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#60

FACULTY WORKING PAPERS

THE THEORY AND PRACTICE OF
DEVELOPMENT AID

Daniel A. Sumner
and
Edward W. Erickson

No. 60 September 1984

DEPARTMENT OF ECONOMICS AND BUSINESS
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Comments Welcome

THE THEORY AND PRACTICE OF DEVELOPMENT AID

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September 1984

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THE THEORY AND PRACTICE OF INTERNATIONAL DEVELOPMENT ASSISTANCE

Introduction

Economic growth has occurred at an uneven pace and also with a quite uneven geographic pattern. Over the last century as the poor became somewhat better off, wealthy nations became relatively even more well-off. Economic growth is a long-term process. The timescale is a matter of centuries, not years. In the thirteen decades from about 1840 to 1965, the Gross National Product (GNP) per capita in the United States grew from about $470 to $3,580, measured in constant 1965 dollars.[1] This record is similar to those of the other wealthy countries of Europe and to those of Japan, Australia, New Zealand and Canada. For example, in the one hundred years from the mid 1860's to 1965, Australian GNP per capita grew from $760 to $2,023. In the same century, many of the poor countries started with about one-tenth the income per capita of the wealthy countries and ended with a per capita income not one-twentieth of that in most of the wealthy nations. This relative attrition occurred despite absolute advances. For example, Indian incomes averaged $86 per capita in the 1960s as compared to $47 in the middle of the nineteenth century.

In the last three or four decades, as many of the poor areas of the globe have become sovereign states, the wealthy countries have provided funds aimed at spurring economic growth among what used to be called the "backward" nations. Prior to World War II, there were limited and sporadic attempts to "help", often in the context of colonial relationships or disaster relief. Only since the 1950's, however, has there been a conscious policy of continuous transfer of development aid from nation to nation.

Defining Development and Development Aid

Economic development means a growth in the number of feasible choices that people have available. It means more potential consumption of all valued goods and services including such things as clean water, healthy foods and safe streets. Development does not mean more happiness for everyone; it does mean more resources broadly available that may be used for a variety of consumption and investment activities.

International development assistance may be distinguished from military or strategic assistance and from disaster relief, though it sometimes merges with each of these other categories of international aid. During times of emergency, disaster relief attempts to alleviate unexpected, temporary, and extreme suffering. Disaster relief contributes little to long-term growth and may even hamper development if the standards of unexpected, temporary and extreme are sufficiently eroded over time so that such relief becomes a permanent component of donor/recipient relations. The gains to the recipients of disaster relief are obvious and the motives of the donors are, for the most part simple charity. The donor feels better and may also expect some thank you in return for his kindness.

Military assistance is aimed at the defense of both the recipient and the donor nations. The military interdependence of our globe is, perhaps, even more obvious than the economic or social interdependence. Therefore, nations actively cooperate in the military development of their allies more than they do in economic development. The self-interest of nations in the military power of their allies may be almost as strong as the self-interest in their own power, so long as they share common enemies or threats. In that sense military aid may not be "aid" at all but only self defense. However, to the extent that it fosters political stability or reduces the probability of war, military aid may contribute to economic growth.

International development assistance is the contribution of resources that are directed towards a sustained expansion of overall economic well-being. Relief of a famine caused by a drought is not development aid. Providing irrigation engineers to develop water projects that smooth farm output over time is development aid. Sending tanks to protect a country's borders is not development aid, but sending tractors that increase farm output and may increase military security is development aid.

Market Oriented Development and Development Aid

The most damaging fallacy in development theory and practice has been that people in poor, rural countries are different from those in wealthy countries in some fundamental way. One particularly pernicious form of this fallacy has been that poor farmers are not normal economic agents. A corollary of this fallacy of attribution is that poor farmers in less developed countries do not respond to opportunities to improve their own well-being and that of their families. These ideas have led to the notion that politicians and government officials must make decisions and create a "planned" economy in order for development to proceed. They have also led to policies that severely distort agricultural input and product prices because, it is gratuitously presumed, poor farmers do not respond to prices anyway.

Basic economic reasoning and overwhelming evidence have each contributed to the collapse of this fallacy. P. T. Bauer and Nobel prize winner T. W. Schultz have been particularly influential in this regard.[2] The practice of development assistance has begun to be influenced by market orientations at the World Bank and the Agency for International Development (see the World Development Report for 1982 for evidence).

Market-oriented development means recognizing the power of the billions of the world's poor to recognize and execute decentralized development initiative. It means using the power of the state to remove, not create, barriers to individual action. In the context of aid, market-oriented development means using international influence to encourage reduced government planning, not the creation of an additional layer of bureaucracy.

In this essay, we consider the facts and theories of aid and argue that the United States can best play a role in actually helping development only if we vigorously support market oriented policies in our own country and abroad.

The International Context of Development Assistance

Some people are poor while others are wealthy. This is the basic fact that conditions development assistance. Other related facts are that there is a potential for economic development among the poor and we live in a world of social interdependence.

Basic Indicators and Progress

Table 1 provides an overview of indicators of development for a few countries. Among the countries listed in the World Development Report, Gross National Product (GNP) per person varies by a factor of over 100, from less than $150 per person in Bangladesh and Chad to about $15,000 per person in Switzerland and Scandinavia.[3] The countries listed in Table 1 represent a wide range of the poor, middle income and wealthy countries of the world.

These figures also indicate the correspondence between income and other characteristics of the population and economy. Adult literacy, for example, ranges from below a quarter to essentially one hundred percent.

Illiteracy contributes to poverty, but it is also implied by poverty in most parts of the world. Infant mortality, besides being influenced by the level of poverty in a society, is also an index of the overall ill health of the population; and poor health leads to poverty.[4]

Food is the fundamental economic commodity, and the production of agricultural commodities is the major economic activity in most societies. Overall wealth tends to be closely and negatively correlated with the proportion of the population of a society engaged in agriculture. That is, progress in agriculture implies more and more output with relatively fewer and fewer people employed in the production of food and fibre because economic development opens up new opportunities as the demand for nonagricultural goods and services expands. Major agricultural exporters--such as the U.S.--have tiny proportions of the work force in agriculture, while poor areas which are food importers--such as Africa--have large proportions of the population farming. Many countries (and many economists) have mistakenly assumed that these facts imply that sound economic development policy should be biased against farmers.[5] The truth is that farming, though all the while declining in relative importance (i.e., becoming a smaller industry measured by proportion of labor force or GNP) can be a leading engine of economic growth.

Table 2 illustrates changes in the basic indicators of development over the period 1960-1981. The world has become wealthier. And most of the poorest nations have shared in this growth. Population has been growing at about two percent per year in the poorest countries, at about 2.5 percent per year in the middle income developing countries, and at somewhat less than one percent per year in the wealthy countries. The population growth has been well below growth rates in output so that per capita GNP has grown at about three percent per year in the low income economies and at about four percent per year in the middle income countries. While some countries, especially in Africa, have had falling GNP per capita, the lot of the world poor has been improving overall.

This basic message shows up more directly in social indicators like literacy and infant mortality. Adult literacy rates have risen from below 20 percent in many parts of the world to close to 50 percent or higher in most countries. The substantial reduction in infant mortality from 165 deaths per thousand in 1960 to below 100 in 1980 is an encouraging statement for world wellbeing. The progress has been slow and uneven both within and across countries, but there _has_ been progress.[6]

The World Pattern of Development Assistance

In the last three decades, the volume of economic interaction between poor and rich nations has expanded tremendously. International trade has increased and development assistance has become a major flow of external resources in some poor countries. Imports and exports of low income countries have each grown at about 4 percent per year. Development aid from members of the Organization of Economic Cooperation and Development

(OECD) has grown from $16 billion to over $28 billion (in 1980 prices).[7]

Egypt, India, Israel and Bangladesh are the world leaders in total aid received. Relative to total GNP, Egypt, Bangladesh, Tanzania and Papua New Guinea are also large recipients from OECD countries. Several nations, including Egypt, Syria, Jordan and Sudan receive funds from OPEC countries rather than (or as well as) receiving OECD contributions. For some small nations, total official development assistance flows have been as much as 15 percent of the gross national product.

Among donor countries, some of the middle eastern oil rich countries contribute well over one percent of GNP to development aid. Of the OECD countries, the U.S. provides the most assistance absolutely, but most of the other wealthy industrial nations spend a larger relative share of GNP in official development assistance.

Table 3 shows some of the patterns of development assistance for selected countries. In the next section we review the record of U.S. assistance in more detail.

A Brief Description of Development Assistance from the U.S.

The U.S. spends billions of dollars each year on development assistance through bilateral or multilateral commitments. The forms and destinations of these funds are outlined in this section.

Characteristics of U.S. Development Assistance

The United States contributes official development assistance through four major channels. The first, contributions to multilateral agencies, has constituted about 40 percent of total official aid. The other aid is coordinated by the Agency for International Development and is essentially bilateral. About one third of the bilateral assistance (or 20% of total U.S. aid has been disbursements under the development assistance program of AID. About forty percent of bilateral assistance (or nearly 25% of total U.S. aid) has been distributed under the Security Supporting Assistance program that attempts to use aid to promote political and military stability. Over the years, high proportions of these funds were used in the Middle East, especially in Egypt and Israel. More recently, Central America has been a focus. The final administrative category of bilateral assistance is food aid under P.L. 480 (the Food for Peace Program). P.L. 480 funds are allocated by AID with U.S. Department of Agriculture input. Funds are used to distribute U.S. farm commodities to poor countries. By law, at least 75 percent of food aid commodities must go to low income countries. Under P.L. 480 a special allocation (Title II) is made for commodities used to meet famine or other urgent relief demands and for malnutrition programs.[8]

The top panel of Table 4 gives a general breakdown of the sectors to which the U.S. has committed bilateral aid. Among these, agriculture received the largest share, about 30 percent of the total. While this share is large relative to other sectors it is small relative to the share of agriculture in the GNP or in the labor force of most of the countries receiving U.S. aid. Other sectors receiving a concentration of aid are health and public utilities. Each of these sectors have considerable government involvement in the U.S. and in most other countries.

The bottom panel of Table 4 shows the amount of total aid from the United States that is tied to specific goods or services. Almost all multilateral aid is untied as it leaves the U.S. Most of these funds are given to particular international agencies, however, so their use is somewhat restricted. Further, the multilateral donors tie aid to particular programs and projects as it goes to the poor countries. The activities pursued by an international agency affect the level of U.S. contributions to the agency.

Bilateral ODA from the U.S. is more tied than untied. Still, about one third of bilateral aid goes to poor nations in the form of untied grants or loans. A large part of foreign aid from every source is tied in the form of technical assistance and expert training. This category includes contributions in the form of student aid, trainees, volunteers, or experts. In the case of the international transfer of experts, the recipients get educators or specialists, usually in technical fields. In 1982, the technical co-operation expenditure totalled $1.1 billion and involved over 22,000 people.[9]

Geographic Distribution of Development Assistance

Table 5 shows the percentage distributions among major recipients of development assistance from the United States, from all the countries of the Development Assistance Committee combined, from the United Nations Development Program and from all multinational sources combined. In the 1980/1981 period the U.S. contributed a total of about $6.25 billion, with 34 percent going to multilateral agencies. The recipients of the largest bilateral shares were Egypt with 14.1 percent and Israel with 12.8 percent. The clear relationship to strategic and foreign policy concerns is evident.

Other countries also have particular foreign policy concerns which determine the geographic distribution of bilateral aid flows. For many donors, aid is related to former colonial relationships. For example, over half of French bilateral aid goes to former French colonies in Africa. Japanese bilateral aid is particularly skewed towards Asia with about half going to the relatively wealthy far eastern countries of Indonesia, Korea, Thailand, Philippines and Burma. Table 5 shows the sum of all bilateral aid from the DAC countries and indicates broad geographic spread among the highly populated and very poor nations. But there is considerable influence of special interests in the distribution as well. The UNDP and other multinational sources spread development assistance even more widely. China, Kampuchea and other communist nations are among the major recipients of development aid from multinational agencies.

Flows of Financial Resources from the U.S. to the Developing World

Over the last three decades, real economic exchange with the poor parts of the world has grown dramatically and official development aid from the United States has not kept pace with world economic growth. If development aid is successful in helping to achieve sustained economic growth, then aid as a fraction of world economic activity should decline over time. The world is more and more a single marketplace and U.S. firms and individuals have taken a major role in trading with and investing in the poor countries. Table 6 divides the total net flows of financial resources from the U.S to the LDC's into four major categories.

Official Development Assistance (ODA) given by the U.S. may be in the form of either grants or loans, grants being by far the major component of the bilateral assistance. Of U.S multilateral aid, two-thirds is in the form of loans. ODA represents 27 percent of the total net economic exchange between the United States and the poor countries of the world. "Other official flows" include loans and equity investments from official sources on commercial terms and represent about 5 percent of all net flows. Grants from voluntary sources in the U.S. are also important and make up a larger share of the flow than do grants from official multilateral agencies.

Direct investment by U.S. firms and individuals into enterprises located in poor countries is one form of private flows. In this arrangement, those companies based in the United States maintain full or partial control of the enterprise. Purchasing a country's stocks or bonds is the largest single component of the flow of economic exchange between the U.S. and the developing countries. Just as in the United States, in developing countries it takes financial investments in the form of purchases of stocks or bonds to generate physical capital and maintain real production in poor countries. Private flows at market terms are important sources of development aid from other countries in addition to the United States. For the developed countries as a whole, these private flows are over twice as large as official aid.[10]

The economic exchange that occurs because of clear expected gain by both parties is not only the largest share of economic interaction with poor nations, it is also the component most likely to benefit the poor.

The Economics of Development Assistance

Development aid can have several benefits for the recipient and can also benefit the donor. But it is clear that such benefits do not actually occur with any regularity. Common anecdotes provide sufficient evidence of the often futile experience of development assistance programs and projects. We will not detail such horror stories, but will rather discuss why aid may or may not help the poor contribute to the objectives of the rich. We will first outline the reasoning behind the assertion that aid can help those in poor countries. Then we will present the argument that aid can contribute to the interests of donor nations. Next we will discuss why the benefits to both parties are so vulnerable. Finally we will examine how the aid that does occur might be made effective.[11]

The Promise That Aid Holds for the Poor

Development means growth, and growth requires investment. There can be no development without investment, and the pace of development depends upon the level of investment and upon the rate of return earned on that investment. At the most basic level, foreign aid attempts to add to the flow of resources available for investment in the poor countries. If the flow of investment is increased, then the rate of growth in output should also increase. Private funds that are attracted into the developing world by the profitability of the potential investments earn a normal rate of return (given adjustments for risk). These funds contribute to growth even if the profits are consumed elsewhere. If aid funds were to be invested in the same way as private market funds, they would make a similar contribution. Proponents of aid hope that the returns to aid investments will provide higher benefits than private market flows, while skeptics note that aid allocated by governments is not likely to be invested as efficiently as private funds. The basic idea that, other things equal, more investment means more growth applies both to aid and to private flows.[12]

The Value of Development Assistance to the Rich

The most direct rationale for international assistance to encourage economic development is that the people of one nation unselfishly care about the well-being of people in other nations and simply want to help. Skepticism aside, this motive is a major force in development aid. But, development aid is more than just short-term charity to alleviate suffering. If successful, it eliminates itself by helping countries achieve self-sustained economic growth. After quite significant flows of aid over many years, countries such as Korea and Taiwan have progressed in the last 30 years to the point that little further development assistance is in order.

Besides simply feeling good about helping one's neighbor, development assistance is often thought to provide more direct benefits to the donor nation. The metaphor of neighborliness is probably appropriate. One may help a neighbor partly to encourage the neighbor's kindness in return. The neighbor may do us a favor in return or may just avoid doing us harm. Much of the "security supporting" development aid has fairly direct potential benefits to the donor nations. Other aid may have less obvious connections to national security but may contribute more generally to world political and economic stability.

Another rationale for aid is that it fosters markets for a nation's exports. This may be a side benefit from aid activities, but cannot be a major factor. Clearly, you cannot come out ahead by giving someone the money to buy a product from you. On the other hand, over the long run we all gain from economic stability and growth in the world economy. Markets expand as income expands, and exports from the United States expand as do exports from everywhere else. To the extent that aid is a form of "public relations" or "goodwill" advertising, U.S. firms may gain from U.S. aid.

Firms in poor countries are also competitors for international markets. Part of the development success of some countries entails reducing imports of U.S. farm goods and competing with U.S. farmers and other business in the world marketplace. Brazil, Taiwan and other fast growing middle-income countries have become formidable competitors as well as important markets.

Aid may also be tied to the purchase of U.S. goods or services. This aid costs the U.S. less than the market value of the flow of goods. U.S. firms get to keep the profits from these sales. However, such tying will also reduce the benefits of the aid to the recipients.[13] If the tying arrangement is binding it means that at least some of the goods or services would have been purchased elsewhere or that other goods would have been preferred. The tradeoff is less development for the aid dollar versus less business for donor country firms. In general, tying aid to the use of donor country products or personnel overstates the amount of aid given, but may be vital in order to make aid politically feasible in the donor country.

The classic example of tied aid has been U.S. surplus food disbursements under the P.L. 480 program. This "aid" has been politically popular because it allowed reductions in embarrassing stockpiles of commodities acquired by the government under farm price support programs. Many have argued that dumping these commodities on world markets at greatly reduced prices has hurt farmers in other countries. As is discussed below, the most adversely affected have often been the rural poor in the very countries that have received the "aid."

The Role of Aid in Maintaining Poverty

Charity can be a mixed blessing. This truth verges on truism and it is of obvious importance to specify and clarify the possible ill effects that aid may have for the poor. Understanding how even the good intentions of donors may be severely frustrated is perhaps more vital to supporters than to denouncers of aid. Recognizing how aid may be likely to turn sour may lead to ways to avoid at least some of the problems. However, it may remain true that many ill effects of aid cannot be remedied and so it may be that aid is of no net help to the world's poor.[14]

Broadly speaking, the ill effect of development assistance is that it necessarily distorts market signals and market incentives. Thus it necessarily diverts the flow of economic resources in poor countries from the most productive uses. Whenever resources are made available to an economic agent outside normal market channels there are unavoidable side-effects for the costs and benefits of related market activity . Overall income is reduced by these distortions because buyers and sellers get inappropriate signals. Sometimes the consequence is major inefficiency, and sometimes the distortions are minor, but they always occur. This general point arises in the context of overall investment and savings levels, in levels of work and investment across sectors of the economy, and in the relative position of collective versus private market activity. These issues will be further developed and illustrated in the context of international aid.[15]

Food aid is the most notorious example of "development" assistance that may actually reduce the growth of incomes among the poor. As cheap food enters a developing country, the farmers in that country find the market for their product eroded. Since most poverty is rural poverty, the net result ends up being lower incomes and lower growth overall. Besides directly distorting agricultural markets, food aid provides governments in the poor countries with an easy out for pursuing domestic pricing policies that are biased against the domestic farming sector. This occurrence has been documented time and time again.[16]

Many of the world's poor nations pursue policies that actively discriminate against their rural sectors. These include overvaluing currencies, making modern agricultural inputs expensive and exports cheap, and instituting explicit cheap food policies in order to subsidize the urban consumer. Food aid is one of the supports that make such policies viable. Governments count on a foreign power (typically the U.S.) to make up the food deficit when their own farmers fail to produce enough, given the distorted incentives facing them. Thus, rural growth, by distorting prices, also allows or encourages LDC policies that are inimical to growth.

Some planners have sought to tie food aid to other required policies designed to make up the difference to the rural sector. It is a standard scheme for government planners to propose a more complex program to remedy the untoward effects of induced market distortions. It is just as standard that these schemes don't work. It is even more true that in an international multigoverment market, complicated political schemes cannot hope to provide clear and direct signals to farmers (or to others) to produce, save, invest and grow.

Land reform is another policy that often follows foreign aid; typically it is as disastrous as food aid. Governments find it easy to require the expropriation of wealth in a foreign state, so the idea of playing Robin Hood in someone else's country is universally appealing. Often little thought is given to why a particular land tenure system evolved and what barriers suppressed strong market incentives to an efficient pattern of farming. Again the policy that tends to go with development assistance is collectivization and central planning.[17]

These examples could go on and on: big water projects, big steel mills, big highway projects, government banks and fertilizer distribution companies, etc. The point, made forcefully again and again by P.T. Bauer and B. Yamey, is that foreign aid by its very nature encourages that power be centralized in the capital city. This power is then very unlikely to be relinquished to the decentralized play of efficient market forces. Planning, itself, is not the issue. The issue is who does the planning and for whom. The implicit plea of Carl Anonsen is revealing. "Who has ever heard of regional planning being a success in developed countries? Why must we always export outdated techniques to developing countries? Probably the words planning and socialist originally appealed to the nationalist leaders of the new states because they seemed to offer accelerated development and serve as an instrument for greater independence, and probably also for increasing their own power."[18] This is perhaps the central criticism of foreign aid and one that must be addressed.

Making Aid an Effective Contributor to Growth

Given the basic idea that an increase in available capital will speed growth, there are several complications in examining the hoped-for contribution of aid to the poor. Many of the arrangements made for the distribution of aid to particular projects or in particular forms are designed to get more growth per volume of aid than would follow from a direct transfer of funds from the government of a rich country to the government of a poor country.

The question of what can be done to make assistance effective in development is related to how to use aid such that it most increases net investment in the poor countries and such that it increases rather than reduces the overall rate of return on investment. The answers are basically: (a) make sure government aid gets used for appropriate government activity, (b) use aid to encourage the policy reforms and stability of property rights that themselves spur development (c) leave the market free to do what it does best--providing the vigor of private incentives to guide the level and allocation of investments. Each of these points will be developed briefly.

(a) Official development assistance from the United States goes from one nation to another and is then invested in government projects and programs. Therefore, to be effective, aid must be used for activities that are appropriately those of a government. In any economy some potentially sound investments are not made by private firms or individuals. This may occur because the returns to the investment cannot be captured by the investor. For example, national defense is normally considered a good investment, but, since it is difficult to exclude non-payers from the benefits of the service, a private firm, without the power to tax, would find it difficult to sell "national defense." This argument suggests government or collective funding of activities that have "public good" characteristics, like defense. It does not imply government operation or provision of these services or activities. Some investments that contribute to development may fall into this "public good" class. Among the most prominent investments for which collective funding is usually accepted are: legal administration and enforcement, basic education, general sanitation and disease control, basic research, and applied research and information dissemination in industries such as farming with many small firms and a broad distribution of consumers.[19]

(b) By providing or withholding aid the United States acquires influence over the governments of other countries. The U.S. must recognize that such influence exists and then use it to encourage policy reform.

If the United States and a recipient country agree on the proper role of the state, then at least one principle of effective aid is more easily satisfied. But disagreement over the scope of government versus private action is widespread even within countries so such agreement is not easy to achieve.

Aid may be provided in the form of general investment funds or as some specific service, capital good or commodity, but economic resources are fungible so the specific form of aid does not necessarily control the form of the net impact on a society. In order to make "tied" aid more tied, countries require matching funds or compliance with some other general guidelines for spending of funds other than those provided by the donor. This may succeed in restricting the activities of the recipient but it may not succeed in satisfying the ultimate interests of the donor.

Some countries may use aid funds as a stop-gap to avoid hard policy choices required to get their economies growing. However, other governments may welcome some help in moving their economies toward more stability and greater market orientation. By allocating aid those countries that show a wilingness to use it effectively, the U.S. can make aid a help rather than a hindrance and improve world growth.

This use of aid does not include becoming involved in detailed policy decision in a sovereign nation. Natives of a developing country almost certainly know more about how things work in their own country than government officials from some foreign power. When a donor nation and a recipient nation agree on the general role of collective action and on how best to use government funds to encourage development, the problems of attempting to control a foreign nation from the outside are reduced. The geographic pattern of ODA is dictated in part by the confidence that donor nations place in the governments of the recipients. Money well spent in a less needy country may do more good than money wasted among the poorer countries.

(c) A market orientation to aid means examining every project and program to avoid centralization and collectivization. A high rate of return to a project is not sufficient unless it can be demonstrated conclusively that market funds would not be used for such an investment. Providers of aid should recognize how easily government activity can distort private market activity. International funding can destroy incentives but can also provide valuable services. It is hard for a government agency to maintain a market orientation. It is even harder when government agencies in both donor and recipient countries are involved.

Implications

In this essay we argue that the poor people in the poor nations are the best judges of how development must proceed and that attempts to impose development plans will be futile.

The urge to help is strong, it is noble, and it should not be suppressed. Using some direct government funds for aid can further the goals of the United States and promote development. This can occur, however, only if we recognize the severe limitations of collective action. The power of the state defines and enforces property rights. A secure and stable set of property rights is required for investment and investment is lacking in many poor nations. Imposing particular investment strategies is folly, but using aid to encourage the development of secure market relationships and to help provide certain services that would not otherwise flow from private sources can be a real contribution to the wealth of nations.

Development assistance will continue and it has a natural tendency to become a force for increased collectivization. Therefore, continued effort is necessary to force a market orientation to every aid activity. This will help reduce the harm that aid might do and will help increase the benefits. Over the long run, the world's poor will become better off and we will all have a more secure future.

Footnotes

[1]What we quantitatively know about long term tendencies in economic growth is based on the work of Simon Kusnets e.g. Economic Growth of Nations, 1971, Harvard University Press. The figures in this note are from section I, "Level and Variability of Rates of Growth."

[2]See the useful summary in the Nobel prize lecture of Theodore W. Schultz, "The Economics of Being Poor," Journal of Political Economy, V. 88, no. 4, August 1980.

[3]The basic source for recent figures on income and related economic information is the World Bank's annual reports, for example the World Bank, World Development Report, 1983, Oxford University Press, New York. There are many well known deficiencies in any international comparisons of income, arbitrary exchange rates, mistaken national income data, inappropriate prices for home consumed produce, etc. Some of these same problems apply to any comparisons of income or well-being. We will present summary data on income and other national aggregates with the knowledge that they must be interpreted carefully and with skepticism.

[4]In his Investing in People: The Economics of Population Quality. University of California Press, Berkeley, 1981, Theodore W. Schultz makes a strong case for the importance of health, especially life expectancy, as a factor in and measure of economic development.

[5]For a discussion of the distortions of incentives facing poor farmers see W. David Hopper, "Distortions of Agricultural Development Resulting from Government Prohibitions" in Distortions of Agricultural Incentives, Theodore W. Schultz, ed., Indiana University Press, 1978 and Theodore W. Schultz, "On Economics and Politics of Agriculture"

in Distortions of Agricultural Incentives, Theodore W. Schultz, ed., Indiana University Press, 1978. Also see G. Edward Schuh, "The Role of Markets and Governments in World Food Economy" in The Role of Markets in the World Food Economy, D. Gale Johnson and G. Edward Schuh, eds. Westview Press, Boulder, 1983. The World Development Report for 1982 also has a very useful summary of world farm policy biases.

[6]Again on this issue of population quality see Schultz, Investing in People, op cit., especially chapter 2.

[7]The basic source of information on development aid is Development Co-operation, OECD, 1983. This annual publication includes some discussion of aid practices as well as a wealth of statistical summary data on both donors and recipients. It provides data on the aid from the members of the Development Assistance Committee and from other aid providing groups such as OPEC and the Communist bloc.

[8]U.S. aid is described in Elliott R. Morss and Victoria A. Morss, U.S. Foreign Aid: An Assessment of New and Traditional Development Strategies, Westview Press, Boulder, 1982, and Hassan M. Selim, Development Assistance Policies and the Performance of Aid Agencies, St. Martin's, New York, 1983. The food aid component is described in an historical and political framework in Mitchel B. Wallerstein, Food For War--Food For Peace, MIT Press, Cambridge, 1980.

[9]These figures are from Development Co-operation, OECD, 1983.

[10]For a discussion of market exchange versus aid in a multilateral context see E. Erickson and D. Sumner, "The U.N. and Economic Development" in A World Without a U.N., Burton Yale Pines, ed., The

Heritage Foundation, Washington, 1984. They present a table similar to Table 6 that summarizes aid and trade for all donors taken as a group.

[11] Our consideration of the impact of aid and the progress of development more generally was influenced especially by Peter T. Bauer and Basil S. Yamey, The Economics of Underdeveloped Countries, University of Chicago Press, Chicago, 1957, and on foreign aid *per se* from the more recent Peter Bauer and Basil Yamey, "Foreign Aid: What is at Stake?", The Public Interest, Summer 1982.

[12] Discussions of aid include those in Gillis et al., Economics of Development, W.W. Norton & Company, 1983, Raymond F. Mikesell, *op. cit.* and Desmond McNeill, The Contradictions of Foreign Aid, Croom Helm, London, 1981.

[13] Many argue that tying aid is self-defeating. See John P. Lewis, "Development Assistance in the 1980s," in Overseas Development Council, U.S. Foreign Policy and the Third World: Agenda 1982, 1982, p. 298 as reprinted in Gerald M. Meier, Leading Issues in Economic Development, Oxford University Press, New York, 1984. Also see V.A. 5 "Improving the Quality of Aid--Note" in Meier for an expression of the basic argument by aid proponents.

[14] See Bauer and Yamey, 1982, *op cit*.

[15] Schultz has been a forceful writer on the ill effects of aid; see his Investing in People, Chapter 7, titled "Distortions by the International Donor Community."

[16] See World Development Report, 1982 or Johnson and Schuh, *op. cit.*

[17] See Grace Goodell, "What Life After Land Reform?" Policy Review, Spring 1983, pp. 121-148.

[18]The article, "Is Planning in Developing Countries Worth the Price," by Carl Anonsen in <u>Poverty and Aid</u>, J.R. Parkinson, ed., St. Martin's Press, 1983, provides further examples of how government planning itself may become an objective and how this creates obstacles for development.

[19]This discussion of "public goods" is essentially standard. See Bauer and Yamey (1957) for these ideas applied to the poor countries. Also see Erickson and Sumner, <u>op</u> <u>cit.</u>, for a related argument applied to the failure of U.N. development efforts.

Table 1. Basic Indicators of Development

	Population (millions) (1981)	GNP per Capita (dollars) (1981)	Adult Literacy (percent) (1980)	Infant Mortality Rate[a] (number) (1981)	Agricultural Labor Share[b] (percent) (1980)
Low Income Economies	2,210	270	52	99	70
Ethiopia	32	140	15	145	80
Zaire	30	210	55	110	75
India	690	260	36	121	69
Middle Income Economies	1,128	1,500	65	81	45
Indonesia	150	530	62	105	55
Peru	17	1,170	80	85	39
Korea, Rep. of	39	1,700	93	33	34
Industrial Market Economies	720	11,120	99	11	6
Japan	118	10,080	99	7	12
Netherlands	14	11,790	99	8	6
United States	230	12,820	99	12	2

[a]Number of infants per 1,000 live births who die before reaching one year of age.

[b]Percent of total labor force engaged in agriculture.

Source: World Development Report, 1983. Oxford University Press, NY.

Table 2: Progress Towards Development

Changes in Basic Indicators 1960-1981

	Annual Growth Rates		Adult[a] Literacy: Change Since 1960	Infant[b] Mortality: Change Since 1960	Agricultural[c] Labor Share: Change Since 1960
	Population (1960-81)	Real GNP per capita (1960-81)			
Low Income Economies	2.1	2.9	18	-66	- 7
Ethiopia	2.2	1.4	--	-30	- 8
Zaire	2.5	-.1	24	-40	- 8
India	2.2	1.4	8	-44	- 5
Middle Income Economies	2.5	3.7	17	-46	-17
Indonesia	2.2	4.1	23	-45	-20
Peru	2.8	1.0	19	-78	-13
Korea, Rep. of	2.2	6.9	22	-45	-32
Industrial Market Economies	.9	3.4	3	-19	-12
Japan	1.1	6.3	1	-23	-21
Netherlands	1.0	3.1	--	-10	- 5
United States	1.2	2.3	1	-14	- 5

[a]Changes in the percentage of literate adults.

[b]Changes in the number of infant deaths per 1,000 live births.

[c]Changes in the percentage of the labor force in the agricultural sector.

Source: World Development Report, 1983. Oxford University Press, NY.

Table 3. Development Assistance to Poor Countries and from the Wealthy Countries

	Total Dollars[a] (millions)	Dollars per Capita[b]	Percent of GNP[c]
TO:			
Low Income Economies	9,850.9	4.46	1.7
Ethiopia	184.3	5.76	4.1
Zaire	329.9	11.00	5.2
India	1,561.7	2.26	0.87
TO:			
Middle Income Economies	12,475.9	11.06	0.73
Indonesia	900.6	6.00	1.13
Peru	184.4	10.85	0.93
Korea, Rep. of[d]	168[d]	4.31	0.25
FROM:			
Development Assistance Committee of the OECD	27,853	38.68	0.35
Japan	3,023.0	25.62	0.29
Netherlands	1,474.0	105.29	1.08
United States	8,202.0	35.66	0.27

[a]Official Development Assistance in 1982 to each of the low and middle income countries from all sources and from the industrial market economies that are members of the OECD, DAC to all recipients.

[b]Using 1981 population estimates and column 1 assistance amounts.

[c]Using 1981 GNP and column 1 assistance amounts.

[d]Average for years 1980-1982. The 1981 value was high and the 1982 value was extremely low compared to previous years.

Source: Development Co-operation, November 1983. Organization for Economic Co-operation and Development.

Table 4: Characteristics of Official Development Assistance (ODA) Provided by the United States

	Millions $	%
A. Allocation of bilateral ODA commitments by the United States, 1982		
Planning and public administration	43.7	1.5
Development of public utilities	335.8	11.7
Agriculture	853.0	29.8
Industry, mining, construction	16.8	0.6
Trade, banking, tourism, services	268.1	9.4
Education	169.3	5.9
Health	408.8	14.3
Social infrastructure and welfare	212.4	7.4
Multisector	6.9	0.2
Unspecified	549.5	19.2
Total	2,863.3	100.0
B. Tying status of ODA from the United States, 1982		
Bilateral ODA		
Untied		
Grants	1,319.5	15.5
Loans	471.9	5.5
Partially tied		
Grants	634.0	7.5
Loans	176.1	2.1
Tied		
Grants	1,574.5	18.5
Loans	982.0	11.5
Multilateral ODA		
Untied	3,226.0	38.0
Tied	119.0	1.4
Total	8,503.0	100.0

Source: Development Co-operation, November 1983. Organization for Economic Cooperation and Development, pp. 196, 203.

Table 5: Geographic Distribution of Development Assistance from the United States and Other Sources[a]

	United States	Total Development Assistance Committee	United Nations Development Programme	Total Multilateral
		(percentage)[b]		
Multilateral ODA	34.0	31.3	N/A	N/A
Egypt	14.1	4.6	1.5	2.8
Israel	12.8	3.3	N/R	N/R
India	3.7	4.3	4.1	18.6
Turkey	3.2	2.7	N/R	N/R
Bangladesh	2.4	3.7	3.5	5.0
Indonesia	2.3	3.7	2.4	1.9
Pacific Islands (U.S.)	1.9	N/R	N/R	N/R
Pakistan	1.5	1.8	2.0	5.5
El Salvador	1.2	N/R	N/R	N/R
Peru	1.0	N/R	N/R	N/R
Portugal	1.0	N/R	N/R	N/R
Sudan	1.0	N/R	N/R	N/R
Somalia	1.0	N/R	N/R	N/R
Kenya	1.0	1.3	1.2	1.5
Tanzania	N/R	2.2	2.0	2.1
Reunion	N/R	2.2	N/R	N/R
Martinique	N/R	1.9	N/R	N/R
Thailand	N/R	1.2	1.4	1.3
Korea, Rep.	N/R	1.2	N/R	N/R
Zaire	N/R	1.2	1.8	1.5
Sri Lanka	0.8	1.2	1.3	1.2
Papua New Guinea	N/R	1.1	1.2	1.0
Philippines	0.9	1.1	1.2	1.0
China	N/R	N/R	2.3	3.4
Kampuchea	N/R	N/R	2.2	2.5
Ethiopia	N/R	N/R	2.9	1.9
Senegal	0.6	0.8	N/R	1.4
Nigeria	N/R	N/R	2.3	N/R
Yemen	N/R	N/R	1.8	N/R
Brazil	N/R	0.7	1.8	N/R
Nepal	N/R	N/R	1.7	1.1
Burma	N/R	0.9	1.6	1.1
Percent of above countries in total ODA from this source	84.4	70.0	39.0	53.8
Percent of ODA from this source going to other countries	15.6	30.0	61.0	46.2
		(millions of dollars)		
Total ODA	6,242.9	26,441.1	594.6	6,958.7

Table 5: (continued)

[a]Annual Average, 1980-1981.
[b]Percent of total allocated ODA.
N/A: Not applicable
N/R: Not reported. Countries reported as ODA recipients in one column may not meet the reporting requirements for inclusion in one or more of the remaining columns. Hence, the designation N/R. For example, Martinique receives 1.9% of the ODA from the DAC, but is not a reported recipient for any of the other three donor classifications. For the United States, the countries indicated N/R are not listed among the top 24 recipients. Each country designated N/R in the U.S. column receives less than 0.6% of total U.S. aid. For the total DAC, countries designated N/R are not among the top 30 countries and each country receives less than 0.6% of DAC aid. For the UNDP, countries designated N/R are not listed among the top 32 countries and receive less than 1.1% of total aid. For total multilateral aid, countries designated N/R are not among the top 31 countries and each country receives less than 0.8% of total assistance from this source.

Source: Development Co-operation, November 1983. Organization of the Development Assistance Committee, p. 210, 211.

Table 6: The Net Flows of Financial Resources
from United States to Developing Countries, 1982

	Net Disbursements	
	Billions $	%
1. Official Development Assistance	8,202	27.2
Bilateral	4,861	16.1
Grants	3,791	12.6
Loans	1,070	3.5
Multilateral	3,341	11.1
Grants	854	2.8
Loans	2,487	8.2
2. Other Bilateral Official Flows	1,578	5.2
3. Private Flows at Market Terms	19,099	63.3
Direct Investment	5,451	18.1
Bilateral Portfolio	12,133	40.2
Multilateral Portfolio	1,210	4.0
Export Credits	305	1.0
4. Grants by Voluntary Agencies	1,280	4.2
Total	30,159	100

Source: Development Co-operation, November 1983. Organization for Economic Co-operation and Development.