to the Commission's questionnaire reported nonmilitary

1/ Excludes Yugoslavia, which is included in Western Europe for this study.

2/ From data submitted in response to questionnaires of the U.S. International Trade Commission. See also written submission by the American Association of Exporters & Importers, June 4, 1985, which contains a report by the Association Pour la Compensation des Exchanges Commerciaux, Nov. 25, 1980. This report indicates only one transaction between France and North America (Canada) and none with the United States.

3/ Statement of James R. Blaker, Deputy Assistant Secretary of Defense, Policy Analysis, on the Impact of offsets before the Subcommittee on Economic Stabilization of the House Committee on Banking, Finance, and Urban Affairs, July 24, 1985, p. 14.

4/ For a list of Memoranda of Understanding between the United States and its Allies see p. 103.

5/ "F-18 Buy Brings Spain $1.8-Billion Offset," Aviation Week and Space Technology, June 4, 1984, p. 17.

6/ Statement of Cord D. Hansen-Sturm, vice president, First Family of Travel, before the U.S. International Trade Commission, May 30, 1985.

countertrade transactions with Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and the Soviet Union.

Prior to 1980, countertrade played a supporting function in trade with Eastern Europe, since Western banks provided generous lines of credit to their Eastern European counterparts for financing imports. Eastern European countries instituted countertrade requirements for products that were difficult to market in Western nations and in cases where Eastern European countries had exhausted their credits from bilateral trade, but yet desired continuing imports. 1/

In 1980, as a response to the Polish debt crisis, Western banks halted the expansion of trade credit lines to Eastern European countries. In turn, Eastern European nations significantly reduced their imports from many industrialized nations and returned to a more bilateral trade approach in an attempt to balance imports and exports. In addition, foreign-currency reserves fell in many LDC's, making it difficult for them to repay their debts to Eastern Europe in hard currency, and this led to an erosion of the Eastern European countries' hard-currency surpluses. As a result, Eastern European countries were forced to resort to countertrade not only with LDC's, but also to increase the use of countertrade transactions with Western corporations. The use of such transactions by Eastern European countries has increased significantly, despite the fact that virtually all these nations officially consider countertrade as inefficient and uneconomical. 2/

During 1980-84, the countertrade situation in Eastern European markets has been changing quite rapidly, with a variety of trends emerging. These patterns include the following:

- Deteriorating quality and product design of Eastern European products that Western firms must accept in countertrade;
- lack of availability of desirable countertrade products, which forces Western companies to purchase other less-marketable goods;
- rising countertrade quotas, which oblige Western companies, in some cases, to accept more than 100 percent worth of goods in countertrade;
- increasing unreliability of Eastern European foreign trade organizations (FTO's) as suppliers;
- rising price levels in Eastern Europe--FTO's use of "unrealistically high domestic price levels to calculate prices of countertrade goods;" and
- increasing use of third-country-limitation clauses in sales contracts, as well as the use of contract clauses preventing

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1/ Herbert Stepic, "Principal Changes in Countertrade Practice with Selected Countries After the Polish Crisis," Countertrade & Barter Quarterly, No. 1, May 1984, p. 14.
2/ Herbert Stepic, op. cit., pp. 15 and 16.

barter houses from fulfilling contracts, both of which act to reduce competition and the "cannibalization" of Eastern European goods on the world market. 1/

Rather than exporting raw materials, most Eastern European nations now promote the export of finished goods, such as machines and high technology products, and services. However, selling raw materials is a more efficient means of earning hard currency in the short term because of the lower amount of local currency used to a produce a product of quality that compares with those produced outside Eastern Europe. Finished goods require a higher local currency input and are frequently more difficult to sell in market economies because of their generally inferior quality.

In recent years the Soviet Union has increased its demands for countertrade from Western companies. Basically, the Soviets promote five types of countertrade, as follows: (1) natural resource/raw-material cooperation agreements with partial or full payments in the resultant products; (2) industrial cooperation agreements (ICA'S) with partial payment in the resultant products; (3) ICA'S with partial payment in unrelated products; (4) licensing agreements with partial payment in the resultant products; and (5) barter arrangements of products and equipment. 2/ Industrial cooperation agreements, outside of natural resource/raw-material arrangements, are business arrangements that extend over a period greater than 2 years, provide for the transfer of production technology, and involve close managerial contacts. The Soviets also engage in another special form of countertrade through a Soviet-Western joint stock corporation organized outside the U.S.S.R. In one such instance, a U.S.-U.S.S.R. joint stock venture (with 50 percent Soviet participation) exchanges fish caught off the U.S. Pacific coastline for Soviet salmon and crab that the U.S. partner markets in Asia, especially to Japan.

United States-Asian countertrade

The value of United States-Asian total countertrade obligations, including offsets, displayed large annual fluctuations but increased overall from $295 million in 1980 to $953 million in 1984 as seen in the following tabulation (in millions of dollars):

Source	1980	1981	1982	1983	1984
Nonmilitary countertrade with Asia	59	48	137	85	154
Military offsets with Asia	236	553	98	160	799
Total	295	601	235	245	953

1/ Op. cit.
2/ Report from U.S. Embassy, Moscow, October, 1982.

The large increases in military obligations in 1981 and 1984 were primarily a result of large-scale U.S. military sales to Israel. The extent to which countertrade is used in the Middle East varies among countries. Turkey, for instance, permits countertrade transactions only on a government-to-government basis. In May 1984, the United States and Turkey signed an agreement to manufacture F-16 fighter planes with some coproduction to occur in Turkey. 1/ Iraq, Iran, and Qater have used crude petroleum in barter deals with foreign governments and companies. Jordan, although not a petroleum producer, similarly uses its primary export--phosphates--in barter transactions. 2/ Israel mandated countertrade in early 1983, particularly in cases involving Government purchases. Israel also receives trade offset arrangements from the United States in its FMS (Foreign Military Sales) purchases. 3/ In December 1983, the United States agreed that Israel would be able to obtain up to 15 percent in offsets in 1984 "based on commercial procurement of American military sales hardware using foreign military sales credits." 4/ Offsets with Israel amounted to $225 million in 1984 and will amount to $200 million 1985. 5/ Saudi Arabia has not mandated countertrade, but in early 1983, a formalized offset policy was established for contracts under its "Peace Shield" defense programs. 6/ According to this program, in which a major U.S. aerospace firm is the prime contractor, the Saudis will spend $1.2 billion for a ground-based air defense command and control and communications system. The size of the offset obligation has not yet been determined but is expected to be implemented over the next 10 years. 7/ As with several other prominent OPEC member countries that are facing a decline in petroleum revenues because of the soft world petroleum market in 1984-85, Saudi Arabia has begun to use countertrade involving petroleum for goods/services. In mid-1984, the Saudi Government concluded a barter deal of approximately $1 billion in petroleum for 10 aircraft from a major U.S. aerospace company. 8/

The extent to which countertrade is practiced in other portions of Asia also varies by country. Pakistan does not officially sanction countertrade, but some State trade organizations have used countertrade to finance certain imports. Similarly, Bangladesh and Burma have limited experience with such trade. Although India does not have a formal policy on countertrade, it has

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1/ "Turkey, U.S. Sign Agreement to Coproduce F-16 Fighters," Aviation Week and Space Technology, May 14, 1984, p. 26.

2/ Rami C. Khouri, "Jordan Turns to Barter to Build Up Phosphate Sales," Financial Times, Oct. 17, 1984, p. 7.

3/ U.S. General Accounting Office, U.S. Assistance to the State of Israel, June 24, 1983, p. 42.

4/ Clarence A. Robinson, Jr., "U.S. Offers Israel 15% in Military Offsets," Aviation Week and Space Technology, Dec. 5, 1983, p. 25.

5/ Statement of James R. Blaker, Deputy Assistant Secretary of Defense, Policy Analysis, on the Impact of offsets before the Subcommittee on Economic Stabilization of the House Committee on Banking, Finance, and Urban Affairs, July 24, 1985, p. 13.

6/ "Reasonable Price and Oil Barter Possible," Financial Times, Apr. 22, 1985, p. 5.

7/ "Boeing Aerospace Wins Bid For Saudi Air Defense," Aviation Week and Space Technology, Mar. 4, 1985, p. 25.

8/ "Saudis Confirm Barter Deal For Ten 747s," Aviation Daily, Aug. 16, 1984, p. 258.

engaged in such transactions through bilateral trade agreements. Since early 1983, Thailand, through its State Trading Company, has engaged in government-to-government countertrade. The Philippines and Korea have also engaged in countertrade transactions. 1/ Indonesia, since early 1982, has encouraged countertrade for public-sector purchases with foreign suppliers. In 1983-84, the Indonesian Government relaxed the restrictions imposed on foreign suppliers. In early 1983, Malaysia expanded countertrade to be included in government purchases involving foreign suppliers and recently began strict enforcement of these laws. The People's Republic of China (China) pursues countertrade transactions primarily to acquire priority products.

United States-other countries

Countertrade including military offset obligations between the United States and other countries reached a peak of almost $1.6 billion in 1981 before dropping to to $431 million in 1984, as seen in the following tabulation (in million of dollars) as compiled from data submitted in response to the Commission's questionnaires:

Item	1980	1981	1982	1983	1984
Nonmilitary countertrade:					
Latin America	70	30	288	58	43
All other	212	98	11	112	226
Military offsets	19	1,423	183	20	162
Total	301	1,551	482	190	431

Nonmilitary countertrade, as reported in this investigation, accounted for slightly more than one-third of such transactions between the United States and other countries during 1980-84. Offset obligations were significant in 1981, totaling almost $1.6 billion, and were principally with Australia and Canada. These obligations were the result of sales agreements signed in 1980 with the United States for major weapons systems. As seen above, nonmilitary countertrade between the United States and Latin America also fluctuated during 1980-84. The large increase in 1982 is, in part, due to the devaluation of the Mexican peso and the resulting regulations restricting imports into that country.

Countertrade (both nonmilitary and military) as reported between the United States and Latin America is not significant in value, compared with the large countertrade agreements that have been reported between Latin American countries and other regions. In the last few years and especially in 1983-84, countertrade has become a significant trade practice in virtually all Latin

1/ However, one U.S. manufacturer demanded a $50 million offset from Korea in return for purchasing a $50 million automobile transport ship. Statement of Mr. Foulds before the U.S. International Trade Commission, May 30, 1985, revised copy of official transcript, p. 126.

American countries. Not all Latin American nations, however, have official policies or laws mandating or encouraging countertrade. Countries with such policies include Brazil, Colombia, Costa Rica, Bolivia, 1/ Ecuador, Honduras, Jamaica, Mexico, Venezuela, and Uruguay. Although Brazil's official policies do not specifically mandate countertrade, Brazilian State-owned enterprises engage in countertrade, and the Government of Brazil has signed bilateral clearing arrangements. In early 1985, Brazil signed a barter agreement with Nigeria to exchange Brazilian goods for Nigerian petroleum worth up to $1 billion. 2/ Mexico also does not mandate countertrade; however, in its December 1982 "Exchange Controls Decree," Mexico established the legal foundations for countertrade. 3/

Although Argentina, Chile, and Peru do not have official policies or laws legitimizing countertrade, they have in the past engaged in such activities. Argentina has engaged in government-to-government countertrade but still maintains laws that consider countertrade as an illegal form of trade in the private sector. 4/ Chile has no formal policy on countertrade and no official process for approving or handling such transactions, but the government recognizes countertrade as a mechanism for preserving foreign exchange. 5/

In a number of Latin American countries, countertrade appears to be concentrated in State-owned enterprises and in government-to-government transactions (e.g., Brazil, Argentina, Jamaica, Chile, Peru, and Venezuela), and in others, countertrade appears principally in the private sector (e.g., Mexico, Colombia, Honduras, Ecuador, and Uruguay). In these countries, regulations and legislation governing countertrade encompass traditional exports (typically agricultural commodities or natural resources) and generally specify that transactions involving these products are to be used to generate hard currency or foreign exchange, with nontraditional export goods to be used in countertrade transactions. Exceptions of these guidelines may occur under certain circumstances such as when a country is using countertrade to strengthen a long-term trading relationship with another trading partner. 6/

Recently, there have been a number of actions taken by Latin American nations to facilitate countertrade transactions among them. In July 1984, Mexico, Argentina, and Brazil negotiated a 3-year agreement to suspend tariffs and import licenses on a triparte basis and to expand the use of unconventional trade mechanisms, especially countertrade, in order to expand regional commerce. The three countries are members of the Association of Latin American Integration (ALADI), an organization that has adopted a procountertrade posture. Prior to this agreement, Bolivia, Peru, and Brazil

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1/ In July 1984, Bolivia enacted legislation legalizing barter transactions.

2/ Andrew Whitley, "Brazil in $750 million Soviet Trade Deal," Financial Times, Mar. 6, 1985, p. 1.

3/ Federal Official Gazette, December 1982.

4/ Thaddeus C. Kopinski, op. cit.

5/ Ibid.

6/ John Cheatle, "Countertrade in Latin America," Countertrade and Barter Quarterly, No. 3, Autumn 1984, pp. 10 and 12. See also Herbert Stepic, "Present Trends in Countertrade: Third World Perspectives," Countertrade and Barter Quarterly, No. 5, Spring 1985, pp. 19-24.

negotiated an agreement to restrict the use of the U.S. dollar in their triparte trade, thus emphasizing unconventional financing, particularly countertrade. 1/ In August 1984, delegates from the Andean Pact signatories (Colombia, Venezuela, Ecuador, Bolivia, and Peru) met in Caracas, Venezuela, to discuss formally the use of countertrade in restoring declining regional trade. However, no conclusions were reached, and no official actions were taken at that time. 2/

Countertrade expanded significantly during 1983-84 in markets in Africa, Australia, and Oceania. Major trends include the increasing emphasis of expanding countertrade transactions to include light consumer and industrial manufacturers (as opposed to being limited to agricultural commodities and natural resources/raw materials) and the increasing use of countertrade in government procurement programs.

Until recently, African nations as a group have resisted countertrade transactions. Resistance to such trade resulted, in part, from IMF opposition to countertrade, "African officials'" aversion to what they view as "primitive," hopes for rapid economic recovery, the preponderance of basic commodities in Africa's export mix, and fears of undercutting established foreign markets, 3/ as well as some adverse experiences in countertrade deals. Opposition to countertrade has begun to soften in the face of economic pressures to reduce external debt. In the past 2 to 3 years, incentives to countertrade include decreased development funds from developed nations and a deterioration of commercial sources of financing. 4/ A number of African nations have engaged in countertrade transactions with Eastern European countries and the Soviet Union through bilateral trade and clearing agreements.

Like Indonesia and Malaysia, Australia and New Zealand have required countertrade in government procurement, although not to the same degree. Australia requires offsets for major government procurements with foreign suppliers. 5/ New Zealand encourages countertrade proposals in all government tenders where the bid exceeds $2 million. Canada has also required offsets in the procurement of major weapons systems.

Impact of Countertrade on U.S. Companies

During 1980-84, the value of goods and services received in countertrade and imported into the United States totaled $2 billion as shown in the following tabulation (in millions of dollars):

1/ "Latin American Actions Facilitating CT Told," Countertrade Outlook, July 30, 1984, p.3.

2/ "Colombia Issues CT Rules; Peru, Bolivia, Venezuela said to Express Interest," Countertrade Outlook, July 30, 1984, p. 1.

3/ "Developing Countertrade Mechanisms for Africa: What MNCs Need To Do," Business International, Apr. 20, 1984, p. 123.

4/ Thaddeus C. Kopinski, op. cit, p. 123.

5/ Extract from the Inglis Committee Report of the Committee of Review on Offsets, Feb. 10, 1985.

Year	U.S. imports received in countertrade	U.S. imports received in countertrade associated with military export sales 1/	Total
1980-------	323	3	326
1981-------	360	25	385
1982-------	366	28	394
1983-------	332	50	382
1984-------	420	105	525
Total--	1,801	211	2,021

1/ Partially estimated by the staff of the U.S. International Trade Commission.

Such imports rose from $326 million in 1980 to $525 million in 1984, or by 61 percent. Nonmilitary countertrade imports accounted for almost 100 percent of total countertrade imports in 1980 but decreased to 80 percent of the total in 1984. The principal source of these imports was Eastern Europe (see table E-7). U.S. imports associated with military export sales rose from almost $3 million or 1 percent of total imports, in 1980 to $105 million, or 20 percent of all countertrade-related imports, in 1984. 1/

Countertrade resulting from offset obligations associated with military export sales are shown in table E-8 by the method of disposal of the goods/services received by the year in which the countertrade transaction begins. The value of such countertrade that was absorbed by U.S. firms in their facilities in the United States or sold in the United States totaled $86.1 million in 1980, decreased to $43.4 million in 1981, and then rose to $313.1 million in 1984.

U.S. exports resulting from sales agreements involving countertrade increased substantially more than did corresponding imports. In fact, the trade balance resulting from countertrade grew from a deficit of $41 million in 1980 to a surplus of $835 million in 1984. The value of U.S. exports of products sold under a sales agreement associated with countertrade (excluding offsets) increased by 377 percent, from $285.2 million in 1980 to almost $1.4 billion in 1984, as shown in the following tabulation:

1/ See table D-1 for the types of goods and services imported into the United States, by SIC codes, for 1980-84.

Period	U.S. exports and planned exports associated with nonmilitary countertrade (million dollars)
1980	285.2
1981	899.2
1982	1,135.1
1983	1,818.7
1984	1,360.1
1985	1,309.2
1986	568.0
1987	309.3
1988	305.0
1989-2000	2,089.0

Exports of aircraft and parts constituted a significant percentage of exports associated with nonmilitary countertrade commitments. 1/ The following tabulation shows the value of exports of SIC code 372--aircraft and parts--sold in contracts associated with countertrade (excluding military offset obligations) and the percentage of such exports relative to total nonmilitary countertrade exports during 1980-84, in (million of dollars):

Year	Exports of aircraft and parts associated with nonmilitary countertrade	Ratio of aircraft and parts exports to total counter-trade exports 1/
1980	17.3	6
1981	555.6	62
1982	417.8	37
1983	1,199.2	66
1984	685.9	50
Total	2,875.8	52

1/ Values are for the year in which the offset obligation was initiated.

When U.S. imports received in countertrade (including offsets) are measured against U.S. imports of goods and services as reported in the U.S. current account balance in 1984, imports represent only slightly more than 0.1 percent (525.3 million dollars' worth of countertrade imports versus $464 billion dollars worth of total U.S. imports of goods and services). 2/ U.S. exports of goods and services related to nonmilitary countertrade contrasted in the same manner represent only 0.37 percent of total U.S. exports of goods and services in 1984.

1/ See table D-1, for the types of goods and services exported from the United States, by SIC codes, for 1980-2000.

2/ U.S. current account balance for 1984 was a deficit of $101 billion. See U.S. Department of Commerce, "Current International Trade Position of the United States," May 1985. This excludes U.S. Government barter.

Sectors

Countertrade (including military offsets) has been practiced more extensively in certain sectors of the economy than others. According to a study by the National Foreign Trade Council Foundation in December 1983, exports of the following industries were most affected by countertrade: aerospace, construction projects, electronics, defense, and minerals and chemicals. 1/ Data submitted to the Commission's questionnaires indicate that the exports of those industries manufacturing aircraft and parts (SIC 372), certain defense articles (ordnance (SIC 348), miscellaneous transportation vehicles (SIC 379), and guided missiles and space vehicles and parts (SIC 376)), and communication and electronics equipment (SIC 366 and 367) were the most affected by countertrade (including offsets), as shown in the following tabulation (in millions of dollars):

Item	1980	1981	1982	1983	1984
Aircraft and parts	6,690	3,995	433	4,145	2,768
Certain defense articles	179	97	171	196	719
Communications and electronics equipment	923	430	241	730	1,182
Total sales	7,792	4,522	845	5,071	4,669

The United States maintains a competitive advantage in each of the above-mentioned high-technology industrial sectors. Although the United States is also a major agricultural products exporter, such exports, according to data collected in this investigation, are only slightly affected by countertrade. However, countertrade of agricultural products occurs frequently among Third World countries. 2/

U.S. firms surveyed by the Commission also reported that countertrade (including offset) obligations were undertaken primarily in the following industries: aircraft and parts (SIC 372); communications and electronics equipment (SIC 366 and 367); and engines and turbines (SIC 351). 3/ These obligations are shown in the following tabulation for 1980-84 (in millions of dollars):

1/ Submission by W.A. Bussard, Vice President, Univex Corporation, Nov. 5, 1984, p. 18.

2/ For a partial list of such countertrade, see Donna U. Vogt, Congressional Research Service, Library of Congress, U.S. Government International Barter, Report No. 83-211 ENR, Dec. 6, 1983, pp. 73-89.

3/ Data on engines and turbines are not presented here because they are business confidential.

Item	1980	1981	1982	1983	1984
Aircraft and parts	471.0	1,400.4	120.5	145.6	840.6
Communications and electronics equipment	57.7	640.6	106.0	362.2	329.7
Total sales	528.7	2,041.0	226.5	507.8	1,170.3

Aside from the large commitments of U.S. firms in these sectors, data from the Commission's investigation reveal that new sources of supply and competitors for certain products are being created by countertrade, particularly in military offset arrangements (see tables E-4 and E-5, for newly created defense and nondefense sources of supply). The products areas of these new sources of supply include metal processing and fabrication, weapons, engines and turbines, aircraft and parts, communications and electronics equipment, and related computer and data processing services.

U.S. firms have also expressed concern over new domestic competitors emerging in a particular industry as a result of countertrade. For example, U.S. travel companies are now competing with U.S. arms and aerospace manufactures in promoting tourism overseas. U.S. companies are currently engaged in military offset arrangements involving tourism with Canada, Australia, Spain, Israel, and Turkey. Commercial aerospace offsets for tourism exist with Finland and Yugoslavia. Greece is reportedly interested in tourism offsets for promoting business conferences. 1/

Respondents also expressed concern that imports resulting from countertrade disrupt domestic markets. The American Iron & Steel Institute, in a submission to the Commission, expressed concern that increasing tonnages of U.S. imports of steel may be the result of countertrade. 2/ One U.S. manufacturer alleged that Romanian and Polish nails imported in 1983-84 as a result of a countertrade deal were sold below the domestic selling price and the domestic cost of production, thus disrupting domestic nail pricing in the Mideastern and Eastern United States. 3/

In some cases, U.S. firms have sought relief from imports associated with countertrade deals. The Commission has conducted two investigations involving countertrade products--anhydrous ammonia and truck trailer axles. In July 1979, the Commission investigated imports of anhydrous ammonia from the U.S.S.R. under section 406 of the Trade Act of 1974 to determine if there was market disruption to U.S. produced ammonia. Although the Commission's

1/ Submission of Cord D. Hansen-Sturm, vice president, First Family of Travel, May 30, 1985, pp. 13-14.

2/ Submission of the American Iron & Steel Institute, May 23, 1985.

3/ Submission of Nicholas R. Owens, President, Keystone Steel and Wire, Nov. 6, 1984, pp. 1-2.

finding was affirmative, 1/ the President took no action. In January 1980, a second investigation was conducted, at the request of the President. The Commission, with newly appointed members, made a negative determination and subsequently no import relief was provided. 2/ During the investigation, the President invoked the emergency powers contained in section 406 to limit imports of anhydrous ammonia from the U.S.S.R. and ordered an embargo on the export of superphosphoric acid. 3/

In February 1981, the Commission investigated whether truck trailer axle-and-brake assemblies and parts were being sold in the United States at less-than-fair-market value and whether the U.S. industry was being materially injured as a result of this importation. The investigation was suspended when the Hungarian manufacturer agreed to revise its prices. 4/

In August 1984, the American Textile Manufacturers Institute, the Amalgamated Clothing & Textile Workers Union, and the International Ladies Garment Workers Union filed petitions for countervailing duties against 13 countries, three of which--Portugal, Columbia, and Indonesia--were alleged to have used countertrade as unfair subsidies. In all three instances, the petitions were subsequently withdrawn.

Measures taken by U.S. companies to facilitate countertrade demands

In the past, most U.S. companies confronted with countertrade demands have taken one of two approaches: refusing to enter into noncash deals or attempting countertrade through outside services and/or the firm itself. In response to the Commission's questionnaires, a number of U.S. firms stated that their corporate policy was not to engage in countertrade or offset obligations (whether or not related to military export sales). As a result, in some instances, U.S. firms have lost sales to foreign competitors, primarily Western European and Japanese firms. During 1980-84, 31 export contracts, totaling $1.0 billion, were lost because of companies' unwillingness to accept nonmilitary countertrade requirements, as shown in the following tabulation:

1/ Anhydrous Ammonia From the U.S.S.R.: Report to the President on Investigation No. TA-406-5, USITC. Publication 1006, October 1979, p. 1. The ammonia imports were committed under a 20-year agreement covering the period 1978-97 between Occidential Petroleum Corp., a large U.S.-based producer of oil and gas, fertilizer, and chemical products, and the Ministry of Foreign Trade of the U.S.S.R. Under a series of agreements, Occidential was to buy approximately 4 million tons of ammonia and related fertilizer products from the Soviet Union annually in exchange for million metric tons of super phospheric acid. Occidential was also to supply designs, equipment, and technology for constructing modern ammonia plants in the U.S.S.R.

2/ Anhydrous Ammonia from the U.S.S.R.: Report to the President on Investigation No. TA-406-6, USITC. Publication 1051, April 1980, p. 1.

3/ Presidential No. 4714, 45 F.R. 387 (Feb. 25, 1980).

4/ Truck Trailer Axle-and-Brakes Assemblies, and Parts Thereof from Hungary: Determination of the Commission in inv. No. 731-TA-38 USITC Publication 1135, March 1981, p. 1. See also 47 F.R. 66 (Jan. 4, 1982).

Year	Number of contracts forgone	Value of contracts forgone In million of dollars
1980	0	-
1981	1	2.0
1982	8	203.9
1983	11	283.1
1984	11	531.4
Total	31	1,020.4

In the case of military export sales, a number of U.S. companies stated that there would have been no sales agreement without accepting the offset obligation.

Today, more U.S. multinational corporations are using, or plan to use, inhouse trading organizations to handle their countertrade arrangements. These inhouse organizations differ both in the size and scope of their operations. Some are established as independent subsidiaries that negotiate countertrade agreements for unrelated companies as well as for their parent companies. They may even be involved in buying and selling commodities as part of a countertrade deal or as an independent transaction. At the other end of the spectrum are those organizations with one or two employees who make arrangements to satisfy their company's countertrade obligations.

The following tabulation, shows the type of organization that was used (or would be used) to arrange countertrades (excluding offsets) and/or to dispose of the countertraded products. U.S companies generally indicated they would use an inhouse organization or a subsidiary to arrange countertrades and to dispose of the products obtained in countertrade.

Item	Arranging and negotiating countertrade	Disposing of products obtained in countertrade
Inhouse organization	40	32
Trading subsidiary of company's firm	14	10
Bank trading company	4	5
Independent trading company:		
Based in the United States	5	10
Based in Europe	4	8
Based in Japan	-	2
Other	2	2
Total	69	69

Respondents to the Commission's questionnaire indicated that the majority of products obtained through contracts in which a nonmilitary countertrade was negotiated were primarily used inhouse, as shown in the following tabulation:

Type of disposition	Number of occurences
Absorbed in house	71
Sold to suppliers	4
Sold by trading company	39
Other:	
Unspecified	5
Sold to firm's customers	3
Sold to third parties	20
None	26
Total	168

Of the 168 reported occurrences, 71 (or 42 percent) were absorbed inhouse, and 39 (or 23 percent) were sold by trading companies. As shown below, of all goods and services associated with nonmilitary countertrade that were imported into the United States, approximately 33 to 50 percent was absorbed for inhouse use, except in 1982 when 64 percent was absorbed:

Year	Value of nonmilitary countertrade imports used inhouse (million dollars)	Ratio of nonmilitary countertrade imports used inhouse to annual imports (percent)
1980	106	33
1981	170	47
1982	233	64
1983	142	43
1984	185	44
Total	836	48

Employment

Respondents engaged in military countertrade generally reported that export sales related to military offsets do not have an adverse impact on domestic employment; rather, such sales agreements have either helped maintain stable employment levels or increased them. Overwhelmingly, the majority of respondents indicated that without the military export sales agreement with the accompanying offset obigation, there would have been a probable overall reduction in work required and jobs available. For other respondents, offsets represented, in many instances, a means of maintaining existing plant capacity and employment.

Practical capacity

Similar to the response concerning U.S. employment effects, responses to the Commission's questionnaire relating to military exports sales associated with offsets showed that practical capacity has not been adversely affected. U.S. companies stated that military export sales associated with offsets have resulted in more efficient utilization and improvement of existing plant and equipment with stable and/or increased production. According to respondents, the major benefits derived from such sales have been larger production lots/runs, lower costs, capital expansion, increased employment, and the development of new technology. In addition, competitiveness has been maintained, and prices have remained stable.

Surge capacity

U.S. companies involved in military export sales during 1980-84 indicated that wartime surge capacity would not be adversely affected because of military export sales involving offset obligations. In general, respondents stated that product schedules could actually be doubled by increasing manpower and shifts so that surge requirements could be more readily achieved. It was reported that such sales help meet surge capacity needs because assets are maintained at the plant, ready for operation. Several companies pointed out that their surge capacity is constrained by lead times on raw materials, parts and purchased equipment, and by plant and equipment limitations, rather than by offset obligations.

Profit center organizations

A few of the larger U.S. multinational corporations have set up trading companies as independent subsidiaries with the expectations that the trading subsidiary will generate enough revenues and earnings to become a self-supporting, profitable enterprise. To achieve this goal, these trading companies supply services, such as market research and development, importing and exporting, customs documentation, financing, and product distribution for a fee to their parent companies as well as to other, usually smaller, firms.

One of the primary functions of the trading company is to dispose of goods that the client firm is under contract to receive in a countertrade deal. It must find a buyer for the goods either through its own network of contacts in world markets or by engaging an agent or broker to arrange more complex deals. When countertrade goods fill an existing need and can be used to replace goods previously purchased with cash, the inhouse trading company may act simply as a procurer of goods for its clients. In doing so, it may take part in setting product specifications and delivery schedules to ensure that the countertraded goods are of comparable quality and compatible technology with those of other suppliers and that the availability of these products meets the needs of the client. When the client company cannot use the countertraded goods internally, the trading company must search elsewhere for a buyer. This may also involve setting product standards to meet a specific demand or quality requirement. When a buyer is found outside the client company, the value of the sale is credited against the client's countertrade obligation.

The inhouse trading subsidiaries also generate revenues and earnings in other ways. They use their trading expertise and networks to locate products to meet certain demands and to locate markets for certain products. These trading companies are active in trade among the LDC's and the Eastern bloc countries and collect fees for their services. Other activities of inhouse trading companies may include purchasing certain goods outright and then reselling them at a profit and entering into joint ventures with manufacturing companies in which the trading company acts as a worldwide marketing organization.

Cost center organizations

The cost center trading organization is a part of the company that is concerned primarily with satisfying the company's countertrade obligations. These organizations are not self-supporting, and their operating costs are considered part of the cost of doing business. In most cases, the expenses of these organizations are built into the product price charged to the foreign buyer.

Some of these inhouse organizations are devoted almost exclusively to finding buyers for countertrade goods supplied by foreign countries. They participate in any negotiations that are likely to involve countertrade and help the negotiators select the best available countertrade products. Because products offered in countertrade may be of lower quality or technology or in other ways unappealing in world markets, the inhouse trading organization is responsible for choosing the most salable products. Once the contract has been finalized, it is the responsibility of the trading organization to market those goods.

Another type of inhouse marketing organization does not directly involve itself in the marketing and distribution of countertrade goods. Instead, it works as an information broker supplying details on products and services that are available in countries with which its company has countertrade commitments. It establishes close ties with third-party agents and buyers both in the United States and foreign countries in order to extend its information base. Whenever an international trade transaction results from information or assistance provided by this trading organization, the value of the transaction is credited toward the company's countertrade obligations. This type of trading organization generally deals only with the products offered in trade and provides no specifications for these products. Since many of these items are not marketable in the developed countries because of quality, style, or technological considerations, this organization deals with many third-party agents and buyers in LDC's.

A third type of inhouse countertrade organization seeks to satisfy its company's countertrade obligations by locating countertrade products suitable for use within the company and not for resale. Large manufacturing organizations require many kinds of raw materials and supplies, ranging from bauxite and crude oil to work gloves and machine tools. With this range of requirements, the inhouse trading organization can choose countertraded goods to fill an existing need and satisfy the company's countertrade commitments. Again, the trading organization must ensure that the countertraded goods are of similar quality and technology as those that would have been purchased for cash and that the delivery schedule is compatible with the company's needs.

Although many of the large U.S. multinationals are moving toward inhouse countertrade organizations, many other U.S. firms involved in countertrade deal through independent agents or trading companies. For some of the companies the reasons are economic; they do not generate a large enough volume of countertrade to justify the expense of an inhouse organization. Other companies regard countertrade as a last resort and avoid any move to make it a larger part of their business.

Discounting goods obtained in countertrade

The trading organization has to be familiar with the potential markets and market values of the countertraded goods as well as with the products themselves, their quality, and the reliability of supply. Often the products offered in countertrade are overvalued by the producer. In this case, the trading company may try to negotiate a lower value that would more closely approximate market value. This may be acceptable to the producer if the products received in exchange fill an urgent need. However, many foreign producers and governments view this as an insult and believe that reducing the value of the countertraded goods lowers the prestige of the producer. Thus, it is often more palatable to inflate the price of the primary goods in the contract to achieve a more accurate value relative to that of the secondary goods.

In order to determine the amount that the countertraded goods must be discounted, the countertrade organization must have extensive knowledge of market values, market dynamics, and the product itself. On the basis of the expected market value and any cost associated with disposing of the product, the trading organization estimates how much, if at all, the countertraded goods should be discounted. The trading organization takes into account the fact that the market value at the time of negotiations may not be the same as at the time of the delivery of the goods. Changing conditions can result in a depressed market and thus a drop in the price of the secondary goods. The trading organizations must build these risks into the price structure of the contract.

Methods of disposing of goods obtained in countertrade

When the countertrade contract has been finalized, the company that has accepted goods in countertrade is faced with the task of disposing of them. If the product is one that the firm can use internally, it may replace supplies purchased for cash with countertraded items. These products are generally of two types. Some are inputs into the production process, such as raw materials and semifinished manufactured goods that the firm can turn into finished products. Others are items that can be used in the operations of the company. These include tools, machine parts, and office and work force supplies.

The inhouse use of countertraded goods can be cost effective if certain conditions are met. First, the products offered in countertrade must be comparable in quality and technical standards with those purchased for cash. Second, they must be delivered on a schedule that meets the needs of the receiving company. Third, they must not exceed the cost of alternative supplies. These criteria may be met at the start of the contract; however, over time, quality control may worsen or delivery schedules may not be met.

Either one of these events could raise the costs of the countertraded goods above that of alternative supplies and are risks that should be taken into account when negotiating a contract. In addition, the company receiving the countertraded goods has to deal with resistance within the company to giving up traditional suppliers.

Products that cannot be absorbed by the receiving company have to be sold elsewhere. This can be done either through an inhouse trading organization or through an agent or broker. Selling outside the company has the advantage of eliminating the risk of inhouse acceptance problems. When the countertraded items are related to the company's lines of business, their disposition is somewhat easier. Distribution channels are already in place for similar items and may be used for countertraded goods as well. There is also the possibility that related products could be sold to subcontractors. Another advantage is that the company can make use of inhouse technical and marketing expertise in choosing goods for known markets and in locating new markets when necessary.

There are some serious risks in selling countertraded goods that are closely related to the company's products. If the items are similar to the company's own goods but of lesser quality, there is the danger that the countertraded products will damage the reputation of the company and its relations with customers. This is especially true if countertraded products are distributed through the same channels as the company's own products. Another danger is that the countertraded goods will cause an oversupply in the marketplace. This would result in lower prices and profits and might cause the company's primary products to lose market share.

If the products accepted in countertrade are unrelated to the company's lines of business, disposal is a much more complex matter. To successfully market these goods, a wide range of knowledge and a large network of contacts are necessary. However, the technical expertise to find products that are marketable and the marketing expertise to find buyers for these products are not usually found within the company. They are likely to be found in a large, independent, inhouse trading subsidiary or a third-party agent or broker. Although this type of deal requires greater knowledge and flexibility, it opens up many more countertrade opportunities, because the company is not limited to a certain group of products.

Growth of U.S. Countertrade Service Industry

Independent trading companies

The recent surge in countertrade as an alternative to cash has prompted many organizations to develop countertrade operations and new trading companies to be formed. Following the enactment of the Export Trading Company Act of 1982, 1/ 50 new U.S. trading firms came into being, and another 50 are expected to start operations by the spring of 1985. In addition, there has been a similar growth in financial and legal services and in inhouse trading companies. Each of these new organizations is looking for opportunities to

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1/ The Export Company Trading Act was signed into law Oct. 8, 1982, S. 734, Public Law 97-290.

market its particular expertise and carve out its own market niche. Several multinational corporations have established independent trading subsidiaries that are expected to be profit-making ventures. For a fee, they arrange countertrade deals for other companies as well as their parent corporations. The primary selling point of these subsidiaries is that they can draw on the parent corporations for whatever market expertise and networks they can provide. To enhance their services they may also hire outside expertise to gain experience or knowledge not available internally or, in extremely complex deals, they may employ a broker or agent.

Established, independent trading companies are adding countertrade units to their staffs, and new trading companies are springing up to meet the needs of aspiring exporters and countertraders. Compared with the trading subsidiary, the independent trading company usually has more trading experience over a broader range of markets and a wider information and distribution network. However, it does not have the close ties with producers and purchasers that the inhouse trading organization has.

Banks and other commercial institutions

Commercial banks are well suited to handle countertrade transactions, since they are already in the business of financing international trade. Some commercial banks are using countertrade as a financing alternative, especially in limiting their risk in certain Third World countries. Commercial banks have an advantage, because their customers are accustomed to coming to them for financing and may trust them more than an untried trading company. Banks use their international network of customers and contacts for countertrade deals. Some banks seek the help of trading companies to consummate deals and further broaden the scope of their business. However, there are some difficulties for banks engaging in international trade--they usually have little practical product experience, and there are legal regulations that restrict a bank's involvement in trading companies.

Legal services

The legal profession has been increasingly called upon to provide legal service to countertraders, including advice on antitrust matters and unfair methods of competition, i.e., dumping. In response to the perceived need for legal services, over the past two or three years, established law firms have added countertrade units. 1/

U.S. Government and Countertrade

U.S. Government Position on Countertrade

In testimony before a subcommittee 2/ of the Committee on Banking, Finance and Urban Affairs, U.S. House of Representatives, the Office of the

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1/ Countertrade and Barter Quarterly, Spring, 1984.

2/ U.S. Congress, House Committee on Banking, Finance and Urban affairs, Subcommittee on Economic Stabilization, The Impact of Countertrade and Offset Agreements on the U.S. Economy, 98th Congress, May 22, 1984, p. 49.

United States Trade Representative described the U.S. position on countertrade as follows:

"1. The U.S. Government generally views countertrade as contrary to an open, free trading system. However, as a matter of policy, the U.S. Government will not oppose U.S. companies' participation in countertrade arrangements unless such action could have a negative impact on national security.

2. The U.S. Government will provide advisory and market intelligence service to U.S. businesses, including information on the application of U.S. trade laws to countertrade goods.

3. The U.S. Government will continue to review financing for projects containing countertrade/barter on a case-by-case basis, taking account of the distortions caused by these.

4. The U.S. Government will continue to oppose government-mandated countertrade and will raise these concerns with the relevant governments.

5. The U.S. Government will participate in reviews of countertrade in the International Monetary Fund (IMF), the Organization for Economic Cooperations and Development (OECD), and the General Agreement on Tariffs and Trade (GATT). (For a discussion of the role of the GATT and the OECD see app. H.)

6. The U.S. Government will exercise caution in the use of its barter authority, reserving it for those situations which offer advantages not offered by conventional market operations." 1/

Several other departments, including the U.S. Department of the Treasury, the Department of State and the Department of Commerce, have been involved in interagency and individual efforts aimed at either developing a U.S. position on countertrade or reviewing current countertrade practices including efforts to encourage the OECD to reach a consensus on constraining government-mandated countertrade. The U.S. Department of Commerce, in addition, has been providing information and advice to U.S. companies regarding countertrade requirements by foreign governments or firms.

The Department of Defense and Department of the Treasury have been active in reviewing offset practices and in formulating positions concerning offsets for their own Departments. 2/ In 1983, for instance, the Treasury Department conducted a study of offset arrangements in cooperation with the Aerospace Industrial Association and the Electronics Industry Association. 3/ Since 1978, the Department of Defense (DOD) has been prohibited from acting as a guarantor in offset involving U.S. contractors under the "Duncan" Memorandum, except in cases where the U.S. Government has an agreement in force with the

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1/ Op. cit.

2/ U.S. General Accounting Office, Trade Offsets In Foreign Military Sales, Apr. 13, 1984, app. 1., p. 9.

3/ U.S. Department of the Treasury, AIA/EIA Study, May 1983.

foreign government. 1/ According to DOD guidelines, a U.S. contractor involved in an FMS is responsible for negotiating any offset arrangement with the foreign government on his own.

There are two laws that encompass offset practices: the Arms Export and Control Act (AECA) and the Defense Security Assistance Agency (DSAA) guidelines on Foreign Military Sales credits. Section 42(b) of the AECA prohibits the issuing of FMS direct credits and guaranteed loans for use in financing coproduction or licensed production of any defense article of U.S. origin outside the United States except in cases where the Secretary of State provides the Congress with full information regarding the impact of such arrangements on employment and production within the United States prior to the proposed transaction. 2/ DSAA guidelines (1) discourage the use of credit financing for sales contracts containing offset provisions; (2) prohibit the use of FMS credit funds for mandatory direct offsets; and (3) authorize the use of FMS credit funds for the U.S.-produced content of a weapons system but prohibit the use of such funds for the foreign-produced content of such systems that result from mandatory offsets. 3/

A number of offset transactions have been initiated as a result of government-to-government agreements between the United States and its allies. These agreements are known as Memorandums of Agreement (MOA's), Memorandums of Understanding (MOU's), and Defense Cooperation Country Agreements. These umbrella agreements, in general, identify the authorities, procedures, and financial arrangements to be used in implementing the agreements. Such agreements are important because of their high potential dollar value (since many contracts are included under one agreement), their long-term nature, and their effects on bilateral relations between the two countries. The following tabulation is a list of all such agreements, by countries and years signed. 4/

1/ U.S. Department of Defense, General Policy on Compensatory Corproduction and Offset Agreements with Other Nations, memorandum, May 4, 1978, pp. 1-2.

2/ Arms Export Control Act, 22 U.S.C.S. 2791(b).

3/ Statement of Deputy Assistant Secretary of Defense, Policy Analysis, James R. Blaker, on the Impact of Offsets before the Subcommittee on Economic Stabilization of the House Committee on Banking, Finance, and Urban Affairs, July 24, 1985, p. 10.

4/ Amendments to the Defense Acquisition Regulation in the form of replacement pages to Appendix T- International Agreements, Federal Register, June 29, 1984, pp. 27033-27113, and the Code of Federal Regulations, Title 32.

Country	Type of agreement 1/	Date signed
Canada------------	Letter of Agreement and Cooperative Agreement	October 1963
Australia---------	Memorandum of Discussion	October 1973
Switzerland-------	Memorandum of Understanding on F-5	July 1975
United Kingdom----	Memorandum of Understanding	September 1978
France------------	do----	May 1978
Norway------------	do----	May 1978
Netherlands-------	do----	September 1978
West Germany------	do----	October 1978
Italy-------------	do----	October 1978
Portugal----------	do----	December 1978
Israel------------	Memorandum of Agreement	March 1979
Egypt-------------	Memorandum of Understanding	October 1979
Belgium-----------	do----	December 1979
Denmark-----------	do----	January 1980
Turkey------------	Supplementary Agreement	March 1980
Spain-------------	Memorandum of Understanding	July 1982
Luxembourg--------	do----	December 1982

1/ All of the above agreements were in effect as of September 1985.

The role of the U.S. Government in military-related export sales associated with offset obligations of more than $2 million can be seen in table 16. The role of U.S. Government as an active party in the negotiations of military export sales under the framework of an MOU/MOA that required offsets to the sale decreased during the period 1980-84. The "other" category increased in 1983 and 1984 owing, in part, to the increasing number of contracts signed in those years. This category includes instances where export licensing or similar U.S. Government approval was required or the items sold were either under an FMS contract or under a contract that had FMS contract financing.

Table 16.--Role of the U.S. Government in military-related export sales associated with offset obligations of more than $2 million, by number of occurrences and years signed, 1980-84

U.S. Government's role	1980	1981	1982	1983	1984
Active party in negotiations under framework of MOU/MOA that required offsets to the sale------------------	5	5	4	3	2
No active role in negotiation but an MOU/MOA did require offsets to the sale---------------------------------	3	3	4	1	8
Other-----------------------------------	12	12	12	16	36

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

In contrast to the U.S. Government's diminishing role in military export contracts with offset obligations, the foreign government played a paramount role in negotiating the offset obligation either as sole negotiator or as an active participant in the negotiations (table 17). However, the foreign government had a substantially smaller involvement in arranging the offset implementation agreement or had to approve the results of the implementation arrangement.

The U.S. Government's role as a party to the sales contracts, offset agreements, and implementation agreements compared with those of U.S. and foreign corporations is substantial (table 18). This reflects that under FMS contracts, the U.S. Government signs the agreement with the foreign government, and in implementing the sales agreements, it purchases the items to be supplied from U.S. contractors. However, as stated previously, the DOD is not involved in arranging the offset agreement, particularly for agreements entered into after 1978. This can be seen in table 18, with the role of the U.S. Government dropping to only 11 occurrences of involvement in offset agreements and no participation in implementation agreements.

Table 17.--Role of foreign government in arranging for foreign military sales contracts, offset agreements of $2 million or more, and implementation agreements, by number of occurrences, 1980-84

Role of foreign government	Sales	Offset agreements	Implementation agreements
Sole negotiator	79	92	30
Active participant in the negotiations	16	20	18
Observer to the negotiations	3	4	5
No role in negotiations or in approval	13	9	13
No role in negotiations but had to approve results	17	6	22
Not identified	15	11	48

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table 18.--Parties to foreign military sales contracts, offset agreements of $2 million or more, and implementation agreements, by number of occurrences, 1980-84

Party to contract agreement	Sales	Offset agreements	Implementation agreements
Another U.S. contractor	5	8	15
A foreign government-owned company	8	13	27
Private foreign company	5	14	46
U.S. Government	38	11	0
Not identified	76	99	67

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Examination of U.S. Government Barter Programs 1/

Historical perspective

U.S. Government barter programs were first provided for in the Commodity Credit Corporation (CCC) Charter Act of 1949 and later incorporated into the Agricultural Trade Development and Assistance Act of 1954 (Public Law 480). These two laws are the basic legislation that allow the U.S. Secretary of Agriculture to barter or to exchange agricultural commodities acquired by the CCC for strategic and critical materials from abroad for the national emergency stockpile, or for foreign-produced supplies and services for U.S. agencies operating abroad (e.g., construction projects for the Department of Defense or projects of the Agency for International Development (AID)). Barter contracts were negotiated only with countries for which the U.S. Department of Agriculture determined that commercial sales displacement would be at a minimum--generally countries with poor balance-of-payment positions. In these transactions, the CCC did not enter into contracts with foreign governments to deliver designated strategic materials or supplies and services originating in specified countries, but rather with commercial firms.

Under the barter program (1950-75), 2/ the value of agricultural commodities exported totaled nearly $6.7 billion. Wheat, corn, other feedgrains, tobacco, nonfat dry milk, butter, and cotton were the major commodities exported under the program. In addition to supplies and services for U.S. Government agencies, receipts under the program included strategic materials such as aluminum oxide, asbestos, diamond (stones), beryllium, bauxite, fluorspar, lead, mercury, and manganese ore.

1/ Barter of agricultural commodities held by the Commodity Credit Corporation--a Federal corporation with the U.S. Department of Agriculture. 15 U.S.C. 714.

2/ The barter program was suspended on June 30, 1973. However, exchanges of materials under contract prior to that date continued until 1975.

During 1950-62, most barter transactions were called strategic material contracts. These transactions involved exchanges of CCC-owned commodities for strategic materials (table 19). By 1962, however, changes in planning for

Table 19.--Value of agricultural commodities exported under strategic material and offshore contracts through the CCC barter programs, fiscal years 1950-75 1/

(In thousands of dollars)

Fiscal year	Strategic material contracts	Offshore contracts	Total program exports
1950	7,782	2/	7,782
1951	8,524	2/	8,524
1952	42,818	2/	42,818
1953	14,113	2/	14,113
1954	34,398	2/	34,398
1955	124,605	2/	124,605
1956	298,387	2/	298,387
1957	400,486	2/	400,486
1958	99,830	2/	99,830
1959	132,255	2/	132,255
1960	149,190	2/	149,190
1961	143,951	2/	143,951
1962	198,369	2/	198,369
1963	47,447	12,641	60,088
1964	43,458	68,715	112,173
1965	31,926	98,222	130,148
1966	32,074	196,745	228,819
1967	22,477	273,170	295,647
1968	6,339	295,948	302,287
1969	1,405	267,788	269,193
1970	2/	467,836	467,836
1971	2/	870,050	870,050
1972	2/	875,894	875,894
1973	2/	1,088,291	1,088,291
1974	2/	293,758	293,758
1975	2/	4,692	4,692
Total	1,839,834	4,813,750	6,653,584

1/ Program suspended June 30, 1973; activity after that date reflects the phasing out of open contracts.
2/ No contracts.

Source: U.S. Department of Agriculture, Foreign Agriculture Service.

wartime needs had reduced stockpile goals, and inventories of strategic materials often exceeded requirements. Also, the surplus agricultural inventories owned by the CCC had been greatly reduced. Thus, beginning in 1963, greater emphasis was placed on the barter of U.S. agricultural commodities from privately owned stocks, as permitted under the CCC Charter

Act. Such barter was for the procurement of foreign-produced supplies and services for overseas military installations and for projects of the AID, rather than for procurement of strategic materials. 1/ These barter contracts were called offshore contracts. In June 1973, when CCC stocks were largely depleted and the supply of privately held agricultural stocks no longer justified the need for such a program, the U.S. Government barter program was suspended. Authority for the President to barter foreign assistance and services for strategic materials also existed in the Foreign Assistance Act of 1974. 2/ This authority has not been used to date.

The recent U.S.-Jamaican barter agreement.--In November 1981, the President directed the Federal Emergency Management Agency to procure approximately 1.6 million tons of Jamaican bauxite for the national defense stockpile. 3/ On February 25, 1982, the Government of Jamaica (represented by the Bauxite & Alumina Trading Company Ltd. of Jamaica (BATCO)), and the Government of the United States (represented by the CCC) signed a barter agreement to exchange CCC-owned dairy products, valued at $13 million, for an equal value of Jamaican bauxite (400,000 tons). In addition, a barter agreement was signed between BATCO and the General Services Administration (GSA) whereby GSA acquired the remaining 1.2 million tons of bauxite through cash purchases and the exchange of excess stockpile materials (mainly tin and tungsten). This was the first major U.S. Government barter agreement since 1967. This agreement partly replenished the U.S. stockpile of bauxite. It also permitted the CCC to dispose of surplus dairy products after consultations with the traditional suppliers (Canada, France, and New Zealand) of such products to Jamaica. The President noted that although the agreement improved the U.S. defense posture, it contributed to Jamaica's strategy of relying on production and exports to fuel its economic recovery. He also noted that the stability and economic strength of Jamaica are important to the national security interests of the United States in the Caribbean. On November 17, 1983, another U.S.-Jamaican barter agreement was signed that called for a total of 1 million tons of Jamaican bauxite to be exchanged for CCC-owned dairy products and wheat valued at $34 million. Delivery of all the products included in the agreement is to be completed in 1985. 4/

Other proposed U.S. barter agreements.--The only other barter agreement that has been formally proposed to the United States (April 1984) was an arrangement whereby CCC-owned nonfat dry milk would be exchanged for fluorspar from Mexico. A decision on the proposal, which was being reviewed by the Working Group on Barter, was delayed pending the completion of the U.S. Government study on the goals of U.S. strategic stockpile. As a result of the

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1/ Donna U. Vogt, Cathyl Jabara, and Dee A. Linse, U.S. Department of Agriculture, International Economics Division, Economic Research Service, Barter of Agricultural Commodities, April 1982, p. 13.

2/ The United States is approximately 90 percent dependent on imported bauxite to satisfy domestic aluminum requirements. Jamaica is the world's second largest producer of bauxite, and that country supplies about 40 percent of the U.S. imports.

3/ Bauxite is a basic raw material used to produce aluminum, a significant component in military weapons and aerospace systems.

4/ These U.S. exports of agricultural products under barter agreements have accounted for only a small part of the total value of U.S. agricultural exports, which declined from $43 billion in 1982 to $36 billion in 1983.

study, lower stockpile requirements were established for fluorspar. In view of these new goals, the Mexican proposal was rejected in November 1984, as it was not in the interests of the United States to acquire flurospar through barter. 1/

Also, in late 1984, the Dominican Republic expressed interest in the barter of bauxite for CCC-owned dairy products and the Republic of South Africa has discussed a possible exchange of fluorspar, platinum group metals, and chromite for CCC-owned corn. In both instances, the U.S. Government requested further details and is currently awaiting further information. In addition, in mid-1984, Kenya discussed with the U.S. Department of Agriculture a possible exchange of pyrethrum (an insecticide) for rice; however, the proposal was not reviewed, since a U.S. Government study was being conducted at the time to consider the removal of pyrethrum from the stockpile. 2/

Existing barter legislation

Current legislation authorizes the President to barter agricultural commodities acquired by the CCC, as well as excess stockpile materials, for critical and strategic materials produced abroad or for supplies and services required by U.S. agencies operating abroad. Such authority includes the CCC Charter Act of 1949 (15 U.S.C. 714 b(h)), the Strategic and Critical Materials Stock Piling Act (50 U.S.C. 98 et seq.), the Agricultural Trade Development and Assistance Act of 1954 (Public Law 480, sec. 310) (7. U.S.C. 1727(g), and sec. 416 of the Agricultural Act of 1949 (7 U.S.C. 1431). The basic goals of these legislative acts are to permit the exchange of CCC-owned commodities or agricultural commodities in private stocks, for strategic and critical materials produced abroad, or for supplies and services required by U.S. agencies operating abroad. The materials acquired through barter are to be transferred, with reimbursement to the CCC, to the stockpile provided for in the Strategic and Critical Materials Stock Piling Act. The stockpiling of these materials is to preclude a costly and dangerous U.S. dependence upon foreign sources of supply in times of national emergency.

To the extent practicable, commercial trade channels are to be used in U.S. barter transactions. In addition, all countries of the free world are to be allowed to participate in the transactions, world prices are not to be disrupted, and normal patterns of commercial trade are to be preserved; nondiscriminatory treatment is to be exercised in procurement as set forth in the GATT agreement on Government procurement. Commodities bartered from CCC-owned inventories are subject to legislated minimum valuations. Their exportation is not to replace dollar sales, and transactions are to occur on a bilateral basis. Generally, transportation of the commodities, unless they are from private stocks, is subject to the requirements of the U.S. Cargo Preference Act of 1954 (46 U.S.C. 1241(b)).

1/ Telephone conversation with officials of the U.S. Department of Agricultural, Foreign Agricultural Service, July 31, 1985.

2/ Telephone conversation with officials of the U.S. Department of Agriculture, Foreign Agricultural Service, July 31, 1985.

Proposed barter legislation

During the 98th Congress, at least 26 bills were introduced to encourage barter or to expand existing barter legislation. A number of the bills would require that barter policy be coordinated within the executive office of the President and opportunities for barter be identified and pursued. Development of new markets was to be encouraged and the negotiation period of transactions to be shortened. Most, if not all, of the bills required that cash sales of agricultural products not be replaced by barter and that world market prices not be disrupted. Private U.S. trading companies were to have initiated and proposed barter transactions, with such transactions subject to approval by the U.S. Secretary of Agriculture. Most of the proposed bills would have eliminated the requirement that the CCC be reimbursed for the commodities bartered, particularly if petroleum were received into the Strategic Petroleum Reserve. Some of the bills provided for foreign nations to transport materials for the National Defense Stockpile to the United States; the materials are to be stored as collateral for their agricultural purchases. In the event of a national emergency or proposed withdrawal of these materials because of shortages, the U.S. Government would have the right to purchase the materials at current market prices.

No definitive barter bills were enacted during the 98th Congress. However, a supplemental provision to a bill for African famine relief, which was enacted, provided the option to barter U.S. agricultural commodities for such purposes. Subsequently, the U.S. Department of Agriculture put out a tender for the sale of agricultural commodities. Another bill enacted by the Congress authorized the use of barter to acquire materials for the National Defense Stockpile, but to date, this provision has not been implemented.

The 98th Congress expressed interest in certain types of countertrade by including section 309 in the Defense Production Act Amendments of 1984 on April 17, 1984 (P.L. 98-265). 1/ Section 309 requires the President to submit a "report on the impact of offsets on the defense preparedness, industrial competitiveness, employment, and trade of the United States," to the Committee on Banking, Finance and Urban Affairs of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate.

During the 99th Congress, a number of bills that have sections dealing with U.S. Government barter or offsets were proposed and in some instances enacted. Eleven bills dealt with U.S. Government barter in promoting the export of U.S. agricultural commodities through the CCC for the purpose of expanding markets or acquiring strategic materials. These include H.R. 201, Argicultural Export Trade Equity Act of 1985; H.R. 1555, International Security and Development Cooperation Act of 1985 (incorporated as an amendment into S. 960); H.R. 1766, Barter Promotion Act of 1985; H.R. 2359, Agricultural Export Reserve Act of 1985; H.A. 304 (House Amendment), an amendment to the Agricultural Trade Development and Assistance Act of 1984; S. 42, Barter Promotion Act of 1983; S. 616, Agriculture, Food, Trade, and Conservation Act of 1985; and S. 1049, Agricultural Fair Trade Act of 1985. H.R. 1239, which was passed as P.L. 99-10, provides for the use of barter in facilitating the emergency relief and recovery in Africa. Two bills, H.R. 1786, and S. 883

1/ See app. B.

were amendments to the Export Administration Act of 1979 and dealt with U.S. Government barter. The Export Administration Act of 1979 Extension (P.L. 99-64), signed into law in July 1985, in section 203(a) requires the Secretary of Agriculture and Secretary of Energy to submit to Congress a report on the status of Federal programs relating to the barter or exchange of commodities owned by the CCC for materials and products produced in foreign countries. Section 203(b) authorizes the President to barter stocks of agricultural stocks for petroleum and petroleum products as well as other materials vital to the national interest. The President is also required to ensure that conventional markets are not displaced by U.S. Government barter and that any such barter transaction is consistent with U.S. international obligations, including the GATT. Another legislative proposal concerning offsets was H.R. 1415, the Conventional Arms Transfer Control Act, introduced in March 1985. 1/ The act would require the President to report on the aggregate dollar value of all commercial manufacturing license agreements approved under the Arms Export Control Act for the previous fiscal year and any offset agreements associated with military export sales.

1/ A description of the Conventional Arms Transfer Control Act appears in the Congressional Record, March 5, 1985, p. E-749.

Appendix A

Notice of Institution of Countertrade Investigation, Notice of Agency Form Submission to OMB, and Notice of Modifications of Hearing Dates

25316 Federal Register / Vol. 49, No. 120 / Wednesday, June 20, 1984 / Notices

INTERNATIONAL TRADE COMMISSION

[332-185]

Assessment of the Effects of Barter and Countertrade Transactions on U.S. Industries

AGENCY: United States International Trade Commission.

ACTION: Institution of an investigation under section 332(b) of the Tariff Act of 1930 (19 U.S.C. 1332(b)) for the purpose of assessing the effects of barter and countertrade transactions on U.S. industries, and the scheduling of a hearing in connection therewith.

EFFECTIVE DATE: June 11, 1984.

FOR FURTHER INFORMATION CONTACT: Mr. Ronald DeMarines, Machinery and Equipment Division, Office of Industries, United States International Trade Commission, 701 E Street NW., Washington, D.C. 20436, telephone 202-523-0259.

Background and Scope of Investigation

The Commission instituted the investigation on its own motion. Barter and countertrade transactions involving U.S. companies are rapidly expanding, particularly in North-South trade. Many Latin American, African, and Asian developing countries have or are in the process of instituting government mandated barter and counter-trade programs. Significant developments are occurring in the United States to assist U.S. companies facilitate countertrade commitments. Export trading companies, spurred in part by passage of the Export Trading Company Act, in-house countertrading organizations of multinationals, and special legal units of law firms specializing in international law are part of the evolving barter/countertrade service industry.

This study will assess the effects of the growing involvement of U.S. companies in international barter and countertrade transactions, examine the effects of such involvement on U.S. industries, provide data on the level of imports and exports and their sources and destinations, and examine the economic conditions that have created the tremendous demand for countertrade on the part of developing countries.

The Commission expects to complete its study by January 1985.

Public Hearing

A public hearing in connection with the investigation will be held in the Commission Hearing Room, 701 E Street NW., Washington, D.C. 20436, beginning at 10:00 a.m., on November 14, 1984, to be continued on November 15, if required. All persons shall have the right to appear by counsel or in person, to present information, and to be heard. Requests to appear at the public hearing should be filed with the Secretary, United States International Trade Commission, 701 E Street NW., Washington, D.C. 20436, not later than noon, November 7, 1984.

Written Submissions

In lieu of or in addition to appearances at the public hearing, interested persons are invited to submit written statements concerning the investigation. Written statements should be received by the close of business on November 9, 1984. Commercial or financial information which a submitter desires the Commission to treat as confidential must be submitted on separate sheets of paper, each clearly marked "Confidential Business Information" at the top. All submissions requesting confidential treatment must conform with the requirements of § 201.6 of the Commission's *Rules of Practice and Procedure* (19 CFR 201.6). All written submissions, except for confidential business information, will be made available for inspection by interested persons. All submissions should be addressed to the Secretary at the Commission's office in Washington, D.C.

Issued: June 11, 1984.

By order of the Commission.

Kenneth R. Mason,

Secretary.

[FR Doc. 84-16430 Filed 6-19-84; 8:45 am]

BILLING CODE 7020-02-M

INTERNATIONAL TRADE COMMISSION

Agency Form Submitted for OMB Review

AGENCY: International Trade Commission.

ACTION: In accordance with the provisions of the Paperwork Reduction Act of 1980 (44 U.S.C. Chapter 35), the Commission has submitted a proposal for the collection of information to the Office of Management and Budget for review. The Commission is requesting an expedited review and approval of the Commission's questionnaire by the Office of Management and Budget on or before December 21, 1984.

Purpose of Information Collection

The proposed information collection is for use by the Commission in connection with investigation No. 332–185, Assessment of the Effects of Barter and Countertrade Transactions on U.S. Industries, instituted under the authority of section 332(b) of the Tariff Act of 1930 (19 U.S.C. 1332(b)). Information called for in this questionnaire pertaining to military related export sales and resulting offset obligations is for use by the President as mandated by section 309 of the Defense Production Act Amendments of 1984 (Pub. L. 98–265), enacted on April 17, 1984.

Summary of Proposals

(1) Number of forms submitted: One.

(2) Title of form: Assessment of the Effects of Barter and Countertrade Transactions on U.S. Industries—Questionnaire for companies that have negotiated countertrade agreements or that have offset obligations resulting from military related export sales.

(3) Type of request: New.

(4) Frequency of use: Nonrecurring.

(5) Description of respondents: Firms manufacturing products in the United States that have negotiated barter or countertrade agreements with foreign organizations or that have offset obligations resulting from military related export sales.

(6) Estimated number of respondents: 150.

(7) Estimated total number of hours to complete the form: 5,250.

(8) Information obtained from the form that qualifies as confidential business information will be so treated by the Commission and not disclosed in a manner that would reveal the individual operations of a firm. Information supplied in connection with this survey associated with military related export sales regarding offsets will be made available in aggregated form to appropriate Executive agencies as designated by the Office of Management and Budget.

Additional Information or Comment

Copies of the proposed form and supporting documents may be obtained from Charles Ervin, the USITC clearance officer (tel. No. 202–523–4463). Comments about the proposals should be directed to the Office of Information and Regulatory Affairs of OMB, Attention: Ms. Francine Picoult, Desk Officer for the U.S. International Trade Commission on or before December 21, 1984. The expedited review is a result of a statutory requirement of Section 309 of the Defense Production Act Amendments of 1984. If you anticipate commenting on the form but find that time to prepare comments will prevent you from submitting them promptly you should advise OMB of your intent as soon as possible. Copies of any comments should be provided to Charles Ervin (United States International Trade Commission, 701 E Street NW., Washington, D.C. 20436).

By order of the Commission.

Kenneth R. Mason,

Secretary.

Issued: November 30, 1984.

[FR Doc. 84-31769 Filed 12-3-84; 8:45 am]

BILLING CODE 7020-02-M

Federal Register / Vol. 49, No. 250 / Thursday, December 27, 1984 / Notices

[332-185]

Assessment of the Effects of Barter and Countertrade Transactions on U.S. Industries

AGENCY: International Trade Commission.

ACTION: Rescheduling of public hearing and deadline for filing written submissions.

EFFECTIVE DATE: December 18, 1984.

SUPPLEMENTARY INFORMATION: The public hearing in connection with investigation No. 332-185 has been rescheduled for April 10, 1985, to be continued on April 11, if required. The deadline for public comments in connection with this investigation has been extended to April 3, 1985. Notice of the Commission's institution of the investigation and the original public hearing in connection therewith was published in the Federal Register of June 20, 1984 (49 FR 25316). The original public hearing, scheduled for November 14, 1984, was canceled.

By order of this Commission.

Issued: December 21, 1984.

Kenneth R. Mason,

Secretary.

[FR Doc. 84-33850 Filed 12-26-84; 8:45 am]

Billing Code 7020-02-M

[332-185]

Assessment of the Effects of Barter and Countertrade Transactions on U.S. Industries

AGENCY: United States International Trade Commission.

ACTION: Rescheduling of public hearing and deadline for filing written submissions.

EFFECTIVE DATE: March 18, 1985.

SUPPLEMENTARY INFORMATION: The public hearing in connection with investigation No. 332-185 has been rescheduled for May 30, 1985, to be continued on May 31, if required. The deadline for public comments in connection with this investigation has been extended to May 23, 1985. Previous notices in connection with this investigation were published in the Federal Register of June 20, 1984 (49 FR 25316) and December 27, 1984 (49 FR 50317). The public hearing previously scheduled for April 10, 1985, is canceled.

Issued: March 19, 1985.

By order of the Commission.

Kenneth R. Mason,

Secretary.

[FR Doc. 85-7243 Filed 3-26-85; 8:45 am]

BILLING CODE 7020-02-M

Appendix B

Defense Production Act Amendments of 1984

DEFENSE PRODUCTION ACT AMENDMENTS OF 1984

For Legislative History of Act, see p. 346

An Act to extend the expiration date of the Defense Production Act of 1950.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Defense Production Act Amendments of 1984.

SHORT TITLE

SECTION 1. This Act may be cited as the "Defense Production Act Amendments of 1984". 50 USC app. 2061 note.

EXTENSION OF THE DEFENSE PRODUCTION ACT OF 1950

SEC. 2. The first sentence of section 717(a) of the Defense Production Act of 1950 (50 U.S.C. App. 2166(a)) is amended by striking out "March 30, 1984" and inserting in lieu thereof "September 30, 1986". 97 Stat. 1267.

DETERMINATIONS REQUIRED BEFORE THE AWARDING OF FINANCIAL ASSISTANCE

SEC. 3. (a) Section 301(a) of the Defense Production Act of 1950 (50 U.S.C. App. 2091(a)) is amended by adding at the end thereof the following:

"(3) Except during periods of national emergency declared by the Congress or the President, a guarantee may be entered into under this section only if the President determines that—

"(A) the guaranteed contract or operation is for a material, or the performance of a service, which is essential to the national defense;

"(B) Without the guarantee, United States industry cannot reasonably be expected to provide the capability for the needed material or service in a timely manner;

"(C) the guarantee is the most cost-effective, expedient, and practical alternative for meeting the need involved; and

"(D) the United States national defense demand is equal to, or greater than, the output of domestic industrial capability which the President reasonably determines to be available for national defense, including the output to be established through the guarantee.".

(b) Section 302 of the Defense Production Act of 1950 (50 U.S.C. App. 2092) is amended—

(1) by redesignating the first sentence as subsection (a); and

(2) by striking out the second and third sentences and inserting in lieu thereof the following: Loans.

"(b) Such loans may be made without regard to the limitations of existing law and on such terms and conditions as the President deems necessary, except that—

"(1) financial assistance may be extended only to the extent that it is not otherwise available on reasonable terms; and

"(2) except during periods of national emergency declared by the Congress or the President, no such loan may be made unless the President determines that—

"(A) the loan is for the expansion of capacity, the development of a technological process, or the production of materials essential to the national defense;

"(B) without the loan, United States industry cannot reasonably be expected to provide the needed capacity, technological processes, or materials in a timely manner;

"(C) the loan is the most cost-effective, expedient, and practical alternative method for meeting the need; and

"(D) the United States national defense demand is equal to, or greater than, domestic industrial capability which the President reasonably determines to be available for national defense, including the output to be established through the loan.".

(c) Section 303(a) of the Defense Production Act of 1950 (50 U.S.C. App. 2093(a)) is amended by adding at the end thereof the following: "Except during periods of national emergency declared by the Congress or the President, the President may not execute a contract under this subsection unless the President determines that—

"(1) the mineral, metal, or material is essential to the national defense;

"(2) without Presidential action under authority of this section, United States industry cannot reasonably be expected to provide the capability for the needed mineral, metal, or material in a timely manner;

"(3) purchases, purchase commitments, or other action pursuant to this section are the most cost-effective, expedient, and practical alternative method for meeting the need; and

"(4) the United States national defense demand for the mineral, metal, or material is equal to, or greater than, the output of domestic industrial capability which the President reasonably determines to be available for national defense, including the output to be established through the purchase, purchase commitment, or other action.".

LIMITATIONS ON THE AWARDING OF FINANCIAL ASSISTANCE

SEC. 4. (a) Section 301(e)(1) of the Defense Production Act of 1950 (50 U.S.C. App. 2091(e)(1)) is amended to read as follows:

"(e)(1)(A) Except during periods of national emergency declared by the Congress or the President, a guarantee may be made under this section only if the industrial resource shortfall which such guarantee is intended to correct has been identified in the Budget of the United States, or amendments thereto, submitted to the Congress, accompanied by a statement from the President demonstrating that the budget submission is in accordance with the provisions of subsection (a)(3) of this section.

"(B) Any such guarantee may be made only after 60 days have elapsed after such industrial resource shortfall has been identified pursuant to subparagraph (A).

"(C) If the making of any guarantee or guarantees to correct an industrial resource shortfall would cause the aggregate outstanding amount of all guarantees for such industrial resource shortfall to exceed $25,000,000, any such guarantee or guarantees may be made only if specifically authorized by law.".

Loans.

(b) Section 302 of the Defense Production Act of 1950 (50 U.S.C. App. 2092), as amended by section 3(b), is further amended by adding at the end thereof the following:

"(c)(1) No such loan may be made under this section, except during periods of national emergency declared by the Congress or the President, unless the industrial resource shortfall which such loan is intended to correct has been identified in the Budget of the United States, or amendments thereto, submitted to the Congress, accompanied by a statement from the President demonstrating that the budget submission is in accordance with the provisions of subsection (b)(2) of this section.

"(2) Any such loan may be made only after 60 days have elapsed after such industrial resource shortfall has been identified pursuant to paragraph (1).

"(3) If the making of any loan or loans to correct an industrial resource shortfall would cause the aggregate outstanding amount of all loans for such industrial resource shortfall to exceed $25,000,000, any such loan or loans may be made only if specifically authorized by law.".

Presidential action.

(c) Section 303(a) of the Defense Production Act of 1950 (50 U.S.C. App. 2093(a)), as amended by section 3(c), is further amended by adding at the end thereof the following: "Except during periods of national emergency declared by the Congress or the President, the President shall take no action under authority of this section unless the industrial resource shortfall which such action is intended to correct has been identified in the Budget of the United States, or amendments thereto, submitted to the Congress, accompanied by a statement from the President demonstrating that the budget submission is in accordance with the provisions of the preceding sentence. Any such action may be taken only after 60 days have elapsed after such industrial resource shortfall has been identified pursuant to the preceding sentence. If the taking of any action or actions under authority of this section to correct an industrial resource shortfall would cause the aggregate outstanding amount of all such actions for such industrial resource shortfall to exceed $25,000,000, any such action or actions may be taken only if specifically authorized by law.".

AUTHORIZATION OF APPROPRIATIONS

SEC. 5. (a) The first sentence of section 711(a) of the Defense Production Act of 1950 (50 U.S.C. App. 2161(a)) is amended by inserting "and paragraph (4)" after "paragraph (2)".

(b) Section 711(a) of the Defense Production Act of 1950 (50 U.S.C. App. 2161(a)) is amended by adding at the end thereof the following:

50 USC app. 2093.

"(4)(A) There are authorized to be appropriated to carry out the provisions of section 303 not to exceed $100,000,000 for fiscal years 1985 and 1986, except that not more than $25,000,000 is authorized to be appropriated for fiscal year 1985.

50 USC app. 2091-2093.

"(B) The aggregate amount of loans, guarantees, purchase agreements, and other actions under sections 301, 302, and 303 during fiscal years 1985 and 1986 may not exceed $100,000,000.".

REPORTS

SEC. 6. Title III of the Defense Production Act of 1950 (50 U.S.C. App. 2091 et seq.) is amended by adding at the end thereof the following:

50 USC app. 2099.
Ante, p. 149.

"SEC. 309. Not later than 18 months after the date of the enactment of the Defense Production Act Amendments of 1984, and annually thereafter, the President shall submit to the Committee on Banking, Finance and Urban Affairs of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate, a report on the impact of offsets on the defense preparedness, industrial competitiveness, employment, and trade of the United States. Each such report also shall include a discussion of bilateral and multilateral negotiations on offsets in international procurement and provide information on the types, terms, and magnitude of the offsets.".

Approved April 17, 1984.

LEGISLATIVE HISTORY—S. 1852:

HOUSE REPORT No. 98-651 (Comm. of Conference).
CONGRESSIONAL RECORD:
Vol. 129 (1983): Sept. 30, considered and passed Senate.
Oct. 4, 6, considered and passed House, amended.
Oct. 7, Senate concurred in House amendment with an amendment.
Vol. 130 (1984): Apr. 5, Senate agreed to conference report.
Apr. 10, House agreed to conference report.

Appendix C

Calendar of Public Hearing

CALENDAR OF PUBLIC HEARING

Those listed below appeared as witnesses at the United States International Trade Commission's hearing:

Subject : Assessment of the Effects of Barter and Countertrade Transactions on U.S. Industries

Inv. No. : 332-185

Date and time: May 30, 1985 - 10:00 a.m.

Sessions were held in the Hearing Room of the United States International Trade Commission, 701 E Street, N.W., in Washington.

WITNESS AND ORGANIZATION

American Association of Exporters and Importers, New York, N.Y.

John Carpenter, Senior Vice President, International Commodities Export Company

Eugene J. Milosh, President, AAEI

The Countertrade Project, Princeton, New Jersey

Willis A. Bussard, Director

Aerospace Industries Association of America, Inc., Washington, D.C.

Dr. Karl G. Harr, Jr., President of the Aerospace Industries Association of America, Inc. (AIA)

Donald Foulds, Vice President for Countertrade, Northrop Corporation

Emery Peter Smith, Vice President, International

Jack Kirtland, Economic Offsets Manager, Duplication System Group, International for FMC

- more -

WITNESS AND ORGANIZATION

First Family of Travel, New York, N.Y.

Cord D. Hansen-Sturm, Travel Industry Economist

American League for Exporters and Security Assistance, Inc., Washington, D.C.

Joel L. Johnson, Vice President, Economic Affairs

Appendix D

Products Associated with Countertrade and Offsets

Table D-1.--Products associated with countertrade sales agreements, countertrade obligations, or fulfillment of countertrade obligations, by types of occurrences, 1980-84 and 1985-2000

Product description (3-digest SIC code)	Sales agreements with countertrade (excluding military offsets), 1980-84	Countertrade obligations (excluding military offset), 1980-84	Countertrade obligations (excluding military offset), 1985-2000	U.S. imports resulting from countertrade (excluding military offsets), 1980-84	U.S. exports associated with countertrade (excluding military offsets), 1980-2000	Sales agreements with military offset obligations of less than $2 million, 1980-84	Sales agreements associated with military offset obligations of $2 million or more, 1980-84	Military offset obligations of more than $2 million, 1980-84	Military offset obligations of $2 million or more during fulfilled, 1980-84
Unspecified	X	X			X				
Field crops, except cash grains (13)		X							
Vegetables and melons (16)		X							
Fruits and tree nuts (17)	X	X			X				
Commercial fishing (91)	X	X			X				
Iron ores (101)	X	X		X					
Bauxite and other aluminum ores (105)	X	X			X				
Ferroalloy ores, except vanadium (106)	X				X				
Miscellaneous metal ores (109)		X		X					
Crude petroleum and natural gas (131)		X		X					
Oil and gas field services (138)	X				X				
Crushed and broken stone, including riprap (142)		X		X					
Clay, ceramic, and refractory minerals (145)		X							
Chemical and fertilizer mineral mining (147)		X							
Nonmetallic minerals (except fuels) services (148)	X				X				
Miscellaneous nonmetallic minerals, except fuels (149)		X							
General building contractors-nonresidential buildings (154)								X	
Heavy construction except highway and street construction (162)	X				X				
Roofing and sheet metal work (176)		X		X					

Table D-1.—Products associated with countertrade sales agreements, countertrade obligations, or fulfillment of countertrade obligations, by types of occurrences, 1980-84 and 1985-2000—Continued

Product description (3-digest SIC code)	Sales agreements with countertrade (excluding military offsets), 1980-84	Countertrade obligations (excluding military offset), 1980-84	Countertrade obligations (excluding military offset), 1985-2000	U.S. imports resulting from countertrade (excluding military offsets), 1980-84	U.S. exports associated with countertrade (excluding military offsets), 1980-2000	Sales agreements with military offset obligations of less than $2 million, 1980-84	Sales agreements associated with military offset obligations of $2 million or more, 1980-84	Military offset obligations of more than $2 million, 1980-84	Military offset obligations of $2 million or more during fulfilled, 1980-84
Miscellaneous special trade contractors (179)		X		X			X	X	X
Canned and preserved fruits and vegetables (203)		X							
Cigarettes (211)	X				X				
Tobacco (chewing and smoking) and snuff (213)	X	X	X	X	X				
Narrow fabrics and other smallwares mills: cotton, wool, silk, and manmade fiber (224)		X		X					
Miscellaneous textile goods (229)		X							
Miscellaneous fabricated textile products (239)		X	X	X					X
Office furniture (252)								X	X
Paper mills, except building paper mills (262)		X							
Building paper and building board mills (266)						X			
Newspaper: publishing, publishing and printing (271)	X								
Commercial printing (275)									X
Service industries for the printing trade (279)									X
Industrial inorganic chemicals (281)	X	X	X	X	X				
Plastics materials and synthetic rubber, synthetic and other manmade fibers, except glass (282)	X	X		X	X			X	X
Drugs (283)									
Soap detergents and cleaning preparations, perfumes, cosmetics, and other toilet preparations (284)									X

Table D-1.—Products associated with countertrade sales agreements, countertrade obligations, or fulfillment of countertrade obligations, by types of occurrences, 1980-84 and 1985-2000—Continued

Product description (3-digest SIC code)	Sales agreements with countertrade (excluding military offsets), 1980-84	Countertrade obligations (excluding military offset), 1980-84	Countertrade obligations (excluding military offset), 1985-2000	U.S. imports resulting from countertrade (excluding military offsets), 1980-84	U.S. exports associated with countertrade (excluding military offsets), 1980-2000	Sales agreements with military offset obligations of less than $2 million, 1980-84	Sales agreements associated with military offset obligations of $2 million or more, 1980-84	Military offset obligations of more than $2 million, 1980-84	Military offset obligations of $2 million or more during fulfilled, 1980-84
Industrial organic chemicals (286)	X	X			X				
Agricultural chemicals (287)	X	X	X	X	X	X			
Micellaneous chemical products (289)									X
Petroleum refining (291)	X				X				
Tires and inner tubes (301)	X	X			X				
Rubber and plastics hose and belting (304)		X		X					
Miscellaneous plastics products (307)		X							X
Footwear, except rubber (314)		X							
Handbags and other personal leather goods (317)		X		X					
Glass and glassware, pressed or blown (322)		X	X	X					
Cut stone and stone products (328)		X	X						
Abrasives, asbestos, and miscellaneous nonmetallic mineral products (329)		X							
Blast furnaces, steel works, and rolling and finishing mills (331)		X		X					
Iron and steel foundries (332)									X
Rolling, draining, and extruding of nonferrous metals (335)		X		X					X
Nonferrous foundries (castings) (336)		X	X	X					X
Miscellaneous primary metal products (339)	X	X	X	X	X				X
Cutlery, handtools, and general hardware (342)								X	X
Fabricated structural metal products (344)	X	X	X	X	X	X	X	X	X

Table D- —Products associated with countertrade sales agreements, countertrade obligations, or fulfillment of countertrade obligations, by types of occurrences, 1980–84 and 1985-2000—Continued

Product description (3-digest SIC code)	Sales agreements with countertrade (excluding military offsets), 1980-84	Countertrade obligations (excluding military offset), 1980-84	Countertrade obligations (excluding military offset), 1985-2000	U.S. imports resulting from countertrade (excluding military offsets), 1980–84	U.S. exports associated with countertrade (excluding military offsets), 1980-2000	Sales agreements with military offset obligations of less than $2 million, 1980-84	Sales agreements associated with military offset obligations of $2 million or more, 1980-84	Military offset obligations of more than $2 million, 1980-84	Military offset obligations of $2 million or more during fulfilled, 1980-84
Metal forgings and stampings (346)	X	X	X	X	X		X		X
Ordnance and accessories, except vehicles and guided missiles (348)						X	X	X	X
Miscellaneous fabricated metal products (349)	X	X	X	X	X		X	X	X
Engines and turbines (351)	X	X	X	X	X	X	X	X	X
Farm and garden machinery and equipment (352)	X	X	X	X	X				
Construction, mining, and materials-handling machinery and equipment (353)	X	X	X	X	X				X
Metalworking machinery and equipment (354)		X		X					X
Special industry machinery, except metalworking machinery (355)	X	X	X		X			X	X
General industrial machinery and equipment (356)	X	X	X		X				
Office, computing, and accounting machines (357)	X	X		X				X	X
Refrigeration and service industry machinery (358)	X								
Miscellaneous machinery, except electrical (359)	X	X		X	X				
Electrical transmission and distribution equipment (361)	X				X				
Electrical industrial apparatus (362)	X	X				X	X	X	X
Electric lighting and wiring equipment (364)		X	X	X				X	
Radio and television receiving equipment, except communications types (365)									X

Table D-1.—Products associated with countertrade sales agreements, countertrade obligations, or fulfillment of countertrade obligations, by types of occurrences, 1980-84 and 1985-2000—Continued

Product description (3-digest SIC code)	Sales agreements with countertrade (excluding military offsets), 1980-84	Countertrade obligations (excluding military offset), 1980-84	Countertrade obligations (excluding military offset), 1985-2000	U.S. imports resulting from countertrade (excluding military offsets), 1980-84	U.S. exports associated with countertrade (excluding military offsets), 1980-2000	Sales agreements with military offset obligations of less than $2 million, 1980-84	Sales agreements associated with military offset obligations of $2 million or more, 1980-84	Military offset obligations of more than $2 million, 1980-84	Military offset obligations of $2 million or more during fulfilled, 1980-84
Communications equipment (366)	X	X		X	X	X	X	X	X
Electronic components and accessories (367)	X	X	X	X	X	X	X	X	X
Miscellaneous electrical machinery, equipment, and supplies (369)	X	X		X					X
Motor vehicles and motor-vehicle equipment (371)	X	X		X	X		X	X	X
Aircraft and parts (372)	X	X	X	X	X	X	X	X	X
Ship and boat building and repairing (373)	X	X		X					X
Railroad equipment (374)	X	X		X	X				
Motorcycles, bicycles, and parts (375)		X	X						
Guided missiles and space vehicles and parts (376)						X	X	X	X
Miscellaneous transportation equipment (379)		X	X	X		X	X		X
Engineering, laboratory, scientific, and research instruments and associated equipment (381)	X				X				X
Measuring and controlling instruments (382)							X		X
Optical instruments and lenses (383)						X		X	X
Surgical, medical, and dental instruments and supplies (384)									X
Ophthalmic goods (385)						X			X
Photographic equipment and supplies (386)						X			
Jewelry, silverware, and plated ware (391)		X	X						X
Toys and amusement, sporting and athletic goods (394)		X							

Table D-1.—Products associated with countertrade sales agreements, countertrade obligations, or fulfillment of countertrade obligations, by types of occurrences, 1980-84 and 1985-2000—Continued

Product description (3-digest SIC code)	Sales agreements with countertrade (excluding military offsets), 1980-84	Countertrade obligations (excluding military offset), 1980-84	Countertrade obligations (excluding military offset), 1985-2000	U.S. imports resulting from countertrade (excluding military offsets), 1980-84	U.S. exports associated with countertrade (excluding military offsets), 1980-2000	Sales agreements with military offset obligations of less than $2 million, 1980-84	Sales agreements associated with military offset obligations of $2 million or more, 1980-84	Military offset obligations of more than $2 million, 1980-84	Military offset obligations of $2 million or more during fulfilled, 1980-84
Miscellaneous manufacturing industries (399)	X	X	X	X	X			X	X
Deep sea foreign transportation (441)	X	X			X				
Air transportation, certified carriers (451)		X						X	X
Fixed facilities and services related to air transportation (458)									X
Arrangement of transportation (472)		X	X	X					
Communications services, not elsewhere classified (489)	X				X			X	
Steam supply (496)	X				X				
Motor vehicles and automotive parts and supplies (501)	X				X				
Furniture and home furnishings (502)		X	X	X					
Metals and minerals, except petroleum (505)		X		X					X
Electrical goods (506)									X
Machinery, equipment, and supplies; chemicals and allied products (508, 516)	X	X			X			X	X
Miscellaneous durable goods (509)		X						X	X
Paper and paper products (511)		X							
Apparel, piece goods, and notions (513)	X				X				
Groceries and related products (514)		X	X	X	X				
Farm products, raw materials (515)	X	X	X	X	X				
Chemicals and allied products (516)	X	X	X	X					X

Table D-1.—Products associated with countertrade sales agreements, countertrade obligations, or fulfillment of countertrade obligations, by types of occurrences, 1980-84 and 1985-2000—Continued

Product description (3-digest SIC code)	Sales agreements with countertrade (excluding military offsets), 1980-84	Countertrade obligations (excluding military offset), 1980-84	Countertrade obligations (excluding military offset), 1985-2000	U.S. imports resulting from countertrade (excluding military offsets), 1980-84	U.S. exports associated with countertrade (excluding military offsets), 1980-2000	Sales agreements with military offset obligations of less than $2 million, 1980-84	Sales agreements associated with military offset obligations of $2 million or more, 1980-84	Military offset obligations of more than $2 million, 1980-84	Military offset obligations of $2 million or more during fulfilled, 1980-84
Petroleum and petroleum products (517)		X		X					X
Beer, wine, and distilled alcoholic beverages (518)		X	X	X					
Miscellaneous nondurable goods (519)	X	X	X	X	X			X	X
Miscellaneous investment (679)		X							
Hotels, motels, and tourist courts (701)		X						X	X
Miscellaneous personnel services (729)								X	
Computer and data processing services (737)	X				X	X	X	X	X
Miscellaneous business services (739)	X	X	X	X	X			X	X
Automotive repair shops (753)	X				X				
Automotive services (754)		X							
Electrical repair shops (762)									X
Miscellaneous repair shops and related services (769)	X				X			X	X
Medical and dental laboratories (807)								X	X
Health and allied services not elsewhere classified (809)	X				X				
Job training and vocational rehabilitation services (833)	X								X
Engineering, architectural, and surveying services (891)	X	X		X	X			X	X
Accounting, auditing, and bookkeeping services (893)	X								
Services, not elsewhere classified (899)	X	X	X	X				X	X

Source: Compiled from data gathered in response to questionnaire of the U.S. International Trade Commission.

Appendix E

Statistical Tables

Table E-1.—Total face value of sales agreements with countertrade obligation, by regions and years signed, 1980–84

(In thousands of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	318	48	153	–	118
Non-NATO countries 2/	33	206	73	113	260
Subtotal	351	254	226	113	378
Eastern bloc 3/	16	65	5	57	55
Asia 4/	319	251	493	151	506
Latin America 5/	145	159	253	45	50
All other 6/	1,015	447	6	663	260
Total	1,846	1,176	983	1,029	1,248

1/ Belgium, Denmark, Italy, Norway, Netherlands, Portugal, Spain, and West Germany.
2/ Austria, Finland, Sweden, and Yugoslavia.
3/ Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and Soviet Union.
4/ China, India, Indonesia, Israel, Japan, Lebanon, Pakistan, Philippines, Republic of Korea, and Turkey.
5/ Brazil, Colombia, Jamaica, and Mexico.
6/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.—Because of rounding, figures may not add to the totals shown.

Table E-2.—Total face value of sales agreements, by types of countertrade (excluding military offsets), and years agreements were signed, 1980–84

(In thousands of dollars)

Type of countertrade	1980	1981	1982	1983	1984	Total 1980–84
Barter	2,291	12,677	9,015	65,578	25,825	115,386
Compensation (including co-production, technology transfer, and subcontractor production)	82,982	19,783	129,338	43,600	23,000	298,703
Counterpurchase	1,675,939	1,109,930	844,477	914,980	1,151,550	5,696,876
Blocked currency:						
Barter	–	–	–	60	–	60
Counterpurchase	–	–	–	2,500	–	2,500
Unspecified	–	–	–	2,567	–	2,567
Best efforts (unspecified countertrade)	85,000	34,000	–	–	26,000	145,000
To be determined	–	–	–	–	21,400	21,400
Total	1,846,212	1,176,390	982,830	1,029,285	1,247,775	6,282,491

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.—Because of rounding, figures may not add to the totals shown.

Table E-3.--Total face value of goods and services of $2 million or more associated with the fulfillment of offset obligations, by types of offset and years of fulfillment, 1980-84

(In millions of dollars)

Type of offset	1980	1981	1982	1983	1984
Direct:					
Coproduction	42	119	125	129	134
Licensed production	-	-	-	22	19
Subcontractor production	82	166	148	135	407
Overseas investment	-	-	-	-	10
Technology transfer	1/	5	1	1/	1/
Direct offsets but not yet specified 2/	-	-	-	-	1/
Combination of subcontractor production and technology transfer	1/	1/	-	1	1
Total	124	290	274	286	571
Indirect:					
Foreign investment	-	-	1/	-	30
Technology transfer	1/	1/	2	4	13
Countertrade	1	13	34	72	140
Indirect offsets but not yet specified 3/	233	158	68	177	254
Total	234	171	104	253	437
Not yet specified	-	-	-	-	-
Contractually bound not to disclose details other than dollar amounts	-	-	-	-	-
National security classified, except for dollar amount	-	-	-	-	1/
Total	-	-	-	-	-
Grand total	357	461	378	540	1,010

1/ Less than $0.5 million.
2/ Includes instances where just "direct" was indicated.
3/ Includes instances where just "indirect" was indicated.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.--Because of rounding, figures may not add to the totals shown.

Table E-4.—Number of countries that are new or enhanced sources of non-defense-related goods and services, by 3-digit SIC codes, 1980-84

Product or service SIC code	Number of countries
Miscellaneous special trade contractors (179)	1
Miscellaneous wood products (249)	1
Office furniture (252)	1
Soap, detergents, and cleaning preparations, perfumes, cosmetics, and other toilet preparations (284)	1
Miscellaneous plastics products (307)	1
Iron and steel foundries (332)	1
Miscellaneous fabricated metals (349)	3
Engines and turbines (351)	2
Metalworking machinery and equipment (354)	2
Communications equipment (366)	1
Electronic components and accessories (367)	7
Aircraft and parts (372)	3
Photographic equipment and supplies (386)	1
Miscellaneous manufacturing industries (399)	1
Fixed facilities and services related to air transportation (458)	1
Electric goods (506)	1
Machinery, equipment, and supplies (508)	3
Computer and data processing services (737)	2
Engineering, architectural, and surveying services (891)	1
Total	34

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table E-5.—Number of countries that are new or enhanced sources of defense-related goods and services, by 3-digit SIC codes, 1980-84

Product or service SIC code	Number of countries
Iron and steel foundries (332)	1
Rolling, drawing, and extruding of nonferrous metals (335)	1
Fabricated structural metal products (344)	3
Ordnance and accessories, except vehicles and guided missiles (348)	3
Miscellaneous fabricated metal products (349)	2
Engines and turbines (351)	8
Communication Equipment (366)	3
Electronic components and accessories (367)	8
Aircraft and parts (372)	8
Guided missiles and space vehicles and parts (376)	2
Optical instruments and lenses (383)	1
Total	40

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table E-6.—Primary reasons for engaging in offset obligations of $2 million or more or implementation arrangements, by years agreements were signed, 1980-84

(Number of occurrences)

Reason	1980		1981		1982		1983		1984	
	Offset arrangement	Implementation arrangement	Offset arrangement	Implementation arrangement	Offset arrangement	Implementation arrangement	Offset arrangement	Implementation arrangement	Offset arrangement	Implementation arrangement
Required by foreign government	14	7	17	11	17	11	19	10	42	24
Provides a competitive advantage to your products	2	2	2	2	2	0	3	2	11	2
Helps repatriate blocked currency	0	0	0	0	0	0	0	0	0	0
Used to help finance your firm's exports	0	0	0	0	0	0	0	0	0	0
Used as a pricing mechanism	0	0	0	0	0	0	0	0	0	1
Used to protect a foreign subsidiary	0	0	0	0	0	0	0	0	0	0
Used to maintain foreign market share	5	2	5	2	4	3	4	3	11	2
Other	4	5	6	4	6	5	4	4	7	7
Not applicable	0	7	0	5	0	5	0	8	0	16

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Table E-7.—Value of U.S. imports resulting from nonmilitary countertrade, by region, by year imported, 1980-84

(In thousands of dollars)

Region	1980	1981	1982	1983	1984
Europe:					
NATO countries 1/	2/	21	21	9	7
Non-NATO countries 3/		8	12	28	19
Subtotal	1	29	33	37	26
Eastern bloc 4/	234	197	119	132	229
Subtotal	235	226	152	169	255
Asia 5/	3	3	7	19	21
Latin American 6/	–	9	132	87	53
All other 7/	86	122	74	56	92
Grand total	323	360	366	332	420

1/ Belgium, Italy, Netherlands, Portugal, Spain and West Germany.
2/ Less than $500,000.
3/ Austria, Finland, Sweden, and Yugoslavia.
4/ Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, Romania, and the Soviet Union.
5/ China, India, Indonesia, Israel, Japan, Lebannon, Pakistan, Philippines, Republic of Korea, and Turkey.
6/ Brazil, Colombia, Jamacia, and Mexico.
7/ Mainly Australia and Canada.

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Note.—Because of rounding, figures may not add to the totals shown.

Table E-8.—Disposition (or planned disposition) of goods and services that were obtained in offset obligations and implementation agreements, by types of disposition and periods disposed, 1980-87

(In millions of dollars)

Type of disposition	1980	1981	1982	1983	1984	1985--1987
Absorbed by your firm in its facility(ies) in the United States or sold in the United States	86.1	43.4	54.9	50.8	313.1	106.6
Absorbed by your firm in its facility(ies) abroad or sold abroad	.5	35.3	-	3.2	111.0	285.0
Sold to a trading company or 3d party with final user unknown	-	300.0	-	.2	92.6	212.1
Not yet determined	-	2.9	-	-	7.4	40.1
All other 1/	1.1	2.6	.9	.6	33.6	11.2
Total	87.7	384.2	55.8	54.7	557.7	655.0

1/ "All other" includes a combination of the 2 categories "Absorbed by your firm in its facility(ies) in the United States or sold in the United States" and "Absorbed by your firm in its facility(ies) abroad or sold abroad."

Source: Compiled from data submitted in response to questionnaires of the U.S. International Trade Commission.

Appendix F

Non-Oil-Producing LDC, NME, and Western Government Involvement in Countertrade

Non-oil-producing LDC government involvement in countertrade 1/

Many debtor countries reacted to the deterioration of their current account balances by turning to countertrade. Official government policy toward countertrade in non-oil-producing LDC's has taken three distinct but often simultaneously occurring forms:

The government itself engages in countertrade deals.--The government's role in countertrade activities varies according to the State's economic control in the country. It can include procuring supplies needed for its administrative functions (e.g., Brazil, Morocco, and Greece) to committing its productive resources in State-owned, or semi-State-owned firms (e.g., Brazil, Indonesia, and Mexico). In some countries (e.g., India) State trading companies purchase commodities for distribution to private firms through commercial channels.

The government mandates countertrade deals.--A government commitment to improve the country's external imbalance through countertrade may result in bilateral trade agreements providing that imports into the country must be linked to purchases by the seller, or by the seller's government (e.g. Columbia, Ecuador, and Malaysia).

The government remains neutral.--A neutral policy in a country strained by external imbalance and a difficult domestic economic situation may indicate the government's "laissez-faire" stance concerning private-sector activities (e.g., Argentina). 2/

NME involvement in countertrade

NME countertrade activities increased after 1980, partly because of increases in NME trade and partly because of stepped-up NME efforts to do business with Western and LDC partners through these trading methods. 3/

NME trade.--NME trade is essentially conducted on an annually balanced barter basis, and it is predicated on the assumption that no structural imbalance will develop among the trading partners. Production requirements specified by the sum total of bilaterally balanced trade agreements are built into national economic plans and broken down to firm level. For an individual NME, the production requirements arising from trade with NME's are as amenable to planning as domestic production targets. To the extent NME trade grows, international countertrade also grows. (In nominal terms, NME trade increased by 24.3 percent from 1980 to 1982, according to NME statistics.)

1/ For a critical survey of arguments in favor of government involvement in countertrade, see Gary Banks, The Economics and Politics of Countertrade, The World Economy, Volume 6, June 1983, pp. 159-182.

2/ Interview with Business International Corp.

3/ The expression "nonmarket economy" itself implies that multilateral relations among firms through domestic markets are kept to a minimum. The economic mechanism under direct central planning is a complex swap of commodities designed by the authorities to fulfill production plans and implement industrial policy. Although nonnegligible departures from direct central planning occurred in all Eastern European NME's, particularly in Hungary, the essential nonmarket orientation of Eastern Europe as a bloc remains prevalent.

NME trade expansion.--The NME's seeking non-NME trade prefer trade relations that conform to their domestic economic mechanism. Active search for comprehensive trade protocols involving bilateral clearing and industrial cooperation agreements (maximizing the countertrade deals under such agreements) with non-NME countries is a major characteristic of NME foreign trade policies. 1/

The growth of countertrade had a major impetus through East-West industrial cooperation when the NME's embarked on their modernization program in the early 1970's. 2/ The NME's have also expanded their trade with the LDC's under bilateral protocol and clearing agreements since the early 1970's. In addition to economic compatabilities that may exist between the LDC's and NME's, bilateral clearing agreements came about with a relative ease between these two groups of countries because (1) in the LDC's the State generally has a greater direct role in economic management than in the West. Thus for systemic reasons, LDC's are more amendable to concluding countertrade agreements with the NME's than are Western countries. Second, given the nonconvertibility of NME currencies and the unwillingness of the NME's to accept LDC currencies as payment for their export, trade protocols and clearing agreements between LDC and NME governments allow those countries to minimize the balance to be settled in hard currency. The current numbers of bilateral clearing agreement between LDC's and NME's is 130, and the volume of LDC-NME trade turnover under the agreement has risen since 1980. 3/

NME efforts to expand long-term bilateral relations with the LDC's are further strengthened by the opportunity that bilateralism provides to increase the role of planning in the Third World. By drawing LDC's into bilateral clearing agreements, the NME's increase the share of decisions by the State while reducing the role of market forces. Annual bilateral agreements leading to a system of long-term economic cooperation gives the NME's political influence in the Third World, which, in turn, increases resources at their disposition.

Western Government involvement in countertrade

The developed countries also employ countertrade when economic reasons justify it. For example, Canada, Australia, and New Zealand procure certain

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1/ Trade protocols and clearing agreements may go into more or less detail in specifying balances in the exchange of commodities. Some of them define required balancing over broad sectors, and others, for industries or for commodity groups.

2/ It may be of interest that trade between East and West Germany, the so-called inner-German trade, is conducted also under a bilateral agreement. Under the agreement, trade is accounted not in currency but in accounting units (verrechnungs einheit) with a swing credit--familiar concept in countertrade--allowed to finance balances. Inner-German trade flourished when world trade declined in 3 consecutive years during the world recession of 1980-83. See Statisches Jahrbuch fur die Bundesrepublik Deutschland, table 11.21.

3/ Interview with Business International Corp.

imports through countertrade. For the maintenance of strategic and critical materials in the United States, Federal agencies have the authority to use barter and exchange as alternatives to cash purchases. 1/ In the Western military equipment trade, the offsets represent countertrade arrangements.

1/ For a description of advantages and disadvantages of barter arrangements for the United States, see Donna U. Vogt, U.S. Government International Barter, Congressional Research Service Report No. 83-211 ENR, Dec. 6, 1983.

Appendix G

Contributing Factors to the Current Account Deterioration of Non-Oil Producing LDC's and Eastern European NME's

Deterioration in the overall terms of trade for non-oil-producing LDC's and Eastern European NME's.--Terms of trade 1/ for the non-oil-producing LDC's fell by an average of 2 percent per year during 1973-81. The deterioration was clearly tied to oil price increases and the effects of such increases on national economic conditions and on international trade. Whereas the terms of trade of this group of countries during 1963-72 improved at an average rate of 0.5 percent per year, the decline in their terms of trade was 7.6 percent in 1974-75 and 7.3 percent in 1980-81. (The terms of trade of industrial countries fell by an average of 2.3 percent per year during 1973-81, with peaks of deterioration observed after oil price increases.) Statistics on the terms of trade of six Eastern European countries--Bulgaria, Czechoslovakia, East Germany, Hungary, Poland, and Romania--are not available, but estimates clearly indicate that the dynamic pattern of deterioration in the combined hard-currency terms of trade of this group was similar to that of other oil-importing regions. 2/

After 1973, the developed Western nations initiated a structural adjustment in their production, reallocating resources from traditional industries to energy-producing, energy-saving, and high-technology industries. Price inflation in the West worsened immediately after 1973. 3/ Non-oil-producing LDC's and NME's that embarked on efforts to make structural adjustments in their economies saw a constant increase in the costs of Western plant and equipment that were necessary for these adjustments. Thus, Western inflation contributed to the overall deterioration in their terms of trade.

Moderation in the growth of industrialized nations.--Growth in the West slowed after the energy crisis, reducing the import absorbing capacity of industrialized countries. The average growth rate of imports of industrialized countries fell from 9 percent (1963-72) to 3.6 percent (1973-81). Tariff preferences granted to LDC's and to some NME's and a redirection of LDC and NME exports to oil-producing countries mitigated the declining demand for their products by the industrialized world. But a contraction of the Western market and a subsequent sharpening of competition on world markets, in general, seriously constrained the revenue-earning capacity of both blocs.

1/ "Terms of trade" is commonly defined as the ratio Px/Pm, where Px is the average price a country receives for its exports, and Pm is the average price it pays for its imports.

2/ Interview with Wharton Econometric Forecasting Associates.

3/ Reasons for Western inflation after 1973 may be summarized as follows: cost-push inflation as a result of energy and other shortages and structural shifts, demand stimulus through expenditure-increasing policies to assure full-employment, and the wage-price spiral through the traditional, society wide, Western bargaining process. (Expansion of the global money supply created the indispensable, immediate condition for the post-1973 inflation.) The weighted average rate of increase in consumer prices for the group of 10 (G-10) countries which includes Belgium, Canada, the Federal Republic of Germany, France, Italy, Japan, Netherlands, Sweden, United Kingdom, and the United States) plus Switzerland was 5.0 percent in 1972; 13.7 percent in 1974; 7.4 percent in 1976; 7.2 percent in 1978; 11.1 percent in 1979; 11.4 percent in 1980; subsiding to 9.3 percent in 1981. Bank For International Settlements, Fifty-Second Annual Report, Basle, June 1982, p. 39.

Increases in the costs of financing from international capital markets.--Servicing external debts did not represent a serious problem for many non-oil-producing LDC's until 1978. In that year, however, a drastic turnabout occurred. Interest rates on capital markets climbed to postwar highs, and the export prices of goods from these countries began to weaken. 1/ Real interest rates on the external debts of non-oil-producing LDC's averaged about -7.7 percent in 1973-77. 2/ This rate increased to 3 percent during 1978-81. At the same time, the forces that increased real interest rates for the group of non-oil-producing LDC's (rising interest rates and weakening export prices) pushed up real interest rates for the Eastern European NME's.

Domestic factors in non-oil-producing LDC's and Eastern European NME's that constrained external adjustment policies.--Expenditure-increasing fiscal and monetary policies created fiscal deficits in many non-oil-producing LDC's. These deficits matched by corresponding increases in liquidity tended to increase domestic inflation, thereby worsening current account deficits. In 1978, when problems of external disequilibrium became obvious in Eastern Europe, only Hungary embarked on the implementation of a market-oriented economic reform aimed at correcting the causes of its current account deficit. Poland and Romania took an alternate route--both borrowed heavily from the West after 1973, but neither seriously attempted to change the basic centrally planned character of their economic system. 3/

1/ For details see Moshin S. Khan and Malcolm Knight, "Sources of Payments Problems in LDC's," Finance and Development, December 1983, p. 3.

2/ The real rate of interest is the percentage increase in purchasing power that the borrower pays to the lender for obtaining a loan. It is calculated by subtracting the inflation rate from the nominal rate of interest. If the rate of inflation exceeds the nominal interest rate, the result is negative.

3/ S. Kartreli: L'Economie Est-Europeenne dans la seconde moitie des annees 80: Apprendre a vivre avec la crise. Politique Etrangere Nov. 1983 pp. 934-946; and a compendium of papers submitted to the Joint Economic, Congress of the United States; East European Assessment, Part 1-country studies, 1980, pp. 15, 231, 299, 377, 483 and 521.

Appendix H

The Role of the GATT and the OECD in Countertrade Activity

The General Agreement on Tariffs and Trade

The General Agreement on Tariff and Trade (GATT) is a set of rules governing most aspects of international trade. 1/ The GATT has 90 Contracting Parties, including the United States and all other major trading countries in the world, and is also applied on a de facto basis by 31 countries. The GATT codes apply to the behavior of governments, not individual business entities. They also do not cover military trade. 2/ Consequently, the GATT rules do not apply to countertrade transactions between private parties or to offset arrangements (in their various forms) for government purchases of defense materials. Opinions differ on the relationship of the various provisions of the GATT to countertrade. The general view, however, is that countertrade per se does not constitute a violation of the GATT but that, depending upon the circumstances of a particular case, countertrade imposed by government law or regulation can be inconsistent with the GATT. Notwithstanding, it appears that government-mandated countertrade transactions tend to defeat the primary goal of the GATT, which is to maintain an open, multilateral world trading system. 3/

Organization for Economic Cooperation and Development (OECD) 4/

During the past few years, countertrade practices in international trade have been under examination by the OECD, and in 1981, an OECD study was

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1/ Donald Zarin, "Countertrade and the Law," George Washington Journal of International Law and Economics, vol. 18, No. 2, 1984.

2/ Michael Gadbaw, "The Implications of Countertrade under the GATT," p. 1.

3/ Donald Zarin, op. cit.

4/ On Dec. 14, 1960, the Organization for Economic Cooperation and Development was formed. The member countries have agreed, among other things, to contribute, both individually and jointly, to the economic development of both member and nonmember countries; encourage a coherent approach to development problems in the OECD as part of the overall national policy of every member country; promote dialogue between developed and developing countries; increase the volume and effectiveness of aid to developing countries; promote imports of goods from the developing countries; maintain and improve the open and multilateral trading system by preventing protectionism and further liberalizing international trade; strengthen trade relations with developing countries by contributing to their economic development and integrating them into the trading system; remove competitive distortions, particularly in such fields as export credits and private, restrictive business practices; promote cooperation on commodity policy in the interest of all producer and consumer countries; and review periodically the main developments and issues in the international trade and trade policy fields. "OECD at a Glance," Paris, France, pp. 1, 6, and 7. Member countries of the OECD are:

Australia	Greece	Norway
Austria	Iceland	Portugal
Belgium	Ireland	Spain
Canada	Italy	Sweden
Denmark	Japan	Switzerland
Finland	Luxembourg	Turkey
France	Netherlands	United Kingdom
West Germany	New Zealand	United States

prepared on East-West countertrade. 1/ The conclusions were similar, with some minor differences, to a 1985 study done on countertrade in the North-South context, e.g., countertrade with developing countries. This OECD Secretariat study examines the trade-distorting effects and the reasons for such countertrade arrangements. 2/

Among the conclusions set out in the paper are the following:

1. Countertrade transactions are only a relatively marginal phenomenon in international trade ($80 billion of total trade in 1983, or 4.8 percent of world exports excluding trade among Eastern European countries and trade under clearing arrangements). However, the frequency and geographical distribution have increased rapidly in the past years. Nonetheless, it appears that countertrade operations involving petroleum increased substantially. 3/

2. Countertrade arrangements have usually been organized in response to immediate economic problems: liquidity crises, shrinking of export outlets for primary products, and disturbance of trade patterns following the imposition of import controls. 4/

3. Developing countries are using countertrade to increase exports to enable them to obtain hard currency and improve their competitive position. 5/

4. Developing countries' continuing interest in countertrade appears to coincide with their external debt. The heavily indebted developing countries are trying to reestablish their external balance through a reduction of their imports and a parallel expansion of their exports. 6/

5. Developing countries generally propose primary products as compensation for their imports. These products are those which continue to be sold through normal commercial transactions. Countertrade operations presumably allow these countries to offer a concealed discount on the selling price, either directly or indirectly. 7/

6. Requests for countertrade do not emanate exclusively from the developing countries. Western firms suggest these procedures to countries that close their borders to their exports. This tendency may well continue as a large number of developing countries are facing problems of liquidity and indicating that countertrade is the only means of maintaining trade with these countries. 8/

7. Countertrade does not furnish a viable basis for a longer term trading strategy, nor should it be established on a permanent basis. 9/

1/ OECD, East West Trade: Recent Developments in Countertrade, Paris, October 1981.
2/ OECD, Countertrade, Developing Country Practices, Paris, 1985, p. 7.
3/ Ibid., pp. 12, 15 and 26.
4/ Ibid., pp. 15 and 27.
5/ Ibid., pp. 16, 17 and 26.
6/ Ibid., pp. 14 and 27.
7/ Ibid., pp. 17 and 26.
8/ Ibid., pp. 19 and 28.
9/ Ibid., pp. 27 and 28.

The study finds that countertrade is often not a good solution for creating new markets, sustaining economic growth, or improving the trade balance. It points out that it is not necessary for member nations to develop any specific control or regulation of countertrade transactions, since usual trading rules can be applied. Notwithstanding this, there are no applicable rules in the multilateral framework that expressly refers to trading based on barter. 1/

In conclusion, according to the OECD Secretariat report, member country governments are not encouraged to engage in countertrade, either officially or unofficially. 2/ The OECD recognizes the economic problems presented by widespread countertrade practices, e.g., return to bilateralism, but OECD member countries have not been able to agree on how to effectively deal with this growing phenomenon. 3/

1/ OECD, Countertrade, Developing Country Practice, Paris, 1985, pp. 8-9.
2/ Ibid, p. 9.
3/ Ibid., pp. 7, 8.

Appendix I

Countertrade Policies and Practices in Selected Countries

Countertrade Policies and Practices in Selected Countries

The information in this section was compiled from U.S. State Department cables, other U.S. Government sources, from interviews with foreign trade officials, and the published results of private research. 1/ Trade officials from Bolivia, Colombia, Ecuador, Indonesia, Jamaica, Malaysia, Mexico and Uruguay were interviewed. In general, some of the country summaries support the following conclusions reached by the present investigation: (1) countertrade figures most importantly in the foreign trade of the NME's; (2) governments in the developing world generally prefer to restrict the use of countertrade to the importation of goods vital for the functioning and the development of their economies and to the promotion of their nontraditional exports and to gaining incremental markets for their traditional exports; (3) although Western firms and governments are on the receiving end of countertrade deals as a rule, they are not beyond initiating such deals when their economic interests so demand it; and (4) countertrade legislation and policies vary greatly from one nation to another.

Europe

Austria.--The country's private firms are heavily involved in countertrade with the NME's, particularly in Eastern Europe. There is no known legislation that applies to these trading activities beyond the country's trade and bank laws that generally apply to private business activities. The Government has, however, on occasion exerted pressure on Western automobile manufacturers to engage in counterpurchase and coproduction agreements with Austrian firms as a precondition for obtaining preferential tariff treatment for their auto sales in Austria. The government has succeeded in concluding several offsets in the purchase of military equipment.

Bulgaria.--Bulgaria's countertrade requirements in commercial contracts with the West are among the highest of the nonmarket economy countries (NME's) with levels from 30 to 100 percent. Countertrade requirements are lower in transactions involving high-priority imports for which hard currency has been set aside. Foreign Trade Organizations (FTO's) are given considerable flexibility in negotiating commercial contracts involving countertrade. The Ministry of Foreign Trade is responsible for overseeing countertrade transactions through its import and export licensing procedures. The FTO Intercommerce, which is under the jurisdiction of the Ministry of Foreign Trade, functions as a clearinghouse by disposing of countertrade products that Bulgaria receives and exporting goods that are difficult to market overseas. Among the products that Bulgaria attempts to market through countertrade agreements are electrical and transport equipment, chemical products, textiles, and foodstuffs. 2/ Bulgarian authorities place increasing emphasis on joint ventures with Western firms.

1/ Thaddeus Kopinski, op. cit., and country profiles of countertrade regulations and practices by Stephen F. Jones, published in Special Report No. 174, The Economist, Intelligence Unit, London, were the most important sources consulted during the course of this investigation.

2/ U.S. Department of Commerce, Pompiliu Verzariu, Countertrade Practices in East Europe, the Soviet Union and China, April 1980.

Czechoslovakia.--Czechoslovakia requires countertrade on all items except hard-currency producing imports and energy technology products. The country's countertrade demands are among the lowest in Eastern Europe due to its favorable hard currency position in comparison to other countries in the region. Since 1983, countertrade demands of over 100 percent have been reported in a few instances. Under Czechoslovakia's 1981-1985 Five Year Plan, countertrade requirements are lowest for energy-related imports and for those products which would contribute to the modernization of its industrial sector. Such imports include: high technology, energy equipment, mining equipment and food packaging machinery. 1/

Denmark.--There is no government countertrade program per se in Denmark. While official statistics on Danish countertrade are not available, less than 5 percent of Danish exports are reportedly tied to countertrade arrangements. Yugoslavia, Romania and Poland are Denmark's major countertrade partners. Countertrade arrangements with the Soviet Union have been very limited. There has been no direct countertrade between the U.S. and Denmark, however, Denmark has been involved with military offset arrangements in the production of the F-16 aircraft. 2/

East Germany.--Countertrade agreements, especially counterpurchase and compensation deals, are an integral part of the country's trade with the West. Countertrade requirements are presented at the beginning of commercial negotiations and strictly adhered to until the deal is concluded. The variety and volume of East German goods that are available under counterpurchase agreements are limited by commitments of the products to domestic usage and by intra-CEMA export limits. Industrial goods are most frequently offered in countertrade deals. 3/

France.--The French government has expressed serious reservations about the use of government-mandated countertrade. However, a countertrade policy and trade facilitation unit (Service de Compensation) has been organized within the Trade Ministry's Foreign Trade Relations Unit. In addition, the government has established an organization known as SODIMEX which is responsible for encouraging purchases of French high-technology products by countries with heavy foreign debts. A semi-official organization known as the Association Pour la Compensation des Exchanges Commerciaux (ACCO) was established in 1978 by various trade associations and five major banks to provide countertrade consulting services to its members which include France's top exporting companies. 4/ ACECO acts solely as an intermediary in counseling its members on negotiations with foreign entities; it does not intervene directly in the negotiating process. France has bilateral clearing agreements with Algeria, China, Iraq, Syria, and Vietnam. Products which have reportedly been purchased through countertrade include coal, phosphates, textiles, agricultural products, coffee, rice, and manioc. France has reportedly sold

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1/ Herbert Stepic, "Principal Changes in Countertrade Practice with Selected Countries After the Polish Crisis," 1983.

2/ Report from U.S. Embassy, Copenhagen, July and September, 1984.

3/ Countertrade Practices in East Europe, the Soviet Union and China, op. cit.

4/ Frederick E. Howell, Carol Henkel, and Jim Walsh, eds., U.S. and Foreign Commerical Service, Countertrade Guidebook, 1985.

anti-aircraft defense systems, fertilizers, wheat flour, butter, insecticides and rice mill through countertrade or offset arrangements. 1/

Greece.--The government of Greece requires offsets, including countertrade, under its government procurement policy. In 1984, the Ministry of Defense issued specific offset guidelines for firms bidding on a command and control system for the Greek Air Force. This was the first attempt by the Greek government to stipulate specific offset sales terms. Each year the Ministry of National Economy issues an extensive list of Greek products available for countertrade. In May of 1984, the International Trade Co. (ITCO), a government-owned export trading company was organized to promote the export of Greek products. ITCO has negotiated export agreements with West Germany, Sweden, Albania, Iran, Bulgaria and Egypt. The trading company has also concluded a 100 percent countertrade deal with the United Kingdom to acquire 70,000 tons of sugar. ITCO is the only government-controlled company authorized to negotiate countertrade contracts with Eastern Europe. 2/

Hungary.--Countertrade has been practiced less frequently in Hungary than in the Soviet Union, Poland or Romania. The Ministry of Foreign Trade oversees countertrade transactions and encourages those deals in which the Western firm is the end-user or has access to a marketing organization which is capable of handling the Hungarian exports. Countertrade demands vary according to the type of import and individual FTO involved in the arrangement. Western firms are encouraged to file complaints with the Ministry of Foreign trade if they are pressured into accepting products which the FTO itself is unable to market in the West. Since 1983, Hungary has increased its countertrade demands in order to improve the country's hard currency position. A large variety and volume of Hungarian goods are offered in countertrade and long-term cooperation agreements are sought in the areas of electrical power, chemicals, machinery and food processing. 3/

Poland.--The country's difficult external finances in the 1980's have been a major factor in generating countertrade between Western and Polish firms. 4/ Poland leads the countries of Eastern Europe in the volume of trade conducted through countertrade arrangements with Western partners. Polish countertrade demands are estimated to range from 30 to 50 percent of the contract value of total exports. The country's requirements for countertrade are particularly strong in the purchase of Western capital goods. Polish imports of Western electronics equipment, for example, may be tied to counterpurchase agreements at an average of 20 to 50 percent of the export contract value. The Ministry of Foreign Trade authorizes Polish FTO's to make countertrade offers. The Western exporting firm can often counterpurchase Polish goods from other FTO's rather than exclusively from the buyer of its goods. 5/

1/ Report from U.S. Embassy, Paris, November, 1984.

2/ Reports from U.S. Embassy, Athens, March and November, 1984.

3/ Countertrade Practices in East Europe, the Soviet Union and China, op. cit.

4/ "Living With A Nightmare," The Economist, March 20, 1982.

5/ Countertrade Practices in East Europe, the Soviet Union and China, op. cit.

Romania.--In 1980, Romania became the first East European nation to legally mandate the use of countertrade. According to legislation enacted during the year, countertrade must be utilized by Romanian FTO's in order to balance the country's foreign trade account. Several government agencies are responsible for implementing countertrade. A section of the Ministry of Foreign Trade and International Cooperation coordinates counterpurchase arrangements of Romania's FTO's. Tera and Mercur are government-controlled FTO's which import goods for resale to third countries, locate suitable countertrade goods, carry out switch operations with Western trading houses, and barter consumer goods. A compensation quota of a least 100% is initially required of all Western firms engaging in countertrade with Romania. Products which are frequently offered by Romania in countertrade include: machinery and vehicles, chemical products, and electrical equipment. Penalties for non-fulfillment of countertrade obligations range from 20-30 percent on machinery and vehicles and 15 percent on chemicals. 1/

Soviet Union.--The Soviet Union is the world's largest countertrader. Soviet countertrade transactions can be grouped into five categories: (1) natural resource/raw-material cooperation agreements with partial or full payments in resultant products; (2) industrial cooperation agreements with partial payment in resultant product; (3) industrial cooperation agreements with partial payment in unrelated product; (4) licensing agreements with partial payment in product; and (5) barter arrangements of products and equipment. 2/

Soviet countertrade demands are highest for chemicals and consumer goods and lowest for iron, steel, electronics, foodstuff in short supply, and machinery considered vital for economic development. If a Western exporter is compensated in Soviet raw materials such as natural gas, which can easily be sold on the world market, countertrade requirements run well over 100 percent.

Buyback arrangements have been used to finance large capital projects, particularly in the chemical and gas sectors. Since 1983, approximately 45 large industrial projects have been commissioned on this basis.

The Main Department for Compensation Arrangements with the West established within the Ministry of Foreign Trade in 1974, is the principal Soviet Government agency that oversees Soviet countertrade deals with Western firms. The Main Department also coordinates the supervisory activities of other Government agencies, primarily industrial branch ministries, which may be involved in countertrade deals. 3/

The Soviet Union has engaged in extensive barter arrangements with Middle Eastern countries, exchanging weapons and consumer goods for oil. These transactions have been conducted mainly with Iran, Iraq and Libya. The Soviet Union then reexports the oil to West European markets at an estimated rate of 600,000 barrels per day for hard currency. 4/

1/ Ibid.

2/ Report from U.S. Embassy, Moscow, October, 1982.

3/ U.S. Department of Commerce, Pompiliu Verzariu, International Countertrade: A Guide for Managers and Executives, 1984.

4/ Stephen F. Jones, "North/South Countertrade," The Economist, Intelligence Unit Special Report No. 174, 1984.

Under a system of 5-year barter arrangements initiated in 1951, the Soviet Union and Finland maintain balanced trade accounts with each other; i.e., each country can buy from the other only as much as it sells. Exchanges between the two countries occur at prevailing world prices and are handled through a clearinghouse system at the central banks in Moscow and Helsinki. Through this system of barter arrangements, Finland's export market has been protected during worldwide recessions. The Soviet Union, on the other hand, is guaranteed a market for energy exports and a source of high-quality goods. 1/

Other countries with which the Soviets have reportedly concluded countertrade deals since 1984 include Brazil, Guyana, Peru, India, Austria, and Romania.

Spain.--The government of Spain has not enacted any specific laws regarding countertrade and maintains a neutral posture towards this type of trade. Countertrade is a relatively new practice in Spain and has been utilized by only a limited number of Spanish companies. The majority of Spanish countertrade deals have been conducted with LDC's in Africa and Latin America and to a limited extent with Eastern Europe. Spain abolished its bilateral clearing agreements with Eastern Europe five years ago and currently maintains such arrangements with only a few Latin American nations. The Ministry of Defense has instituted offset requirements for major Spanish military purchases. A recent example of an offset arrangement is the FACA program to supply American fighter aircraft to Spain. 2/

Sweden.--Traditionally, the Swedish government has discouraged countertrade. However, in June 1984, the government acquired a controlling share in SUKAB, a private-sector trading company established during World War II. The government hopes that SUKAB, in its new quasi-official status, will be able to compete with state trading companies in Western Europe and the Third World. Countertrade is expected to account for more than 8 percent of total Swedish trade by the end of the decade. Approximately 20 percent of Sweden's sales to Eastern Europe are affected by countertrade. Sweden has also concluded buy-back arrangements with China and Brazil. Offsets are a growing factor in Sweden's trade with OECD countries, particularly with regard to military and telecommunication equipment. Recent examples of Swedish trading arrangements involving offsets include: the JAS fighter project with the U.S., a sale of communications equipment to Canada and Australia; and the purchase of the West German MB-105 antitank helicopter. 3/

West Germany.--The West German government is philosophically opposed to countertrade and has not established an official program in support of such activities. Countertrade is not included under the country's Foreign Trade Act, which governs West German trading practices. However, in practice, the government realizes West German companies must engage in countertrade in order to maintain foreign sales to countries faced with foreign exchange shortages. In general, the government is willing to accommodate East-West countertrade rather than North-South countertrade. West Germany has reportedly exchanged

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1/ Barbara Cory, ed., Countertrade & Barter International, April 1984.
2/ Report from U.S. Embassy, Madrid, October, 1984.
3/ Report from U.S. Embassy, Stockholm, July, 1984.

auto technology, machine tools, chemical plants and equipment for engines and oil. West German machine tool companies are required to make compensatory purchases of at least 10 percent when exporting to the Soviet Union. In 1983, exports of machine tools to the Soviet Union totaled DM 1.5 billion. Nigeria, Libya and Saudia Arabia have also required countertrade in conjunction with deliveries of machinery. At least five major barter companies have been established in West Germany. 1/

Yugoslavia.--Countertrade has been unofficially required for almost all Yugoslavian imports since mid-1975. However, there is no officially-stated policy on countertrade nor do any published countertrade regulations exist except for indirect references to countertrade in Yugoslavia's import regulations. In the absence of publicly available countertrade regulations, a system of semigovernmental community organizations or "sizs" has developed to monitor such arrangements. The sizs are established at the federal and provincial levels of government and must approve every import or export contract. Countertrade arrangements are also managed at the provinical level, thus requirements and available products for countertrade may vary from region-to-region. In general, requirements are higher for consumer than for capital goods and range from 40 to 100 percent. Since countertrade is not recognized as an official policy, the government assumes no responsibility for locating suitable countertrade goods, leaving the task up to foreign firms. High priority military items are often excluded from countertrade. Those imports which have been associated with Yugoslavian countertrade deals include aircraft, crude oil, and petroleum products. 2/

Asia

China.--Since 1978, China has emphasized compensation and buyback arrangements as a means of modernizing its industrial sector. Administrative regulations were drafted in 1979 and revised in 1981 that establish an approval process for countertrade deals and give special customs tariff incentives for compensation transactions. 3/ China has concluded hundreds of these agreements with Western nations, which are attracted by China's low labor rates, in order to acquire capital equipment and technical assistance for its factories. The majority of compensation arrangements undertaken thus far have involved projects in light industry, electronics, and foodstuffs, located primarily in the coastal provinces and in Special Economic Zones.

The Chinese have also negotiated joint ventures that involve buybacks and exports derived from new production capacity. Such arrangments have involved the United States, Japan, and West Germany. Other forms of countertrade have been carried out with Albania, Brazil, Burma, France, Ghana, India, Thailand, and the U.S.S.R. 4/

Indonesia.--Imports through countertrade by the private sector are negligible, and the Government does not mandate countertrade to private firms. The Ministry of Trade formulates policies on countertrade. The

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1/ Report from U.S. Embassy, Bonn, October, 1984.

2/ Report from U.S. Embassy, Belgrade, August, 1984.

3/ International Countertrade: A Guide For Managers and Executives, op. cit.

4/ Stephen F. Jones, op. cit.

cabinet-level Coordinating Team (Team of 10), composed of senior cabinet officers, enforces these policies. Until recently, the policy of using countertrade in Government procurements had been strictly applied. According to some reports, Indonesia is not in the process of liberalizing its countertrade laws. 1/ Known regulations stipulate that with the exception of development projects financed through concessional loans from multilateral organizations, all government imports in excess of 500 million rupiahs ($500,000) must be compensated by Indonesian products.

Imports through government countertrade are often distributed to private users. The major items of import through countertrade are fertilizers, electrical plants, textile-manufacturing machinery, diesel locomotives, other railroad and telecommunications equipment, cement, and raw materials. As compensation, the Government offers to its potential sellers about 33 products to choose from. These goods include rubber, coffee, pepper, tobacco, manioc, cement, saw timber, plywood, textile products, etc. Depending on the availability of the listed products and on the trading partners' special requirements, some other Indonesian goods--not on the list--are also available for countertrade.

West Germany, Japan, the United States, Singapore, and Romania are the country's major countertrade partners.

Iran.--Countertrade requirements became important in the country's foreign trade policy in 1981 and 1982. Japan, the Soviet Union, Brazil, Pakistan, and Taiwan are some of Iran's significant countertrade partners. Oil is the country's chief countertrade commodity.

Iraq.--Since 1973, Iraq has opposed barter trade involving oil, however, the war with Iran has forced the country to make limited commitments to use oil in settling obligations with French, Korean, Italian and India companies. According to some reports, Iraq occasionally countertrades oil for military equipment. 2/

Israel.--The Industrial Cooperation Authority within the Ministry of Industry and Trade is responsible for administering the country's countertrade. All substantial procurements by the government and publicly owned companies carry local-content requirements. Authorities emphasize long-term industrial cooperation as the most beneficial form of countertrade for the country's economy.

Japan.--There is no known legislation in the country encouraging the use of countertrade. In trade with the NME's and debtor countries, particularly in Asia, however, Japanese firms are being confronted with strong demands to engage in countertrade.

Republic of Korea.--The Government has a comprehensive official offset program. 3/ There is no official policy toward nonmilitary countertrade,

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1/ See Thaddeus Kopinski, op. cit., pp. 248-253.

2/ International Countertrade: A Guide For Managers and Executives, op. cit.

3/ For the general guidelines of the Korean offset program see Defense Industry Bureau Ministry of National Defense Republic of Korea, General Guide For Korean Offset Program.

however, a Government agency, the Countertrade Promotion Committee within the Ministry of Commerce and Industry, monitors countertrade developments. 1/

Malaysia.--The Government is willing to engage in countertrade arrangements with any country or foreign trade organization. The Government will engage in countertrade with any of the following five groups of countries: (1) countries that supply goods for major Malaysian development projects; (2) countries with which Malaysia is experiencing persistent trade deficits; (3) developing countries that are important and growing markets for Malaysian commodities facing sharp competition; (4) socialist countries experiencing similar difficulties; and (5) oil producing/exporting countries that obtain their imports in proportion to purchases of oil from them. The Malaysian Government has no legislation requiring private firms exporting to Malaysia to engage in countertrade.

A special Government agency within the Ministry of Trade and Industry called Unit Khas Countertrade of the International Trade Division is in charge of the following functions relating to countertrade: (1) formulating and implementing policies and guidelines on countertrade; (2) collecting and disseminating information on products available for countertrade, and on potential sellers and buyers of countertrade goods; (3) handling and approving proposals for countertrade deals from domestic firms as well from foreign governments and firms; (4) advising other Government agencies on the use of countertrade in their purchases; and (5) monitoring implementation of the countertrade deal. Bill of lading, packing list, commercial invoices, customs declarations in Malaysia and letters of credit are the accepted evidence of performance by a foreign partner.

All Government agencies must include countertrade conditions in tender documents for certain Government procurements. Commodities used in infrastructure development projects, such as agricultural and energy development projects, fall into this category. Quasi-state firms (e.g., the National Petroleum Co. and firms producing cocoa and palm oil) also export commodities through countertrade. Although the Government strongly recommends the use of countertrade to private firms, it does not mandate countertrade. The Government lists the following commodities that may be acquired through countertrade: rice, wheat, sugar, iron ore, cotton, coal, animal feeds, chemical products, fertilizers, machinery and equipment, defense equipment, and vehicles. Malaysian footwear, textiles, articles of rubber and wood, foodstuffs, and electrical goods and components are among the manufactured and semimanufactured goods that the government lists as available for countertrade. The Government restricts the use of primary commodities in countertrade when such goods can be easily moved in international markets or when the purchasing country has demonstrated foreign exchange to purchase such goods.

The following criteria are used in approving countertrade arrangements: (1) the countertrade goods must be destined to the country of origin of the tenderer, although a different destination may be approved on a case-by-case basis; and (2) the countertrade goods must not displace exports for currency; thus, they must be directed to new markets and must not involve goods that may otherwise be sold for currency on world markets.

1/ See, Stephen F. Jones, op. cit.

Pakistan.--The country has bilateral trade agreements with several NME's. These agreements entail countertrade to some extent. The State monopoly enters into countertrade deals with foreign governments. Private companies may enter into such deals with other firms from market economy countries but not with foreign governments. The Government of Pakistan has declined various proposals by Western firms to engage in countertrade deals (including offsets).

Philippines.--The Ministry of Trade and Industry issues guidelines on countertrade. According to these guidelines, raw materials vitally important for the national economy, goods in scarce supply, and goods that can be readily sold to a third party are allowed to be imported through countertrade. The goods given as payment for countertrade imports are required to represent incremental exports or exports to non-traditional markets. Each countertrade proposal is evaluated by the Central Bank and the Ministry of Trade and Industry. The Countertrade Committee (also referred to as the "Trade Development Promotion Committee") within the Ministry is responsible for coordinating opinions among Government agencies on countertrade deals. There is a special trading company that negotiates and administers deals with the NME's. The country's major countertrade products include food products, tobacco, petroleum, chemicals, manufactured goods, and machinery and transport equipment. 1/

Saudi Arabia.--The country has a formal policy requiring offsets on certain defense contracts. 2/ An intercabinet committee reviews this policy and monitors the execution of particular deals. On occasion, Saudi Arabia requires industrial investment from foreign firms wishing to obtain crude oil entitlements. There is also interest in the country to institute a countertrade policy designed to promote nontraditional exports. 3/

United Arab Emirates.--Countertrade appears to be limited to transactions involving payments with petroleum and petroleum products for vital imports. Further interest in increasing the use of these trading methods depends largely on the country's intentions to scale up its industrialization efforts.

Latin America

Argentina.--The Government has not developed a comprehensive policy concerning countertrade; however, a high-level review of current regulations that prohibit barter in the private sector is underway. The Government's involvement with countertrade in the past has been limited to clearing arrangements with several countries including the Soviet Union, China, and Iraq. In 1984, Argentina and Mexico signed a clearing agreement under which packages of proposed exports cannot exceed the proposed imports by more than 10 percent on a product-by-product basis. Products that have reportedly been exported in countertrade deals include grain, wine, wool, beef, and other foodstuffs. 4/

1/ Stephen F. Jones, op. cit.

2/ For details, see Thaddeus Kopinski, op. cit. pp. 219-220.

3/ Stephen F. Jones, op. cit.

4/ Pompiliu Verzariu, U.S. Department of Commerce, International Countertrade: A Guide for Managers and Executives, November 1984.

Bolivia.--Requests by private firms to purchase capital goods from abroad must be submitted at the cabinet-level ministry, which has jurisdiction over the applying firm's line of commerce (i.e., industrial firms apply at the Ministry of Industry and agricultural firms at the Ministry of Agriculture). The appropriate ministry consults with the country's central bank over the availability of foreign exchange for the requested purchase. Under guidelines determined by the Government, the bank approves or denies allocation of foreign exchange for the requested import. If a firm's request for currency is denied but its import request is approved, the firm has two alternatives: (1) if the goods produced by the importing firm qualify to be used in countertrade, the firm may ship a stipulated amount of its goods to the appropriate ministry, the ministry will contact a State trading company that will countertrade these goods for the requested import; or (2) if the firm's products cannot be used in countertrade, the firm will have to pay in local currency for the amount of Bolivian goods that a State trading company will use in deals in order to acquire the approved import.

The Government uses countertrade for the acquisition of capital goods required for the completion of infrastructure development projects. It often imports goods (e.g., medicine and foodstuffs) for distribution to local governments or to private users through commercial channels.

The Chamber of Commerce and the Chamber of Industry (trade associations) pool information for the Government on the availability of Bolivian goods for countertrade. Although there is a fairly large variety of available goods, minerals, coffee, and wool are the country's major countertraded goods. Many of the country's countertrade deals take place under bilateral clearing agreements. For example, Bolivia has substantial bilateral clearing agreements with Argentina, Brazil, members of the Andean group, and with those of the Latin American Association for Economic Integration (ALADI). In addition to these countries, the United States is one of Bolivia's most important countertrade partners.

Brazil.--Brazil has no formal policy governing private sector countertrade, but its state-owned company (Petrobras) has engaged in countertrade with oil-producing countries through its subsidiary (Interbras). Since 1983 when it was faced with a shortage of foreign exchange, Brazil has attempted to pay for oil imports with other means than cash. The majority of Brazil's countertrade agreements, including one with Nigeria, have involved the exchange of Brazilian goods such as sugar, salt, cotton, chemicals and construction materials for petroleum. Brazil has also signed countertrade agreements with Ecuador, the Soviet Union, Angola, China, the United Arab Emirates, and Indonesia involving iron and steel, petroleum derivatives, agricultural and textile products. In November 1984, Brazil passed legislation requiring offset concessions for aircraft purchases. 1/

Columbia.--Columbia has engaged in countertrade to a limited extent for many years. In 1983, the government instituted several regulations governing special trade practices such as barter and compensation. These regulations were modified by a temporary law in February 1984 which mandated countertrade as a precondition for the importation of some 30 products. However, due to

1/ Report from U.S. Embassy, Rio de Janeiro, November, 1984.

uncertainty among the business community and government agencies regarding the implementation of these regulations, few deals have actually been consumated. In January 1985, the tax reinvestment certificate for exports associated with countertrade was eliminated and sixteen products were prohibited from being exported through countertrade, including cotton, tobacco, sesame, rice, coffee, bananas and flowers. 1/

Ecuador.--The Monetary Board, Ecuador's highest level economic policy-making body, determines policy guidelines and general rules on countertrade. The Board has limited the resale of Ecuadorian countertrade goods to third parties, and it requires that the end user of Ecuadorian countertrade goods be reported to the authorities. These rules are aimed at assuring that the loss of monetary export revenues will be minimal. Regardless of the specifics of a contract involving countertrade between private trading partners, the Government does not issue an import license to Ecuadorian firms until acceptable proof of export by these firms is presented. The policies and rules determined by the Monetary Board are implemented by the Ministry of Industry, Commerce, and Integration (MICEI). This Ministry is in charge of registering and approving individual contracts involving countertrade by private firms. The criteria of approval are intended to assure that only goods that are difficult to move on international markets will be countertraded. Oil, cocoa, tuna, shrimp, coffee, and fishmeal are currently excluded from the list of countertrade goods. Bananas may be used only if the countertrade deal helps open new markets.

Various Government ministries import commodities through countertrade for use in performing their regular functions. Thus far the Government has had little success in acquiring commodities for the country's infrastructure projects through countertrade, and it does not mandate countertrade to private firms. The United States, West Germany, France, the Soviet Union, and Eastern European countries are the country's major countertrade partners.

Jamaica.--The Jamaican government supports the use of countertrade as a means of overcoming the country's foreign exchange shortage. 2/ The government agencies which are primarily responsible for implementing these policies include: the Ministry of Mining, Energy, and Tourism, and the Bank of Jamaica. Private firms need the authorization of the Bank of Jamaica to engage in countertrade deals. Authorization is granted on a case-by-case basis. The major criteria for approval are that a countertrade deal must not displace exports for hard currency and that it must provide a minimum margin of benefit to the Jamaican national economy. The Government in some instances mandates countertrade to private firms. 3/

Jamaica's two major State-owned trading companies (the Bauxite-Alumina Trading Company and the Jamaican Commodity Trading Company) are both heavily involved in countertrade. In 1983, Jamaica signed a barter agreement to exchange 1 million metric tons of bauxite for $13.6 million of U.S. dairy products. 4/

1/ Howell, op. cit.
2/ Howell, op. cit.
3/ Stephen F. Jones, op. cit.
4/ "Jamaica, U.S. Agree on Bauxite Barter, Journal of Commerce, November 21, 1983.

Jamaica's major countertrade goods are bauxite, alumina, bananas, sugar, and tourism. The United States, Yugoslavia, and European countries are Jamaica's major countertrade partners.

Mexico.--The government of Mexico permits commercial (non-governmental) countertrade, but does not specifically encourage such practices. 1/ The Economic Cabinet is responsible for issuing and reviewing Mexican policies including countertrade. According to Mexican export regulations which were issued in March, 1983, barter and countertrade transactions must be authorized by the Bank of Mexico and approved by the Ministry of Trade and Industrial Promotion (SECOFIN). In 1984, additional guidelines were issued stipulating when and how export proceeds in hard currency are to be utilized in conjunction with advance purchases and other forms of countertrade. Those products which have reportedly been exported under countertrade deals include coffee, honey, fluorspar, and sulfur.

Nicaragua.--Most of Nicaragua's countertrade arrangements have been carried out with neighboring countries such as Guatemala. Countertrade transactions must be approved by the Ministry of Foreign Commerce. According to Nicaragua's regulations governing foreign trade, commodities such as textiles and processed oats may be countertraded, but coffee and cotton cannot be involved in countertrade deals. 2/

Peru.--The Government of Peru has no official policy towards countertrade. However, it has engaged in a limited number of countertrade deals with Western countries and several NME's. The single largest countertrade deal was a 1976 agreement between Peru and Japan to build the trans-Andean oil pipeline. The agreement included an extended payment period for the pipeline and a supply contract for oil.

The Government gives priority to labor-intensive products, to imports aimed at job generation, to agro-industrial products and to forest products. Commodities which have been exported in conjunction with countertrade agreements include copper, fishmeal and canned fish. 3/

Uruguay.--The country's policies on countertrade are formulated mainly by the cabinet-level Secretariat of Planning and Coordination. The Foreign Trade Office within the Ministry of Economy and Finance implements these policies. This office grants permission to private firms to engage in countertrade on a case-by-case basis. The major criterion of approval is that Uruguayan exports incidental to barter and countertrade deals should not result in the loss of export revenues. The Foreign Trade Office often acts as an information broker between potential foreign sellers and Uruguayan producers, thus encouraging countertrade among them. 4/

Venezuela.--The government of Venezuela does not have a formal policy governing countertrade and only a few such arrangements have been negotiated in this country. There is no legal framework or appropriate coordinating

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1/ Howell, op. cit.

2/ "How CT is Developing in Third World Countries," Business International Corp., 1984.

3/ Ibid.

4/ Ibid.

agency to conduct countertrade transactions. 1/ The government demands payments in hard currency for its petroleum exports which account for over 90 percent of the country's export revenues. However, outside the petroleum sector, the Venezuelan Institute of Foreign Trade and the Venezuelan Exporters Association are developing expertise in countertrade in order to increase nontraditional exports from the private sector. In addition to other Latin American countries, Japan and West Germany are among Venezuala's major countertrade partners. Venezuela has exported aluminum under a major buy-back arrangement and has indicated that bauxite and steel are available for countertrade. 2/

Other

Australia.--Since 1970, the Australian Government has required offsets on all overseas military and civilian purchases where Government funding or decisionmaking is involved. Private commercial transactions are not affected by this policy. The primary purpose of Australia's offset program, which is administered by the Department of Defense Support, is to upgrade the technology of its local industries. The Government prefers, but does not require that the offset be directly related to the initial purchase. When the contract value is $1 million or more, offsets exceeding 30 percent of the contract value are required. In 1984, a Review Committee on Offsets was established to examine the effectiveness of the current policy, and the Government announced it would strive toward stricter enforcement of its offset policy. 3/

Ghana.--Countertrade has been an important feature of Ghana's foreign trade policy for the past 25 years because of its continuing shortage of foreign exchange. During the 1960's and 1970's, Ghana undertook countertrade deals with the U.S.S.R., Czechoslovakia, Poland, and China. Recently, Ghana has signed several large-scale compensation deals with the German Democratic Republic, Bulgaria, and Egypt. The Government has established an administrative system for negotiating and monitoring countertrade deals. 4/ The Central Bank examines the proposed Ghanaian export to determine whether or not it can be sold instead for hard currency. The commodities that Ghana most frequently offers in countertrade are cocoa, tropical timber, rubber, frozen and canned fish and seafoods, gold, maganese, and bauxite. 5/

Ivory Coast.--The Government published guidelines on countertrade in 1984, which cautiously encourage the use of these trading methods. Each countertrade proposal is examined to determine whether it is in the interest of the economy and must be approved by the Ministry of Finance. The Ministry of Agriculture decides the quantity, type, and price of the products to be offered in countertrade. Recently, the main commodities offered by the Ivory Coast in countertrade deals have included bananas and coffee. 6/

1/ Report of U.S. Embassy, Caracas, November, 1984.

2/ International Countertrade: A Guide for Managers and Executives, op. cit.

3/ Ibid.

4/ Stephen F. Jones, op. cit.

5/ Business International Corp., op. cit.

6/ Ibid.

Libya.--Through its State oil-producing enterprises, the country offers surplus oil and oil products in countertrade. Counterpurchase arrangements are the preferred form of countertrade. Libya's principal countertrade partners are Mediterranean countries. Expanding bilateral ties with the NME's may result in increased Libyan oil exports through countertrade.

Mali.--The Government has instituted a number of local-content requirements for Western firms operating in the country. These requirements include the employment of locals and the use of domestically produced inputs. In addition, performance requirements such as increasing exports and restricting imports may also act as incentives to increase countertrade.

Morocco.--Countertrade transactions represent an insignificant amount of Morocco's total trade. The government has not issued any written regulations or legislation prohibiting countertrade. However, as part of the import license process, countertrade arrangement involving private firms must be approved on a case-by-case basis by the Ministry of Commerce, Industry and Tourism and by the Office des Changes. 1/ The Government phosphate monopoly (Office Cherifien des Phosphates), arranges barter deals if the foreign supplier can locate a local supplier as a partner. Until the late 1970's, this agency negotiated many barter deals with Eastern European countries. Other items that may be countertraded include minerals, textile products, foodstuffs, agricultural products, wine, and leather articles. 2/

New Zealand.--The New Zealand Department of Trade and Industry is responsible for examining countertrade proposals and in monitoring such sales. 3/ In 1982, this agency concluded a $150 million arrangement with Iran in which oil was exchanged for lamb. More recently, in January 1985, the New Zealand Meat Board concluded a barter deal with Poland involving an exchange of lamb for heavy industrial equipment. 4/ Since 1980, Government purchases exceeding NZ$2 million have invited the tenderer to submit proposals that would offset the procurement costs through domestic manufacturing or counterpurchase arrangements. This is not a mandatory requirement and does not affect private-sector procurement. Offset proposals that relate to the development of primary processing in sectors such as forestry, fishing, and horticulture are given special preference. Counterpurchases of horticultural products and exports of fish and derived products are encouraged if they will lead to new markets. 5/

Tunisia.--Trade agreements and protocols with the NME's have increased the role of countertrade in Tunisia's foreign trade. However, several other countries, including France, have also concluded major countertrade deals with the country. Primary goods and semimanufactures are Tunisia's chief countertrade exports. Efforts to industrialize the country may give rise to large industrial cooperation agreements with both market countries and NME's.

Zimbabwe.--Of all African countries practicing countertrade, Zimbabwe has the most detailed countertrade policies and rigorous enforcement of these

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1/ International Countertrade: A Guide for Managers and Executives. op. cit.
2/ International Business Corp., op. cit.
3/ International Countertrade: A Guide for Managers and Executives, op. cit.
4/ Report from U.S. Embassy, Wellington, September, 1982,
5/ International Countertrade: A Guide for Managers and Executives, op. cit.

regulations. Zimbabwe prefers government-to-government deals rather than those involving individual companies, because they are easier to administer. The Government examines countertrade proposals on a case-by-case basis and plays a major role in assisting firms with countertrade negotiations. In 1981, the International Committee for Special Trading Agreements was established to coordinate countertrade policy. This special committee is composed of representatives from four Government agencies and the private sector. 1/ In 1983, the Interministerial Committee established guidelines to be used in evaluating countertrade deals, including the following: countertrade is to be used only as a last resort (i.e., cash payments are preferred); the export product must be one that is hard to market; the deal will be permitted if it will open a foreign market that would otherwise be closed to Zimbabwean products and the price of both the imported and exported good must be "acceptable" (i.e., any discount must be "reasonable"). The government prefers countertrade deals involving exports of raw materials against imports of industrial raw materials and semifinished goods. Countertrade deals for imported manufactured goods requiring spare parts are prohibited. The Government gives priority to countertrade deals that involve imports of products that would normally be paid for with convertible currency. 2/

Since the Interministerial Committee was set up, less than 10 countertrade deals have been concluded with Romania, the German Democratic Republic, Bulgaria, the United Kingdom, and others. The commodities that Zimbabwe has exchanged through these transactions include ferrochrome, nickel, high-nicotine tobacco, and maize surpluses.

1/ Ibid.
2/ Business International Corp., op. cit.

APPENDIX J

ORGANIZATIONS IN SELECTED FOREIGN COUNTRIES THAT ARE INVOLVED IN NEGOTIATING AND OVERSEEING COUNTERTRADE (INCLUDING MILITARY OFFSET) ARRANGEMENTS

Country	Countertrade negotiating organization
Australia	Department of Industry, Technology, & Commerce Federal Economic Chamber Department of Productivity
Belgium	Ministry of Economic Affairs
Brazil	Petrobras Comercio Internacional S.A. - Interbras Calex LOTAC - run by Civil Aviation Department Ministry of the Navy Ministry of Commerce/Trade
Bulgaria	Isotimpex, Foreign Trade Agency, Sofia
Canada	Department of Regional Industrial Expansion Canadair, Ltd. Department of Industry, Trade, and Commerce Department of Supplies and Services Ministry of Aviation Industry
China	China National Technical Import Corp. China National Aerotechnology Import & Export China National Chemicals Import/Export Corp. Beijing Metalurgical Bureau Ministry of Machine Building Industries
Czechoslovakia	Foreign Trade Ministry
West Germany	Bundesantalt fur Flugsicherung
Finland	Finnair
East Germany	Foreign Trade Ministry Trading Companies for the Machine Tool Industry F.C. Gerlach on behalf of Ministry of Foreign Trade
Hungary	Hungarotex - State Monopoly for Textiles Monimpex FTO & EGRI Dohanygyar
India	Secretary of Defense - Production MMTC - Minerals & Metals Trading Corp. of India
Indonesia	Ministry of Manpower and Transmigration Department of Trade & Cooperatives Pertamina
Israel	Industrial Subcontracting Authority Bezeq - The Israel Telecommunications Corp., Ltd. Ministry of Defense, Mission to the U.S. Industrial Cooperation Authority
Italy	Ministry of Foreign Industry

Country	Countertrade negotiating organization
Jamaica	Jamaica Commodity Trading Co.
Japan	Japan Defense Agency
Mexico	Bureau of Mexican Federal Government of National Assets and Industrial Promotion
Netherlands	Fokker
Philippines	Philippine Technology Transfer Board - a division of the Board of Investments
Poland	Cziech Polsr (Polish State Trading Co.) Elektrim (Polish Foreign Trade Co.) Prezedsiebiorstwo Handlu Zagraniczego Agros Foreign Trade Ministry
Portugal	ICEP Insittuto do Commercio Externo The Portuguese Airline (TAP)
Romania	USINEXPORT IMPORT I.C.E. Terra - Foreign Trade Co. Chiminportexport Danubiana Chemical Import-Export Foreign Trade Ministry
South Korea	Air Force Navy Ministry of National Defense
Soviet Union	Autopromimport V/O Sourybflot, Ministry of Fisheries Techmashimport
Sweden	Saab-Scania through JAS Organization
Yugoslavia	Duvanska Industrya NIS Yugoslavian Federal Secretariat Zeleznisko Gospodarstuo Ljubljana Bilroad The Federal Committee on Energy and Industry
Zambia	Metal Marketing Corp. of Zambia