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**FOREIGN ECONOMIC AID  
BACKGROUND AND MAJOR POLICY CONSIDERATIONS**

**STAFF PAPER**

**THE UNITED STATES COUNCIL  
of the  
INTERNATIONAL CHAMBER OF COMMERCE**

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## FOREWORD

In the opinion of the members of the Committee on Foreign Investment and Economic Development foreign aid is one of the most important and complex problems facing our country.

Particular attention is now being given in this country to that part of our foreign aid designed to assist other nations speed the rate of economic development. There are different views as to the wisdom of extending such aid. There is an even greater divergence of views concerning the nature and form which aid to economic development should take.

Because of the importance and complexity of the questions involved in development aid, the Committee has agreed to conduct continuing discussions of this field. As a first step, the Committee asked the staff of the Council to prepare a background paper setting forth the basic questions of policy concerning development aid. The Committee found this paper useful. It felt that other members of the Council would likewise find the paper useful and requested its publication. It is particularly timely now to members of the U.S. Council since economic development is one of the main subjects for discussion at the XVIth Congress of the International Chamber to be held this May at Naples.

The Committee will welcome the views of other Council members on any of the policy questions raised in the paper.

August Maffry  
Chairman of the Committee  
on Foreign Investment and  
Economic Development

FOREIGN ECONOMIC AID:  
BACKGROUND AND MAJOR POLICY CONSIDERATIONS

Foreign aid is today a major instrument of United States foreign policy. Tax financed aid (unlike private foreign aid) can have no justification if it does not contribute as much to national security and welfare as money spent on other purposes.

This brochure sets forth briefly the major policy questions concerning economic development aid, i.e. that part of our foreign aid which is rendered to increase the rate of economic growth in under-developed countries. Development aid is used here to include technical assistance and grants or loans of capital.

An organization of businessmen can most profitably concentrate its attention on this part of our foreign aid program. The other components of our aid are less appropriate topics for such an organization to consider. The reconstruction phase following World War II, once a major aid objective, has now ended. Military aid is largely determined by strategic considerations. Emergency aid to other countries following a disaster such as a major crop failure requires a case by case determination.

Before attempting to appraise the role of development aid it will be useful to state what seem to be the dominant facts which our foreign policy must meet.

I. THE MAJOR ELEMENTS OF THE CURRENT SITUATION

A. The rising power and continued hostility of the U.S.S.R.

Although the Soviet bloc contains 900 million people and a land area four times the size of the United States, it is still smaller than the United States in economic terms. Steel production in the Soviet bloc, for example, totals only sixty million tons annually, compared to 120 million in the U.S.

In the U.S. we generate three times as much electric power as the Soviet bloc. If the resources of Western Europe are added to those of the U.S., the economic predominance of the Atlantic group of nations is much greater.

The rate of economic growth in the Soviet bloc is higher than in the U.S. and considerably higher than in Western Europe. Economic growth in the Soviet bloc has been uneven with much greater emphasis given to capital goods than to consumer goods. A recent study by the Council on Foreign Relations concluded that the present rate of growth in the Soviet bloc is roughly one and a half times that of the Western nations and saw no basis for assuming that this rate of growth will diminish substantially. It is estimated that gross investment in the Soviet Union currently amounts to a quarter or more of the gross national product whereas in the United States gross investment has fluctuated between one-sixth and one-fifth of gross national product.

In spite of the higher rate of growth in the Soviet bloc, at present the annual absolute growth in the West each year is larger. The larger economic base in the West accounts for this difference between the rate of growth and the absolute growth of the two areas.

The present rulers of the U.S.S.R. seem committed to the ultimate destruction of the United States and other western nations. Recently, for example, Khrushchev boasted that the communist nations will be on hand to "bury" the democracies. In pursuit of this objective the U.S.S.R. is pressing its economic penetration of the underdeveloped nations. It is estimated that the U.S.S.R. over the past three years has extended some \$1.2 billion of aid to these countries in the form of long-term, low-interest credits and other types of assistance. Furthermore, the Soviets are making intensive efforts to send their technicians to the underdeveloped nations. Economic

penetration of Afghanistan, Egypt, India, and Syria has been particularly notable. Poor performance on trade agreements, however, has caused the U.S.S.R. to lose ground in some countries.

B. Rapid changes occurring within Atlantic community

Far reaching changes are occurring in Western Europe which will alter our relations with our closest allies. The United Kingdom and France face grave difficulties. Both nations have weakened their relations with the underdeveloped nations. Both have failed to solve the problem of inflation and suffer chronic trouble with their balance of payments. Both will be affected by the continued uncertainties over the availability of middle eastern oil.

Another major development in Western Europe is the proposal to create a common market among the six nations of the European Coal and Steel Community. If this plan goes forward, a new economic grouping will have been formed with a skilled and disciplined population equal in size to the United States and with a combined output of roughly one fourth that of the United States. This group of nations today supplies us with one tenth of our imports and is the market for one seventh of our exports. Great Britain and other European countries may also become associated with the common market through a free trade area. If these plans mature we can expect that Western Europe as a whole will be in a position to act with more vigor and independence than has been possible since World War II.

C. The demand of the underdeveloped nations for a more rapid rate of economic growth.

1.2 billion people live in the underdeveloped, non-communist lands of Asia, Africa, the Middle East, and Latin America. Conditions vary widely among these countries as regards endowment of natural resources, population pressure, political tradition, present outlook for economic growth, and

so forth. They have in common a very low level of income (usually less than \$200 per capita), shortage of capital and savings, widespread disease and ignorance. They share an intense desire to improve their own economic situation. Those nations which were formerly colonies also have great sensitivity against anything which seems to them to resemble a renewal of colonialism.

In many of these countries impatience for rapid results and a shortage of private entrepreneurial talent and capital have led to governments taking considerable initiative in planning national economic development. Some of these countries proclaim themselves socialist, and in some foreign private investment has been viewed with suspicion.

D. The growing dependence of the United States on foreign sources of raw materials.

Today the United States is a net importer of raw materials to the extent of about ten percent of our domestic needs. The President's Materials Policy Commission estimated that with proper policies we will be able to import roughly a quarter of our raw materials needs by 1975, and even at that the PMPC considered that the net drain on our domestic resources would be greater than desirable. We are almost totally dependent upon imports for our industrial diamonds, tin, nickel, asbestos, chromite, graphite, manganese, mercury, mica, tungsten, and cobalt. Our dependence on imported copper, lead, zinc and iron ore is rising sharply.

As the PMPC made clear, the choice before this country is not between expanding our dependence upon foreign sources or facing ruin. The choice is between seeking the lowest cost sources of raw materials (whether foreign or domestic) or seeing the cost of production in this country steadily rise because of undue reliance upon higher cost domestic sources.

## II. PAST EXPERIENCE WITH FOREIGN AID

The U.S. has been extending foreign aid of all types continuously since the end of World War II. To date this aid has amounted to over \$55 billion. This aid has been given for a wide variety of purposes: emergency relief, reconstruction of war destruction, rearmament of friendly nations, support to help maintain larger armed forces than a nation could afford, and to stimulate economic development. Of these various purposes we have had most obvious success and have spent by far the greatest share of our aid on reconstruction and assistance to nations in increasing their defense capacities.

Since the start of the Marshall Plan in 1948 through the middle of 1956 according to International Cooperation Administration reports only about \$1.4 billion has been committed on actual economic development aid. The regional shares have been roughly as follows: Latin America \$115 million; Africa \$45 million; Far East and South East Asia \$390 million (primarily India); and the Middle East \$635 million (three-fourths to Israel and Iran). This aid has financed technical assistance and some capital development. Some of the assistance which we have given in support of foreign military forces has also been of an essentially development nature. Recently we have also begun to move our agricultural surpluses to some of these nations as a form of economic aid. Under the agreements to sell these agricultural products, the major share of the proceeds from the sale of these goods is accumulated by the recipient government as a source of development capital.

## III. THE MAJOR POLICY QUESTIONS

1. What contribution can a program of development aid make to the security and general welfare of the U.S.?

This is, of course, the most basic question since an answer of "little or none" would lead to the conclusion that there should be no development aid

program. Insofar as an answer has been given by the interplay of presidential and congressional action, it is on the side of saying that at least a modest expenditure for these purposes is clearly in the national interest. So far there has been fairly limited experience with what outside assistance to economic development can do.

The importance of keeping the underdeveloped lands independent of communist control and reasonably stable is apparent. We cannot expect to maintain our free society surrounded by hostile, totalitarian states. Many of these countries have ancient cultures which can add to the richness of our own lives and provide stimulus for our own creativity. The underdeveloped lands supply many of the raw materials for the developed nations. They contain nearly half of the world's population.

Past experience indicates that economic development as such will not insure political or social stability. The process of growth may even be a disturbing factor as old social patterns break down. However, if the people of a country feel that economic conditions are improving, even if only slowly, they are likely to support the existing regime. It is also important to social stability that the people of a country feel that rewards and burdens are being distributed in an acceptable fashion, that the government is not corrupt, and that basic human rights are honored.

Economic aid cannot insure that there will be economic development. The process of economic growth is complex. In the typical underdeveloped country long-standing attitudes which may be opposed to business or other practical pursuits must change; the level of education must be substantially raised; the appropriate balance must be struck between the various branches of economic activities so as to avoid shortages and wasteful surpluses; the willingness to save and invest must be increased; and so forth. Foreign aid

can help to reduce the force of two factors which retard economic growth:

- (a) the shortage of capital which exists until an economy reaches a stage where it can generate enough savings to finance its own further growth; and
- (b) the shortage of people trained in the necessary skills.

2. What conditions should be attached to our development aid?

Since foreign aid is an instrument of foreign policy, it should be used as effectively as possible to advance our total foreign policy. There has been a tendency, particularly in the Congress, to interpret this position to mean that we should attach to our economic development aid conditions which relate to other parts of our foreign policy. The Battle Act imposes the specific conditions that a nation must agree to prevent the shipment of strategic goods to the Soviet bloc if it is to receive economic aid. One of the factors causing Congress to reduce aid to India in the past was dissatisfaction over Indian foreign policy - a strongly implied condition for further aid.

When conditions of this sort are attached, however, a problem is always created as to whether reduction or withdrawal of aid to enforce compliance does effectively contribute to our overall objectives. Since the non-economic conditions we have attached to our economic aid relate to matters which both we and the recipient countries consider highly important, it should be expected that when disagreements occur the question of whether or not aid is continued at a certain level may not be of paramount influence in determining the action of the recipient.

At the same time when aid is reduced or withdrawn the chances of achieving the basic purposes for which the aid was originally rendered are thereby reduced.

Another type of condition is that which relates directly to the purpose of economic development. We could, for example, make it a condition of aid

that countries adopt monetary and fiscal policies which encourage savings and productive investment, that they improve their educational system, that they develop a feasible plan for economic growth, and so forth. It is not always easy, however, to agree on what conditions are conducive to proper economic growth.

### 3. How much economic aid should be extended?

A basic consideration in judging what size development aid program might be undertaken is the estimate of how much foreign capital could usefully be employed by the underdeveloped countries.

A team of economists at the Center for International Studies, MIT, has concluded that the underdeveloped countries together could usefully employ about \$3.5 billion per year of additional foreign capital if they made a vigorous effort to step up their own economic development on the expectation that capital would be forthcoming for sound projects. According to their estimates such additional capital would make possible an annual increase in living standards of between 1 and 2 percent per capita. In actuality they anticipate that these countries would never be able to meet this theoretical goal and that increased foreign capital flows might never exceed \$2 billion per year. They anticipate that with the right kind of effort and with this outside assistance the underdeveloped countries could reach a stage of self-financing growth in ten or fifteen years.

This increase in capital to the underdeveloped nations could come from private sources, the International Bank for Reconstruction and Development, and other governments as well as from the United States government. As a basis for judging the possibility of expanding these other sources of foreign capital, the following table indicates current annual rates of investment in the underdeveloped countries from these sources:

	<u>Millions of dollars</u>
Private U.S. investment (net)	500
IBRD (net)	98
Other countries, public and private, excluding investments in dependencies (net)	50

4. What sort of time limit should be set on the development aid program?

U.S. aid programs have been authorized on a year to year basis. Each year the Congress re-examines the basic authorizations as well as making the appropriations. This is consistent with general congressional budgetary practice although for large, domestic construction projects the Congress does make appropriations which have no time limit. The present procedure insures an extensive annual congressional review of the aid program. It has also produced a fair degree of continuity in spite of the sharp questioning of the program which occurs each year.

Since the process of economic growth is a slow one which involves the development of many long range plans, it has been suggested that development aid would be more effective if funds could be committed which would assuredly be available for at least several years.

For this reason it has been suggested that a modified development aid program should be undertaken which would avowedly be for several years and which would in some degree indicate the intention of this country to continue making assistance available for this period subject always to the conditions established. Of course, no congress can legally bind a succeeding congress, but such a statement of congressional intent would be significant.

5. Should development aid be mainly in the form of loans or grants?

The arguments in favor of making development aid primarily in the

form of loans are as follows:

1. Long continued grant aid creates a bad donor-recipient relationship between nations.
2. The recipient may come to take grants as a matter of right and suspect any conditions attached to such aid.
3. The donor may try to use grant aid as an instrument of political pressure.
4. Grants may be used more carelessly than loans and thus actually harm the economic development of a country.

The arguments in favor of making development aid primarily in the form of grants are as follows:

1. If government aid of this sort is needed, it is needed to meet requirements which cannot be filled by the IBRD, Export-Import Bank, private investment, or other sources of loan funds.
2. If a way around this dilemma is sought by having the government make soft loans (exceptionally low interest, long term, or repayable in the currency of the borrower), these loans would be competing unfairly with hard loans so that nations would be less inclined to seek private investment or IBRD financing.
3. A nation which had borrowed through government channels on easy terms would be less able to attract regular lenders because the borrowing capacity of these countries is limited.

6. The relation of military aid programs to economic aid programs.

Although military and strategic considerations must play a large part in determining the type and extent of military aid rendered to other nations, the effects of military aid on the economies of other countries should not be overlooked. The influence of such aid in the Far East is particularly apparent.

In South Korea, a nation of 20 million people, a standing army of 400,000 is maintained. In Formosa with 8 million people an army of 300,000 is maintained. Forces of this size could not be kept up without substantial military and economic aid from the United States. Forces of this size also place a severe drain on the domestic resources of these nations.

7. The effect of aid programs on the place of private enterprise in the underdeveloped nations.

There is first a serious semantic problem to cope with. Many of the leaders of the underdeveloped countries proclaim themselves to be socialist. They may mean by this belief in equality of opportunity, equitable distribution of income, protection of the individual against risks over which he has no control, and so on. These are a fundamental part of capitalism as it has developed in the United States. Leaders of many underdeveloped countries may also equate capitalism with exploitation of the people, tremendous concentrations of economic power in a few irresponsible hands, ruthless and wasteful competition, etc.

A more fundamental question concerns the actual effect which aid might have on the future role of private enterprise in the underdeveloped countries. There are those who believe that aid rendered to governments which are avowedly socialistic will strengthen such governments in the way of government control over the economy. Aid channeled through governments will tend to expand the government sector of the economy. Based on this belief some have suggested that a condition for aid should be that recipient governments must create a favorable climate for private enterprise.

Another viewpoint is that a period of government directed development is necessary to lay the foundations for the development of a private enterprise economy. Thus the government would be expected to build the transportation

and communications systems, improve the level of education, and even assume many normal business risks during a period when the economy is still too immature for private enterprise to take such risks. According to this view once an economy begins to flourish, private enterprise will inevitably become more important in the economy because it is a superior method of carrying on production and distribution.

8. Should aid be primarily through bilateral arrangements between this country and others or through multilateral arrangements?

Both bilateral and multilateral aid can be used simultaneously. Furthermore, there is not a sharp line separating bilateral from multilateral aid. The Colombo Plan, for example, combines elements of multilateral and bilateral relations between nations.

There is a question of what the major vehicle of an aid program should be. The arguments in favor of bilateralism are:

1. This procedure gives the U.S. more control over the distribution of aid between various countries.
2. It gives more control over the use of aid within a country.
3. Bilateral programs are said to be more efficient and more flexible.

The arguments for a multilateral program are:

1. Sensitive new nations will more readily take guidance in connection with development plans from a multi-national group.
2. Other capital-exporting nations would be expected to contribute to such a program.

**The United States Council of the International Chamber of Commerce** is an association of private commercial enterprises and trade associations representing the American business community in the International Chamber of Commerce. The ICC is a federation of similar associations representing the interests of private enterprises in thirty-five countries.

The International Chamber of Commerce draws upon the combined experience and judgement of business executives in many nations to develop solutions to international economic problems. The United States Council, in addition to providing for American participation in this process, makes independent studies of developments in the United States that affect our nation's international commercial interests.

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