

PROPOSAL FOR A NEW UNITED STATES FOREIGN ECONOMIC POLICY

by

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Chapter I

THE PURPOSES OF THE PROGRAM

The Thesis

It is the thesis of this book that a much expanded long-term program of American participation in the economic development of the underdeveloped areas can and should be one of the most important means for furthering the purposes of American foreign policy. We believe that such a program is one of the few concrete instruments available to us for achieving the twofold result of: (1) increasing the awareness elsewhere in the world that the goals, aspirations, and values of the American people are in large part the same as those of peoples in other countries; and (2) developing viable, energetic, and confident democratic societies through the Free World. We believe, therefore, that such a program could be a principal and effective instrument in our efforts to produce political, social, and psychological results in the national interest.

The program we propose would require U. S. government expenditure somewhat larger than current spending for economic aid. But the amount of additional money needed would be small compared to what we shall have to spend in emergency efforts either to salvage situations which have been permitted to degenerate, such as South Korea and Indo-China, or to put out additional brushfires if they got started. The total costs of such a program would be insignificant compared to the costs of waging limited wars.

The Foreign Policy Context

We are acutely aware that, insofar as the U. S. national interest is taken as a point of departure, there are fundamental differences of American opinion as to what constitute the principal dangers and opportunities confronting us in our relations with the rest of the world. It is important, therefore, before developing in detail the case for a new economic assistance program for the United States, to outline the foreign policy context into which the program we propose is designed to fit.

There are two priority tasks for U. S. foreign policy.* The first of these is to meet effectively the threat to our security posed by the danger of overt military aggression, a threat now inherent in the present capabilities and possible future intentions of the Communist bloc countries. This threat is to be met primarily by maintaining or increasing U. S. military strength and by solidifying alliances with other countries in a position to contribute significantly to that strength. One of the instruments to be used in this effort is economic assistance to countries with important industrial potential, mainly the NATO powers, designed to make that potential militarily more effective. This military aid is part of our current policy and will not be discussed further in this book.

The second priority task of U. S. foreign policy is to promote the evolution of a world in which threats to our security and, more broadly, to our way of life are less likely to arise. Success in this

*These general tasks of American foreign policy are considered at greater length in Chapter XIII and related to our proposals.

task would mean the freeing of a large amount of resources from military to more constructive uses. More important, it would mean freeing our society from the pressures inevitably associated with a garrison state, pressures which threaten our most cherished values. It is this task with which this book is mainly concerned.

What does success in this second task require?

Here there arise among thoughtful men the most serious differences on foreign policy. Some would emphasize the importance of organizational arrangements for collective security--a better structure for the United Nations; a system of bilateral, multi-lateral, or world-wide international agreements; institutions to reduce the importance of national sovereignty like European Union, World Federalism, and the like. Some would emphasize ideological considerations--the necessity to counter and expose systems of thought like communism which have a built-in commitment to violence as an instrument of change; the importance of restating systematically and promulgating widely the values of western democratic liberalism in a form which would be irresistibly persuasive to peoples everywhere. Some would emphasize the importance of creating social, economic, and political conditions in which violence and protest would lose their appeal because more attractive methods were available for satisfying personal and collective aspirations. Obviously all these approaches and others besides are needed.

Underlying the proposals in this book is the conviction that we have put relatively too much emphasis in recent years on pacts, treaties, negotiation, and international diplomacy and too little

on measures to promote the evolution of stable, effective, and democratic societies abroad which can be relied upon not to generate conflict because their own national interests parallel ours and because they are politically healthier and wiser. This conviction, in turn, is based upon an estimate of the nature of the forces at work in the world making for change.

The Great Transition

It has become a commonplace that we are in the midst of a great world revolution. For centuries the bulk of the world's population has been politically inert. Outside America and Western Europe, and even in parts of the latter, the pattern of society remained until recently essentially feudal, the possibility of change for most people seemed remote, and political activity was confined to an extremely small elite. Within the past forty years two world wars and a phenomenal increase in the ease and effectiveness of communication have fundamentally altered the perspectives of hundreds of millions of people. Countries with populations aggregating over half a billion have just won their independence and are trying to cope with their new status. The rapidly accelerating spread of literacy, mass communications, and travel, which has only begun, will produce even more unsettling results over the coming years.

This revolution is rapidly exposing previously apathetic peoples to the possibility of change. It is creating in them new aspirations for education, social improvement, and economic develop-

ment. At the same time, it is tearing down old institutions and culture patterns which in the past held societies together. In short, the world community is rapidly becoming interdependent and more fluid than it has been at any point in its history, a condition which presents us both with a great danger and a great opportunity.

The danger is that increasing numbers of people will become convinced that their new aspirations can be realized only through violent change and the renunciation of democratic institutions. That danger has no single cause. It is inherent in the revolutionary process. But it is greatly increased by the existence of communism--not because of any authentic attractions in its ideology but because the Communists have recognized their opportunities to exploit the revolution of rising expectations by portraying communism as the road to social opportunity or economic improvement or individual dignity and achievement or national self-respect, whichever fitted a given situation.

Thus, the dangers of instability inherent in the awakening of formerly static peoples would be present even in the absence of the Communist apparatus, as is demonstrated by the existence of trouble spots like Kenya and Morocco--apparently relatively unconnected with Communist subversion. But the danger is, of course, greatly intensified by the focus which both Communist thought and Communist organization give.

We have not presented a consistent and persuasive alternative in terms of the democratic process. It is the unpleasant truth that the United States has come to be regarded increasingly in the

uncommitted areas of the world as a theater of self-destructive and at worst aggressive, preoccupied with military preparations and with a game of international power diplomacy which has no meaning for the newly awakened ordinary citizen. We are no longer identified, as we once were, with the aspirations of people for social and economic improvement or with their Utopian image of a society designed to satisfy those aspirations.

The American Opportunity

Our great opportunity lies in the fact that we have developed more successfully than any other nation the social, political, and economic techniques for realizing widespread popular desires for change without either compulsion or social disorganization. Although our techniques must be adapted to local conditions abroad if they are to be effective there, they represent an enormous potential for steering the world's newly aroused human energies in constructive rather than destructive directions.

Moreover, deep in American society, hankering for effective expression, capable of mobilization, is a dedication to the fundamental principles of national independence and human liberty under law. In their largest sense our proposals are designed to give fresh meaning and vitality to the historic American sense of mission to see these principles extended on the world scene.

While it is obvious that the political, social, and economic development of foreign areas is a task for the peoples of these areas themselves, and that we alone cannot insure that they will do it:

well or badly, two considerations suggest that it would be inexcusable for the United States and the other people and nations of the Free World not to exert to the utmost whatever influence they have. In the first place, we have a compelling national interest in promoting a world environment in which we ourselves can live freely, secure both from the menace of hostile states and the distraction of chaotic ones. In the second place, American society is at its best when we are wrestling with the positive problems of building a better world. Our own continent provided such a challenge throughout the nineteenth century. As our emergence into national maturity lifts our horizons beyond our own shores, we need the challenge of world development to keep us from the stagnation of smug prosperity.

The economic development program outlined in the balance of this book is conceived as one of the instruments for carrying on the task just described. It stands or falls on the acceptance of this task as a top priority objective of U. S. foreign policy. It cannot be too strongly emphasized that it is only one of many instruments which must be used in a coordinated way if we are to maximize our influence to promote the development of stable, effective, and democratic societies elsewhere in the world. There are important roles for information policy, for military assistance policy, and for the conventional diplomacy also which these instruments are not now playing. Economic policy by itself will not achieve the desired result. Nor will it have the desired effect unless it is consciously designed with this end in view. If a new development

assistance policy is adopted with a different rationale and different purposes, it may well even backfire and have effects detrimental rather than favorable to our interest.

Chapter 17

SOME WRONG APPROACHES

Since a program adopted for the wrong reasons may well be worse than useless, it is important to examine some current misconceptions as to the purposes of assistance programs. The confusion of the debate over assistance policy results partly from the wide variety of expectations current as to what kinds of results economic assistance programs are likely to produce. Are they mainly to win friends for the United States? To strengthen the military capabilities of our allies? To induce other countries to follow foreign policies to our liking? To reduce the appeal of communism to the poverty stricken? To benefit the United States economically? To induce healthy internal political development abroad? To raise living standards for humanitarian reasons?

Since many of the challenging criticisms of foreign assistance programs arise from misconceptions of the political and psychological effects that such programs can be expected to have, it is well to take a look at some of these misconceptions before proceeding to develop the positive case.

We would note four widely prevalent errors.

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Should Aid Bring Us Friends?

The simplest misconception is that assistance extended by us will insure friendship and gratitude and that these in turn will insure behavior in our interest. Anyone who has had experience of the psychology of the grantor-grantee relationship will not consciously fall into this error. The relationship is a complex and frequently corrosive one. The grantee's sense of dependence often produces feelings of resentment toward the grantor which may worsen rather than improve relations between the two. We must expect that an incidental result of assistance may frequently be the appearance of less rather than more spirit of cooperation and mutual respect even, and perhaps especially, if the assistance is successful in achieving its real objectives. Although this fact is accepted intellectually by most perceptive observers, even those who are clearest about it are often emotionally hurt by evidences of what look like gross ingratitude. Such an emotional reaction produces a state of mind in which serious mistakes may be made in the design of economic programs; for the measures which can be taken to lessen the hostile reactions to economic assistance are often the precise opposite of those likely to be taken by an official smarting from hurt or spurred by a Congress so "hurt."

Surely, our central objective is not to get people to say they like us and will join with us. Winning fair weather friends is not a fundamental objective of U. S. policy. It is therefore essential to conduct aid programs so as to prevent, as far as possible, reactions

which might lead to a rejection of the aid program by the recipient themselves which have the quite different consequences for the aid program in this case. Our public role as the donor's obligation must be maximized. Exaggerated credit must be given the recipient for his own contributions. Demands for demonstration of alliances and agreement must be reduced rather than increased.

In a deeper sense it is, of course, altogether likely that a program of this kind, demanding that many countries work side by side with others in a common enterprise of mutual interest, will develop friendship and a sense of national comradeship. This was an important long term by-product of the Marshall Plan and, incidentally, even of this important kind, is not the primary justification for the effort required of the United States in the program outlined here.

Should Aid Strengthen Foreign Military Capabilities?

A second misconception is that the central purpose of economic aid programs is always to enable the recipient countries to carry a much larger share of the burden of military build-up against Communist armed forces. We believe there is an excellent case for military assistance to allies who, as in Western Europe, have real industrial potential, but that this case has been extended much too indiscriminately to the less developed areas.

In the first place, the resources of most of the underdeveloped areas are so limited that even with massive aid the contribution they can make to defense against Communist forces is very small.

nations inevitably would be very small. We must face squarely up to the fact that resistance to determined military aggression by the Soviet bloc powers is a job for the United States with help from the NATO powers of Western Europe, and that any hope that we can create and maintain such a defense cheaply by organizing the manpower masses of Asia is largely illusory.

In the second place, while the underdeveloped countries can help to resist minor aggression and should be able to maintain order internally, weapons and military potential are ineffective without the will to use them. Some countries appear to have this will, others clearly do not. Our efforts to force military assistance on countries which do not want it may actually weaken such will as exists. Such efforts convince them that we are trying to involve them for our own purposes in disputes which they could otherwise stay out of, and they compound the widespread conviction in Asia that U.S. objectives are mainly military and aggressive.

There is a further consideration which suggests that, even in those underdeveloped countries whose governments are willing or eager to expand their military establishments beyond the requirements of internal order, we should proceed only with caution to meet their wishes. A crucial, perhaps decisive, difference between the Communist formula for economic growth and the Free World formula is that the Free World formula offers to all the citizens of a country the hope that their emerging aspirations for economic, social, and political betterment

can be at least partly satisfied as the process of development proceeds. The Communists promise this but are unable to make good on their promise precisely because their pattern of development emphasizes the heavy industrial growth important to military power at the expense of the agricultural and light industrial development essential to improved citizen welfare. It is this perversion of economic development to the creation of military power which, in turn, makes necessary many of the instruments of force and repression which characterize Communist states. The collection of grain to supply the food requirements of armies has been used in China, Indo-China, and elsewhere to justify the abandonment of freedoms and the corrosion of the political process at the village level.

Pressing for a disproportionately large military investment by a poor country runs the risk of either preventing the economy from growing or persuading the country's leaders to adopt totalitarian measures to force growth in the face of lack of popular enthusiasm.

Should Aid Guarantee Reliance on Private Enterprise

The expectation that American aid programs can and should be used to halt or reverse the trend toward "socialism" present in many underdeveloped areas may find expression in either of two kinds of policy attitudes.

Some argue that we should use offers of assistance to force countries to abandon proposed government enterprises and to establish conditions favorable to the maximum degree of domestic and foreign private investment. These persons believe that the attractions of economic assistance are great enough to induce countries to abandon their already adopted avowedly socialist goals and reorient their whole philosophy of the relation between the state and the economy to that which prevailed in nineteenth century America. The second group believe that, although any country should be permitted to adopt any philosophy it likes, no U. S. resources should be devoted to assisting governments which have socialist objectives. If they go all out for a free private enterprise system, we will provide capital to support their economic growth; but if they adopt a different view, as India and Burma have done, for example, we shall not interfere-- but we shall let them go their way without our help.

The authors believe that either of these attitudes is likely to frustrate what we conceive to be the basic purposes of economic assistance. We agree with those who hold that a private market system with opportunity and incentive for individual enterprise will in the long run promote self-sustaining growth better than a highly bureaucratized system dominated by central government. But we believe that we shall ultimately promote reliance on private incentives more effectively by not insisting on any particular economic philosophy as a condition of aid than by attaching private enterprise strings. In many situations a

favorable environment for private investment can be established only after a period of rather heavy capital formation under government auspices. This is what happened in Japan in the decade after 1868. More recently, the whole set of measures instituted by the Indian Government in the period starting in 1951 and by 1956, created an environment in which the Indian private sector is undergoing rapid growth.

Thus we believe on the one hand that crude attempts to force a free private enterprise philosophy on recipient countries as an explicit or implicit condition for aid are almost certain to be self-defeating; on the other hand we believe there are good reasons for expecting countries now avowedly socialist but determinedly democratic to move toward greater reliance on private incentives as their development proceeds. Taking this attitude, our national policy should reflect a well-grounded confidence that, in the light of the experiences of the postwar decade, socialists all over the world have abandoned or are in the process of abandoning their old doctrinaire faith in nationalization as a cure-all.

Part of the reason for this paradox lies in the meanings attached to key words. Among intellectuals in many Asian countries, the term "socialism" has become synonymous with values to which we also are dedicated: equality of opportunity, the public welfare as the test of economic performance, equitable distribution of income, protection of the individual against risks over which he has no control,

acceptance by each citizen of his social responsibilities, and so on. On the other hand, in these same countries, the term "capitalism" has assumed a meaning largely derived from Marxist literature. To many Asians, capitalism implies exploitation of the less fortunate, pursuit of selfish private gain with no regard for public welfare, huge concentration of economic power in a few irresponsible hands, and wasteful dog-eat-dog competition ruthlessly destroying the weak or idealistic. Such stereotypes blind both Americans and Asians to the fact that there is a large body of values both groups share. Such stereotypes often misrepresent the actual organization of economic activity. In the avowedly "capitalist" United States the government directly determines some 20 per cent of the output of the economy, while in avowedly "socialist" India government determines only about 8 per cent.

But whatever the actual character of the economies, the stereotypes exist; and they are deeply rooted. Technical assistance programs which provide opportunities for us to demonstrate how we in fact approach concrete economic problems can over time have a very helpful influence in correcting these false images of what our economic system is like. They can also correct false images in the United States of what Asian and Anglo-Scandinavian "socialism" stands for. To connect our assistance with a frontal attack on socialist ideology will result in all probability in a refusal of aid and a vigorous reassertion of socialist principles.

... from some ... of the degree to which substantial state promotion is essential for a rapid transition from stagnation to economic growth. Many of the kinds of investment required are inherently of a public character. Roads, harbors, communication and transportation facilities, sanitation, and community services of all kinds often must be developed ahead of the market demand for them. Even in the United States it was federal, state, and local government units rather than private enterprise which provided these overheads in the nineteenth century. Moreover, many types of investment which in advanced economies can be expected to be undertaken privately under market incentives may have to be launched initially by public bodies in the underdeveloped economies. The risks of many kinds of industrial investment in a preindustrial economy are not of a sort private capital can be expected to bear. In economies where no substantial body of entrepreneurs has yet been developed, adequate managerial and administrative talent may be very scarce in the private sector but relatively abundant in a civil service which has traditionally recruited the best talent in the society. Where the institutions for mobilizing private capital are rudimentary or non-existent, only government may be able to muster the resources for major investment. For these and other reasons, then, there are situations in which development must already be firmly under way before it is reasonable to expect private investment to take primary initiative for pushing it forward. In such situations, insisting that investment must be wholly or largely privately administered from the start may prevent the preconditions for private investment from being established.

These conclusions are all based on the authors' conviction to the belief that in any society any extension of government activity beyond minimal caretaker functions carries with it the gravest threats to political liberty and individual freedom. The present authors do not share that belief. We believe that the crucial prerequisites for a free society are a dedication to voluntary rather than compulsory methods, a widespread dispersion throughout the citizenry of power over crucial decisions, the presence of genuine freedom of debate and dissent, and a legal framework which insures against the arbitrary use of the instruments of force. In addition, we believe that sustained economic growth in a democratic society probably requires a pattern of incentives which encourages maximum participation in economic decision-making from all the alert and imaginative elements in the society. A largely private business system such as ours in the United States is one way of achieving this participation. Other ways may be more adapted to the preconceptions and culture patterns of other societies, at least in the early stages. The hope that we can, through aid programs, force upon these other societies the precise type of economic institution we prefer is bound to lead to disappointment and frustration.

The other side of the coin is the reasonable hope that, as societies achieve some success in spreading the benefits of economic growth among their peoples, as education becomes universal, as markets expand, as a managerial class is established, as the prerequisite social overhead of transport, communication, power, and community facilities are

established, as early as the beginning of the century private ventures, there will be increasing scope for private economic activity whatever the name attached to the economic philosophy. This is particularly likely if the choice between public and private enterprise is, in practice as against theory, made on pragmatic grounds. "Socialist" Britain and "capitalist" United States have much more nearly identical economic systems than the doctrinaire economic philosophers of either would have one believe. The increasing opportunity for the private sector will not occur if, as in Russia, there is a commitment to centralization of power for purposes of political control, brought about almost irreversibly by revolutionary means.

Therefore, although one must not fall into the error of employing our aid program to dictate another nation's economic philosophy, we can appropriately insist that we will aid only countries dedicated to advancing standards of living and encouraging widespread local initiative. With this condition, we need not be too concerned in the long run if some large-scale ventures are started under government auspices or if there is a preference for describing economic goals in socialist language.

Should Aid Stop Communism by Eliminating Hunger?

A final and serious misconception which exposes proposals for economic programs to effective attack is that revolt and protest are the result of hunger and poverty; that relieving hunger and reducing poverty will reduce revolutionary pressures; and that, therefore, if we

can supply the wherewithal to feed people better, they are much less likely to support Communist or other extremist movements. Such reasoning is derived mainly from ignorance of the forces affecting social and political change.

In the first place, the spirit of revolt does not breed easily among people who are chronically destitute. In the rigid feudal societies which still characterize some parts of the world the poor have for generations accepted a fatalistic view that it is in the nature of things that they should be poor; and people do not revolt when they believe change to be inherently impossible. At the grass roots of a feudal society one of the first effects of an economic development program is a dawning awareness that change can occur; and it is not poverty but this awareness combined with the energy-stimulating effects of better nutrition that is likely to release psychological and political pressures for change which may find expression in revolt. All this is well understood by the Communists, who concentrate their efforts not among those who are hopeless but among those in whom expectations have already been aroused. The Communist line is that these newly aroused expectations can never be satisfied except under revolutionary Communist leadership. This line is carefully tailored to whatever expectations and aspirations turn out to be most powerful in the particular people they are trying to influence. Moreover, once expectations have been aroused, a failure to do anything effective about them is grist to the Communist mill.

In the second place, even if the creation of wealth alone could satisfy a peoples expectations, there is a limit to the rapidity with which economic development can increase national wealth and well-being. Under the most favorable conditions the maximum rate of growth of physical output likely to be achievable by countries in the early stages of development is 3 to 5 per cent per year. Where populations are increasing by 1 1/2 to 2 per cent per year this means that the maximum rate of improvement of individual welfare is 2 or 3 per cent per year. But if growth is to become self-sustaining, some fraction of this increase must be plowed back into further investment. Therefore, the maximum rate of increase in consumption per person averaged over the population as a whole is not likely to exceed 1 or 2 per cent per year. It is true that even at a growth rate of only 1 per cent per year the standard of living will double in two generations and we should not ignore the importance one generation may attribute to prospects for improvement in the lot of its children, especially in peasant societies. And 1 per cent compounded over fifty years performs miracles, especially since, as the process goes on, the percentage will probably grow. But in the modern world of rapid communication political and social processes are greatly accelerated and will not give us fifty or even twenty years. The newly awakened peoples demand increasingly visible evidence of rapid progress.

Finally, most important, and wholly ignored by those who accept the crude materialist thesis that progress consists exclusively in "the extra food in the stomach," is the fact that an increase in consumption unaccompanied by many subtler changes in the society will not by itself guarantee orderly political development. This truth helps to explain the phenomenon which has been so puzzling to observers in a number of countries where Communist gains appear in some instances to have been greatest in areas where the government has been doing something about the economic problem rather than in those where nothing has been done.

Economic development efforts create potential unrest by dislodging convictions and habit patterns which have in the past insured stability. The education which accompanies economic change contributes to unrest. People who can't read can't be subverted by literature. Once they can read, the process of widening knowledge and changing ideas of what the world is like and what is possible in it proceeds with great rapidity. With a growing understanding of the great inequalities in the possession of wealth in backward societies comes a growing awareness that these inequalities are not the inevitable result of fate. In addition to this awareness there are other significant social and cultural effects of the very process of industrialization and urbanization. People brought up in the economic and psychological security of a traditional extended family system or a communal village structure are uprooted, moved to unfamiliar surroundings, plunged into a competitive world of individual

effort with no paternalistic small group units to fall back on, and find their core values and beliefs subjected to daily challenge. They have a desperate need for new common goals and an experience of common effort and loyalties with some group which can give promise of reestablishing their confidence and their sense of private and social harmony. If these are not provided by the existing social and political structure, they will seek them in a dream of a wholly new structure provided, for example, by a locally adapted Communist line. It is certain that increase in material welfare alone will not satisfy spiritual and emotional needs.

It should be plain to us that if all that we have to offer to offset the disturbing effects of the breakdown of traditional cultures and the development of widely expanded expectations is the actual physical increment of new product created in two or three years by development, the picture is bleak indeed. Such a crude materialist conception of the way economic programs are supposed to work, is not only wrong for the reasons given. It can be very dangerous. The conviction is already widespread in Asia that we value only physical consumption and have no understanding of things of the mind and spirit. If we promote economic programs with this false conception in mind, we shall not only be disappointed in their results but also create additional hostility and contempt in the people we are trying to influence; and we may drive them to seek solutions more congenial to them than ours.

Chapter III

THE DEVELOPMENT OF MATURE DEMOCRACIES

In the face of the obvious possibility that whatever the economic effect of economic programs (and we have yet to examine whether even an economic effect can be expected) the political and psychological effects can be contrary to our interests, would it not be better to leave the peoples of the underdeveloped areas of the world in a state of placid stagnation rather than arouse expectations that neither we nor they can possibly satisfy and thus expose their societies to the risk of social and political disintegration?

The question implies an option that is not in fact open to us. The process of change is already inevitably and irreversibly under way, the expectations are already aroused, and the economic, political, and social revolution of the underdeveloped areas is already inexorably on the march. The unprecedented spread of communication throughout the world in the last twenty years has already fundamentally altered the images of the future of the bulk of the world's population. Even if the Communists were not everywhere promoting and encouraging the process for their own ends, this alteration would be accelerated in the coming decades. The alternative of supporting semi-feudal stability is a mirage.

Moreover, and much more to the point, there exists a powerful, positive case for an active promotion of economic development. The

substance of this case can be found in the political, social, and psychological effects that a well-conceived economic development program can be made to have.

We postulated earlier that one of the highest priority tasks for U. S. foreign policy is to use our influence to promote the evolution of societies that are stable in the sense that they are capable of rapid change without violence, effective in the sense that they can make progress in meeting the aspirations of all their citizens, and democratic in the sense that ultimate power is widely shared through the society. Such societies are not likely to constitute a military threat to us or to attach themselves to others who pose such a threat. Under modern circumstances some increase in the per capita availability of material goods, while not enough by itself, is certainly a necessary condition for the development of stable and peaceful societies and for the viability of democratic institutions. Even more important are the confidence generated by a sense of progress, the social mobility, the outlet for leadership energies, the national cohesion, the consolidation of new individual and group values, the discovery of new sources of satisfaction and achievement which a concentration of social and economic development can bring.

By actively promoting economic development in well-conceived programs of common action with the peoples of the new nations we can undertake to help them reach their goals. We can demonstrate more effectively than by any verbal propaganda the wide range of values we share with them. And in so doing we can use our margin

of influence to move toward the realization of our own national interest in a world made up of free democratic societies.

The question, then, is not whether we should actively promote economic development programs but how such programs can serve these lofty ends.

Before we can determine the role that economic programs can play, we must first be clear as to some of the principal requirements that must be met if the underdeveloped countries are to achieve political maturity.

a. There must be posed for the leadership and the people of each country challenging and constructive internal tasks which will capture the imaginations and harness the energies of persons throughout the society. The peoples of the countries of Asia, the Middle East, and Africa have until recently been dominated either de jure or de facto by the will of foreign powers of different races from their own. To the extent that their peoples have achieved a degree of common purpose it has been in opposition to this external influence. Wherever they have achieved their independence from colonial control, this symbol of their common purpose has lost some of its energizing force. Many of them are trying to retain their sense of dedication and direction either by retrospectively fighting over again in their minds and in their political speeches the glorious revolutions they have already accomplished, or by identifying themselves with the revolutionary aspirations of countries still not independent. A prime requirement for their political development is that they now turn their constructive energies on a broad scale to the real problems

of their own internal future. Only when these problems of internal change have become the earnest concern of a large part of the population, and individuals throughout these societies see ways in which they can make useful contributions to the solution of these problems, will irresponsible extremist movements whose focus is on the battle symbols of the past lose their attraction and the institutions and forms of democracy become meaningful.

b. The constructive issues around which unity and cohesion are to be forged must relate to the emerging aspirations of all classes and regions in the society. The fight against international communism is neither sufficiently meaningful nor sufficiently related to the current hopes of most of the peoples of the underdeveloped areas to be an effective standard around which to mobilize political activity. First, it is a fight against and not a fight for something. Second, communism is not seen as a menace in many of these areas because their peoples have had no personal contact with what it can mean; and those who are aware of the struggle between the Communist bloc and the Free World regard it as something that matters to us but not to them. Third, since the Communists have very skillfully soft-pedalled the ideological elements in their position and have identified themselves with local causes, to attack communism in principle sometimes gives us the appearance of attacking the whole idea of trying to solve local problems. The best counter to Communist appeals is a demonstration that these same problems can be solved by other means than those the Communists propose. Unless there is a rapid spread of the conviction that purposive action

within a democratic social order can make progress in attaining newly formulated goals, movements to alter the order by violence will become increasingly successful.

c. These countries must find ways of developing new, young, and vigorous leadership. Many of their leaders are either men who have spent their lives organizing opposition or men selected by occupying colonial powers because they had a stake in the maintenance of the status quo or because they could be trusted to administer without having too many ideas of their own. There are remarkable exceptions like Mr. Nehru who have been able to convey to their peoples an image of what their country might be like if they mobilize their human and material resources. But an expansion of the pool from which leadership can be drawn is everywhere a crying need. The development of the right kind of young leadership will require stressing problems which are challenges and opportunities rather than threats and which therefore appeal to constructive rather than conservative motives. There are reserves of leadership potential throughout the populations of the underdeveloped areas, but they must find a focus for their energies in problems they regard as real rather than symbolic.

d. Related to the recruitment of new leadership is the need for greatly increased social, economic, and political mobility. One reason for the widespread impression that leadership material is scarce in these countries is that the base from which such leadership could traditionally be drawn has been pathetically narrow. One of the things the Communist movement does is to provide outlets for the awakening

energies of young men previously denied opportunity by the rigid feudal class structure of their societies. Young leadership is in fact appearing. If it is not provided a role in constructive programs, it will lead destructive ones. In particular, recruitment of non-Communist leadership has too frequently been confined to the urban centers where a small fraction of the population is concentrated. There are human resources which have been largely untapped in the rural areas where 70 to 90 per cent of the people in the underdeveloped countries live. Outsiders cannot force the recruitment of such leadership, but programs of rural development can uncover much leadership potential.

e. Related to this fact is the requirement, if these countries are to achieve mature political development, of finding ways to bridge the existing gulf between the urban classes, often Western educated, and the countryside. In many instances the educated classes often know less--and, more important, care less--about their own countrymen in the rural districts than do we or other foreigners, a situation which has a doubly unfortunate influence. Where urban leaders do little about some of the country's most urgent problems, the mass of the people lack the conviction that their leaders are centrally concerned with their problems and aspirations. Those countries like India which are making the most progress toward maturity are those in which this gulf is being bridged--more through economic programs which yield a sense of common purpose derived from common effort than by any other means.

In this connection it is worth noting the special role played

by the military in many of the underdeveloped countries. The army is frequently important to economic and political growth for three reasons. First, a military career is often the only channel to positions of leadership and responsibility open to members of the less privileged classes and especially to men with rural backgrounds. It is thus often a good place from which to recruit new elements of leadership for nonmilitary programs. Second, the army is often the only career in which a man has an opportunity to acquire both technical and administrative skills. Many of these skills are easily transferable to such civilian tasks as the building of roads and communication systems or the organization of a local community for improved sanitation. Third, military service provides vocational training which transforms rural into urban men suitable for industrial work. Countries could well pay more attention to these effects of conscription.

When we speak of recruiting new leadership, we do not mean solely or even primarily leadership at the national political level. Local, regional, and functional leadership are at least as crucial to orderly development. Indeed, when we talk of the development of democratic societies we tend to think too largely in terms of the mechanical process by which national leadership is chosen. Power and decision making cannot be decentralized, whatever the electoral process, unless there are competent and dedicated people available at lower levels to whom decisions can be delegated. A country which is formally a dictatorship but whose government encourages local and group initiatives and is responsive to them may be more democratic

than one which goes through the motions of national elections but has no political vigor at the grass roots. Since the problems of maintaining national cohesion in the face of rapid social and economic change are so unsettling, the newly independent countries may have to pass through a variety of transitional political forms in their search for a democratic framework appropriate to their own situation. The crucial test is whether local leadership and local participation in decisions of local interest are being nurtured.

f. Perhaps the most critical requirement for the growth of political maturity is that the people of these countries develop a degree of confidence both as a nation and as individuals and small communities that they can make progress with their problems through their own efforts. The principal reason for believing that some growth in economic output, even at a slow rate, is critically important to political stability is that such growth has become an increasingly important symbol to them of their capabilities, their national worth, and their national dignity. If this growth is widespread through the country and based upon a good measure of local community initiative, it can become a vital symbol of individual and community as well as national achievement. The Communists are saying through the countryside, "Your leaders are bankrupt. You can do nothing under the present system to work toward the satisfaction of your hopes. Join us and we will give you a meaningful mission." There must be an alternative to this appeal if democratic evolution is to succeed.

It should be emphasized also that a sense of confidence is the

chief prerequisite for the development of satisfactory external relations with the rest of the world. At the moment many of these countries are fearful that other nations have objectives and values different from their own which threaten their national integrity and security. Once they see that they are wholly capable of standing on their own feet, they can afford to be less quixotic and nervous in their foreign policies. It is generally true that a nation's foreign policy is an index of the state of its domestic society.

Chapter IV

WHAT AN ECONOMIC PROGRAM COULD DO

It should be apparent that whether economic programs have desirable political and psychological effects in terms of the principal requirements for the growth of political maturity will depend on how they are carried through. We have had experience with aid programs which justify all the scornful strictures of their opponents, and which have been not merely neutral in their effect and hence wasteful but positively harmful to our interests. We have learned that benefits do not follow any more automatically from the voting of sums of money by the Congress in this field of policy than in any other. But past mistakes do not alter the basic fact that economic programs are one of the few levers of influence available to us which have a serious chance of influencing in important ways political developments in the underdeveloped areas.

Why is this so? The answer lies in the social and political connotations of the economic growth process.

A Constructive Outlet for Nationalism

The possibility of economic growth presents a real challenge to the constructive energies of the people of the newly independent countries. Some countries, like India, have already demonstrated that this challenge can have much greater appeal as a rallying point for national effort than the preservation of their societies from what

we believe to be an external threat. Indeed, in India the problems of internal development have already started to replace such issues as colonialism, race discrimination, and relations with foreign countries as the burning issues of national and local politics. The present government has tied its fortunes to the success of its five-year plans and has generated a quite remarkable degree of interest in these even down to the remote villages. Performance under the five-year plans has become important not merely as an index of the effectiveness of the present government but as a major symbol of Indian national aspirations, independence, and dignity. A realization of forward movement in this effort, even if the visible economic results are not spectacular, has become a prime factor in the national consciousness. There is an even more widespread awareness among Indians of India's competition for success in growth with Communist China. It is not accidental that India's internal political situation, while still full of disturbing elements, is in better shape than that of most other Asian countries. India's effective absorption in a constructive economic effort is not the whole story, but it is such an important part of the story that a reversal of the trend of progress which has been started could lead to a rapid deterioration in the political scene. It is plain that if we support efforts like the Indian one and encourage the development of such efforts in other countries we can influence the over-all political scene.

A Social Solvent

More specifically, development assistance can be made conditional upon the submission of convincing evidence that a country's leaders have thought through the needs of all sectors of their population. There is a tendency for the urban-educated elite to think first in terms of factories and other urban-centered activities. Requirements of economic balance can literally force them to get into the countryside where the bulk of their people live and find out about rural conditions and prospects. Indian intellectuals are learning, slowly but surely, to work with peasants, to soil their hands, to interest themselves in the issues peculiar to their own nation rather than in the intellectual fashions of the Western world. As a result, although there are still villages in India where people have never heard of Nehru, much less of community development, the number of these is shrinking with amazing rapidity. A more energetic focus on development, accompanied by an insistence on balanced programs, could have similar effects in countries where the gap between city and country is still almost unbridged and where the Communists therefore have a clear field in the rural areas.

The Development of Leadership

One of the significant aspects of programs of agricultural and village development is that they probably provide the best opportunities for uncovering and encouraging new sources of young leadership--essential to the growth of political maturity. The village worker training programs which several countries in Asia are undertaking

are recruiting from sectors of the population outside of the castes and classes to which opportunity has traditionally been limited. Even in the cities, industrial development is beginning to be accompanied in a few places by a labor movement that is shifting its focus from political agitation to increasingly responsible concern with the economic welfare of the working classes within the framework of existing institutions. This process has a long way to go, but it is moving in the right direction. The failure of efforts at economic growth could rapidly reverse this trend and drive labor and peasant organizations back to a concentration on political protest instead of constructive effort. More vigorous promotion of growth with opportunities for these groups to realize some success in their efforts to improve their welfare could greatly accelerate the emergence of responsibility in such organizations.

Confidence in the Democratic Process

Psychologically, as was pointed out above, confidence that people have it in their power to improve their own lot is one of the most essential requirements for political responsibility. Economic evidences of success are among the most persuasive ones. Seeing new factories, better farming methods, improved public health and education, and better transport actually becoming realities in response to their own efforts can supply this confidence. The more widely spread these activities and the more universal the efforts of which they are the tangible evidence, the more likely is the political effect to be salutary.

Similarly, many of the economic problems provide opportunities to demonstrate political democracy in action which are much more convincing than either abstract discussion or the operation of electoral machinery divorced from real problems. If voting is to be made an activity which is more than an interesting new gadget, there must be something to vote about which directly concerns people, and some test of candidates other than their oratorical powers or the width of their circle of acquaintances. Economic issues are, of course, not the only ones with real vitality, but in countries where a majority of the people live close to the margin of subsistence, most cultural, educational, and social issues are directly related to economic problems. Village education requires schools, equipment, and the support of teachers; public health requires medical services, better nutrition, and better housing; social justice frequently depends on land redistribution and community services; a wider communication of ideas depends on roads, communication media, and the like.

International Solidarity

International cooperation on economic issues offers opportunities to demonstrate not only the common goals shared by the peoples of one country with those of another but also helpful ways in which those goals are being pursued abroad. Such demonstrations correct false images of foreign societies. One of the most politically effective programs we have carried out to date has been the sponsoring of visits to American industry by European productivity teams. The ostensible purpose of these visits was to give the visitors new ideas about tech-

nical and organizational ways to increase productivity. Their most dramatic consequence, widely attested to, was to spread an understanding of what labor-management relations were really like in America. Visitor after visitor from both European management and labor expressed amazement at the degree of democracy and mutual human respect they found in American labor-management relations.

Ideology, values, and principles of political organization can be much more quickly grasped and promoted through programs of common action than through debate or "education." In advising and consulting on labor-management relations, on the organization of cooperatives, on agricultural extension, on educational methods, on land reform, on local government, on training and recruitment of specialists, managers, foremen, civil servants, administrators and the like, both nationally and especially locally, the United States has endless opportunities to illustrate American values as they relate to democratic action, social responsibility, free mobility of persons, and so on in the persuasive form of practical application unobscured by unfamiliar ideological terminology.

It is perhaps necessary to repeat that economic problems are not the only focus for constructive effort. But almost all the challenging things people can be stirred to want to do with themselves and their societies require some additional resources. Without economic growth neither the human energies necessary nor the physical resources required for the satisfaction of the aspirations of their peoples will be available to the poorer countries of the world. Not only is economic growth a prerequisite for political, cultural, and social improvement, it can in many ways be an engine of such improvement.

The American Objective Re-Stated

We have a unique opportunity. We alone in all the world have the abundant resources to make such growth possible.

Others can and should contribute for a variety of reasons. We should promote not an exclusively American program but a partnership program in which all the industrialized countries should be invited to participate. If we take the leadership in such a program we need not fear, and we can even welcome, Soviet participation. The Communist bloc is probably both unable and unwilling to supply by itself the volume of assistance that could fruitfully be used. As long as we fail to exert leadership and restrict our efforts to a meager scale which the Communist world can afford to match, communism will make effective political capital out of the aid "competition." But if we take the initiative boldly and on an imaginative scale we can actually encourage Soviet contributions without fear that they will dominate the program.

To put the argument of this book another way, our basic objectives are "political" in the sense that our most pressing interest is that the societies of the world develop in ways that will not menace our security--either as a result of their own internal dynamics or because they are weak enough to be used as tools by others. But our capabilities to influence political development by direct argument or intervention are very slight. Indeed, direct political intervention is almost certain to set up resentments and resistances which will produce the exact reverse of the result we seek. Economic programs which are neutral with respect to the political issues which rouse men's passions

nonetheless can be effective instruments of political influence--not because they will recruit allies but in a much more fundamental sense because they can develop political responsibility. They are thus a way--we would argue the best and perhaps the only way--around the impasse with which we are confronted when we try to use our political influence directly.

An important illustration of this principle is to be found in our policies toward colonialism. We should be more vigorously on the side of freedom and independence for subject peoples. But, apart from the difficulties of direct political intervention in the affairs of our European allies, it is not at all clear that we contribute to the peace and stability of the world by encouraging colonial peoples to rally their energies around the goal of violent revolution. There is some merit in the argument of the colonial powers that to turn loose their colonies before they have acquired the capacity to deal with their own affairs is to do the colonies as well as the world at large a disservice.

On the other hand, it would be hard for the colonial powers to deny that a vigorous and world-wide program of assistance to economic development must logically include the colonial areas. We can and should apply the same conditions to these as to other recipients of assistance, notably that responsibility for economic programs must be accepted by the people of the area themselves at both local and national levels. We can insist, through economic programs, on seeking out and developing local leadership. We can argue persuasively with the occupying powers that such programs will provide an outlet for the energies

of local communities which will reduce their preoccupation with subversion and violence against Europeans. We can with equal justice insist that our aim in supporting these programs is to speed the time at which the colonial peoples can secure that independence to which we as well as they are dedicated. We can show the peoples of the colonies that we are effectively securing independence for them by forcing, as a technically necessary condition for economic growth, the delegation to them of an increasingly important share of the decisions that affect their daily lives and welfare. Thus the formal status of political independence will become both less emotionally urgent and more attainable. To describe all the ways in which this can be done would take more space than we can devote to it here. But we are convinced that a skillful program of economic and technical assistance could both accelerate independence and take much of the dynamite out of the symbols of colonialism if it is pursued with vigor and imagination well before the dynamite has begun to explode.

The impact of such a program on the economies of the developed countries of the free world will be discussed later. Equally important, however, are the possible political and psychological effects on the other developed nations of a program of development in which they participate as partners. Our common efforts with them to date, with the notable exception of the Marshall Plan, have been largely military and have had the negative if vital objective of confining the expansion of Communist military power. Given the role of atomic weapons in modern warfare and the preponderant strength of the United States in these

weapons and the means of their delivery, our European allies have felt themselves in an awkward dependent position, largely observing the American-Soviet arms race, on which their security depended but to which they could only marginally contribute. It is important for our relations with them that, now that the Marshall Plan is largely over, we demonstrate that we have always been and are still interested in more constructive tasks and that they have a world-wide role of major responsibility to play in carrying them out. A joint effort to which we make a major contribution which has as its objective the building of successful democratic societies could have important effects in holding the alliance together and substituting the cement of hope through common effort for the binding force of fear.

Chapter V

THE STAGES OF GROWTH

The Pattern of Experience

It is argued in the preceding chapters that it is in the American interest to do what we can to support the efforts of the underdeveloped countries to develop their economies. Any detailed program to serve this interest must be based upon an understanding of the economic problems these countries face and of the possibilities and limitations of the role outsiders can play in helping them to solve these problems. No two of these countries are alike, and the problems of growth will be shaped in each by its resources, its culture, its history, and its political institutions. Nonetheless there is emerging from the intensive work of social scientists on the development problem over the past few years a recognition that there are common elements in the patterns of development of different countries which have implications for development policy everywhere. Since our proposals grow out of our conception of some of these common elements, it is important to try to summarize them.

Once societies are stirred from the lethargy of traditional economic stagnation, their transition to mature self-sustained growth can be divided into three stages.

Establishing the Preconditions

First, there is a period during which the preconditions for economic progress are established. The idea that economic progress is possible spreads. Education, for some at least, broadens and changes

to suit the needs of modern economic activity. New enterprising men come forward willing to undertake ventures and to take risks in pursuit of profit. Institutions for mobilizing capital appear. Basic capital is expanded, notably in transport, communications, and products, such as raw materials, which can be sold in export trade. The orbit of commerce, internal and external, widens. And, here and there, manufacturing enterprise appears. But all this activity proceeds on a limited basis within an economy and a society still mainly characterized by traditional low productivity techniques and by the old values and institutions which developed in conjunction with them.

During this period, which generally lasts some time, two things stand in the way of more rapid growth. The first is that these countries are desperately poor and the margin above bare subsistence is small. They must learn to channel this small margin into productive investment before they can get off dead center. This often requires important political and social change and takes time. In the meanwhile, virtually the entire output of their economies is required merely to keep their populations alive on a miserable pittance. Indeed, when bad harvests or other misfortunes occur, even this is not possible and widespread starvation is likely. In good years it may be possible to set aside a small part of output for future use, but any impetus this gives to growth is likely to be wiped out by a few bad years. Thus the precondition stage is commonly marked by a series of false starts in which some early signs of growth appear, only to wither later with a return of the economy to stagnation.

The second obstacle is that even if capital is available from outside, the capacity to absorb it in many sectors of the economy is very low. It does little good to supply money to build plants if

There are no skilled workers to operate them, no competent administrators to manage them, inadequate transport to bring in their raw materials and carry away their product, no repair facilities to maintain them, inadequate power to run them, and insufficient purchasing power to buy what they produce. To some extent skills and knowledge can be provided from outside along with financial resources, but the take-off into continuing growth cannot occur until certain minimum preconditions of education, skills and attitudes, and basic transportation, communication, and power facilities have been established. Included among the preconditions is the establishment of reasonably effective government and civil order. Roughly this precondition stage lasted in Great Britain until about 1783, in Japan until 1880, in Russia until around 1890, and in Indonesia up to the present.

Did the United States have to go through this process of establishing the preconditions for growth? Yes. The United States belongs among a small group of countries which were well endowed with rich agricultural land and relatively small population, like New Zealand, Australia, and Canada. It took the United States from about 1790 to 1840 to establish the preconditions; but unlike the underdeveloped nations of the modern world Americans ate well and enjoyed a relatively high standard of living in the period before its take-off.

The Take-Off

Following this precondition stage there comes a second stage during which the country makes the complex transition to a position where sustained economic growth becomes possible. Under the impact of

a particular stimulus, sometimes technological, sometimes political, the economic surges forward. The surges for economic progress, which have yielded marginal bursts of activity, expand and become decisive factors. The rate of savings--the part of its product a country ploughs back into its own future growth--rises from, say, 5 per cent of the national income to 10 per cent or more. Even more important is the mechanism by which this occurs. The economy organizes itself so that a high proportion (25-50%) of any increase in output is ploughed back into further investment. New key industries expand rapidly, yielding profits which are substantially reinvested in new capacity. New techniques spread in both agriculture and industry, as increasing numbers of persons are prepared to accept them and the deep changes they bring to ways of life. A new class of businessmen (usually private, sometimes public servants) emerges and acquires control over the key decisions determining the use of savings. New possibilities for export and new import requirements develop. The economy exploits unused backlogs in technique and natural resources.

This is the stage when the need for foreign capital is at its peak. Often, particularly toward the end of this stage, the burgeoning enterprise attracts substantial private international capital. In a decade or two the basic structure of the economy and the social and political structure of the society are transformed in such a way that a steady rate of growth can be sustained with a diminishing inflow of capital. Roughly, this was the process through which Britain had passed by 1815, the United States by 1860, Japan by 1900, Russia by 1913, and through which India seeks to pass in the next decade or so.

Third comes the long period of regular if fluctuating progress. Some 10-20 per cent of the national income is steadily ploughed back into expanding productive capacity. The structure of the economy changes continuously as technique improves. The economy of the country becomes more intimately related to the international economy. The society makes its terms with the requirements of modern and efficient production. As rapid growth provides the margin of resources from which additional investment can be made, the need for capital from abroad slackens; ultimately it ceases entirely, and domestic savings become so abundant that they begin to seek profitable employment abroad in economies even more recently launched on the growth sequence.

Underdevelopment Clarified

In the contemporary world the so-called underdeveloped countries stand at different points in relation to the three stages of economic growth. Most of the countries of central Africa and the Middle East and a few in Latin America like Bolivia and Ecuador have barely begun the process of developing the preconditions for the transition to growth. Others, like Indonesia, and perhaps Peru and Iran, are approaching a point where a sustained effort to make the transition may become feasible within, say, a decade. India, Burma, and the Phillipines are beginning the transition, and Mexico is, perhaps, emerging from it. A few like Argentina and, perhaps, Turkey have, on the whole, passed through this transition with success and now confront the problems of regular growth itself, often involving painful structural adjustments.

to determine the stage in which a country finds itself, two indices are useful. If a country has maintained an average rate of growth of per capita income of at least one or two per cent per year over at least a five year period, and if this cannot be explained by adventitious events such as a series of exceptionally favorable crops, or abnormally high prices for its exports, this is good evidence that it is passing from the precondition stage into the stage of transition. A further test, though this may be statistically hard to determine, is what proportion of its annual product it is able to set aside for investment purposes. In the precondition stage this is unlikely to be more than five or six per cent. During the transition it climbs until in the third stage it reaches fifteen percent or better. Of course, these statistical tests are only indicators, which must be interpreted in the light of a fuller examination of the characteristics of the economy and the whole society of which it is a part by someone intimately familiar with the way it operates; but they provide useful rules of thumb.

The assistance which countries need from outside if they are to develop is of two kinds. In the first place they need capital, both to establish the preconditions of growth and to make sure during the second stage that growth is maintained until they reach a point where they can be reasonably sure of maintaining it out of their own increasing output. Two sorts of capital may be required. They will need from outside some of the equipment and supplies required to construct

particular development projects. They will also frequently need a certain volume of food and consumer goods to permit them to divert their own labor and other resources from output for consumption to development efforts. But in addition to capital they will also need a great deal of technical assistance, the transfer of knowledge and skills from other parts of the world to permit them to make effective use both of their own meagre supplies of capital and of whatever is made available from abroad.

Policy Implications

The capital and technical assistance needs of a Free World growth program will reflect these different stages of growth and, therefore, the different requirements of the various countries involved. At an early stage, basic education may be the prime requirement in many countries, and in others such overhead capital as ports and railways. In many, technical assistance of various kinds may be more urgently needed than capital. In a few, industrial capital equipment itself may be the urgent prerequisite for continued progress. Most country programs should have all these elements within them, in different degrees. Each country must work out its program individually. There are no general rules of thumb such as the balance of payments deficits which so powerfully affected Marshall Plan allocations.

The different stages of growth have several important implications for foreign economic policy. The first is that substantial outside capital can be productively used by an economy in the first or precondition stage only in a few fields like transport, irrigation,

mining, and power. Some capital can be absorbed in agriculture and industry, but the amounts will be quite small. In the transition stage opportunities for productive investment spread to more and more kinds of activity but there continue to be sharp, if continually rising, limits on how much can be absorbed. These limits on the amounts that can be productively used, sometimes termed the technical absorptive capacity, are set by such factors as the technical and a managerial capacity available, the size, stability, and motivations of the non-agricultural labor force, the level of skills and education, the development of markets, the state of basic facilities for transport, communications, power, and community services, and the like. In the third stage technical absorptive capacity ceases to be a limiting factor on the volume of investment, which is then limited rather by how much of its output the economy is willing to set aside for investment and how much it can borrow in normal international capital markets.

Certain limited types of investment, such as in the production of raw materials for export, depend for their productivity not on the state of the domestic economy but on the level of demand in world markets. Oil wells can be drilled, rubber plantations established, tin mines opened by foreign capital with foreign technicians largely irrespective of technical absorptive capacity. But for precisely this reason the impact of investment of this kind on the domestic economy of the country or its capacity for general development is likely to be small. With these types of investment, which existing private

capital can be relied upon to undertake and which contribute little to broad development we are not here particularly concerned. But outlets for investment to serve domestic markets or to supply domestic industry will be very limited in the early stages. This does not mean that large projects will never be required by countries in the first stage. Certain types of investment in transport, irrigation, power, and the like may have to be undertaken before there is any evidence that the economy as a whole has begun to expand. As a rule, management talent for such projects will have to be supplied. Thus, as explained later, it would not take a very large program to supply all the capital requirements of the presently underdeveloped areas under suitable criteria of absorptive capacity.

Second, the principal risks attending investment in underdeveloped areas are those associated with the question of whether or not the economy will in fact grow continuously in the future. These risks are highest in the precondition stage. It is difficult to predict with precision when the take-off will occur or how much capital will have to be supplied before it will take place. These risks are so great that no more than a fraction of the needed resources can probably be supplied on a loan basis to countries in the first stage. The bulk of it will have to be grants and technical assistance. Because absorptive capacity in this stage is low, and only a limited number of projects justify the risk, the magnitude of grants need not be very great.

When the country reaches the take-off stage, its absorptive capacity goes up and the risks of repayment go down. There is still, of course, the chance that the whole program will fail, but a better

evaluation of that chance is possible. In this stage an investment program can shift from a grant to a loan basis, but the loans must, to achieve the objective of the program, carry longer maturities and lower rates of interest than would obtain for comparable investments in developed economies. Many of the risks, since they involve estimates of the future performance of the whole economy, are of a sort that private investors cannot be expected to bear. In this second stage, therefore, when a substantial amount of external capital must be supplied if the country is to get over the hump, this capital must be supplied in part at least by other than private investors. This is so both because the risks are higher and because the terms must be more favorable to the borrower than for alternative investments in the developed countries. It is worth exploring whether devices could not be worked out for supplying capital from public sources on an equity basis to countries in this stage, repayment and interest to be contingent on a minimum rate of growth of the national product.

Finally, when the country has demonstrated its capacity for growth, two things reduce the requirement for extraordinary channels for the provision of outside capital. First, the country is now generating out of its own rising output the resources to plough back into its own capital formation; and, second, investment opportunities are emerging which compare favorably in profit prospects with those in other developed countries. Thus the normal channels of international capital supply can be relied on to take over the burden of any net capital inflow still required.

In summary, then, in the precondition stage the demands for capital are low because of severely limited capacity to absorb it. In the

second stage they are a good deal higher, though compared to levels of investment in developed countries they will still be small. But this second stage is in any case of limited duration, say ten or fifteen years, and the supplying countries can look forward to a time when extraordinary measures to insure capital from outside can be discontinued.

In the light of this analysis it is essential to note that the proposals set forth in this paper do not open the United States up to an endless, open-ended world-wide claim on its resources. The American purpose would be to assist countries in establishing the preconditions for growth (mainly through technical assistance) and to assist them with capital in the decisive period of transition. When a country has passed the transition, it should be in a position to operate on its own with help only from normal international capital market institutions. Thus our proposals do not involve American commitments beyond a margin of resources which we can mobilize without great strain.

Chapter VI

THE PROPOSAL

Partnership for Economic Growth

The central proposal of this book is that the United States should, for reasons stated in Chapter I, take the leadership in a new international partnership program for world economic growth.

The strictly economic purposes of the program would be: first, to make available sufficient capital to permit the low-income countries to launch an ultimately self-sustaining process of economic development; second, to stimulate and assist the underdeveloped countries to overcome obstacles to their own development other than capital availability; and, third, to create a climate of international economic activity in which the economies of the industrialized countries of Europe and Japan, as well as the United States, could flourish and continue to grow.

Fundamental to the proposal is the thesis, explained in the preceding chapter, that there is a particularly critical period in the economic development of every country which determines whether that country will emerge into a long-run process of growth with expanding levels of per capita welfare or sink back into economic stagnation at the margin of subsistence. If it does the former, there is hope that the political results described in Chapter III will follow. If it does the latter, the probabilities of political chaos and instability--giving way to some form of totalitarian government--are very high. External capital

is required to prepare countries for the transition to self-sustained long-run economic growth. In the transition itself external capital will often make the critical difference between an upward spiral of economic, social, and political development and a downward spiral of stagnation and decay.

More specifically, what we propose is that the U. S., in participation with the other developed nations, should give assurance to every underdeveloped Free World country that it could secure as much capital as it could demonstrate that it could use productively, meeting fairly strict criteria of productivity. Countries would be divided into three categories: (1) those in the precondition stage, which would be offered an expanded volume of technical assistance and such capital as they could demonstrate they were ready for, much of it on a grant basis; (2) those in the transition stage, which would be offered continued technical assistance and as much capital as they could well absorb and wished to borrow at favorable rates of interest and with long maturities provided there was agreement that proposed programs and projects met appropriate criteria of productivity; and (3) those which have achieved self-sustaining growth, whose access to foreign capital would be determined by their credit worthiness as judged by existing international sources, private and public.

We believe, as explained in Chapter X below, that the amount which would be taken up under such an offer over the next ten years or so would not at the most be more than two or three billion dollars a year higher than current levels of international capital movement. Only a portion of that amount would need to be in the form of funds provided

by the U. S. government, a major fraction of that portion could be in the form of loans rather than grants, and a part of it (15 to 25 per cent) could be supplied in the form of U. S. agricultural surpluses.

A Banking Concept

Several elements of this proposal distinguish it from past practice, of which the amount of money involved is not the most important. One of these key characteristics of the plan is that the problem of how to allocate the available funds equitably among recipient countries would not arise. Every request for assistance which met criteria of productivity to be described later would be granted. In the early stages some countries like India which are at a stage of development where they can absorb additional capital readily would get the lion's share. As other countries were able to demonstrate that they were overcoming the difficulties of establishing new institutions to carry on economic activity, developing a labor force with the necessary skills, training administrators and managers capable of operating new ventures, and drawing up detailed investment programs to insure balanced and consistent growth, they would become eligible for higher levels of assistance. Meanwhile, as incomes rose in the faster moving countries, they would be finding themselves in a position to supply a larger and larger part of their own capital requirements out of their own savings.

The essential idea of this program is that the allocation of funds is based on a banking concept rather than a subsidy concept. A banker does not list all his potential customers and then try to decide how to allocate his loanable funds in such a way as to be fair to each. He sets certain criteria for the soundness of loans and then welcomes all

customers who can satisfy him that they meet the criteria. As explained later, the criteria in this program would be somewhat broader than those normally applied by a bank. They would relate not merely to the soundness of each particular project taken by itself but also to the prospects for the entire economy in which the project was to be located. But the distribution of funds among countries would be determined by absorptive capacity rather than by considerations of equity or politics.

Built-in Incentives

A second key characteristic of the proposal is that it is designed to provide maximum incentives to the governments of the underdeveloped countries to take the steps necessary to promote development, and thus make their countries eligible for assistance. It is a fundamental assumption of this program that the development of capacity to use capital effectively to promote growth is a job mainly for the underdeveloped countries themselves. A properly designed world program of technical assistance can help greatly in supplying the know-how and in carrying out the needed programs of training and education. Present technical assistance programs should be suitably expanded to this end; and the task of a new program should be not merely to make more capital available but also to advise and assist countries in preparing themselves to use capital productively. But the bulk of the task must be done by the people of the developing country itself. They must develop the necessary institutions, generate the required energy and initiative, acquire the requisite wisdom and courage in planning and controlling resource use, learn the necessary skills and techniques.

The partnership program here proposed would remove the one bottleneck over which the underdeveloped countries cannot have much

control--lack of capital. If the program were adopted, with a clear intention to maintain it for some time, each Free World country would know that whenever and wherever it was able to demonstrate that it could use resources productively in the context of a sensible program, the resources would be made available without any sort of military or political strings. The impact of this knowledge, consistently at work over a period of years, would be a powerful force pushing countries to take the steps needed for their own growth.

The program would place the burden of responsibility for economic growth squarely on the underdeveloped countries themselves. At present, political leaders in these countries can excuse their own failures to themselves and to their constituents on the ground that their national resources are simply not equal to the task, and that the richer countries refuse to help on terms they can accept. But if over a period of years the internal prerequisites for effective and productive use of capital are continually reiterated by a respected and impartial international body, and if the knowledge spreads that loans or grants necessary to progress will be forthcoming wherever and whenever adequate steps are being taken to meet these prerequisites, the pressure on governments for effective performance will become irresistible.

The Development of Absorptive Capacity

It is basic to our analysis that if this plan were accepted, economic growth in many areas would depend more on the development of absorptive capacity than on the availability of capital funds. A third key element is, then, that the plan provide for the expansion of absorptive capacity. To develop absorptive capacity in its widest sense is the basic function

of technical assistance. We recommend, therefore, that existing technical assistance programs be reviewed in the light of the experience of the past decade and if necessary expanded, and that they be purposefully reshaped to mesh with the proposed program of loans and grants. In general, where the bulk of a country's loan or grant applications fail to meet the proposed criteria, a prima facie case for expanded technical assistance would exist.

There are several kinds of technical assistance which may deserve more priority and resources than they have hitherto been given:

(1) We have emphasized the great importance for the underdeveloped countries of working out consistent and detailed development programs. In the early stages and for many countries the lack of such well-considered programs will be a principal limitation on their ability to absorb loans and grants. In recent years the pool of talent and experience in programming techniques has been growing rapidly. It should be possible to supply countries just starting the programming process with technical assistance which could greatly accelerate their progress.

(2) One of the most serious bottlenecks inhibiting the development of absorptive capacity in the underdeveloped countries is a shortage of managerial and administrative skills. Two kinds of assistance would be useful here. The first would be help in establishing educational and training programs designed to develop a bigger supply of indigenous managerial and administrative talent; and the second would be devices to assist, in the meanwhile, to find ways of using foreign managerial expertise without compromising domestic control. We should explore new forms of management contracts which will accomplish this end.

(3) Existing technical assistance programs under both U. S. and U. N. auspices are already providing valuable engineering advice. If the plan we propose is adopted, the need for such assistance will expand greatly. Some thought should be given to the organization of an international pool of engineering experts with experience in the problems of adapting engineering design to the conditions present in underdeveloped areas. Such a pool, in addition to consulting on projects on request, might conduct research into problems of engineering design common to a number of countries.

(4) More fundamentally, a purposeful effort should be made to apply new scientific knowledge to the economic problems of the underdeveloped areas. One of the resources in which the United States is richest, our scientific skill and imagination, has been of necessity rather heavily focussed in recent years on the development of weapons. Many of our top scientists would eagerly welcome an opportunity to turn their energies to constructive problems relating to human welfare. The same kind of concentration of first-class minds on a specific problem that has produced one breakthrough after another in military technology should be capable of opening some of the technological bottlenecks to growth in the underdeveloped areas.

The arrangements being set up for the development of atomic energy for peacetime uses could be made the focal point for a more general cooperative scientific program. Peacetime use of atomic energy is only one of many exciting new technical developments which should be pursued. Imaginative effort on an adequate scale might well produce important developments on such problems as making fresh water from sea

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water at low cost, rainfall control, the capture and use of solar energy, the development of algae as food sources, and chemical means of population control. Regional laboratories or institutes could be established to work on these problems, and scientists and engineers from the entire Free World could be brought to them.

The Well-Understood Objective

This incentive effect of the program will be strong only if a number of other key elements of the proposal are preserved. A fourth such key element is that the recipient countries must be convinced that the program does not have narrowly political or military objectives. Its basic political objective--the development of stable, effective societies moving in a democratic direction--is one with which no non-Communist country will quarrel. But if it is believed that it is designed as a way to force neutrals into our camp, to secure acceptance of particular American foreign policies, or to draw other countries into conflicts which they believe, however rightly or wrongly, do not concern them, none of the more fundamental results we seek will be secured. The underdeveloped countries, many of them recently fresh from successful efforts to throw off political domination by colonial powers, are highly sensitive about their political independence. If they believe this independence is in any way compromised by accepting assistance from us, either in grant or in loan form, they will reject that assistance, as some of them have done in the past, however desperately they need it for their own growth. Many of them believe that if assistance is channeled through an international body, they will be better protected from political strings. How far we can or should accept this view is

discussed in Chapter XI. but the more we are crystal clear in our own minds that our purposes in undertaking this particular program are neither to strengthen the military forces of our allies nor to buy adherence to our foreign policy by an international institution can protect the program from our misadventures. If we do achieve consensus and clarity on this point in the United States, international safeguards become much less crucial.

The Positive Criteria

It is, of course, as important to have agreed positive criteria of eligibility as it is not to apply wrong criteria. Our purpose is not a giveaway program without strings of any kind. We have a very specific purpose in adopting such a program, --to promote the economic growth of the underdeveloped countries, --and we should be very sure that any money we make available, in either grant or loan form, will serve that purpose. We believe, as explained further in Chapter XI, that a set of criteria can be established which will have the agreement and respect of both the recipient countries and other participating suppliers of capital. These should include the general conditions that development be undertaken for the benefit of the entire population of the recipient country and that the goals of its development program be related to the aspirations of all of its people. Beyond this, they should include quite severe technical conditions governing the economic effectiveness of assistance in promoting development. Programming discussions must result in agreement that the recipient country has worked out: (1) a consistent development program, (2) practical ways of implementing it with available skills and facilities, and (3) effective ways of mobilizing the country's

own national resources, including a high rate of saving for development. The application of these criteria will require great judgment, skill, and understanding. No formal set of rules can substitute for wise administration. Nonetheless, the subject of criteria is such a sensitive one that we believe an effort to develop an explicit code of ground rules for an assistance program is worth while. The United States agencies responsible for this program should set up such a code to govern their own behavior and should discuss this code both with participating suppliers of capital and with recipients.

International Sponsorship

Related to this is another key element of the program, namely that its sponsorship should be international rather than national. This does not mean that all administration of the program must be turned over to the United Nations or some other international organization. There are many countries now contributing to development assistance through many agencies, both national and international. Each has its own approach and function and no purpose would be served by consolidating them all. It is quite possible, however, to retain a large number of separate channels of financing and at the same time bring them all within the framework of an internationally agreed program. We have already suggested the desirability of establishing an international code of criteria which would set the basic philosophy and ground rules to which both supplying and recipient countries would adhere. As suggested later in Chapter XI, this could be supported by an international secretariat, perhaps broken down into regional commissions, to maintain information, review programs, coordinate and interrelate various elements in the international flow of capital, and where needed act as a broker between countries needing

assistance and potential sources of supply of finance.

An important reason for internationalizing the program to as great a degree as is consistent with efficiency is the contribution this could make to the sense that the countries of the world were engaged in a great common constructive effort. This is perhaps more important to the morale of the industrialized countries than to that of the under-developed ones.

A World-Wide Program

We believe the incentive effects of the plan will be much more pronounced if it is world wide in application than if it is limited to one or two regions of the world like Southeast Asia and the Middle East. It should be clear from what has gone before that we do not think it should be labelled as an anti-Communist or anti-Soviet program. We are as interested in stability and growth, in the long run, in Africa and Latin America, as we are in Asia. Since much of Africa consists of colonies, there would be difficulties in launching an African program unrelated to anything else. In the context of a global program, Africa clearly deserves a place; and many of the conditions which should be set down for programs elsewhere can and should be applied there. This does not, of course, mean that all planning and administration must be on a global basis. Regional units are both more meaningful and more efficient. But once again, the philosophy and ground rules of the program would gain great support from being placed in a global context.

Continuity

Lastly, the program will have very little incentive effect if it is not assured of continuity over a number of years. The steps that must

be taken to prepare a country for effective use of additional investment resources are complex, time consuming, and difficult. If an offer of assistance is to stimulate action in compliance with its conditions, it must be a standing offer effective over an extended period. Even where the general environmental conditions are already favorable, project planning, the adjustment of development programs, and the like may require two or three years. Where more fundamental deficiencies in education, statistical information, labor and entrepreneurial skills, transport and communications, and public administration exist, the lead time may be a decade or more. Even quite a large program will lose most of its effectiveness if it teeters along always on the verge of Congressional disapproval with no more than a one-year lease on life. The limited magnitude and great uncertainty of our programs for the underdeveloped areas to date go far to explain the lack of response to such offers as the President's special fund for Asian regional development.

Avoiding Autarky

Finally there are two other key aspects of this proposal. First, though the underdeveloped countries will establish home industry, and will become somewhat more self-sufficient, they must not develop autarkically. Their experience with dependence on world trade has not been a happy one, and it would be understandable if they were to press for making themselves as economically independent of the rest of the world as possible. They can be persuaded that their own rapid growth requires that their development be based on a considerable international division of labor. If we and they follow trade and monetary policies designed to restore an effective international trading community, and if their investment programs are consciously designed to exploit their international comparative advantage, not only will we and they benefit, but the other

industrialized nations, especially in Western Europe, will be able to maintain rates of economic growth they would otherwise have difficulty supporting. This is explained at greater length in Chapter VIII.

The Productive Use of Agricultural Surpluses

Second there is a resource which, with a little intelligent planning, could be made to play a much more important part in international efforts to promote development than it has done to date. This is the large agricultural surpluses of the United States and the other agricultural exporting nations. Development is still inhibited in a number of areas of the world for lack of an assured supply of food and fibres, while in other areas an excess of agricultural production continues to be an embarrassment. Chapter IX suggests ways in which this paradox could be resolved to the mutual benefit of both sets of countries.

Chapter VII

CRITERIA OF ELIGIBILITY FOR ASSISTANCE

Four Banking Standards

We have emphasized that capital should be made available only where there is reasonable assurance that it will be productively used. Indeed, our central idea of allocation of funds according to a banking concept of credit worthiness and technical absorptive capacity hinges on the question of whether it is possible to establish reasonably objective criteria such that experts would be able to agree as to whether a given application of resources was likely to be sufficiently productive to justify making them available. While the element of judgment will, of course, always be important, as it is in any banking operation, we believe it is possible in practice to set forth with considerable precision the considerations on which judgment must be based.

At least four kinds of considerations must be involved:

a. It must be within the technical and administrative capabilities of the receiving country to carry out its proposed project with reasonable efficiency, and steps must be under way to remedy any weaknesses which exist.

b. Steps must have been taken to insure that the rest of the economy of the receiving country is being developed sufficiently to make the proposed project fully productive in the time period envisaged by the loan.

c. The receiving country must have an overall development program designed to make the most effective possible use of its resources, including not only a series of interrelated capital projects but also necessary educational and training programs.

d. The receiving country's development program, of which the project is a part, must be consistent with the requirements of expanding world commerce and the international division of labor.

Management

Each of these criteria deserves explanation. The first is for the most part of a kind that any lending organization would automatically apply. Are there trained managers to run the project? Is adequately skilled labor available? Has provision been made to insure competent technical supervision? Any investment banker could spell out these requirements in detail. The application of these rather simple criteria will probably exclude in the first instance a large proportion of the proposals of the underdeveloped areas; but lending agencies should not confine themselves to ruling that the criteria have not been met. An essential part of the plan is that lending agencies should provide advice and assistance to make good the deficiencies discovered. They may do this directly themselves, or they may refer the case to the national or international agencies specifically responsible for supplying technical assistance.

Balance

The second criterion is likewise one that lending agencies customarily apply. Do markets exist or can they be foreseen for the product of proposed installations? Are transport, communications, and public services adequate to serve the needs of the project, or will they be developed in

time to do so? Have complementary activities producing the materials and services needed by the proposed project been planned on the required scale? Again, rejection of project applications because of failure to meet this second criterion should be accompanied by recommendations for action to eliminate the deficiency.

The Case for an Over-all Development Program

These two are frequently the only criteria applied in international investment operations. But, while important, they are much less important in a program of the scale here contemplated than the remaining two. Let us look, therefore, in some detail at the requirement that the receiving country have a correctly designed over-all development plan.

For any substantial expansion of international investment above existing levels it is essential that investment programs (not merely projects) be developed by the receiving countries. Such programs are necessary to insure: (1) that the various component projects interrelate and reinforce each other; (2) that the general objectives implied in the entire pattern of projects are ones which the people of the country will support; (3) that the collection of projects and measures undertaken will produce a faster growth of national product than any other which is consistent with the goals of the society; (4) that the resources of the economy have been tapped for the maximum contribution they can make to its development; and (5) that foreign exchange requirements have been minimized.

Such programs should cover both the investment planned by public authorities and some estimate of what can reasonably be expected from the private sector. In other words, they should project forward for a reasonable period the total pattern of investment for the entire economy, together

with estimates as to the sources from which resources for investment, both public and private, can be secured. Whether the economic philosophy of the country calls for close regulation of private investment or permits private capital very freely to seek its own outlets, some estimate of the forms it will take is essential to the planning of whatever supporting public activity is contemplated. The need for programming derives from the fact that it is characteristic of the transition stage of development that the success of many particular investment projects depends upon the entire set of investments being undertaken simultaneously.

At the least, the existence of such a development program is evidence that the country has explicitly faced certain fundamental choices about its development--such as the relative weight to be given to agriculture as against industry; the fraction of resources to be devoted to social overhead capital such as railroads, public utilities, and the like; the importance to be placed on consumers' capital such as housing as against more directly productive instruments. A national program will naturally reflect the values and goals of the people of the country for which it was drawn. The purpose of review by an agency outside the country is not to pass on those values but to insure the program's internal self-consistency, to make certain that all relevant issues have been faced, and, where the program rests strictly on economic or technical relations, to see that they have been correctly applied.

An important consideration must be whether the measures undertaken by the country to capture the maximum flow of savings from its own citizens are adequate. The financial mechanism and the tax structure must be so designed as not to leave pockets of either unemployed or misapplied

resources. Savings channels must be set up to maximize the flow of savings, both small and large, into developmental investment. Fiscal management must be so designed as to prevent unhealthy inflation. All of these criteria are capable of generating frictions and differences of view between supplying and receiving countries. They must, of course, be applied in a wise and realistic manner with an understanding of what is politically and administratively possible in the particular country in question. But we believe frictions can be minimized and understanding and agreement promoted by the international adoption of a code such as is suggested in a later section.

There are few countries which will be able to meet this third criterion while in the first stage of growth. Nevertheless, investment can go forward on the basis of the first two criteria where it is clear that the national project in question would be part of any sensible development program, whatever its details. Many investments in transportation, public services, basic power sources, improvement of agricultural techniques, and the like, will be of this character. Thus, some modest expansion of existing investment programs could probably be approved in the absence of national program planning; but before the levels of investment contemplated in our proposal can be fully reached, many underdeveloped countries must institute much more sophisticated programming procedures than they now have. Indeed, in most cases it will be impossible to pass on the soundness of an individual project, even according to conventional investors' standards, without familiarity with the program of which it is a part. In a developed economy the environment of a project often changes slowly enough to be taken as given. In an economy

undergoing sudden transition everything changes together, and the whole pattern of change must be examined to evaluate any part. Agencies applying this third criterion to investment projects can be of great help in assisting countries to undertake effective programming.

One criterion in particular which the private banker customarily employs must give way to this broader criterion of contribution to a consistent program. Private loans often hang on the question of whether the project to be financed is self-liquidating in the sense that its operation will directly produce the revenues necessary to repay the loan. This is a very poor criterion for development loans. A project may be self-liquidating because it discourages other investments which would otherwise take place and attracts to itself revenues which constitute a diversion rather than an increase of total product. On the other hand, a project such as an irrigation scheme may greatly expand total output but may be of such a character that it is not possible to collect equivalent added revenue from the immediate beneficiaries.

All projects taken together, that is, the whole national effort, should be self-liquidating in the sense that the national product created over time exceeds the national cost incurred. Moreover, each individual project should clearly produce over time a sufficient increase in the total product of the country to more than cover the costs of interest and amortization of the capital it requires. For example, the increase may take the form of lower costs to other industries, and need not accrue in an identifiable way to the project. The narrow criterion of whether a project can repay from its own revenues is at best irrelevant and at worst may be seriously misleading.

Generating Foreign Exchange

A distinction must be made between the productivity of an investment in creating new output within the country where it is made and its productivity in creating foreign exchange earnings out of which foreign borrowings can be repaid. It seldom makes sense to apply the test of foreign exchange earning power to particular projects. The possibilities of repayment of a foreign loan will depend on the entire balance of payments position of the borrowing country at the time interest and amortization payments fall due. The risk of foreign exchange difficulties in the period of repayment is greatest for a country in the first or pre-condition stage, less in the second stage, and least in the third or self-sustaining stage. This is true partly because as development proceeds the economy becomes more diversified and flexible. Its opportunities of production for foreign markets grow, partly because, as development becomes regularized, it can more easily attract new capital to replace that being withdrawn. This constitutes an added reason for supplying a good part of the limited amounts of capital needed in the first stage in the form of grants, soft loans with local currency repayment, or equities which can only be recovered if the economy in fact moves into the transition.

Whether foreign exchange difficulties will be encountered in the second and third stages depends partly on the kind of international trading environment which has been established by that time. This in turn depends partly on whether our fourth criterion has been observed that countries pay attention to the possibilities of the international division of labor. To this problem we turn in the next chapter.

Chapter VIII

THE INTERNATIONAL DIVISION OF LABOR

How Autarky Arises

The fourth criterion deserves special attention, since its observance is important not only to the underdeveloped countries but to the economies of the industrialized countries including the United States as well. It is, moreover, a criterion on which we cannot insist unless we are prepared to set an example by modifying our own trade policies so as more nearly to conform with its requirements.

Planning officials in the underdeveloped countries, understandably preoccupied with internal problems, may well fail to pay adequate attention to the ways in which their own economies can gain from being integrated into an expanding world economy. In a stable world of free trading relations such as are sometimes mistakenly thought to have characterized the nineteenth century, the development program for any country which produced the largest internal rate of growth would also be the one which took most advantage of the possibilities of international specialization and division of labor. But in the contemporary unstable world, plagued by extreme fluctuations in the prices of basic commodities, subject to almost daily changes in the terms and conditions on which international trade is carried on, and, above all, subject to the overriding risk that foreign areas may be cut off altogether at almost any moment by political or military developments, programming authorities are under great pressure to abandon the obvious benefits of international trade for the security of some degree of autarky.

This results in decisions of two sorts. In the first place these countries are slow to see and to give priority to opportunities to invest in the production of things that could be sold abroad. There are still undeveloped mineral and raw material resources in many of them which could be further exploited to provide the supplies needed by the industries of Japan, Western Europe, and the United States. But partly because extractive industry has been associated with colonialism and partly because international markets have been unreliable they have frequently been reluctant to give serious consideration to investments of this sort. Beyond this there are possibilities of specialization as among the underdeveloped countries themselves which have not been considered because development planning in each country has stopped at its own borders.

In the second place these countries have imposed partly through tariffs and quotas and partly through exchange controls severe restrictions on the import of many kinds of goods in the hope that they could develop efficient production of these things themselves under an umbrella of protection. Some of these restrictions are justified, given the situations of many of these countries. Where internal taxation procedures have not been adequately developed import duties have been one of the few effective ways available to them of restricting the luxury consumption of the very wealthy classes. Economists have long recognized that there is some validity to the infant industry argument for protection in a young country. Industries must attain a certain scale and acquire a certain amount of experience before they can hope to reduce their costs to the level of large established

competitors abroad. Without some protection such industries can never get started. Nevertheless it would be hard to contend that all the trade restrictions applied by the underdeveloped countries could be justified by rational arguments of this sort.

Tempering Autarkic Tendencies

In the interests of maximizing productivity in the underdeveloped countries, a new program of capital assistance to development should contain safeguards against an exaggerated trend toward autarky. The economic costs of attempted self-sufficiency in some industries in which the underdeveloped countries have no experience would probably be great enough to thwart their own prospects for growth; for many of them are comparatively small countries with markets inadequate, both now and in the foreseeable future, to support many industries requiring large-scale operation. Although diversification is a reasonable goal for an economy, it makes no economic sense to push it to the extreme of attempted self-sufficiency, --especially in a small economy.

More positively, there are substantial possibilities of economies which could result from regional cooperation in investment plans, since through such cooperation each country could devote its efforts to investment in enterprises in which it had comparative advantages, secure in the expectation of a market larger than its own population and perhaps justifying a scale of operation not possible within its own borders. Indonesia, with cheap natural gas, might make fertilizer for the whole South Asian area, India might be a source of light engineering, and so on. This would require discussion among the programming authorities of the various countries of a region and possibly long term agreements, but it might yield big dividends in productivity for all the participants.

The Interest of the Industrialized Nations

There are also important reasons for promoting the international division of labor growing out of the requirements of the industrialized nations whose economic advancement it is also in our interest to further. The plan proposed in this book can help substantially in meeting their economic problems. They no longer face a shortage of resources for self-sustained economic development, but they do face a problem of continuing adjustment to the international economy.

For their economies developed in an era of international specialization and international trade; and without continued specialization and trade they certainly cannot provide expanding incomes for their people and may not be able even to maintain their present standards of living. They need two things: markets in which they can sell those goods they can produce most cheaply, and sources for food and raw materials which they cannot efficiently produce at home. Without a restoration of international trade there is little hope of finding a solution for the growth problems of the developed countries of Western Europe and Japan.

At the moment, the international position of the Western European countries appears to have improved. Most of them have succeeded in increasing their reserves of foreign exchange, and the gap between black market exchange rates and official rates has narrowed in many instances. However, it should be kept in mind that the total flow of aid, military and economic, has not been going down in the last few years. The impact of a sharp reduction in this flow with no change in the burden of military expenditure, would be serious. Furthermore, expanding levels of income in Europe will require expanding levels of trade both because greater production in Europe requires greater

Imports of materials and because it needs the stimulus of expanded markets. The Japanese situation is much more serious. Japan has been able to maintain her level of activity only because of the extraordinary disbursements of the United States to Japan connected with the Korean War and its aftermath. The Japanese economy, whose prewar prosperity was built on trade, needs a trade revival merely to survive, let alone to grow.

In the short run it would be foolish to exaggerate the economic importance for the developed countries of access to the materials and markets of the underdeveloped ones. The flow of raw materials from Asia, Africa, and Latin America is not going to be abruptly interrupted, and trade among the industrial countries themselves has always been more important to each of them than trade with low income areas. Nonetheless as time goes on the policies of the underdeveloped areas can become increasingly critical to the small margin of trade opportunities which makes the difference between growth and stagnation in Europe and Japan. If investment in extractive industries for export stops or falls off sharply in each area as it achieves independence from colonial rule, raw material costs will rise and countries dependent upon imported materials will suffer with no corresponding advantage to the exporting area. If, on the other hand, some part of the capital resources of the underdeveloped countries continues to be devoted to reducing the costs of raw material exports, their short run foreign exchange position will be improved, and in the long run their own growing economies will benefit from lower cost domestic raw materials. This is not an argument against desirable diversification of the underdeveloped countries, but it is an argument against a complete neglect in development of their raw material resources.

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such devices as long term purchase agreements to reduce somewhat the violence of fluctuations in raw material export prices, and it should be a firm objective of the under-developed areas progressively to increase the extent to which they themselves process their own raw materials before export.

So far as markets are concerned, in the short run the process of development itself generates requirements for capital goods and equipment which can provide an important outlet for European and Japanese manufactures. Some of these sales can be financed by the capital contributions the other developed countries can make in loan or grant form to development programs. Their capacity to finance their own exports has, however, narrow limits. Dollars supplied to the underdeveloped countries by the United States can do double duty here if we have the intelligence not to attach "buy American" strings to them. Some portion of our dollar contribution to development, spent in Europe and Japan for capital equipment, will strengthen the dollar buying power of these countries and thus indirectly stimulate our own exports. Thus our development assistance contribution, can if we do not restrict its spending to this country, become an important lubricant of international trade everywhere and hasten the day when currency and trade restrictions growing out of the postwar dollar shortage can be done away with.

In the longer run, as the underdeveloped countries develop and become industrialized, their participation in world trade can become quantitatively much more important to total world trade flows. Fears that as they develop they will become competitors of presently industrialized countries and thus reduce export opportunities should be quieted by the history of industrialization everywhere it has

occurred. As standards of living rise in a country, the growth in the magnitude and variety of its demands much more than compensates as a rule for such reduction as occurs in those limited types of imports it now produces at home. The trade possibilities opened up when several hundred million people experienced an expansion in their incomes from fifty dollars per year per head to four or six or ten times that amount are almost impossible to visualize.

An American Responsibility

All this depends in considerable degree, of course, on U. S. commercial policy. It is very much in our interest that the underdeveloped countries themselves earn through export to dollar areas as large a part of the resources needed for their development as possible. This will not be much in the immediate future. As their economies grow, however, there will be an increasing number of areas in which they should be able to compete effectively in U. S. markets if our tariff policies do not prevent them from doing so. In the long run our development loans can be repaid only if they or their customers can so compete.

Second the lubricating effect on international trade of a flow of development dollars from this country will depend entirely on our not thwarting that effect by insisting that the dollars be immediately spent in this country. The pressures to maintain "buy American" provisions will be strong from particular export interests. The national interest, and even the longer run export interest of the United States will be much better served if those pressures are resisted.

Perhaps more important than a fear of money, however, is the force of our example. If we, the strongest most advanced economy in the world, do not regard the free world economy as legitimate foreign competition, we can hardly expect that our actions to the rest of the world to abide by the principles of free trade will be received with good grace. We certainly cannot insist on an acceptance of the principle of international division of labor as a criterion for eligibility for development assistance unless we are prepared to abide by that principle ourselves. And it will be increasingly to our own economic as well as political interest to have that principle accepted elsewhere as time goes by.

Creating the Conditions for Convertibility

A word is in order as to the relation of this plan to the problem of general free world convertibility of currencies. We do not believe that the institution of convertibility will, by itself, do much to solve the underlying problems of the industrialized countries, let alone the underdeveloped ones. Convertibility can be achieved only if the underlying conditions for it exist. A commitment by the United States and other dollar areas, however, to provide the world's trading system with a substantial increment of dollars, for development purposes which meet the criteria of efficient international specialization, would be a necessary condition for a convertible arrangement. It would also be a necessary part of the larger world development plan.

tied to dollar purchases. We are convinced that the desire for convertibility is strong and general enough to bring it about once confidence in the scale and stability of U. S. action is established. Such confidence can be produced by U. S. willingness to proceed with these proposals; but it cannot be produced by negotiating pressure.

Chapter IX

THE ROLE OF AGRICULTURAL SURPLUSES

Putting Surpluses to Work

We believe that in the context of the program proposed in this book arrangements could be worked out for the use of very much larger quantities of foods and fibres in development programs than have been utilized to date, without disrupting international commodity markets or interfering with the sale of foods and fibres in those markets by other exporting nations. The underdeveloped countries need a program designed not merely to supply capital goods or other items available only from abroad, but also to expand their general resources in all ways which will promote domestic capital formation.

Many of the underdeveloped countries have a huge unemployed or underemployed labor force which could be used for developmental purposes. In most of the Asian countries there are many people now idle or ineffectively employed whose labor, if mobilized, could be used to build roads, buildings, canals, and irrigation works, to reclaim land, to modernize villages, and the like. Indeed this supply of underemployed labor is not only a potential economic resource, but if not given employment can constitute for these countries a serious political problem. India, for example, in spite of a quite ambitious second Five Year Plan, does not now expect to

be able to reduce her large volume of unemployment significantly over the next five years, since new employment opportunities will barely match increases in her labor force resulting from population growth.

Why Labor Is Underemployed

Three things stand in the way of utilizing this pool of underemployed labor for development. The first is a scarcity of administrative and managerial talent to supervise such projects. This is being slowly overcome both by the efforts of the countries themselves and by the technical assistance programs operating with them. The second is the unavailability of the minimum amounts of capital equipment required to undertake even the most labor intensive types of projects. This shortage could be largely overcome by procedures already discussed as part of the program proposed in this book. The third obstacle is that the unemployed are underfed and underclothed. It is this third obstacle with which we are concerned here.

If the unemployed are put to work at wages supplied by the government, they will spend those wages largely on additional food and clothing. If the additional food and clothing is not available, the additional expenditure will push up the prices of these essential articles, and general inflation will result. In other words, the volume of wage payments which the authorities of the underdeveloped countries feel they can safely undertake is limited by their estimate of the likelihood that such payments will indirectly push up prices, especially the prices of essentials. An estimate of these risks

is complicated by the uncertainties of the weather. An undertaking which would be safe if the season turned out to be favorable might produce disastrous inflation if there were a bad harvest. Storage facilities in the underdeveloped countries are in general most inadequate, and there is thus no way for them to build up adequate stocks to prepare for contingencies.

A Specific Proposal

We believe that, should there be established an international food and fibre bank of which the underdeveloped countries could draw, and should some additional capital be provided which they could count on for a period of years, they would and could implement plans to employ productively a considerably greater part of their presently idle labor force. Demands on the food and fibre bank would, we believe, be very substantial. But favorable results could be expected only if there were some assurance that both the capital and the food and fibre supplies would be available over a period of years. It takes time and scarce resources to organize labor intensive projects, and, once started, they cannot easily be discontinued at short notice. The horizon of an international food and fibre program should be at least five and preferably ten years.

A warning is necessary here. Where the other two conditions are not met, the movement of agricultural commodities to underdeveloped countries can have very damaging effects. For if there is an increase in agricultural supplies without any corresponding increase in demand, agricultural prices may fall sharply, reducing the incomes of

peasants and slowing or stopping programs of agricultural and village improvement. Furthermore, some of the underdeveloped countries which export agricultural surpluses depend on the sale of such surpluses for the imports which they, in turn, require for their own development. Thus the unplanned dumping abroad of agricultural surpluses can be much worse than useless. It can be disastrous.

Meshing With Commercial Markets

A plan for the use of agricultural surpluses must have several features if it is to avoid interfering with the normal marketing of agricultural products both within the receiving countries and by the exporting nations. In the first place, countries should be assured that they could draw on food and fibre supplies if necessary to meet expanding demands or abnormally short supplies; but that they would be under no obligation to take such supplies if domestic supplies and normal imports were adequate. The pragmatic test would probably be the behavior of prices of food and fibre. Indeed, to protect the exporting countries, the program should probably contain a provision that no country would be permitted to draw on the stocks in the international food and fibre bank unless prices in its domestic markets rose above certain normal levels.

A second protection for the exporting countries would be that they would themselves be invited to participate in supplying commodities to the international stockpile on a basis determined by their normal shares in international commodity movements.

Exporting countries like Canada which are suppliers of developmental capital for the underdeveloped countries would be encouraged to make their contribution partly in agricultural commodities. Exporting countries like Burma, which are in need of developmental assistance, would receive such assistance partly in the form of purchases of Burmese rice for the food bank with hard currencies which Burma could use for developmental purposes.

This food and fibre program looks on the face of it very like a number of international commodity stabilization schemes which have been put forward in the past. It differs from them in that, by providing assurances that food and fibre would be available to prevent expenditure from having inflationary effects, it would encourage countries to undertake local developmental expenditure. As to payment, the food bank should probably accept at least in the early stages local currency which would be held in a counterpart funds account. This fund could be used for developmental purposes in the recipient country as part of the capital supplying program of the developed countries, or, if the monetary situation required, it could be held idle pending future developments.

How Much of the Job Can Surpluses Do?

Experts who have studied the problem in the full light of these facts are convinced that, in a development program which also provides capital goods and which is planned for some years ahead in the light of the various bottlenecks existing in the economy of the recipient country, there are possibilities for the use of a very substantial volume

of agricultural commodities in assistance programs. The FAO, for instance, has estimated that something like \$100 million worth of agricultural surpluses could be used annually in India in connection with an expansion of \$250 million per year in her investment program. In general it appears that from 15 per cent to 25 per cent of all foreign capital required by all underdeveloped countries could take the form of agricultural commodities.

If this estimate is correct, and the estimate of total capital requirements given in the next chapter is reasonable, agricultural surpluses could be used to the extent of around \$500 million worth per year over and above extraordinary relief requirements in exceptionally bad crop years. Various ideas have been put forward for distributing more food through channels entirely outside the market mechanism, like school lunch programs, special free meals for project workers, and the like. In our view such schemes are likely to be both inefficient and quantitatively quite limited. Some such program as we propose for food and fibre stocks to provide insurance against the inflationary consequences of additional wage payments offers more hope for substantial use of agricultural surpluses in development efforts. The plan will be more effective, of course, the larger the number of essential commodities which can be included in the reserves.

Chapter X

THE MAGNITUDE OF CAPITAL REQUIREMENTS

What Determines the Price Tag

Preceding chapters have outlined our proposal that the developed countries of the world should undertake, through a variety of channels, to make available to the underdeveloped countries sufficient capital to meet all requests for such capital which satisfy certain criteria. This proposal at once raises three questions: (1) If this offer were made, what is the maximum amount which might have to be provided annually to make good on it? (2) What are the chances that this amount would be sufficient to set in motion a process of self-sustaining growth in the underdeveloped areas? (3) What is the probable level of eligible requests over the next five to ten years?

Several factors limit the volume of capital assistance that the underdeveloped countries are likely to be in a position to absorb productively. A limit on the size of a development program and on the number of desirable and feasible projects is set by the ability of the underdeveloped country to organize, administer, and carry out projects and to relate them to each other in such a way that the output of each project is used productively. Foreign technical assistance and advice can raise this limit somewhat, particularly in certain specialized types of projects. The countries themselves, however, are reluctant to turn over project management and control too largely to foreign experts; and, even if they

were not politically sensitive on this point, it is doubtful if their own long-run development is really promoted by starting enterprises for which they do not take a share of responsibility.

It is extremely hazardous to attempt to estimate technical absorptive capacity, which will vary widely from country to country, depending partly on a country's state of development and partly on its history and traditions. We believe, however, that it is reasonable to assume that the average maximum expansion in the level of capital formation that can be achieved by countries in the early stages of development is from 30 to 50 per cent in the first three or four years after planning for such expansion is initiated. There will be some cases in which even this is too high a figure, and others in which a single project like a dam or an irrigation system may involve expenditures exceeding this limit. However, an examination of individual country plans gives us some confidence that this is a reasonable order of magnitude.

It is most unlikely that countries in the very early stages of development can find sufficient resources within their own economies to make more than a very small contribution to such an expanded level of investment. Since their populations are at the margin of subsistence, consumption cannot be reduced in order to free resources for investment. Furthermore their relatively primitive methods of mobilizing such savings as they are capable of generating are unlikely to tap more than a fraction of these. There are certain cases, notably the oil producing countries, in which the revenue from an exportable resource provides the means for development expenditure without cuts in consumption by the population as a whole, but these do not bulk large in the total of capital requirements for development.

Accordingly, it seems reasonable to assume that for countries in the pre-condition stage of development virtually all of the additional capital needed to launch the growth process must be supplied from outside.

Once the growth process is under way, two things happen which affect the need for external capital in opposite ways. In the first place, the capacity of the country to absorb capital rises rapidly. A trained class of administrators appears; skilled labor is increasingly available; transport, power, and communications are increasingly able to fill the needs of new enterprises; markets are expanding; and the motivations required to stimulate innovation, risk-taking, and efficiency are more and more developed. At the same time, as income rises, a portion of each year's income becomes available to be plowed back in further investment, and the society becomes increasingly capable of mobilizing this fraction for development. The fraction of this increase in income which can be saved is much larger than the fraction of total income saved. Although the average rate of savings in Asia, for instance, is probably not much above 5 per cent, the marginal rate of saving from increases in income can be pushed as high as 20 to 25 or even 30 per cent. Thus, at the same time that the capacity of the economy to absorb capital rises, its capacity to supply its own capital needs out of its own resources also rises. If additional external capital is supplied at an annual rate something like 30 to 50 per cent of the rates of investment prevailing in a country at the beginning of the development process, the country can mobilize sufficient saving out of the increases in its income to keep pace with its own growing capacity to use capital. Indeed, once the take-off occurs, that is, once a regular rate of growth in national income has begun, the

requirement for a net inflow of capital on a substantial scale is unlikely to last for more than ten or fifteen years. After that period of time the country can put itself in a position to supply all of its own requirements out of its own resources. It may still attract foreign capital, but it can do so on terms attractive to private international investors.

Some Rough Figures

To estimate, then, the amounts of foreign capital that could productively be absorbed by the underdeveloped countries, one must consider countries in two categories. First, for those which have not yet entered into the transition phase of growing national income the estimate can be made by taking 30 to 50 per cent of present levels of capital formation. For those which have begun to grow, the percentage will be less, being the smallest for those farthest along in the growth process. These estimates, explained in greater detail in the Appendix, result in the following figures:

	<u>Billions of Dollars</u> <u>Per Year</u>
India, Pakistan, Ceylon	0.8 - 1.0
Balance of non-Communist Asia (excluding Japan)	0.4 - 0.6
Middle East (excluding Pakistan but including Egypt)	0.3 - 0.5
Latin America	0.8 - 1.0
Africa (excluding Egypt and Union of South Africa)	0.2 - 0.4
TOTAL	<u>2.5 - 3.5</u>

Since our purpose was to estimate the maximum amounts of foreign capital which underdeveloped countries could use productively, we may as well take

the higher end of the range as our figure for planning purposes, recognizing that actual demands are likely to be somewhat lower.

Our second question is whether levels of investment of the magnitude suggested in this table would be sufficient to launch the underdeveloped areas into a period of growing per capita levels of income. Computations are given in the Appendix which suggest that these levels of capital formation should produce rates of growth of per capita incomes of at least 1 or 2 per cent per year. The procedure used in this demonstration is roughly as follows: Starting with estimates of the national incomes of all the underdeveloped areas, one can make estimates of the capital output ratio which may apply in each region, that is, of the number of units of capital required to produce an increase of one unit per year in output. The capital output ration used in these computations was 3:1. This is believed to be a conservative, that is, a high, figure. The figure used in the Indian Second Five Year Plan, for example, is about 2.3:1.

Applying this capital output ratio to the levels of total investment which would obtain in the underdeveloped areas if the amounts of capital in the above table were supplied from foreign sources, one gets rates of growth of national income ranging from 2.5 to 3.5 per cent. Since population growth ranges from 1.5 to 2.0 per cent in most of the underdeveloped areas, the resulting per capital rates of growth of income are from 1 to 2 per cent per year. In countries already launched on the growth process, which will be making increasing contributions to capital formation annually out of their own resources, the rates of growth of per capita income may be somewhat higher.

India illustrates the general principles set forth above. Foreign

capital requirements for India included in the above table represent about 40 per cent of the level of capital formation achieved in India in 1953. India's Second Five Year Plan, beginning this year, calls for a much higher level of capital formation than in recent years. However, because India's national income has begun to grow, the proportion of her capital requirements that she can meet out of her own resources has also begun to grow. Her requirement for foreign capital for the Second Plan represents, therefore, less than 20 per cent of the investment programmed for the whole five year period.

The figure of 3.5 billion dollars arrived at above assumes that every country confronted with the possibility of securing whatever capital it can productively use will within two or three years be able to submit acceptable programs and projects which would utilize 30 to 50 per cent more capital than it has been investing in the recent past. At first, of course, the flow would be much less than the suggested figure. But we assume that, were a standing commitment to finance well-designed programs up to a given limit announced and maintained, what is called technical absorptive capacity could be stepped up on the average by about 40 per cent within about three years. Very few governments will make the effort of preparing national investment plans for which no resources are in sight, but once the assurance is given that capital will be forthcoming, their planning effort will increase considerably. We assume that after the announcement of the program we propose roughly two years might be required for the elaboration of well-prepared country programs and projects, and perhaps an additional third year for solving the problem of logistics (selecting proper equipment, purchasing organizations, etc.).

Thus, if all countries were equally efficient at working out acceptable programs and projects, a commitment made today of a target amount of annual aid should lead to disbursements beginning on a large scale only after about three years. If by this process absorptive capacity were increased by 30-50 per cent, the amount of foreign investment called for would be, at a maximum, about 3.5 billion per annum. This amount would make possible a rise in per capita output of at least 1 or 2 per cent per year. Technical absorptive capacity would continue to rise after the first three years by 5-10 per cent per year, but the additional capital required to take advantage of this rise could be supplied from domestic savings.

In practice, the rate at which countries will be able to qualify for capital will vary according to their stage of development. Some countries are probably prepared right now to absorb productively substantial additional sums (e.g., India); some might organize themselves to use sizable amounts in a few years (e.g., Indonesia); some may require a decade or more before the preconditions for effective investment on any scale are established (e.g., certain African regions). Thus it seems most unlikely that, if a commitment to make available 3.5 billion dollars annually is entered into, the rate of actual disbursement will rise above, say, 60 per cent of that amount. Thus, on the average, we would predict an annual actual flow, once the program got going, of something like 2 billion dollars.

It should be emphasized, however, that for such a program as we envisage to exert real pressure the commitment must be greater than expected disbursements. If the commitment is pared below the above-suggested figure, the actual disbursements will also fall at least in proportion. We regard it as of the highest importance that sums of the full order of magnitude

suggested above be offered to insure that capital is forthcoming whenever clear criteria for productive investment are met.

Where: The Money Might Come From

The maximum figure of 3.5 billion dollars refers to the total annual additional foreign capital inflow into the underdeveloped areas from whatever source. Present capital inflows constitute part of the base on which the 30 to 50 per cent addition was computed. Thus the 3.5 billion dollar figure is in addition to what is now flowing. It should be noted that the net capital flow abroad from the United States to the underdeveloped areas outside Latin America has been quite small. Only a very small fraction of our U. S. aid program has been devoted to capital for developmental purposes. The bulk of it has been either military assistance, general assistance to current budgets to permit recipient countries to maintain a large military establishment, or relief and rehabilitation in such areas as South Korea and South Vietnam. In Latin America there has been a good deal of American private investment, but it has been offset to a considerable degree by current amortization payments on foreign debt by the Latin American countries. Well over half the capital inflow currently going to the underdeveloped areas represents the provision of capital by the European countries to their Dependent Overseas Territories.

It is difficult to be precise about the breakdown of the 3.5 billion dollars by sources of supply. Under appropriate conditions there is room for a substantial expansion of private investment. Against the background of the intergovernmental effort envisaged, it is believed that over time major progress might be made in increasing the flow of private capital to the underdeveloped areas. Changes in the U. S. revenue code may help

encourage more direct investment, as would a revitalization of the transfer guarantee by the Export-Import Bank. The recently established International Finance Corporation (IFC), affiliated with the International Bank, is a hopeful device for encouraging the participation of private capital in international ventures. We would support the development of similar institutions, such as the Indian Development Corporation, within receiving countries.

Since successful private investment projects generally require a favorable environment in terms of developing local markets, available transport and communications facilities, and the like, their share in the early stages of development must necessarily be low. Public loans, by helping to create the necessary environment, can pave the way for greatly expanded private investment as growth takes hold. We should not set our hopes for private investment flows too high; but the effort to expand their role should be pushed with vigor.

The lack of success hitherto achieved in negotiating a more favorable climate for private investment should not be taken as evidence that further efforts will be futile. International private capital flows have been held up partly by insufficient availability of public credit and partly by political and psychological blocks which have perceptively diminished although they have by no means disappeared. In the context of this program it may well be appropriate for the international development council proposed in Chapter XI to explore a Free World code for capital movements which would incorporate the best lessons of recent experience in protecting both the international sovereignty of the recipient and the legitimate economic interest of the lender.

The International Bank could step up its lending rate substantially if new projects were eligible under its rules. Its resources for carrying on such operations could be expanded by additional sales of its securities

Of the remainder to be supplied through public channels, it is certainly desirable that a portion should come from other developed countries. Europe has expanded its own economic base enough since the war to make a significant additional contribution. In our judgment, the importance of generating substantial capital commitments from the well-developed countries of the Free World other than the United States cannot be overestimated. Joint creation of capital funds not only will make the concept of partnership more persuasive in the United States; it is also essential in order to impart the international character to the enterprise requisite for its acceptance and continued support in the underdeveloped areas.

The problem of what proportion should be loans and what proportion grants is also a difficult one. Grants would be appropriate primarily to countries at the earliest stage of development where the prediction of repayment capability is the most hazardous, and the credit-worthiness is limited. Since these will be the countries with the lowest technical absorptive capacity, it is reasonable to assume that grants would be a quite small part of the total.

On the basis of these considerations the supply of the maximum figure of 3.5 billion dollars might break down by source as follows:

Grants:

U. S. Contribution	\$ 360 million
Other country contribution	240

Direct Private Investment	500
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Additional International Bank Loans	400
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Public Loans:

U. S. Contribution	1,700
Other country contribution	300

TOTAL	\$ 3,500 million
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The American Contribution

Thus the maximum burden of our proposed program on the U. S. Treasury would be about 2 billion dollars per year, of which over 80 per cent would be loans. This maximum would almost certainly never actually be reached. It is based on maximum estimates of the absorptive capacity of the recipient countries on the assumption that they did everything within their power to increase that capacity. Actual demands for the first two or three years would be much smaller than this; and, because some countries will be much slower to develop absorptive capacity than others, the rate of withdrawals is unlikely ever to exceed 60 per cent or so of this figure, or a U. S. government obligation of about 1.2 billion dollars per year.

In addition to the capital program, the level of U. S. technical assistance, offered either directly or through the United Nations, should probably be raised about 100 million dollars per year. Also, we have made no allowance here for the special needs of Japan. Although Japan had passed into the third or self-sustaining phase of development before World War II, that war exposed her not only to serious physical destruction, but more important, to a reorientation of her trade which has not yet been successfully accomplished. If all the measures advocated in this paper were adopted, including the liberalization of trade restrictions and the supplying of capital without "buy American" strings, it would be our hope that the Japanese balance of payments problem could in the long run be largely solved. There will probably be a transitional period of five to ten years, however, during which loans of one or two hundred million dollars a year for Japan will be necessary. Taking all these things together, the total U. S. Treasury burden of a program such as is here advocated would not be likely to exceed

1.5 billion dollars; and this level would not be reached for several years, by which time the requirements for military assistance spending might have been somewhat reduced.

We must emphasize again, however, that while this is our best estimate of the amounts that would actually be drawn upon, it is an absolutely essential feature of this proposal that the amounts offered be sufficient to cover greater demands in the event that more countries should be more successful in increasing their capacity to use capital productively than we have assumed.

It is important to be clear as to the economic purpose of the proposed loans and grants. They would not be designed to meet a requirement for foreign exchange or for particular goods which can be supplied only from abroad. They would be designed to supplement the over-all resources of the underdeveloped countries in order to permit them to add to their productive equipment at a rate faster than would be possible without such loans. They would be used for the import of such equipment itself or for the import, for example, of food to meet the higher demand resulting from greater employment in developmental activities. Indeed, as explained in Chapter IX, a significant part of the total U. S. contribution could be in agricultural surpluses. Criteria would be rigidly set to prevent the use of loans and grants for an unproductive and temporary expansion in consumption.

One requirement cannot be shirked if the plan is to succeed. The United States must discover a device for guaranteeing a continuity in capital loans and grants which would avoid an annual Congressional renewal of the effort. Without a firm conviction that the U. S. portion of the effort

will be sustained, none of the larger benefits of the proposal can be envisaged. One possible device would be to appropriate the necessary funds in a once-for-all act, looking ahead, say, five years, leaving discretion for their release to the Executive Branch of the government, following broadly the technique of appropriation now used with respect to the Export-Import Bank.

On the tentative but not unreasonable criteria set out above, the U. S. government commitment in loans and grants might come to 2 billion dollars per annum, of which 1.2 billion dollars might be disbursed, on the average, if sound criteria for efficient use were applied. Thus, the initial Congressional appropriation, under the organizational principle set out above, might be 10 billion dollars for allocation over a five-year period.

We believe that a program conceived on this scale, stabilized for a substantial future period, founded on an incentive system which would remove the bottleneck of capital lack and throw the burden of responsibility on the developing areas, would maximize the pace of economic growth in the Free World.

Chapter XI

INSTITUTIONS TO CARRY OUT THE PROGRAM

Organizing the Job: Two Extreme Positions

One of the issues most hotly debated in discussions of programs such as the one presented in this book is how they should be organized. Many proposals have been put forward for channeling all assistance through an international body such as the United Nations. The most comprehensive of these calls for the establishment of a Special United Nations Fund for Economic Development (SUNFED) to which the developed countries would make contributions and which would in turn make capital available to those countries in need of it. On the other side of the argument are those who assert that the United States and other supplying countries neither will nor should turn over large sums for distribution by any such international body. Capital assistance, in this view, should continue to be arranged bilaterally so that the supplying country can satisfy itself that the resources it supplies are being efficiently used to promote objectives of which it approves.

The Real Issues

There are two issues raised by this debate which must be dealt with in any proposed institutional solution. In the first place, if any given underdeveloped country is to receive assistance from a number of different foreign sources, there must be some mechanism

for satisfying each lender that its contribution forms part of a consistent and coherent program. In other words, the supplies of capital from various different sources must somehow be coordinated and related to each other. In the second place, the issue derives most of its heat from the concern of the underdeveloped countries that the criteria to be applied in deciding whether assistance is to be supplied should be such as to protect those countries from undue political or economic influence from any other single nation. They believe that an international body representing a variety of different national interests is less likely to attach political or military strings to assistance and is more likely to rely exclusively on technical considerations of economic effectiveness in making loans and grants.

Looking first at the practical problems of coordination, it should be born in mind that international loan or grant activities are already being undertaken by a multitude of agencies. An underdeveloped country may deal with the Export-Import Bank, the International Bank, the U. S. International Cooperation Administration, the Colombo Plan, the national and international technical assistance agencies and other specialized agencies of the U. N., the agencies of governments of creditor countries other than the United States, and perhaps others. Proposals are afoot for the creation of numerous other instrumentalities. A program of the sort here proposed might be handled through one or more of these existing channels; through a new agency set up for the purpose; or through some combination of

new and existing agencies. It is tempting to suggest that all these operations be combined into one master operation under international direction which could insure coordination. This seems to us a bad and probably political unacceptable solution. There are many agencies now because there are many suppliers of many kinds of capital and many purposes for which capital is supplied. A large single organization would lose the advantages of specialization, would deprive lending countries of ultimate control over their funds, which some like the United States would be unlikely to accept in a program of the size proposed, and might be subject to some of the bureaucratic diseases of inertia and red tape which plague all large organizations.

But if programs are to be carried forward by existing agencies plus such new ones as the United Nations or lending countries like the United States may choose to set up, how is coordination to be secured so that the many different flows of funds produce a consistent integrated result?

Coordination

We propose that in the first instance the function of coordination be performed by the borrowing countries themselves. It is the borrowing countries which will be faced with the problem of how to make a series of separate loans and grants contribute to a unified result. If they undertake effective programming, and if they fit all capital inflows into the framework of the program, and if the program reflects international as well as national considerations, the necessary

coordination will have been secured.

There is still the question of how lending agencies are to be satisfied that these three conditions have been met without imposing on the borrowing country the necessity of explaining and defending in detail its whole program separately with each potential contributor. To meet this need we propose the establishment of an international body which would not itself dispose of any funds but which would collect and maintain information on development programs and on sources of funds on behalf of both borrowers and lenders, review and analyze development programs according to agreed criteria, maintain contact among various suppliers of funds to any given program, and in general act as a broker between countries needing assistance and countries and agencies prepared to supply it.

This body might have a quasi-legislative assembly consisting of representatives of all the capital supplying and all the capital receiving countries as well as organizations like the International Bank which participate in development activities. This assembly would meet infrequently for limited periods. The body would also have a small permanent secretariat which would maintain complete and current information on all international capital movements, on applications for grants pending, on all development plans and programs, and, so far as possible, on the status of progress under such plans and programs. It would also arrange for consultation among suppliers and participants relating to any particular program or set of programs. The usefulness and influence of this body would of course depend on how carefully it was set up and above all on

the calibre of the men who could be persuaded to staff it. If two or three of the most important capital sources, like the United States and the International Bank, and two or three of the most important borrowers, like India and Egypt, were determined from the start to give this body a real function to perform, we believe it could be an important focus for development activities and could satisfy in part the legitimate desire of many countries to see development assistance internationalized. If it acquired the respect of both lenders and borrowers, each country's programming authority would need to discuss its program with only one international agency, which in its turn would have liaison with all other agencies. Once the program was agreed upon, that is, once the priorities of sectors and projects were established, any agency would be free to participate in its financing. Individual lending agencies would presumably continue to make their own judgments concerning the feasibility of particular projects they were asked to finance, but they could rely on the international body for an advisory opinion as to whether and how such projects fit into a country's over-all investment program.

Maintaining the Criteria

This leaves the problem of internationalizing the criteria determining eligibility for assistance. It should be recognized at the start that this will be possible only if the most important suppliers are themselves willing to abide by criteria which could gain international acceptance. Unless the United States makes up its mind firmly that it will not attempt to use this program as an

instrument to pursue political or military objectives unacceptable to a number of Free World countries, there is no point in discussing international criteria. No institutional device will achieve something the Congress and the public have not decided they want to achieve. But if America does decide, as we believe it should, that its economic assistance under this program should be guided by the kinds of criteria outlined in Chapter VII and only by those criteria, there is real merit in an effort to secure international acceptance of the criteria. Our agreement to abide by such an internationally established code would be very important evidence to other countries that our concern with the success of their own internal development efforts was serious.

It should be made crystal clear that commitments to an international economic development program, governed by such general standards, would not preclude continued, parallel programs of military assistance. Nor would it preclude special bilateral economic assistance to countries which, in the American view, required it because of special circumstance; for example, Southern Viet Nam. The code would apply to that part of the nation's effort allocated to the international economic development program proposed here.

Machinery for establishing and reviewing such a code could be set up within the international assistance organization proposed above. The assembly of that organization could establish a small quasi-judicial council whose function it would be to draw up the basic code intended to govern the activities of grantors and grantees,

lenders and borrowers, to establish criteria to be applied in evaluating applications, and to review those criteria in the light of developments.

This council should consist of no more than perhaps ten members. They should be picked, like judges of the International Court, not as representatives of their countries but as individuals of great reputation and stature. A code of criteria and practices, once drawn up by such a council, should be ratified by the larger assembly. Similarly, modifications and amendments of the code should be subjected to ratification by the assembly. Membership on the Council should rotate, and members should be chosen from both supplying and recipient countries. In addition to establishing criteria, the Council might be called upon from time to time by either lenders or borrowers to pass judgment on the degree to which particular programs met the agreed criteria.

On the question as to whether the international body here proposed should be a presently existing agency of the United Nations given this new function or a new body integrated into the U. N. structure, we have no fixed views. Since the effectiveness of this organization will depend on its widespread acceptance, this should be determined only after extensive discussion with the proposed members.

It might be desirable to decentralize some of the information-gathering and coordinating functions of the international development body to regional organizations. For example, in Asia the

Colombo Plan organization, considerably strengthened and expanded, might perform some of these functions. This issue should be decided only after extensive consultation with both supplying and receiving countries to ascertain their views.

Whatever detailed organization may be finally agreed upon, the essence of it must be that it combines ultimate unilateral responsibility and control of funds with multilateral responsibility for the application of common criteria of eligibility and the coordination of capital supplies from different sources.

Chapter XII

THE PROGRAM IN SUMMARY

The proposals made in the foregoing chapters may be summarized as follows:

a. The United States should launch at the earliest possible moment a long-term program to promote sustained economic growth in the Free World. This program would make available to the underdeveloped areas sufficient additional capital and technical assistance to satisfy all likely demands for such assistance which meet fairly high standards of eligibility based on the prospective productivity of investment. The levels of investment assumed would be sufficient to make possible at least an over-all 1.5 or 2.0 per cent annual increase in real income per capita for all the underdeveloped countries of the Free World. In practice, some would grow faster, some slower than this rate.

b. As part of this program the U. S. government should offer to provide a new long-term capital fund of from \$10 to \$12 billion to be available over a five-year period for loans and grants to accelerate economic growth in underdeveloped areas. In many cases individual loans and grants should be in the form of standby agreements covering the full period of a development program. Although an initial five-year allocation is recommended, the plan would look ahead for a longer period, at least a decade.

c. This sum should be accompanied by commitments from the governments of other advanced industrialized countries to make additional loans and grants of from \$2 to \$3 billion over the same time period as part of a unified Free World program.

d. Concerted measures should be taken to enlarge the international flows of private capital. Such measures might yield an addition over present levels of \$2.0 to \$2.5 billion during the first five-year period.

e. These sums must be made available to Free World countries without any military or political strings, but under strict businesslike criteria designed to guarantee that the loans and grants could be effectively used and that the loans could be repaid within a reasonable period of time.

f. Although it is most unlikely, if such criteria are enforced, that the whole of the sums offered would be taken up, it is essential that availability of the full amount be guaranteed in order to remove lack of capital as a bottleneck to economic growth and to provide maximum stimulus for the governments and peoples of the underdeveloped countries to expand their capacities to use capital effectively.

g. A systematic plan should be worked out for establishing international stocks of agricultural surpluses to be made available for development purposes. Such a plan must insure that distribution of such stocks would not interfere with the normal markets of exporting countries.

h. Loans and grants should be administered by existing national and international agencies, including the Export-Import Bank, the International Bank, and the Colombo Plan organization; but new machinery must be created to set the ground rules and secure acceptance of the criteria for the investment program.

i. If the U. S. capital made available under this program is to have its full potential effect in providing a lubricant to international trade, we must refrain from attaching "buy American" conditions on our contribution.

In addition, if we are to persuade the underdeveloped countries and the other industrialized nations to move toward an increasing volume of trade and an effective international division of labor, we must set a more persuasive example by pursuing more vigorously the relaxation of our own barriers to international commerce.

We cannot emphasize too strongly that this program will not achieve its basically political and psychological purposes unless its fundamental features are preserved. Dilution could prove extremely dangerous. The sharp edges of policy which must be preserved appear to be these:

1. The additional sums envisaged must be large enough to remove lack of capital as a bottleneck to growth, under the tough criteria of productivity envisaged.

2. There must be no tie between economic aid and military pacts; and no explicit political conditions within the Free World beyond the requirement that development goals be democratically established. An aid program with strings yields satellites, not partners.

3. The plan must look to a long future and envisage a sustained U. S. effort.

4. There must be a real measure of international contribution and international administration.

Chapter XIII

THE PROPOSAL IN THE SETTING OF NATIONAL POLICY

It is time, now, to draw back from the details of our proposal and to examine how it relates to fundamental American interests; how it relates to the threats which confront the nation; how it could affect our relations with the Communist Bloc. This appraisal requires a definition of the national interest and a characterization of the dangers we face.

What is the National Interest?

The fundamental task of American military and foreign policy is to maintain a world environment for the United States within which our form of society can continue to develop in conformity with the humanistic principles which are its foundation. We must, of course, physically protect our own country; but the protection of American territory is essentially a means to a larger end--the protection of our still-developing way of life.

If the problem of national security is viewed in these terms--not merely as a question of protecting the nation's real estate but its basic values as a society--it follows that the United States has two distinct but connected interests in the vast continent of Eurasia. Since the combined resources of Eurasia could pose a serious threat of military defeat to the United States, it is our interest that no single power or group of powers, hostile or potentially hostile to the United States, dominate that area. Since, whatever the military situation might be, a Eurasia under totalitarian dictatorships would

threaten the survival of democracy both elsewhere and in the United States, it is equally our interest that the societies of Eurasia develop along lines broadly consistent with both our own conception of the proper relation of the individual to the state and with their own cultural heritages.

We do not seek societies abroad built in our own image. We do have a profound interest that societies abroad develop and strengthen those elements in their respective cultures that elevate and protect the dignity of the individual as against the claims of the state. Such elements of harmony with the Western democratic tradition exist in different forms everywhere; and they have been strengthened by the attractiveness of the Western democratic example at its best, notably by the example of the American revolution and the values on which, historically, our society was erected and on which, by and large, it has subsequently operated.

We have, in short, a major and persistent stake in a world environment predominantly made up of open societies; for with modern communities it is difficult to envisage the survival of a democratic American society, as an island in a totalitarian sea.

In terms of geography, it is a persistent interest of the United States that no single power or power grouping militarily dominate either Western or Eastern Eurasia. In Western Eurasia the threat of such an outcome is posed for us by the virtual absorption within the Soviet empire of East Germany and Eastern Europe. The threat would become virtually a reality should West Germany be lost to the Free World. In the East the threat of such an outcome is posed for us by the close

alliance of the Soviet Union and Communist China. The situation in Asia is, however, more complicated than in Europe. Whereas in Europe West Germany, by and large, is the crux of the matter, in Asia there is Japan on the one hand and the whole area of Southeast Asia on the other, Southeast Asia stretching from Indo-China around Thailand, Burma, Malaya, Indonesia, India, and Pakistan. In Asia the threat would become virtually a reality should either Japan or Southeast Asia be lost to the Free World.

It is plain, then, that the Communist world poses two threats to the United States--a military threat and an ideological threat. These threats are clearly related: the ideological loss of India, for instance, would raise important military problems; the military loss of northern Indo-China has raised important problems of ideological orientation throughout Southeast Asia. But the two American interests are not and should not be considered identical. The time necessary and the kind of effort required to cope with the military threat are likely to differ from those required by the ideological threat. The military threat to South Korea was dealt with in a few years; defeating the ideological threat to South Korea may prove a creative Free World task for a generation.

If this view of the American interest is correct, the debate which has been proceeding in the United States over recent years as to whether the nation's interests should be defined in power terms or in terms of the ideological principles to which American society is attached, is a somewhat misguided debate. This is so in two respects.

First, if the essential American interest is to preserve a world environment within which our form of democratic society can persist and develop, then the nation's stake in the ideological and political balance in Eurasia is as legitimate as its interest in the military balance of power in Eurasia. Two national efforts, one military and the other political, interacting intimately, must go forward together as part of a total effort to protect the interests of American society.

There is a second sense in which the debate appears misguided. It appears to be a characteristic of American history that this nation cannot be effective in its military and foreign policy unless it believes that both its security interests and its commitment to certain moral principles require the nation to act. From the Spanish-American War to the present the nation has acted effectively only when both strands in its interest were believed to be involved: in the Spanish-American War itself; in the First and Second World Wars; in the effort to reconstruct Western Europe, in 1947-1950; in the early phases of the Korean War. When idealism alone seemed to be the basis for the positions we have taken, the nation did not back its play; for example, in the Open Door Policy and in Wilson's ideological formulation of the American interest at Versailles. Equally, the nation has not been effective when it is confronted with situations where its power interests might be involved but where a persuasive moral basis for American action was not present. The notion of American imperialism, popular in certain American circles at the turn of the century, died quickly when it confronted the deep American instinct in support of political independence, in the case of the Philippines and elsewhere. Similarly, a major reason

why the United States was ineffective in the Indo-China crisis of 1954 was that it was then extremely difficult simultaneously to deal with the Communist menace and to disengage from French imperialism in that area.

In general, then, a sound American policy should be based on a day-to-day awareness of the military and nonmilitary actions required to defend and perpetuate the quality of our society as well as to maintain its physical security and upon an awareness of the American need to believe that both interests and ideals are at stake, before sustained and effective public support can be evoked. The art of American statesmanship is to formulate causes of action which harmonize in specific settings, abiding American interests and abiding American ideals.

The Threats to the American Interest

In the light of this conception of the American interest it is possible to define in reasonable order the threats which the nation now faces. The American interest is threatened by three potential forms of Communist military aggression. It is also urgently and immediately threatened by the psychological, economic, and political offensive now being conducted from Moscow and Peking, designed to disengage the United States from power and influence in the Eurasian continent. The military and nonmilitary aspects of Communist policy are closely linked. In addition to these immediate military and nonmilitary threats, the American interest faces a long-run danger of isolation from Eurasia, quite independent of current Communist activities and independent, even, of the existence of a world-wide Communist movement. This whole spectrum of threats can be defined as follows.

The Three Military Threats

The most obvious danger the United States confronts is that the Soviet Union may acquire in the technological arms race a lead sufficient for the men in Moscow rationally to envisage a sudden attack designed to eliminate American retaliatory power at a blow. The achievement of such a decisive lead is by no means easy in the modern world; and it should not be identified with a lead in one form of delivery technique; for example, the possible current Soviet edge in medium range and intercontinental guided or ballistic missiles. It is possible for one power to have a very substantial lead over the other and still find it irrational to envisage an all-out attack, because it could not count on sufficient destruction of the other's retaliatory power to avoid grievous if not decisive damage being done to its own society. Nevertheless, notably in the case of long-range missiles, it is evident that the first charge on American security policy is to avoid any possibility of being so outstripped technologically by the Soviet Union as to be vulnerable to the wiping out of the American retaliatory force in a single wave of attack.

While the danger of a successful Soviet aerial blitzkrieg is real but not imminent, the erosion of the American military position in Eurasia, because of Soviet equality or superiority in weapons of mass destruction, is already under way. The Soviets have succeeded over the past decade in rapidly closing the gap in weapons of mass destruction, in the means of their delivery and in the means of defense against them. They have used this developing capability to support, in effect, a program of political blackmail. By means which are either subtle

or unsubtle, as occasion demands, Moscow is telling American allies and potential allies that American military strength can no longer protect them; that should major war come, the United States could not prevent their national destruction with Soviet weapons. Therefore, Moscow argues, the only rational course for other countries is to disengage from alliances with the United States, an argument of some evident persuasiveness from Iceland to Ceylon. This policy of blackmail almost certainly could not be effective if conducted in Stalin's inimitable style: by and large when men are sufficiently frightened they cling together and exhibit considerable courage in the face of the raw threat of force. The present Soviet leadership, however, has conducted its policy of threat with some subtlety. It has gained considerable force from the fact that it is accompanied by a psychological, political, and economic policy that is designed not merely to make association with the United States unattractive but also to make association with Moscow more attractive. Soviet policy is now an extremely effective mixture of stick and carrot; and it threatens to break up the American military alliances in Eurasia and to disengage us from some of our major overseas bases.

The third military threat is that of limited war conducted under circumstances where the United States finds it impossible to bring into play the major instruments in being of its military strength; that is, American air and naval power, applying atomic weapons. By and large Moscow and Peking have behaved since the summer of 1951 as though they regarded limited war as an unsatisfactory instrument

for expanding Communist influence and authority. Nevertheless, in Asia, the Middle East, and Africa the Free World is vulnerable to degrees of military aggression, along the lines of the Free World's experience in Greece, Berlin, Malaya, Indo-China, and (least likely) Korea. The degree of vulnerability to limited war depends in substantial part on the political, social, and economic soundness of various Free World areas, since the effective use of Communist techniques of limited war hinges on the exploitation of weak, divided societies and the internal disintegration that follows. In the revolutionary transitions through which many societies in the Free World are now passing we can mitigate periods of weakness and division by our nonmilitary policy, but we cannot guarantee that they will not occur. We cannot, therefore, rule out the possibility of having to face "brushfire" wars.

These problems may assume two distinct forms corresponding to two different possible Communist strategies. One now familiar form of outbreak could arise where external Communist support is given a local insurrectional group, within which Communist leadership is predominant. We have confronted this kind of problem, for example, in Greece, the Philippines, and Indo-China. In these situations the Communists hope that by backing militarily a faction over which they have pretty complete control, they can directly gain control over a disputed area.

A second form of outbreak may be more probable in the future. It is a cardinal principle of Communist doctrine that in areas where an immediate seizure of power by a Communist Party is not possible their

long-run interest is best served by weakening "bourgeois" governments in any ways that present themselves. Outside Communist dominated areas their purposes are served by encouraging chaos and conflict. This is the kind of problem faced potentially in the Middle East, in Kashmir, and in parts of Africa. It is an evident interest of Moscow to promote such disruptive schisms in the Free World by raising the level of tension, sometimes egging on both parties to a conflict, even though there are in prospect no immediate gains for local Communists. The American interest, on the other hand, is opposed to the heightening of tensions anywhere since the long-run constructive forces which we believe will assert themselves if they have a chance cannot operate in crisis situations. Men who are close to violence cannot direct their full energies to building stable, effective societies. American nonmilitary as well as military policy must be designed to cope with this second type of brushfire as well as with the first.

The Urgent Nonmilitary Threat

The most evident and urgent threat to the American interest now consists in the psychological, political and economic policy by which Moscow and Peking seek progressively to eliminate the United States from influence and power in Eurasia, and, in appropriate stages, to draw the nations of Western Europe, the Middle East, Africa, and Asia into the orbit of communism. Moscow's method is to associate itself systematically with the aspirations of the people of the Free World for peace, economic progress, and political independence. This policy

has been under way since, roughly, the summer of 1951; it was articulated by Stalin at the Nineteenth Congress of the Communist Party in 1952; it was developed with great vigor and tactical imagination after Stalin's death; and it has been notably reinforced by the dramatic, symbolic acts of the Twentieth Party Congress in 1956, notably the theological demotion of Stalin and the elevation to unique ideological stature of Lenin.

The political, economic, and psychological elements in the present Soviet and Chinese Communist offensive are being adapted with skill to the problems and possibilities of different areas in the Free World. In France and Italy the principal emphasis is on the building of Popular Front governments and creating an environment in which they are likely to thrive. In Germany the bait of German unity is being steadily held out in return for a rupture of the NATO tie. In Britain and Japan as well as in Western Germany the possibilities of trade with the Communist bloc are held forth. In the Middle East the association with unsatisfied national aspirations is linked with credits, technical assistance, and trade in products difficult to market within the Free World under current circumstances. In Southeast Asia the objective is to use very economic, political, and psychological devices to encourage neutralism wherever it exists and to create the foundations for the development of local communism on a Popular Front basis.

In the context of American policy over the past five years the Soviet offensive is formidably effective. It threatens not only to undermine politically American military alliances and the possibility of maintaining the American base structure, but it threatens also to

reduce progressively the political influence of the United States in Eurasia and to open the way for later degenerative processes that might make possible actual Communist takeover.

A Longer Run Danger to the American Interest

In the opening of this chapter the American interest was defined in terms which include but transcend the problem of countering Communist aggressive objectives and techniques. The American interest has been rather considered to be the maintenance of a military and political environment in Eurasia such that American society can continue to develop along lines consonant with the nation's basic historic values. At the moment the spectrum of threats which confronts the nation stem from a systematic exploitation by Moscow and Peking of certain conditions within the Free World. Looking ahead over the next 50-100 years, however, it is altogether possible that the United States could be confronted with major dangers even if communism should wither away or even disappear as an effective international force. Specifically, there are two long-run dangers. The first is that the underdeveloped areas develop along lines hostile to the West and Western tradition. The populations of these areas constitute a very high proportion of the world's population. Should their basic orientation be anti-Western and anti-American, the United States would confront a very grave set of problems as their societies were modernized and their strength became more effective. And such an evolution is not at all impossible. The colonial heritage of these regions, their powerful latent sense of hostility due to the problem of color, the difficulties through which they will have to pass if they are to gain modern status for their

societies, all might well lead to attitudes of fixed and dangerous hostility which might eventually split the world on new lines. It is an American interest from the present forward so to associate ourselves with the evolution of these underdeveloped areas that the possibility is maximized that when they emerge to modern status the lines of association rather than of conflict between the United States and these areas are dominant. Their aspiration for the values of individual dignity, national independence and material welfare make the triumph of these more hopeful strands by no means impossible.

The Role of the Proposed Program

The proposal made in this book emerges, then, as a substantial portion of a total policy designed to protect the nation's interest against the threats which confront us, both in the immediate future and, foreseeably, over the longer term.

It is, of course, no substitute for an adequate well-designed military policy; although it is an indispensable element in a policy designed to minimize the possibilities of limited war in the underdeveloped areas. And, as the arms race in major weapons moves into what may be a protracted stalemate, this kind of war may be the most real form of military engagement we confront.

It is a positive answer to the immediate threat posed for us by the current political, economic, and psychological offensive of the Communist bloc.

Over the long pull, it is the most promising instrument we can devise to assure that the industrialized and underdeveloped areas ultimately emerge from the present revolutionary phase of history as part of common, harmonious world community, dedicated to the proposition that the state is the servant of the individual.

Relations with the Communist Bloc

How might a proposal of this kind affect our relations with Moscow?

Its first and fundamental consequence would be to place the current Communist offensive in the underdeveloped areas in perspective and reduce its effectiveness and its danger to the Free World. The Communist offensive has gathered strength mainly because there has been a vacuum in American and Western policy in this area. It is a firmly established fact that a number of leaders in the underdeveloped areas, having taken the measure of Moscow's intentions, are anxious to rebuild their relations with the United States and the West on some such basis as that proposed here. The Communist offensive is clearly opportunist in character and disruptive in intent.

Against the background of a gap in American and Western policy, that offensive has exercised a strong attraction in the underdeveloped areas and has had important effects. Against the background of an American initiated program of the kind proposed in this book, it would be vastly less impressive.

The United States and the Free World generally might then examine its economic relations to the Communist bloc in a new setting of poise and confidence.

Specifically, two questions arise: (1) what position should we take with respect to participation in the program by Soviet bloc countries, and (2) how might our policy with respect to East-West trade be affected by the plan.

Communist countries might participate in two opposite sense. The Soviet Union itself could supply some capital for development, while some of its satellites, particularly China, might be potential recipients of loans. Our calculations of capital requirements and possible sources of supply have all been made on the probably reasonable assumption that the entire Soviet bloc would remain outside the program, both as lenders and as borrowers. Consideration should nevertheless be given to whether Communist countries should not be invited to participate on the same terms as everyone else. No particular problems would seem to be raised by inviting contributions from Russia, so long as Moscow would agree to the kinds of criteria which the Free World would regard as acceptable, and so long as the question of Soviet participation was not permitted to slow down the development and execution of the scheme. If Moscow is invited to participate in order to remove the "economic competition" from the cold war, it must evidently be on the basis of no veto power in the international development body. On this condition there would seem to be every reason to make the invitation. If it is accepted, much of the political advantage Moscow has secured from the competition would be gone. If it is rejected, it will be a clear signal to the world that the Soviet Union wishes to use aid as a bilateral political tool. With a major, sustained Western initiative under way, based on positive principles, we could afford to let Moscow contribute as it would to the development of the Free World. There is no need for a purposeful, active Free World, grappling with its common problems on the scale those problems require, to take fright at the presence of a handful of Soviet technicians or even at Soviet credits and trade.

As to the satellites, some of the Eastern European states could only qualify as contributors; a few (probably Bulgaria, Rumania, and Albania) might qualify as borrowers, in addition to Communist China. The criteria of submission of detailed economic plans of potential borrowers for international inspection and approval would, however, almost certainly exclude them in practice. The desirability of making the gesture would have to be determined by weighing the possible dangers of such a move against the not inconsiderable virtues of being able to announce that the plan is open to every country in the world which is willing to abide by the wholly nonpolitical conditions set upon participation.

For Moscow, of course, the proposed program would create an acute dilemma. The present Soviet policy in underdeveloped areas is based on a failure of the United States to associate itself positively with their constructive aspirations.

If the proposed program were successfully launched Moscow would face the hard choice of joining it as a junior member, under circumstances likely to advance Free World interests or proceeding on its present bilateral course under unpromising circumstances, so far as Soviet purposes are concerned.

With respect to East-West trade we believe that this plan, if put into operation, might render this issue a less divisive one in the Free World than it is at present. Important groups in Europe and Asia have seen in an expansion of East-West trade one solution to the international economic problems of their countries, and have therefore strongly opposed our policy of restricting such trade.

It is our view that in fact their hopes of a real solution in trade with the Communist bloc are in many cases illusory. The economic position within the bloc combined with its political policies make it in fact most unlikely that any substantial increase in East-West trade would take place if all controls by the West were dropped. It is certain, for example, that Communist China could not supply the commodities needed by Japan, on the requisite scale, without dismantling its trade ties with the Communist bloc: an outcome not in sight. Recent Soviet purchases of rice from Burma and cotton from Egypt have suggested dangers from the emergence of the Soviet bloc as a major buyer of agricultural surpluses. If the selling countries can sell their surpluses to no one else and can secure capital for development in no other way, this is indeed a disturbing phenomenon. But if the West provides alternatives, we do not have to be concerned about the Soviet lure.

Our allies, both the developed countries like Germany, Britain, and Japan, and the underdeveloped ones like Burma and Egypt, will tend to be attracted by dangling offers of East-West trade so long as they feel the pinch of inadequate Free World markets and inadequate supplies of nondollar foodstuffs and raw materials. Moscow and Peking can be relied upon to exploit this sense of marginal strain so long as it exists. These proposals, taken as a whole, would in our judgment permit a solid Free World solution without East-West trade, leaving the Free World to take or leave trade with the Communist bloc as it suited Free World interests.

Politically, East-West trade is neutral. Depending on the posture of the two trading partners, it can just as well pull on the East as on the West; or it may not pull either way. The basic rule of the West should be: the only safe East-West trade is that trade we are prepared to redirect on short notice. This requires, in general, a viable growing Free World economy of the kind envisaged in these proposals. It may require, in addition, special stockpiling provisions for those commodities coming from the Communist bloc, designed to permit a quick transfer of source of supply.

Against such a background the Free World would be able to play the game of East-West trade from a position of strength, on a take-it-or-leave-it basis.

Generally speaking, then, the proposal presented here should remove the dangers arising from the blandishments of Communist economic foreign policy and permit the Free World to proceed with its business, with or without Communist participation and East-West trade, from a position of poise and confidence.

Chapter XIV

THE AMERICAN MISSION

In its essence, our proposal calls for a sustained effort by the United States to associate its purposes and efforts with those of the aspiring new nations in the underdeveloped areas. Quite aside from its virtue as a means of protecting the national interest this association could have profound and wholesome effects on the quality of our domestic life.

The United States has now come close to solving the range of issues which dominated its political life since 1865. Broadly speaking, the central problem was to reconcile the fact of industrialization with the abiding principles of democracy. The farm problem, the status of big business in a democratic society, the status and responsibilities of organized labor, the avoidance of extreme cyclical unemployment, social equity for the Negro, the provision of equal educational opportunity, the equitable distribution of income--all these great issues are certainly not wholly solved, but there is a national consensus on them within which we are clearly moving forward as a nation. The achievement of this consensus absorbed the bulk of the nation's creativeness and idealism over the past ninety years. If we were to continue to devote our attention in the same proportion to domestic issues, we would run the danger--like, say, Sweden and Switzerland--of becoming a bore to ourselves and the world. We would be quarreling over increasingly smaller margins, increasingly narrower issues, and, essentially, enjoying the material

fruits of a very rich and somewhat complacent society, progressively isolated from the vital issues of the rest of the world.

Our proposal does require that the United States allocate increased resources for loans, technical assistance, and, perhaps, some grants to other nations. The order of magnitude of these increased outlays are, however, exceedingly modest. Our annual gross national product is of the order of \$400 billion, and it should regularly increase each year by about \$12 billion. There is no question here of sacrificing our standard of living or of disrupting the workings of our economy. We can obviously afford to do the job. What is required to launch and execute this proposal is will, understanding, and a positive sense of our national purpose on the world scene.

From the revolutionary beginnings of our history the United States has, on balance, acted in loyalty to the conception that its society had a meaning and purpose which transcended the nation. Down to the present day the peoples of the United States and of the world in general have not wholly lost the sense that this nation represents a continuing, unique experiment in the development of free societies. If over the coming decades the United States should turn its back on the great revolutionary transformations going forward in the underdeveloped areas, devoting itself almost exclusively to domestic chores and objectives, American society might progressively lose some of those basic spiritual qualities which have been historically linked to the nation's sense of world mission. The nation runs the long-run danger of helping bring about, by its own spiritual decline, a kind of self-enforced isolation which, should it

come about, would further damage the military and nonmilitary bases of national security.

On the other hand, the execution of the proposals presented in this book require an active rededication to the fundamental principles which have given American life its distinction, its transcendent quality. The nation will have to sustain an effort at association over many years, with its taxes and its talent, its sympathy and understanding. It will have to learn much of other peoples and come to know problems which the United States has long since outgrown or which it never faced.

All of this is to the good; for America at its best has never wholly lost a sense of the community of human destiny:

One thought ever at the fore--
That in the Divine Ship, the World, breasting
Time and Space,
All peoples of the globe together sail, sail the
same voyage,
Are bound to the same destination.