The President's Task Force on International Private Enterprise: Report to the President

A publication prepared by the President's Task Force on International Private Enterprise with the cooperation and support of the Agency for International Development.

December 1984
Washington, D.C.

Dear Mr. President:

In May 1983, at a time of severe international economic turbulence, you established the President's Task Force on International Private Enterprise. During our meeting in the White House, you requested that the Task Force identify ways to strengthen the economies of developing nations. In particular, you asked us to examine how U.S. foreign assistance could be used to stimulate private enterprise development and promote investment in and trade with developing countries.

We submit this report with a mixture of satisfaction, apprehension, and hope.

We submit it with satisfaction because we genuinely feel that as a result of our 18 months of often intense study, discussion, and debate, we succeeded in defining some of the key issues that will help to shape the twenty-first century. These policy questions center on why the developing countries are important to the United States, and what principles and actions should govern U.S. economic policies toward them. We believe our recommendations, if adopted, will contribute significantly to the security and prosperity of both the United States and those nations still struggling for a place in the modern world. For this opportunity, we are deeply grateful.

We submit this report with apprehension because we know that some of our recommendations are highly controversial, some are highly technical, and all of them, taken together, challenge the nation to a vigorous review of its economic relationships with the rest of the world, a review that requires a rigorous rethinking of many long-standing policies. We can expect various government agencies to oppose our report because it may pose a threat to their existing authorities. Some may fault our heavy emphasis on government encouragement of trade and investment. However, we believe that the only way the private sector can fulfill its development potential is for government to create an environment that supports the growth of private sector activity.

We submit this report with hope because we believe that the logic behind these recommendations is strong, the needs they address are urgent, and the opportunities they present for the people of this and other nations are compelling. We hope that others will draw the same conclusions so that insight will lead to action and want will give way to abundance.

We are business people. Ours is a business perspective.

We recognize that in some public policy circles there is an ingrained hostility toward business, a suspicion that policies proposed by the business community are proposed for its own gain. On the other hand, many business leaders are skeptical of policies proposed by politicians or bureaucrats. In this case, we believe that the American business community is prepared to work with the public sector to advance what we feel strongly is in our combined national interest. Certainly, the members of your Task Force will stand behind you in the implementation of those recommendations you choose to accept.

We believe that our particular perspective on economic development is uniquely valuable precisely because it is a business perspective; because we are intimately familiar with the kinds of considerations that lead to real-world investment decisions; and because we have wrestled with problems of production, distribution, and marketing in a wide variety of economic and social conditions. These are not questions of political ethics or social morality. They are questions of economic fact.

In the course of this study, we have consulted widely with government officials and have carefully examined the workings of government programs both here and abroad. It has given us a greater understanding of the potential for and the limitations of these programs, and an awareness of the considerations that must go into their design and execution. We have come out of this experience with great respect for the dedication of many of those who administer our aid and trade programs. We have also gained an appreciation for the difficulties they must often surmount.

The future belongs to all of us; we all share a vital stake in world economic development. Clearly, the job ahead of us will require the best efforts of both the public and the private sectors. There are some tasks government can accomplish effectively, some tasks business can handle best, and some tasks that are more appropriate for voluntary agencies and organizations. There are other tasks that can only be accomplished by the people and governments of the developing countries themselves—such as adopting policies that encourage rather than discourage the kind of enterprise, investment, and risk that make development possible. However, governments—including our own—are the only institutions capable of removing substantial impediments to private sector growth. Once government does its job, the private sector will do its job.

We urge that this report be considered on two levels: the conceptual and the programmatic.

We have identified a strategy that calls for the consistent, institutionalized integration of economic concerns into the nation's policy processes at the highest level, greater recognition of economic matters as a key priority in U.S. relations with developing countries, and reliance on private sector incentives to achieve long-term economic development objectives. We have also suggested various ways to implement this strategy. While some of these means may cease to be appropriate as conditions change, we believe the strategy is one we must continue to pursue.

The conceptual aspects are the heart of the report. Our programmatic recommendations have grown out of our conceptual analyses. What we propose conceptually is a substantial redirection of what have been many of our nation's prevailing policy thrusts for many years. We believe that the key to world prosperity lies in the adoption of appropriate economic policies by both the developed and the developing countries. But we also recognize that specific programs and organizational changes are needed to carry out those policies and we have tried to be diligent in finding the best means to translate policy into action. To this end, we have included in the appendix special "action briefs" that elaborate further on how some major recommendations can be specifically implemented.

The central policy that must inspire U.S. development efforts is this: A proud, forceful insistence on what our experience so clearly teaches, that the way to create wealth is to create incentives and to rely on the market mechanism rather than the constraints of undue government interference. Unless the less developed nations accept this, development aid will fail. If they model their policies accordingly, then development aid can be seed sown in fertile ground. Third World country economies will grow stronger. Economic interaction between developed and developing nations will increase.

In past years, it was fashionable to dismiss foreign economic assistance as a "giveaway" that did little long-term good in recipient countries and offered nothing in return to the United States. Nothing could be further from the truth. Whatever waste there may have been in the past, a properly conceived aid program can be an investment in the future of America and in the developing countries that will pay for itself many times over. With economic aid, we can gain stability in vital, but vulnerable, Third World countries. We can open new markets, increase trade, create new jobs, spread hope, and build the sort of climate in which freedom can flourish in future generations. The more we invest in economic development now, the less likely we are to have to spend on arms later. In the global struggle between free enterprise and statism, our most effective weapon is our economic strength. One of the critical determinants of which side prevails during the next century will be the degree of our success in sharing that strength with the developing world.

Few, if any, interests of the United States are, in the long run, as central to its future as the economic interaction between this and other countries. This interaction often takes complex and subtle forms. Sometimes it requires forcefulness, at other times diplomacy, insight, or a sophisticated understanding of highly technical and often abstruse factors far removed from most people's experience. Some believe that the present structure of our government to deal with international economic crises or policies is effective and requires no new organization or process. Many will agree with us, however, that we are not adequately structured to plan for the future or avoid tomorrow's crises. For this reason, we believe that our recommendation to establish an Economic Security Council in the Executive Office of the President to formulate and coordinate domestic and international economic policies is our most important recommendation. The United States needs an institutional mechanism in the executive branch to integrate complex issues, harmonize past and present actions, and develop a coherent, constant vision of the future as a framework for making decisions. This is a classic case of a situation in which policy without structure is futile.

In the world of the twenty-first century, the security of the United States and the developing nations will depend increasingly on how well our economies interact. We need a new policymaking structure that will address these critical economic issues.

In the report that follows, a wide variety of policies and programs that affect the developing world are discussed. These include private sector investment, foreign assistance, trade, food assistance, and training. Most of our recommendations do not require new funding. Rather, they involve a change in program emphasis. Those that do require initial funding will result in future increased revenue and budget savings. For example, our recommendation to increase food aid could be offset by reduced farm support payments. Our recommendation to promote trade and fight foreign subsidies requires no new funding authority. And it is possible to double current training efforts with only a modest reallocation of existing aid resources.

We have also prepared a separate *Private Enterprise Guidebook* that provides U.S. Government policymakers with basic information on the potential of private enterprise in development and identifies many available U.S. resources that are not now fully utilized.

Mr. President, we wish to congratulate you on your reelection. We believe our report is timely as you begin your second term. In many ways, what we propose can become the blueprint for peace and prosperity in the developing world, following on the principles you espoused at the Cancun summit in 1981. Your acceptance of these proposals would, indeed, be a fitting legacy from the Reagan administration to future generations.

In the hope that these documents will make a substantial contribution to the development of private enterprise throughout the world, we respectfully commend these ideas to you and to the nation. For all of us on the Task Force, it has been a great honor to be of service.

Sincerely,

Dwayne Andreas

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Chairman

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Contents

Abbreviations

AADC
American Agricultural Development Corporation

ADC
Advanced Developing Country

AID
U.S. Agency for International Development

BHN
Basic Human Needs

BIT
Bilateral Investment Treaty

CBI
Caribbean Basin Initiative

CCC
Commodity Credit Corporation

CCCT
Cabinet Council on Commerce and Trade

CCEA
Cabinet Council on Economic Affairs

CDSS
Country Development Strategy Statement

CFEP
Council on Foreign Economic Policy

CIPE
Center for International Private Enterprise

CMEA
Council for Mutual Economic Assistance

DAC
The Development Assistance Committee of the Organization for Economic Cooperation and Development

DEC
National District Export Council

DOD
U.S. Department of Defense

EAA
Export Administration Act

EEC
European Economic Community

EEC-CSP
European Economic Community-Common Sugar Policy

EPB
Economic Policy Board

ESF
Economic Support Fund

ETC
Export Trading Company

Eximbank
U.S. Export-Import Bank

FAO
Food and Agriculture Organization

FCIA
Foreign Credit Insurance Association

FRG
Federal Republic of Germany

GATT
General Agreement on Tariffs and Trade

GNP
Gross National Product

GSP
Generalized System of Preferences

HHS
U.S. Department of Health and Human Services

ICI
Intermediate Credit Institutions

IDA
International Development Association

IDB
Inter-American Development Bank

IDCA
International Development Corporation Agency

IESC
International Executive Services Corps

IFC
International Finance Corporation of the World Bank Group

IMF
International Monetary Fund

IMI
International Marketing Institute

JACC
Joint Agricultural Consultative Corporation

LAAD
Latin American Agribusiness Development Corporation

LCI
Latin Caribbean Investments

LDC
Less Developed Country

ODA
Official Development Assistance

OECD
Organization for Economic Cooperation and Development

OEF
Overseas Education Fund

OICD
Office of International Cooperation and Development

OPD
Office of Policy Development

OPEC
The Organization of Petroleum Exporting Countries

OPIC
Overseas Private Investment Corporation

NIC
Newly Industrialized Country

NSC
National Security Council

Partners
Partners for International Training and Education

PEFCO
Private Export Funding Corporation

PFP
Partnership for Productivity

PTE
Private Trade Entity

PVO
Private Voluntary Organization

SBA
Small Business Administration

SEZ
Special Economic Zones

SIG-IEP
Senior Interagency Group-International Economic Policy

S&T/IT
Office of International Training, Bureau for Science and Technology (AID)

TDP
Trade and Development Program

TPC
Trade Policy Committee

UNCTAD
United Nations Commission on Trade and Development

UNIDO
United Nations Industrial Development Organization

U.S.& FCS
United States and Foreign Commercial Service

USDA
United States Department of Agriculture

USIA
United States Information Agency

USTR
United States Trade Representative

VITA
Volunteers in Technical Assistance

WFC
World Food Corporation

WID
Women in Development

YPO
Young Presidents Organization

Executive Summary

The United States now faces the challenge of leading the world to a new era of prosperity created, in significant part, by unleashing the dynamism of the private sector in the Third World. Meeting this challenge successfully is a matter of our own long-term national security and is the direct requirement of a world grown more interdependent. As they have in the past, U.S. economic policies will continue to reflect and be dictated by traditional humanitarian concerns.

We believe that the United States and developing countries share a vital interest in Third World economic development, that economic growth can best be achieved through the development of the private sector, and that economic growth provides a necessary base for long-term political stability.

Among the Task Force's general recommendations are the following.

☐ **Elevate international economic policy to a level comparable to national security.**

In the world of the twenty-first century, the security of the United States and of developing nations will depend increasingly on how well our economies interact. One of the critical determinants of our security will be the degree of our success in sharing our economic strength with the developing world. This will also require giving heightened significance to international economic policy and devising ways to share our economic know-how with developing countries.

☐ **Establish an Economic Security Council.**

Responsibility for the formulation of international and domestic economic policy is fragmented, with portions scattered throughout the U.S. Government. A well-coordinated U.S. economic policy would mean more jobs, increased exports, and increased stability at home and abroad. We propose the creation of an Economic Security Council, responsible for formulating, coordinating, and integrating international and domestic economic policies. Some of the matters with which such a council would deal are the debt crisis, trade and agricultural policy, technology transfer, and foreign assistance.

☐ **Expand Opportunities for Private Enterprise.**

The private sector in developing countries is hampered not only by the lack of capital and the lack of technology and management skills that accompany direct investment, but also by the absence of positive government policies toward entrepreneurship. By urging, encouraging, and using our resources to help developing countries adopt policies that attract foreign direct investment and by helping businesses identify investment opportunities in the Third World, we can make a crucial contribution to the economic development of those countries. The Task Force's *Private Enterprise Guidebook* provides specific advice on how to use U.S. resources to attract foreign and local investment.

☐ **Reorient U.S. foreign aid programs.**

Perhaps the greatest paradox in our foreign aid programs has been that while U.S. economic success is based upon private enterprise, we have done far too little to help developing countries attract private enterprise, trade, and investment. U.S. foreign assistance programs should substantially expand their efforts to help developing countries adopt policies that will strengthen the opportunities for private enterprise. To the maximum extent feasible, the U.S. Government should not channel its foreign assistance resources to governments, but to the private sector in developing nations. For the mutual benefit of the United States and developing countries, the U.S. Government should also integrate its foreign assistance and trade programs and policies to make better use of its resources. The Task Force's action brief on strengthening AID's private enterprise thrust and its *Private Enterprise Guidebook* will serve as a blueprint for this reorientation.

☐ **Press for Increased Trade Flows.**

American firms increasingly find themselves competing overseas with foreign firms that are supported by their national treasuries. Not only are U.S. companies losing large amounts of business to mercantilist nations that provide heavy subsidies to their firms, but these practices distort the whole pattern of international trade to the detriment of the United States, developed countries, and developing countries alike. In fact, we believe the practice of "mixed credit" trade subsidies has become a major threat to international private enterprise. To protect U.S. firms and the free enterprise system, we recommend that the United States fight fire with fire. Specifically, we believe that the Administration should make sufficient mixed credit resources available in order to convince other nations that such practices are not in anyone's "best interest." This will press our foreign competitors to the negotiating table and bring an end to such predatory practices. In Part V of this report we recommend that the Agency for International Development (AID) and the Export-Import Bank (Eximbank) blend their resources and that, if necessary, Eximbank use the full extent of its authority. This could amount to a mixed credits program of several billion dollars.

☐ **Constructively use U.S. Agricultural Abundance.**

We cannot afford, financially or morally, to idle large parts of our productive farmland. Rather, we must devise ways to harness our agricultural abundance so that we can increase exports from the United States and alleviate chronic starvation and malnutrition in the developing world. Food can also be used to ease the pressing foreign exchange needs of Latin American, Asian, and African nations caught in the international debt crisis. The U.S. Government can provide large amounts of food to these countries on a concessional basis to enable them to use their limited foreign exchange to meet other objectives. The Public Law (P.L.) 480 Program is one of the President's most effective tools. In Part V of this report we recommend doubling the program. Given the current costs of farm subsidy programs, the impact of this increase would be a net reduction in the Federal budget.

In designing a strategy to address current crises and long-term economic development needs, the Task Force has been guided by the following precepts.

☐ Market-oriented economies work, excessively planned economies do not.

☐ The United States has an important role to play in leading the world toward balanced and equitable economic growth.

☐ A free and open trading system offers the greatest hope of achieving widely shared economic growth and prosperity. However, U.S. industry and agriculture must be able to compete with the terms offered by mercantilist nations until such time as we can meet our competitors on a level playing field—in fair and open competition.

☐ United States agricultural abundance must be harnessed more effectively to address the human and development needs of the people of the Third World.

Specific Findings and Recommendations of the President's Task Force on International Private Enterprise

The following findings and recommendations are discussed in the report that follows. They are the result of substantial research and the subject of extensive deliberation by members of the Task Force over the past several months. If adopted, our recommendations will strengthen the economy of the United States and other developed and developing nations.

THE IMPORTANCE OF PRIVATE ENTERPRISE AND INVESTMENT TO DEVELOPMENT

Finding: page 34
Countries that fail to create conditions—including appropriate laws and policies—that will attract investment will relegate themselves to slow growth. At the present time, there is no central source of advice to help developing countries foster the conditions necessary for private sector growth.

Recommendation: page 36
The United States, working with other donor nations, developing countries, multilateral institutions, and private business, should establish a Private Enterprise Institute that will serve as a research center to advise developing countries on how to create those conditions necessary to attract investment and foster trade.

Finding: 37
New foreign investment will be difficult to attract for many debt-ridden LDCs as long as insufficient foreign exchange is available to the private sector.

Recommendation: 37
The United States should take the lead in assuring that private needs for credit and foreign exchange in LDCs are not pushed aside by preferred access of the public sector.

Finding: 38
The United States and other donors do not make sufficient effort to increase private investment and improve the investment climate in developing countries.

Recommendation: 38
The United States should strongly encourage international dialogue on ways to support increased foreign direct investment.

Recommendation: 39
The United States should substantially increase its support of private investment activities in developing countries.

Finding: 40
In order to increase foreign investment, developed and developing countries need to adopt uniform standards for host country and investor responsibility and conduct.

Recommendation: 40
The United States should encourage developing nations to negotiate bilateral investment treaties. The United States should assign priority in its aid programs to those countries that sign such treaties.

Finding: 41
Expanded investment insurance (or guarantee) is a key to increasing investment in developing countries.

Recommendation: 41
Overseas Private Investment Corporation (OPIC) funding and insurance capability should be substantially increased and its mandate broadened to include a full range of financing and services to U.S. business, large and small.

Recommendation: 42
The United States should support a multilateral investment guarantee program administered by the World Bank.

FOREIGN ASSISTANCE PROGRAMS AND PRIVATE ENTERPRISE DEVELOPMENT

Finding: 45
The U.S. Government does not sufficiently encourage or assist recipient developing countries in making the policy changes necessary to allow private sector growth.

Recommendation: 46
The United States should sharply increase its efforts to guide developing countries toward market-oriented policies; it should reward those countries that adopt strategies that will lead to a positive climate for business and investment.

Recommendation: 47
U.S. food assistance should be used to a greater extent as an incentive for developing countries to adopt market-oriented policies that encourage the private sector to increase agricultural production.

Finding: 48
U.S. foreign assistance programs are often required to address problems other than those related to long-term stability and economic growth.

Recommendation: 48
The economic component of U.S. foreign assistance programs should have a higher national priority.

Finding: 49
The links between our foreign assistance program and U.S. foreign trade are inadequate.

Recommendation: 49
The scope and financing of the Trade and Development Program (TDP) should be expanded.

Recommendation: 50
TDP techniques should be applied to other foreign assistance programs, specifically those carried out by AID, to the maximum extent possible.

Finding	Recommendation
	Recommendation: 50 U.S. foreign assistance resources should be used to build up the trading capacity of developing countries.
	Recommendation: 50 U.S. foreign assistance resources should be used to assist in China's modernization process.
	Recommendation: 51 U.S. foreign assistance agencies—such as AID, OPIC, and TDP—should package their financial and other resources to promote greater two-way trade between the United States and developing countries.
Finding: 51 In implementing its agricultural development policies, AID has not given private agribusiness activities the attention and support they deserve.	**Recommendation:** 51 Private sector efforts to form private sector agribusiness development corporations should be encouraged and supported.
	Recommendation: 52 Developing country agricultural entrepreneurs should be supported by qualified U.S. executive-managerial and technical personnel "on loan" from the private sector to assure the ongoing progress of companies and individuals being financed with U.S. foreign assistance funds.
Finding: 53 The international financing institutions play a constructive role in Third World development.	**Recommendation:** 53 The United States Government should utilize its resources to support broad economic changes in developing countries and, where appropriate, coordinate its efforts with those of the International Monetary Fund, the World Bank, and the International Finance Corporation (IFC).
	Recommendation: 53 The United States should continue to support the multilateral development banks' efforts to support private enterprise development.

Finding: 54
The breadth and scope of AID's private enterprise activities are too limited. In order to expand them, AID needs a clearer mandate, improved skills, and greater flexibility.

Recommendation: 55
AID's congressional mandate, its policies, its programs, and its organization must be revised to reflect greater private sector emphasis.

Recommendation: 56
AID should turn to the U.S. business community to assist it in developing practical modes of business-government cooperation.

Recommendation: 57
The U.S. Government, to the maximum extent feasible, should channel its foreign assistance resources through the private sector and not through governments: AID should substantially increase its support of private intermediate credit institutions (ICIs).

Recommendation: 57
AID should increase its equity financing through ICIs.

Recommendation: 58
AID should serve more as a broker between U.S. businesses and prospective overseas partners by providing inexpensive, current, and easy-to-use information on the investment climate and operating conditions in developing countries.

Recommendation: 58
AID should support the formation of trading companies and other business brokering institutions that have developmental potential.

Recommendation: 59
AID should encourage joint undertakings between businesses and private voluntary organizations in developing countries.

Recommendation: 60
AID should streamline its administrative and procurement processes.

Finding: 61
Training, in various forms, is one of the most effective long-range means of promoting development. Fulfilling training needs offers the United States a significant opportunity.

Recommendation: 61
The United States should significantly expand U.S.-based training and place stronger emphasis on private sector participation and needs.

THE FORMATION OF U.S. ECONOMIC POLICY

Finding: 69
In order to cope with new and changing circumstances, a new institutional structure is needed to ensure better formulation and coordination of U.S. international and domestic economic policy.

Recommendation: 71
The President should establish an Economic Security Council (ESC) to formulate and coordinate domestic and international economic policy.

Recommendation: 72
The President should designate an Assistant to the President for Economic Affairs who would participate in the Economic Security Council.

Finding: 73
Both legislatively and administratively, our foreign assistance programs suffer from confused mandates, divided responsibility, and often from a perception that economic development has a low priority.

Recommendation: 74
There must be greater, more regularized consideration of developing country issues in the policy deliberation process.

Recommendation: 75
Changes must be made in AID's mandate and organization in order to improve the effectiveness of foreign assistance programs.

Finding: 76
Responsibility for the U.S. Government's trade policies and programs is fragmented among several government agencies. Policies and programs do not operate within an overall strategy aimed at benefiting both the United States and developing countries, nor are they designed to address both U.S. trade objectives and broader U.S. economic objectives.

Recommendation: 76
The U.S. Government must develop an aggressive, consistent trade policy that mixes aid and trade resources, enables U.S. firms to be more competitive in world markets, and meets the challenges posed by the growing governmental role in world competition.

Recommendation: 77
The United States must link its trade and foreign assistance programs.

Recommendation: 78
The United States should consider ways to give higher priority to the need for a freer and more open international trading system and continue to press for

a new round of multilateral trade negotiations. This new round should include adopting a trade in services code, the application of trade rules to middle-income developing countries, and strengthening enforcement procedures against government-subsidized trade.

Recommendation: 79
The authority of the United States Trade Representative (USTR) as trade policy negotiator and manager should be strengthened and expanded.

Finding: 80
The United States needs a more coordinated policy to integrate domestic agricultural programs, food assistance programs, and agricultural trade programs.

Recommendation: 80
The United States must integrate its agricultural trade, food aid, and domestic farm policies.

Recommendation: 81
The Administration should seek to better relate U.S. response to LDC food and domestic security requirements.

Finding: 82
Some U.S. Government measures have discouraging or disadvantageous effects on American firms that are involved or might become involved in long-term relationships with private enterprise in developing countries.

Recommendation: 82
The U.S. Government should coordinate more effectively its efforts to assure that U.S. laws and regulations reflect greater sensitivity to structural changes in the international marketplace.

TRADE AND FOOD ASSISTANCE

TRADE

Finding: 92
The United States has not adopted a strong enough stance in its negotiations to stop foreign governments from using unfair methods of subsidizing export finance.

Recommendation: 93
The United States should use aggressively the mixed credits authority of the Export-Import Bank (Eximbank) to counter competitors' mixed credit offers.

Recommendation: 94
AID should also use its limited mixed credit authority, although the Export-Import Bank will be the major source of mixed credit financing.

Finding: 94
The current debt crisis in the developing countries requires close cooperation between the U.S. private and public sectors to assure that adequate trade financing is made available.

Recommendation: 95
U.S. Government foreign credit programs should operate under consistent guidelines.

Recommendation: 96
As part of an integrated trade policy, the participation of the U.S. private sector in countertrade should be facilitated when it is in the best interest of the United States.

FOOD ASSISTANCE

Finding: 100
Many developing countries face chronic food shortages that will undermine their political stability and economic development.

Recommendation: 101
Food aid should be at least doubled to help avert starvation, alleviate poverty and malnutrition, expand developing country agricultural markets, and support private sector growth.

Recommendation: 102
A much larger share of total U.S. foreign assistance should be food assistance.

Recommendation: 103
Agricultural export credit programs should be significantly increased to help lessen the development impact of large food deficits and large debt burdens.

Finding: 104
Present U.S. food assistance programs do not emphasize private enterprise development and U.S. private sector involvement in development assistance.

Recommendation: 105
The U.S. Government should follow the instructions and intent of the law that most counterpart funds generated by P.L. 480 should be channeled through businesses and not through government.

Introduction

TODAY'S POLICIES, TOMORROW'S WORLD

This report is about wealth and poverty. It is about how the United States can better help lead the world toward abundance in the twenty-first century.

The key to global prosperity in the next century lies in the rich lode of experience we have accumulated. This century has been tempestuous, tumultuous, torn by strife and cruelty, and wracked by heart-rending want. Yet, we have also seen economic advances that were breathtaking in their sweep and scope. These advances have been achieved not only in the previously industrialized West, but also in countries whose people, just a short time ago, clung precariously to the bare edge of subsistence.

Nearly 40 years have passed since the end of World War II. That global cataclysm ushered in the modern world as we know it and ended the old system of European empires. It unleashed forces of nationalism that swept through what came to be known as the "Third World." Sometimes the old colonies became new democracies. More often, sometimes after a brief flirtation with the form but not the substance of democracy, they came under one-man or one-junta or one-party rule. Hopes were raised and then dashed—hope for freedom, hope for an escape from hunger, hope for release from conflict and bloodshed, hope for a better and more abundant life.

Privation, famine, and primitivism still stalk much of the Third World. But not all of it. Some of the most dramatic economic success stories in the world's history were written during this same period by nations that were poverty-stricken backwaters barely more than a generation ago.

Surely there are lessons in all of this. Surely there are reasons why one emerging country is a spectacular economic success while its neighbor is an equally spectacular failure. And surely the goal of those who seek to promote development worldwide should be to understand and encourage those conditions that foster success and discourage those that do not.

We can learn from this century's successes and failures. Both have ranged from the modest to the monumental. As we examine them, certain clear patterns emerge. The importance of these patterns prompted us to develop the second volume of our report, the *Private Enterprise Guidebook*, which seeks to identify some of the elements contributing to successful economic development. If we care about the future, we would do well to heed carefully the lessons of the near past.

THE UNITED STATES AND THE THIRD WORLD

If it is important to determine what we should do, it is also important to understand why we should do it.

Why should the United States care about the Third World? Why should we exert ourselves to promote development, alleviate hunger, and encourage trade?

Basically, these questions should concern us for two reasons: because our national interest requires it and because conscience demands it.

What may once have seemed a pious cliché about the increasing interdependence of the world's nations has become a critical fact of economic life for the United States. Table 1 highlights the vital role that developing countries play as trading partners with the United States. Consider the following facts.

☐ Developing countries accounted for most of the growth in American exports from 1975 to 1980.

☐ A decline in U.S. exports during the last half of 1982 caused our Gross National Product (GNP) to fall during that period, instead of registering what would otherwise have been a 2 percent gain.

☐ Approximately 30 percent of U.S. corporate profits are derived from international investment and trade.

☐ Agricultural exports claim one out of every three acres of American farmland in production, while agricultural exports to developing countries account for one out of every five acres.

☐ For the United States, exports play a vital role in job creation and overall employment, particularly in the manufacturing and services sectors. In 1982, total export-related employment accounted for one out of every eight jobs in manufacturing (as opposed to one of every ten jobs in 1972), one of every six jobs in nonmanufactured goods, and one of every thirty jobs in services. In 1982, over five million U.S. jobs were due to American exports. With markets so intricately tied, it is no wonder that the cutback by Latin American countries of imports from the United States by $16.3 billion between 1981 and 1983, had a sharply negative impact on U.S. jobs and private sector profits. Clearly, developing nations are of great importance to our economy in conventional GNP terms.

They are also important to us because their economic troubles often contribute to political instability, which ultimately bears directly on our national security. Since World War II there have been 120 wars, which have brought 10 million deaths. These have all been fought on the soil of Third World countries. In most, the killing and destruction have been contained within those countries, though they have been no less human tragedies because of this. In many cases, the Western powers have been drawn in to one extent or another; some of these conflicts have risked collision between the superpowers. In these conflicts, the United States has suffered hundreds of thousands killed or wounded and has spent hundreds of billions of dollars. Rising prosperity will not end the danger of all war, but it will reduce the likelihood of many.

During the next century, the nations of the Third World— already three billion people strong—will take their places increasingly in the forefront of world affairs. It is in our national security interest, no less than in our national economic interest, that they do so on a rising tide of prosperity and hope, rather than in the grip of despair, hate, and desperation.

The people of developing nations are also important to us. We Americans pride ourselves on being humanitarian and charitable; it is in developing countries that most of the world's starving, ill, and uncared for eke out a meager existence. The poverty of the Third World is not something that in conscience we can ignore. Just as the economic importance of the developing countries appeals to our logic, the dire human needs of their people cry out to our hearts.

The United States has two basic, overriding interests in the world: peace and prosperity.

Peace includes security; it requires freedom from aggression, whether direct or indirect, overt or covert. It is a basic rule of international relations that the security of all depends on the security of each. In the Third World, hungry nations are vulnerable nations. Rising standards of living are no guarantee of political stability, but they are an essential element of it. Hope is essential and that hope has to rest not just on promises, but on actual, demonstrated progress.

TABLE 1:
U.S. Trade with Developing Countries by Commodity Group from 1975-1981

		Total U.S. Trade ($ billion) 1975	1981	Developing Countries Share of U.S. Trade (percent) 1975	1981	Average Annual Growth in U.S. Trade (percent) 1975-81	Average Annual Growth in U.S. Trade with Developing Countries (percent) 1975-81
Exports	Food, feeds, and beverages	$19.1	$37.9	35.0%	41.2%	12.1%	15.4%
	Fuels	4.8	10.7	14.6	19.6	14.3	20.1
	Industrial supplies	25.4	57.0	39.4	40.4	14.4	14.9
	Capital goods	35.4	80.2	43.0	45.1	14.6	15.6
	Automobiles	10.1	18.0	27.4	33.7	10.1	13.9
	Consumer goods	6.5	15.8	35.6	44.3	16.0	20.4
	Other	6.4	14.1	53.3	42.9	14.1	10.2
	Total (or average)	$107.7	$233.7	38.2%	41.1%	13.8%	15.2%
Imports	Foods, feeds, and beverages	$9.6	$18.1	59.4%	58.0%	11.1%	10.7%
	Fuels	26.6	82.0	78.6	79.9	20.6	21.0
	Industrial supplies	22.2	52.6	23.9	25.7	15.5	16.9
	Capital goods	9.6	34.5	18.8	24.9	23.8	29.8
	Automobiles	11.7	29.7	2.6	3.4	16.8	22.2
	Consumer goods	13.7	38.7	42.3	53.0	18.9	23.4
	Other	2.7	5.7	22.2	24.6	13.3	15.2
	Total (or average)	$96.1	$261.3	42.0%	46.3%	18.1%	20.1%

SOURCE:
U.S. Foreign Policy and the Third World Agenda 1983, Overseas Development Council, 1983.

Prosperity is a condition; it is also a process. We must measure it in both absolute and relative terms. In comparing the level of prosperity for two countries, it is not enough to compare their respective levels of per capita GNP. One must also compare the rate of increase. This evidence of improvement—and the expectation of continued improvement—is central to a people's sense of well-being, economic security, and hope for their own and their children's future.

Like an organism that grows as its cells divide, prosperity increases by being shared. It is in the nature of economic growth that activity begets activity. Therefore, as we help to increase the prosperity of others, we also increase our own. More people with more to exchange means more goods, more jobs, more abundance for everyone. It also means greater security, both economic and political. For prosperity, like peace, is most secure when it is most widely shared.

DEBT SHOCK, DEBT CRISIS

The world has been jarred in recent years by repeated economic shocks, most dramatically the successive oil shocks and the debt shock. The debt shock has become a debt crisis that we in the United States see as a threat to the international monetary system. But what we see as a debt crisis, some developing countries see as a survival or poverty crisis. Among debtor nations it affects not only those that are dangerously overextended now, but also the many others that still need capital for their own future development.

Developing countries borrowed heavily in the 1970s. Some of the borrowing went into ambitious—in some cases, overly ambitious—government investment programs. Also, much of it went for consumption, while too little of it went into efficient and productive enterprises. Like many U.S. consumers during the same period, some of the borrowing countries were lured by low interest rates that, in a time of rapid inflation, seemed to be a bargain. Many of the loans supporting investment had short-term maturities, while projects for which the funds were used had long gestation periods. Then, when interest rates suddenly rose as the global recession brought sharp declines in export earnings, the borrowing countries found themselves caught in a desperate financial vise.

By the end of 1983, developing country debt totaled more than $800 billion; interest payments alone amounted to almost $100 billion last year. In many countries, debt service consumed 50 percent of export earnings and, in some cases, much more. While there have been numerous debt delays and reschedulings, either approved or in process, the worst of the debt service crunch almost certainly lies ahead. A means must be found to allow the heavily indebted developing countries and the international financial system to make some fair accommodation so that the countries can meet their debts over a reasonable period of time without stifling their ability to finance efficient growth.

Not only must our private financial institutions work toward this accommodation, but a way must be found to marshall all available U.S. resources toward this effort. Expanded and more flexible trade financing mechanisms must be sought, economic development funds must be available to fill critical development financing needs and stimulate productive enterprises, and U.S. food abundance must be generously and effectively used to counter the short-term impact of staggering debt burdens and agricultural production shortfalls.

In the short term, it is vital that we buy time in which longer term solutions to the debt crisis can be put in place. But it is equally vital that we then use that time wisely. Ultimately, solving our debt crisis means solving the borrowers' debt crisis and this, in turn, means enabling them to earn their way out of debt. This means economic development and it also means trade.

If collectively we fail to devise a longer term solution, the inability of developing nations to pay their debts could result in a further reduction in lending to these countries that could, in turn, throw them into political and economic chaos. It could also result in the failure of major U.S. banks, which could devastate U.S. and global economies. Even if we managed to avoid the worst pitfalls, we would continue to move from crisis to crisis, draining enormous human resources from the developing countries and diverting these countries and the United States away from constructive, long-term economic policy management. The longer top economic talent spends its energy designing quick-fix financial remedies, the less opportunity there is for real, long-term progress. The goal of constructive public policy is to design systems for crisis prevention, rather than to be mired in crisis management. This has particular urgency in relation to the debt thundercloud that now hangs over the world.

THE KEY TO PROSPERITY

As we noted, a long-term solution to the debt crisis requires enabling the borrowing countries to earn their way to solvency. And this brings us back to the lessons we have learned in the twentieth century.

Some 35 years have passed since foreign aid as we think of it today—development assistance for the Third World—was introduced with President Harry S. Truman's Point Four proposal. Certainly the intentions of foreign aid were noble and some of the results were very good. But some of the results and many of the experiments that were tried could, with the benefit of hindsight, be improved upon.

As we now re-examine both the precepts and performance of our aid programs over this past third of a century, one lesson stands out above all others: Market-oriented economies work; overly "planned" and regulated economies do not. Therefore, development assistance can be most effective if it works in conjunction with a market-oriented system; it tends to be least effective when it props up state institutions that seek to substitute for private sector initiative. Development assistance can and should support governments by financing critical infrastructure necessary for private enterprise growth, such as electricity and roads. It should not abet government in competing with or replacing the private sector.

Above all, if there is one central concept that must inspire our development efforts, it is a proud, forceful insistence on what our experience so clearly teaches: The way to create wealth is to create incentives and to rely on the market mechanism, rather than the constraints of undue government interference. This is the way others must do it if they want to succeed. This is what common sense tells us.

Governments are good at wielding power, but bad at creating wealth.

Collectivism serves well the political needs of the leaders of new nations, but it does not serve the economic needs of the people of those new nations.

To succeed, the LDCs must create an attractive climate for investment. They must also forego the political temptation to inveigh against foreign investment.

The West still suffers from a post-colonial guilt syndrome that is characterized by an unwillingness to confront the faults, failures, and foibles of those who lead Third World nations.

For several decades, the fashionable Western attitude toward the Third World was patronizing. Third World nations were not believed to be above criticism, but beneath it; we glossed over their sins and shortcomings as the failings of those of whom nothing better was expected. This was intellectually bankrupt and practically devastating. Millions of people are suffering today because of it.

Just as a banker does a client a disservice when he makes a bad loan, the United States does a disservice to developing nations by providing foreign assistance without pressing for policies that foster economic growth through private enterprise and investment.

We must also recognize, and vigorously counteract efforts to scare away Western investment from the less developed countries (LDCs) by those fostering hostility against "multinationals," "economic imperialists," and a whole range of collectivist hobgoblins.

Consider the paradox: Every developing country wants capital, but most shrink from the idea of capitalism. Yet capitalism is simply the packaging of capital with incentives, know-how, experience, business acumen, and creative ideas. Wherever capitalism takes root, wealth spreads. Those that reject capitalism remain undeveloped; those that welcome capitalism prosper.

And consider this parallel paradox: Even in the poorest countries, the powerful are rich. The people, not the leaders, are those who suffer poverty. The oligarchs hang on to their political power, and by doing so protect their economic positions. In the name of "the people," they keep economic power in political—or their own—hands. The bogeyman they try to frighten people with is often capitalism. What keeps their people poor, however, is not capitalism, but statism. Western-style capitalism—free enterprise capitalism—creates wealth, liberates people from state control, raises living standards, and disperses power. An economy that offers opportunity to new entrepreneurs who seek to enrich their lives through hard work is vital. While those political leaders whose first concern is preserving their own power and pre-eminence may rightly view these activities as a threat, they are the path to deliverance for the citizens of these countries.

We should make it perfectly clear that when, for their own political reasons, statist regimes balk at allowing private enterprise to function, the onus of that nation's continued poverty lies squarely on the shoulders of the leaders of those regimes.

We should not, we must not, continue to acquiesce in the statist slander that private enterprise is somehow inconsistent with freedom or that it represents economic servitude. Only when the developing nations accept private enterprise will they realize their true potential. This must be our clear, unambiguous message. It must also be at the heart of our development policies. The United States is already working to assist developing countries to adopt strategies leading toward private sector growth, but we must do more. We owe it not only to ourselves, but to the people of the developing countries to try to persuade their governments that what we are convinced is true is, in fact, true. The key to development lies in a vigorous private sector.

The twentieth century has been a time of extraordinarily varied political and economic experimentation. As with any set of social experiments, some of those launched with the best intentions produced the worst results. For our purposes, it is not necessary to assess the intentions; it is enough to examine the results. In the twenty-first century, the world's prosperity depends on sweeping away those failed experiments. In the future, some other system may be devised that works better than the market system. But the evidence is clear that the market system is more effective than any other yet devised, emphatically including those systems controlled by the state and administered by bureaucracies. Unless the less developed nations accept this, development assistance will fail. If they model their policies accordingly, then development aid can be seed sown in fertile ground.

THE ECONOMIC GIANT

To an extraordinary degree, the world's economic health depends upon that of the United States. In exercising whatever discipline is needed to keep the dollar sound and the American economy on a course of steady, noninflationary growth, we are serving not only our own interests, but those of the world.

While the United States has had a very strong recovery, the picture remains shadowed. The United States had a trade deficit in 1983 of $61 billion, which is expected to rise to $130 billion this year; the dollar is seriously overvalued; real interest rates remain high; and the U.S. budget deficit is still enormous.

If these budget and trade deficits erode the confidence of foreign nations in the U.S economy, the ability of the present international economic system to moderate shocks will be sorely tested and the United States will no longer be able to provide the impetus for economic recovery in other countries.

Figure 1 shows the rise in the U.S. budget deficit, trade deficit, interest rates, and LDC debt load since 1980. We believe there is a direct connection between the rise in the U.S. budget deficit and our overall interest rates. High interest rates, in turn, greatly diminish the ability of developing countries to pay their debts to major U.S. banks.

We recognize that the recent U.S. economic recovery has been the key stimulus to worldwide economic recovery. We applaud the Administration's efforts to reduce the budget deficit and urge it to do everything in its power to continue on this track.

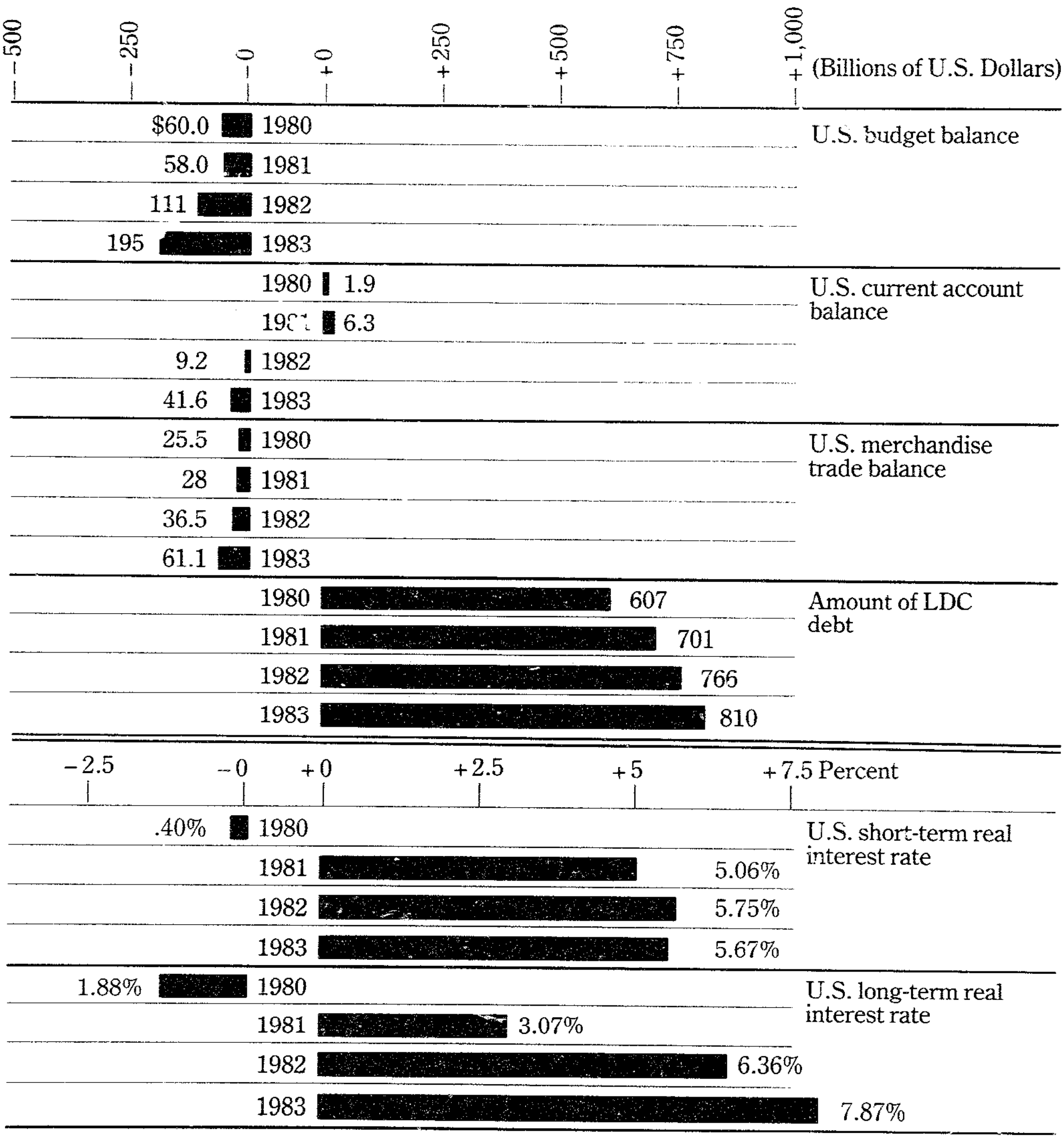
ORGANIZING FOR SUCCESS

Ultimately, principles are only as effective as their application; policies are futile unless put into practice. Government is a constant struggle to reconcile or balance competing interests and conflicting concerns. The way a government organizes itself often determines which of its priorities are served and which are sacrificed. Those that do not have a designated champion of sufficient stature and authority to make themselves heard are likely to be neglected, particularly when they lack a single, vocal, domestic constituency.

The economic interaction between the United States and other countries is central to the future of both. This interaction often takes complex and subtle forms. Sometimes it requires muscle, at other times diplomacy, insight, or a sophisticated understanding of highly technical and often abstruse factors that are far from most people's experience.

FIGURE 1:
Key Economic Indicators

SOURCES:
Economic Report of the President, Council of Economic Advisers, 1984; U.S. Department of Commerce Survey of Current Business, 1984; World Debt Tables, The World Bank. 1983-1984; Federal Reserve, Financial Market Section, 1984.



We believe that our recommendation to establish an Economic Security Council in the Executive Office of the President to ensure adequate coordination of and attention to economic matters is the most important recommendation we make. Without such a council or some similar mechanism in place, it will be extremely difficult to carry out effectively our other program recommendations or to address emerging economic issues in the integrated, comprehensive way that our national interest will require in even the near-term future. This is a classic case of a situation in which policy without structure too readily succumbs to futility.

FREE TRADE, PREDATORY TRADE, AND PROTECTIONISM

Trade is vital to developed and developing countries alike, particularly to those seeking to escape from crushing burdens of foreign debt. Trade represents a far more significant proportion of many developing countries' foreign exchange earnings and expenditures than does Official Development Assistance (ODA). For example, in the aggregate, the $580 billion in developing country export earnings in 1980 amounted to 17 times their net inflow of foreign aid.

Ultimately, foreign borrowing is a form of paying for current imports with deferred exports. In due course, a borrower has to exchange something to repay those debts. Unless current imbalances can be rectified through increased long-term trade opportunities, the debt crisis will never be resolved.

Open trade competition stimulates efficiency and lowers costs to consumers. Recognition of this fact has been a driving force behind U.S. trade policy since the end of World War II. In recent years, however, governmental intervention in trade, whether by subsidizing exports, managing imports, or unfair trade financing practices, has severely affected the patterns of global trade competition. These government interventions distort global competition, to the long-term disadvantage of all participants. When each country closes off its own markets while subsidizing its exporters' entry into others, the result is a clash of interests and a deterioration of trade and true competition. For many years, the United States thought that persuasion would bring a more open trading system. The United States has not seriously used the leverage of its own market since the "Chicken War" of the early 1960s. Nor has the retaliatory authority enacted in the Trade Act of 1974 ever actually been fully applied. It has become increasingly clear, however, that tougher short-term actions may be the only way to accomplish desired long-term objectives.

In this report we propose that the United States embark on an aggressive program of counter-measures including mixed credits financing. We know that this is controversial, but we believe it is needed for two purposes: to deter such practices by others in the future and to protect our own legitimate trading interests in the present.

Although we regret the need for such

measures, the United States should not be apologetic about taking them. There is no inconsistency between using American economic muscle to counter predatory trade policies by U.S. competitors in the short term, and working toward more open trading conditions in the longer term. It is quite the contrary: the first is necessary in order to make the second possible. If other nations were not grossly violating the rules of free trade, there would be no need for coercive or competitive countermeasures. The best way to move the world back in the direction of free trade—not only for our own benefit, but for the benefit of all nations—is to make those predatory measures too expensive. If this means fighting fire with fire—and it does—then so be it. The reason the expression "fighting fire with fire" became a part of the lexicon in the first place is that there were some situations in which firefighters found this technique to be the most effective method of containing the damage. The same holds true in the international economic arena.

It should be very clear that we resort to these methods, not because we like them or believe in them, but because their use by others makes them a competitive necessity for us. We should stress that whenever our competitors are willing to enter into economic disarmament talks, they will find us ready and eager partners. But meanwhile, we cannot leave ourselves disarmed unilaterally.

HARNESSING OUR AGRICULTURAL ABUNDANCE

In fashioning aid and trade policies, we need to make a clear distinction between the long term and the short term, between the ideal and the expedient, between investment and charity, between emergency aid and development assistance. It is essential that we provide both short-term emergency aid and long-term development assistance. But it is equally essential that we not confuse the two. Many of our failures have resulted from precisely that confusion—from supposing that what was needed in the short term was also useful in the long term, or that the same principles applied to both. For example, a critical need of any society is to ensure its people access to sufficient food. All else is secondary; food is the first necessity. America's agricultural abundance is one of the wonders of the modern world. This results partly from abundant, fertile land. But it also results from a highly developed agricultural technology—from advances in farm mechanization, fertilizers, pesticides, finance, storage, transportation, processing, and distribution. In the United States, the 3 percent of the American people who live on the farm not only feed the other 97 percent, but also produce surpluses that feed much of the rest of the world. By contrast, in Bangladesh, 74 percent of the people live on the land and they still have to import over a million tons of food just to maintain inadequate consumption levels.

An ancient proverb tells us that if you

give a man fish, he has food for a day; if you teach him to fish, he has food for a lifetime. One clear lesson of the world's present condition and future prospects is that its people must learn how to multiply their own agricultural production—they must find the way to have food for a lifetime. And because we can help them do that, we must. But while they are learning, they need food to keep them alive. And because of our abundance, we must also help to provide this. Since 1954, U.S. food assistance, under the Food for Peace (or P.L. 480) Program, has provided both the short-term sustenance and long-term development assistance so critically needed today. Rather than waste this country's most productive asset by idling productive farmland, we must use our agricultural abundance to feed the hungry and malnourished multitudes today and teach them to feed themselves tomorrow.

America's own long-term interests have always paralleled the real interests of the world's people, precisely because of the kind of nation we are. Ours is a nation founded on an ideal. Ours is the only nation made up of the people of all nations. We grew rich not by being predatory, but by being productive. And people on every continent have looked to us, whether with admiration or with envy, as an example of what they want for themselves.

GUIDING PRINCIPLES

We believe that three principles should govern U.S. economic relations with the Third World.

- ☐ First, we and the Third World countries have a mutual interest in their economic development. Cooperation between us that serves that mutual interest will benefit both.
- ☐ Second, economic growth is best achieved through vigorous development of the private sector.
- ☐ Third, economic and social development, which fairly benefits all, provides the firmest base for long-term political stability.

In this report, we have sought to put flesh on those principles. We carry them not only into the techniques of economic development, but also into the means of organizing for economic development. We examine ways in which the extraordinary inventive genius of American business can be enlisted more fully in the task. We detail new policies that we believe are needed to expand international trade, to make U.S. exports more competitive, to use U.S. agricultural abundance to feed the world's people, and to share more broadly not only the fruits, but also the roots of our own economic success.

The short-term, narrow question before the nation is how do we get more impact from the billions in aid, credits, guarantees, and other related forms of assistance that the United States now provides? The longer term, broader question is how do we more effectively use our resources and our wisdom to create the kind of world we want for the world's people in the twenty-first century?

It is this broader question we have sought to address. We believe that our generation has an obligation to the world to do what it can to make the twenty-first century—our children's century—one in which the world's people at last enjoy what man's wisdom, invention, and initiative have made possible.

PART III

Economic Development: Private Enterprise, Investment, and Foreign Assistance

The Importance of Private Enterprise and Investment to Development

INTRODUCTION

Developing countries are trying to compress in a few short years the sort of economic progress it took centuries to accomplish in the developed world. This places enormous pressure on these societies. If they are to achieve rapid development, they must find ways to attract and use large quantities of capital, technology, and know-how in an effective and efficient manner. Government can create conditions that will make this possible, but government itself cannot be counted on to produce the goods and services. Success depends on the vigorous stimulation of local private enterprise, combined with a sufficiently high level of foreign investment.

Coming late to the game, the LDCs are burdened with having to move faster to catch up. However, they do have the offsetting advantage of being able to draw on the experience and resources of those who preceded them.

Lessons from the Past

When the nations of the industrialized West first organized modern economies in the nineteenth and early twentieth centuries, government played a very limited role. That role began to expand in the latter part of the nineteenth century, and in many countries it increased still further in the middle third of the twentieth century.

In many developing countries, particularly since World War II, the role of government has been dominant. A view of government as the primary instrument for promoting economic growth has been widespread among leaders, particularly in many nations emerging from colonialism. Whatever the social, historical, or political causes, the effect has been a dramatic increase in government's role in the economy and in the public share of GNP. This has been coupled with substantial growth in public sector ownership and control of the means of production and related activities including manufacturing, extractive industries, finance, and trade. Today, many governments control over half of their nation's capital formation.

Although many countries have gained independence since 1945, only a handful of developing countries have achieved substantially higher living standards for their people. In general, these high-growth countries have been those that have emphasized market-oriented economies and encouraged entrepreneurial initiative.

For various reasons, there has been relatively little academic research or theoretical analysis concerning the role of private enterprise, free markets, and competition as instruments of economic development. However, the empirical evidence is clear that where they exist, development flourishes; where they are absent, development fails. Perhaps the most striking examples of success are in Southeast Asia, where determined market-oriented policies have brought high economic growth rates, significant domestic and foreign investment, and manageable levels of foreign debt. Hong Kong, Taiwan, Singapore, and Republic of Korea alone now account for 50 percent of all LDC manufactured exports.

A limited but increasing body of literature, research and data, Southeast Asian success stories, and a growing awareness among Third World leaders that excessive reliance on the public sector works to their disadvantage are beginning to have an impact on developing country policy approaches. The Task Force believes that many developing country leaders are beginning to rethink and reassess the pros and cons of market-oriented strategies and private investment. The time is ripe for the United States to provide encouragement, advice, and assistance to those developing countries prepared to pursue private sector strategies and to support businesses that are in a position to take advantage of these new attitudes.

The Role of Foreign Direct Investment in the 1980s

During the 1970s, foreign direct investment in developing countries more than tripled. Most of this investment was in the more advanced countries—Latin America, for example, received more than 50 percent—with little directed to the poorest nations. The increase was partly due to the expansion of the world economy, but other factors included the adoption of global manufacturing and marketing strategies by multinational companies, an increase in the standardization of products, and the growth of restrictive trade policies that forced companies to invest in order to retain their markets. During this same period, the U.S. share of foreign investment declined as some of the other more advanced countries, particularly Japan, Germany, and France, increased their investment programs.

However, even this threefold increase in direct investment was of less significance than it might appear. ODA, bank loans, and export credits grew even faster. At its peak, foreign direct investment accounted for only 15-20 percent of total foreign financial flows to the LDCs during this period. Table 2 compares investment flows with other sources of capital in recent years.

At the same time, the relatively low interest rates of the 1970s, high international liquidity, heavy public expenditures, and restrictions placed by countries on direct investments led to massive debt assumption by many countries, with no concurrent increase in internationally competitive productive capacity. In addition, there is strong circumstantial evidence of a loss of confidence and disinvestment on the part of nationals in many countries. Capital flight on a large scale scares off investors; any country suffering massive outflows of capital is not likely to attract much private investment, domestic or foreign. As a result, there has been a significant deterioration in the quantity and quality of indigenous investment.

A recent survey of major corporate investors by the Group of Thirty indicates that these companies plan to increase their foreign investment, but at reduced rates. Further, their plans contemplate a significant increase in the Far East and a decline in Latin America where the debt problem makes it particularly urgent to attract investment capital.

Moreover, the companies intend to finance much of their expansion with locally retained earnings, which may partially reflect their inability to repatriate, and other external sources of finance rather than with new financing from the parent companies. The outlook for new investment in the poorest countries is particularly dismal, with a decline in total assets projected by 1987. While these projections do not tell a complete story, they illustrate the direction in which many investors are heading unless something is done to change their plans.

This study underscores the need for developing countries to find ways to attract more foreign direct investment. The rapid, easy growth years of the 1970s are behind us; bank credits are not likely to increase at the same rate, if at all; ODA cannot provide the needed capital; and export credits will be much more difficult to secure. Thus, foreign direct investment will be even more critical for developing countries in the coming decade and beyond. However, this investment will not take place unless there is significant change in LDC attitudes and the internal conditions that are necessary to attract such investments.

These changes have to come from both sides: investors and host countries. In the past, foreign investors have been much maligned in the developing world. Too often they were portrayed as predators who added little to the domestic

TABLE 2:
Total Net Resource Receipts of Developing Countries from all Sources, 1970-1982 (constant prices)

economy. In fact, the role and attitude of most foreign investors have changed dramatically over the last two decades, while public perceptions have lagged.

The benefits of such investments are demonstrable and increasingly essential to development. Foreign investment creates jobs, often at wages higher than the prevailing rates; it attracts additional, often domestic, investment; it pays taxes, in many cases more honestly than national institutions; and it brings technology, know-how, and management skills.

The obligations of and benefits to investors and host countries must be clearly defined and understood. Investors must be willing to consider creative forms of investment that will meet their needs and still satisfy the political and economic realities of host countries. Production-sharing agreements, licensing and service contracts, franchising, and other contractual types of investment can reduce or eliminate negative perceptions in the host countries that sometimes surround foreign ownership and control, while still providing the investor with necessary incentives and protection.

For its part, the host country must provide basic assurance of fair and equitable treatment for the investor, reasonable access to a continued supply of raw materials, and freedom from unreasonable interference with company decision making, as well as stable and predictable laws and policies. When these essential elements are provided, private investment—both domestic and foreign—will increase. The results—

I. Official Development Assistance
A. Bilateral
1. DAC countries
2. OPEC countries
3. CMEA and other donors
B. Multilateral agencies
II. Grants by private voluntary agencies
III. Non-Concessional flows[a]
A. Official or officially supported
1. Private export credits (DAC)
2. Official export credits (DAC)
3. Multilateral
4. Other official and private flows (DAC)
5. Other donors[b]
B. Private
1. Direct investment
2. Bank sector[a]
3. Bond lending
Total receipts (I + II + III)

Memorandum items:
Short-term bank lending
IMF purchases, net[c]
GNP deflator (1981 = 100)

SOURCE:
Development Cooperation, 1983 Review, Organization for Economic Cooperation and Development.

($ billions)

1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982d
21.30	22.18	21.48	24.72	29.10	32.03	30.19	28.82	33.53	33.79	36.21	36.62	34.97
18.45	19.03	18.47	20.90	24.13	26.16	24.45	22.18	26.36	27.19	28.65	28.70	27.37
14.58	15.31	14.43	13.80	14.51	14.97	14.09	13.85	15.66	17.28	17.56	18.28	18.93
1.00	1.07	1.44	3.96	7.32	8.69	7.67	5.88	8.23	7.36	8.47	7.61	5.63
2.86	2.65	2.60	3.14	2.29	2.51	2.69	2.46	2.47	2.54	2.62	2.81	2.81
2.86	3.16	3.01	3.82	4.97	5.87	5.74	6.63	7.17	6.60	7.56	7.93	(7.61)
2.22	2.21	2.27	2.67	2.15	2.05	2.00	2.04	1.97	2.06	2.24	2.02	2.36
28.22	28.71	29.04	38.71	34.94	52.46	51.77	61.21	69.11	61.08	54.71	69.27	(57.84)
10.20	11.94	8.19	9.47	13.47	16.10	18.78	21.62	22.92	19.81	21.81	22.14	23.12
5.39	6.58	3.14	2.26	4.23	6.76	10.00	12.14	11.58	9.37	10.79	11.33	(9.19)
1.52	1.75	1.62	2.20	1.41	1.83	2.06	1.98	2.65	1.83	2.39	2.01	(2.50)
1.83	2.23	2.21	2.55	3.19	3.87	3.77	3.70	3.68	4.40	4.70	5.68	6.82
0.64	0.68	0.98	1.99	1.46	1.15	1.19	0.86	1.62	1.21	2.17	1.96	(3.07)
0.82	0.70	0.24	0.47	3.18	2.49	1.76	2.94	3.39	3.01	1.77	1.16	(1.53)
18.01	16.77	20.86	29.24	21.46	36.36	32.98	39.59	46.18	41.27	32.90	47.13	34.73
9.51	8.03	9.24	9.20	3.33	17.37	12.33	13.49	13.83	14.20	10.22	16.13	(11.24)
7.73	8.01	10.48	18.91	17.64	18.35	18.84	21.70	27.68	26.35	21.34	29.00	(21.45)
0.77	0.73	1.14	1.13	0.49	0.64	1.81	4.40	4.67	0.72	1.34	2.00	2.04
51.75	53.11	52.79	66.10	66.19	86.54	83.96	92.07	104.61	96.93	93.16	107.92	95.18

							21.98	20.29	16.93	25.22	25.00	17.36
0.88	0.12	0.66	0.70	3.07	0.95	4.42	−0.59	−1.01	0.55	2.53	6.40	6.86
38.80	41.20	45.80	51.30	56.70	65.40	67.40	72.80	83.80	94.50	103.10	100.0	97.90

NOTES:
a) Excluding bond lending and export credits extended by banks which are included under private export credits. Including loans by branches of OECD banks located in offshore centers, and for 1980, 1981, and 1982 participation of non-OECD banks in international syndicates.
b) Incomplete data for other official flows from OPEC countries, CMEA countries, Luxembourg, Spain, Yugoslavia, India, Israel, and China.
c) All purchases minus repayments including reserve branches but excluding loans by the IMF Trust Fund included under multilateral ODA above.
d) ( ) estimated

Figures concerning non-DAC member countries are based as far as possible on information released by donor countries and international organizations, and completed by OECD secretariat estimates based on other published and unpublished sources. They may therefore not comply in all respects with the norms of criteria used by DAC members in their statistical reports made directly to the OECD secretariat.

more economic activity, a rise in employment, increased public revenue, improved technology, and a higher standard of living—will benefit all.

The U.S. Government's Role

Whether foreign investment will flow to a developing country depends primarily on the actions of the host country and investors. However, the U.S. Government also has an important role to play. Not only must U.S. policies encourage the free flow of investment, whether in the form of capital, technology, or intellectual property, but U.S. foreign assistance resources must be enlisted to stimulate increased flows to developing country markets. The positive impact of direct foreign investment must be communicated to LDC officials and the impediments to achieving policy changes must be identified and clearly stated. Finally, we must be prepared to support positive policy responses through appropriate use of foreign assistance resources.

As an adjunct to this report, we have prepared a *Private Enterprise Guidebook* to provide guidance on ways investment can be encouraged and development aided through creative use of private enterprise. We consider the Guidebook to be a unique and significant contribution by the Task Force. It is designed for use principally by U.S. Government personnel at home and abroad. Essentially, it arms the U.S. Government official with facts, ideas, examples, and arguments to help persuade developing country officials that their countries will be better served by taking the market-oriented route. The Guidebook provides examples of how foreign assistance funds have been used creatively to foster private enterprise. We believe that this Guidebook can significantly increase the effectiveness of our representatives overseas in aiding development, enlarging trade, and promoting prosperity.

FINDINGS AND RECOMMENDATIONS

Finding

Countries that fail to create conditions—including appropriate laws and policies—that will attract investment will relegate themselves to slow growth. At the present time, there is no central source of advice to help developing countries foster the conditions necessary for private sector growth.

Overview: Without economic growth there is little to distribute, whether to a stable or expanding population. Governments establish the basic conditions that determine whether private initiative can flourish and growth can take place. Private initiative is necessary to create that growth. Among the necessary conditions, the key factors are affirmative support for private ownership and the right to transfer such ownership. Both law and custom must recognize the right of private ownership not only of property, but also of the means of production; private contracts must be recognized and enforced; and the right of individuals to form associations for the purpose of doing business as private enterprises must be protected. In addition, there must be sufficient freedom for businesses to make their own decision and a general attitudinal climate that encourages, rather than inhibits, private enterprise. Other conditions of a general nature are also important, including reasonably free access to markets in which to buy and sell, adequate supporting infrastructure, a stable operating environment, and the availability of labor.

When conditions are attractive, business responds with investment. When conditions are not right, foreign investors will not invest and, worse, even local investors will send their funds elsewhere. The responsibility of the developing country government is to ensure that the proper conditions exist.

Developing country demand for domestic and foreign investment will far outstrip the amount likely to be available in the coming decade. In effect, there will be a seller's market for capital. Those countries that fail to create an attractive investment climate will attract less investment, whether domestic or foreign. They will thus relegate themselves to a period of slow growth in which they fall further behind. Developed countries must seek to stimulate increased private investment flows to the developing world. For those countries with limited resources, it simply makes common sense to encourage the channelling of those resources where they will do the most good.

In the case of the United States, total foreign direct investment abroad is estimated at over $220 billion, of which about one-fourth is in the developing world. Because of the need to supply raw materials and other inputs to foreign subsidiaries or outlets, some 30 percent of U.S. exports are directly related to foreign private investment. However, many U.S. investors have found it extremely difficult to operate in some countries. In these instances, they have been unable to achieve satisfactory earnings and repatriation of capital and profits, which has reduced their enthusiasm. They need encouragement from the host countries. They also need encouragement in the form of incentives from the U.S. Government.

In 1983, President Reagan issued a statement clarifying U.S. policy on foreign investment. Its fundamental premise was that "foreign investment flows which respond to market forces will lead to more efficient international production and thereby benefit both home and host countries." It strongly supported measures to improve the investment climate, eliminate restraints on the free movement of investment, and secure equitable treatment of national and foreign investors. This statement provides a solid underpinning for U.S. efforts to improve the international environment for the free movement and protection of capital, technology, and intellectual property. It can be an important foundation for future action.

Recommendation

The United States, working with other donor nations, developing countries, multilateral institutions, and private business, should establish a Private Enterprise Insitute that will serve as a research center to advise developing countries on how to create those conditions necessary to attract investment and foster trade.

Discussion: The debate over how best to foster development has been dominated by those who believe that centralized economic management is the most effective and equitable means. As a result, there is a massive amount of academic and official literature dealing with such development approaches, while relatively little provides qualitative and quantitative analyses on the effect of open markets and private enterprise on a country's development. No central point for research, information, or statistics exists to consolidate knowledge about the private sector and its impact on development. The International Monetary Fund (IMF), the Development Assistance Committee of the Organization for Economic Cooperation and Development (OECD), and the World Bank are all very good sources of information and statistical material. But because their focus is not directed specifically toward the private sector, significant gaps exist in terms of available information and analysis.

Recent establishment of the Center for International Private Enterprise (CIPE), under the auspices of the U.S. Chamber of Commerce, is a creative effort to give business a greater voice in promoting democracy abroad. It cannot fill the present void, however, because it speaks only from the American experience. A broader perspective is needed in order to establish credibility throughout the world.

To respond to this need, we propose that an independent Private Enterprise Institute be established. To win wide acceptance, the Institute must have the broad-based sponsorship and active participation of donor and developing countries, international institutions, and the private sector itself. The Institute's primary functions would include the collection, analysis, and distribution of information pertaining to the private sector's role in economic development. It would collect and catalogue case studies on how the private sector functions in those countries that have the best rates of economic growth and development. It would promote the development and adoption of international standards to facilitate trade and investment. It would also examine the causes of slow growth. It would give special attention to projects funded by ODA that encourage private sector development. The analysis would be useful to governments as well as businesses interested in knowing how and where the private sector works best; an element of training would be included to assure appropriate dissemination of the information and ideas developed.

Finding

New foreign investment will be difficult to attract for many debt-ridden LDCs as long as insufficient foreign exchange is available to the private sector.

Overview: The effect of the massive assumption of debt by many LDCs, particularly in Latin America during the 1970s and early 1980s, has been devastating to those countries in various ways. One effect that has not received sufficient public attention is the impact on privately owned businesses when foreign exchange is not made available to them for their reasonable needs.

During periods of foreign exchange shortage, private enterprise is usually at the end of the queue at the Central Bank. It is often difficult or impossible for businesses to secure foreign exchange to pay for needed imports in order to keep an investment operative, to service foreign debt or, for that matter, to repatriate capital. Such difficulties diminish the prospect that new foreign investment will be attracted to the developing country.

To date, the United States has followed a five-point strategy for dealing with the debt situation on a country-by-country basis. That strategy calls for:

☐ continued pursuit of economic adjustment policies by debtor countries;

☐ sustained world economic growth and recovery with open markets;

☐ encouragement of the adjustment process through strong support of the IMF;

☐ emergency infusions of liquidity, as necessary, to allow countries financial breathing space; and

☐ adequate amounts of commercial bank financing, both medium-term and trade.

At the London Economic Summit in June of 1984, the leaders of the major industrialized countries took a somewhat longer term approach to the problem, stressing the need for longer term reschedulings, substituting long-term debt for short-term debt, and encouraging the flow of long-term direct investment. Foreign investment will remain at depressed levels and trade will continue to be distorted, however, until a more active and positive approach takes hold. The more positive approach will create the needed international confidence that the debt crisis will be equitably resolved and foster the perception that private enterprise will not be disadvantaged in international transactions.

Recommendation

The United States should take the lead in assuring that private needs for credit and foreign exchange in LDCs are not pushed aside by preferred access of the public sector.

Discussion: Foreign exchange shortages have resulted in the government allocation of available convertible currencies in most borrowing countries. Private firms in need of hard currencies to pay for imports or to service their foreign debt generally compete unsuccessfully for allocations of foreign exchange against government entities that are more likely to be favored by the government allocation system. Private enterprises lose their creditworthiness and, as a consequence, potential investors become unwilling to invest. The result is exactly the opposite of what is needed: encouragement of the dynamic forces of the private sector.

The United States should take the lead in making this problem clear to LDC debtor countries and in devising ways to secure more balanced foreign exchange allocation systems where they are needed. This is a subject that should be addressed by those responsible for the U.S. position in LDC debt negotiations, whether in connection with official obligations to the U.S. Government, or as related to coordinated approaches to commercial bank debt. Essentially, U.S. negotiators should be looking for ways to assure more reasonable private sector access to scarce foreign exchange in any allocation process.

Finding

The United States and other donors do not make sufficient effort to increase private investment and improve the investment climate in developing countries

Overview: Among the principal investing countries, there is a general recognition of the need to improve the investment climate in developing countries and to establish ground rules under which investments can be made. This need is less well-recognized among the developing countries, although acceptance of the idea is growing.

Recommendation

The United States should strongly encourage international dialogue on ways to support increased foreign direct investment.

Discussion: The key to the economic success of the United States is its reliance on private enterprise and free markets. We should transfer this success through all available means, including our foreign assistance programs. We should, in effect, use our diplomatic and aid programs to teach other nations how to move away from government-dominated economies toward open markets. In 1982, the leadership of the OECD recognized the growing importance of international investment flows for global economic growth and the need to strengthen international cooperation on investment issues. The organization has begun to "identify ways to increase the flow of foreign direct investment to developing countries and to enhance the contribution of this investment to economic growth, development, and world trade." Several OECD committees are examining this subject, with particular attention to the types of policies—for both developed and developing countries—that will increase the flow of foreign direct investment. Some of the areas under consideration include institutional reforms, the establishment of policy advisory services, increased capital investment in intermediate credit institutions, infrastructure essential to the industrial sector, and subsidies to small and medium-sized private foreign investors in certain sectors. The Task Force believes that all of these subjects are worthy of further consideration and study.

United Nations bodies have also sought to address aspects of the foreign direct investment issue. For example, the United Nations is attempting to develop a Code of Conduct for Transnational Corporations that is acceptable to both host and home countries. The United Nations Industrial Development Organization (UNIDO) established a service in New York to conduct training of LDC officials as a way to assist these countries in their efforts to attract U.S. private investment. UNIDO has also formed a Caribbean Investment Promotion Service (CIPS), partially financed by AID, for investment promotion in that area. The United Nations Center on Transnational Corporations is closely involved in data gathering and responding to private investment questions. Related issues have also been discussed in the United Nations Commission on Trade and Development (UNCTAD) as well as other United Nations fora.

We do not expect these United Nations efforts to provide any near-term breakthroughs or to substantially increase common understanding between the United States and the developing world concerning foreign investment. They are useful, however, in reducing the emotional content of the debate and in sensitizing policymakers to the issues and stakes involved.

Recommendation

The United States should substantially increase its support of private investment activities in developing countries.

Discussion: Under existing procedures and practices, the prospects for channelling significant U.S. foreign assistance resources directly to the private sector in recipient countries are severely limited. There are various reasons for this, including the fact that responsibility is spread among several U.S. Government agencies, with no single entity having the development of the LDC private sector as its primary mandate. Generally, this issue is given insufficient attention within the U.S. bureaucracy. Conversely, in many developing countries, private sector proposals are given too much scrutiny by the government. This makes investment decisions difficult and stifles private sector initiatives.

The United States should demonstrate its commitment to, and belief in, market-oriented private sector solutions to development problems by allocating substantial resources for private sector development and investment, particularly through intermediate credit institutions. (For additional discussion on this subject, see page 57.) More U.S. foreign assistance funds should be available for purely private entrepreneurial undertakings, supporting those frequently disadvantaged in obtaining foreign exchange and other scarce resources that are usually provided more readily to state-run enterprises through state-controlled development budgets. The African

Economic Policy Initiative (see pages 46 and 97) is consistent with this approach.

To encourage continued U.S. private sector participation in these efforts, existing tax and other incentives for U.S. business involvement in developing countries should be maintained; new incentives for investment in selected industries or countries should be considered.

Finding

In order to increase foreign investment, developed and developing countries need to adopt uniform standards for host country and investor responsibility and conduct.

Overview: Many developed countries with long histories of active external investment and trade have found it useful to enter into agreements with developing countries on the treatment of their nationals when they invest. Some countries, such as the Federal Republic of Germany (FRG), make investment treaties a precondition for investment insurance. In fact, Western industrial countries now have over 200 such investment treaties in place.

Recommendation

The United States should encourage developing nations to negotiate bilateral investment treaties. The United States should assign priority in its aid programs to those countries that sign such treaties.

Discussion: The United States has signed five investment treaties with developing countries since 1981 and is discussing such treaties with a number of others. The purpose of the Bilateral Investment Treaty (BIT) program is to improve the investment climate in recipient countries (the treaties apply to investment in both directions) by providing certain protections and guarantees to foreign investors.

The common objective is to provide a stable and predictable legal framework for investment and business operations. The treaties establish the ground rules for investment as well as the terms under which business is conducted. Generally, areas that are covered include: equal treatment with national investors or most favored nation status; prompt, adequate, and effective compensation for expropriation; the right to transfer profits; dispute settlement procedures; and the right to international arbitration.

The Bilateral Investment Treaty approach has not been as successful as it might have been. In fact, no country with significant U.S. private investment has yet signed such a treaty; only relatively small countries, or those with little appeal to investors, have accepted the provisions. To date, those developing countries with large American investment have felt no compulsion to enter into such an agreement. A major related problem is that in Latin America, many countries adhere to the Calvo Doctrine, which essentially requires dispute settlement in the country where the investment is made. The effect of this doctrine is to eliminate one of the main potential benefits that might be obtained from the investment treaty.

Nonetheless, the effort to negotiate such treaties with foreign governments should be continued. The dialogue surrounding the negotiations, even though unsuccessful in the short run, is an effective means of educating LDC leaders to the benefits of encouraging the private sector. Consideration should be given to negotiating a wider range of possible agreements, from more limited protocols and understandings to the full range of assurances desired in a complete bilateral investment treaty. More limited agreements might be entered into with countries that, although they are logical recipients of U.S. investments, are not yet prepared to negotiate a full scale treaty.

As a means to underscore the importance the United States attaches to these treaties, AID should give priority to nations that sign or adopt the principal components of such treaties.

Finding

Expanded investment insurance (or guarantee) is a key to increasing investment in developing countries.

Overview: Investment insurance (or guarantee) is one important direct means by which investor countries can ease the way for expanded investment in developing countries. The objective of most such programs is not to remove commercial risk, but to protect against certain risks peculiar to investment overseas.

While many investor countries provide some form of investment insurance for their nationals, in all cases it is limited in amount and restricted as to which countries are covered. Further, each investor country has its own rules and regulations. With each investor country negotiating separately, the developing countries are faced with a plethora of different terms and conditions.

Recommendation

Overseas Private Investment Corporation (OPIC) funding and insurance capability should be substantially increased and its mandate broadened to include a full range of financing and services to U.S. business, large and small.

Discussion: The Overseas Private Investment Corporation (OPIC) mobilizes and facilitates the flow of investment capital and skills from the United States to developing countries. It insures U.S. private investment against certain political risks, as well as providing direct financing and limited amounts of commercial guarantees for projects of U.S. investors in eligible countries. OPIC is self-sustaining, earning over $82 million in FY 1983. (It has received no appropriations since 1975.) OPIC has requested additional authority, but no new appropriations, for commercial guarantees and direct loans.

The Task Force recommends a substantial increase in OPIC's authorities to provide direct loans, loan guarantees, and investment encouragement. The OPIC board should consider various ways of broadening OPIC activities, such as increasing support for agriindustrial projects and reducing the threshold of U.S. business participation to a minimum requirement of 20 percent ownership. OPIC should also consider additional forms of insurance coverage for U.S. business that would contribute to further risk reduction and facilitate additional investments in developing countries.

The 124 projects insured or financed by OPIC in 39 countries in FY 1983 represent $4 billion in investment. Over half of these projects were in the poorest developing countries. In the recipient developing countries, during the first five years of operation, these projects are expected to generate approximately 25,300 jobs, including 4,000 at the management level. Additional employment will also be created as a result of local procurement of goods and services. During the same five-year period, the projects are expected to generate net foreign exchange savings for the developing countries of over $400 million per year.

During their first five years of operation, these projects will generate over 33,000 U.S. jobs in manufacturing, mining, growing, processing, and shipping of additional U.S. exports related to the projects. As the economies of the project countries develop, additional U.S. employment can be expected with increased demand for U.S. equipment, material, and services. The U.S. balance of payments position will also be improved; OPIC estimates that the net direct trade benefit to the United States will amount to $2.4 billion. More fundamentally, these programs are instrumental in engaging small and medium-sized U.S. businesses in international investment activities that would otherwise be beyond their grasp. These programs are well regarded by U.S. business and deserve continued support. At the same time, we are encouraged by the increasing availability of private insurance for some of those purposes.

Recommendation

The United States should support a multilateral investment guarantee program administered by the World Bank.

Discussion: The World Bank has estimated that less than 20 percent of the investments flowing from developed to developing countries are covered by insurance from national agencies such as OPIC; private insurers cover an even smaller proportion of the total. Most investment, then, is not insured against the political risks inherent in the exposure of capital in developing countries.

The concept of a multilateral insurance or guarantee program has been discussed since the 1950s. In the early 1970s, the World Bank made a major effort to establish such an insurance program, but failed to secure the support of enough members. The differences were not only those of approach; they also arose because developing countries feared the loss of sovereignty, while many donor countries feared competition with their national insurance programs. The Inter-American Development Bank (IDB) made an effort in the late 1970s with regard to minerals and energy investments, but it failed for the same reasons.

A specific proposal for a multilateral investment guarantee program has been raised again in World Bank circles. An investment guarantee agency would be established under the auspices of the Bank to protect investments that are not being insured by national institutions or private insurers, thus increasing total investment flows. The new agency would cooperate with existing national insurance programs and would complement them through coinsurance and reinsurance programs. The agency would be funded by World Bank members and it would negotiate its own agreements, furthering the prospect for greater standardization in this area.

At this point, the proposal appears to be gaining support among the members of the World Bank. Nonetheless, the underlying concerns of the developing countries continue to stem from fears related to loss of sovereignty and control, while some developed countries continue to see it as a potential competitor for their national insurance and guarantee programs. The United States should strongly support this attempt to improve the conditions under which foreign investments can be undertaken.

Foreign Assistance Programs and Private Enterprise Development

INTRODUCTION

Foreign assistance can have only a limited impact as a resource transfer mechanism, given the size of developing country economies and the problems they face because of debt burdens, the global recession, and internal economic difficulties. (On a global basis, the foreign assistance disbursements of all OECD members would cover interest on LDC debt for less than six months.) Nevertheless, much more could be accomplished if aid resources were concentrated on a few critical areas—particularly on strengthening private enterprise in, and fostering trade and investment with, developing countries.

Over the nearly four decades since the Marshall Plan came into existence, U.S. foreign assistance has grown into a complex of programs and budgetary accounts, each with a separate justification, legislative history, constituency, and reason for continuance. Many foreign assistance practitioners themselves get lost among the shifts of nuance in definition and purpose from one assistance form to another.

The Congress has not provided a clear direction either for the goals of aid, or for the terms under which it should be provided. Over the years, foreign assistance legislation has been heavily amended, with layer upon layer of requirements, caveats, prohibitions, and special instructions. Our foreign assistance efforts have become a patchwork of programs, addressed to different constituencies and based on various theories of economic and social development.

Through our foreign assistance resources we should continue to foster both economic and social development. But in the programs as they are now structured, there is an imbalance between those aimed at meeting social needs and those that address economic needs. Public health, population, nutrition, and education programs, while important, are not at the core of economic development. With economic development come the resources necessary to pay for the social programs which can, in turn, help accelerate the development. The flaw in our past foreign assistance strategy was that it put the cart before the horse. The "cart" is social development; the "horse" is the productive economic base to support social development. And this means private enterprise. The Task Force reviewed U.S. foreign assistance programs, past and present, seeking to determine which have had the greatest positive impact and why. It is clear that if we were starting from scratch, the present system would not be ideal. The questions now are what is optimal, given the structure of the U.S. Government; what impact would any change have; and how long would it take to effect such change.

In this section, we deal with major changes we believe necessary in the U.S. foreign assistance program to:

1. ► effect long-term policy change;
2. ► develop a long-term economic assistance strategy;
3. ► improve linkages between U.S. trade and aid efforts;
4. ► expand agricultural assistance;
5. ► support multilateral institutions;
6. ► strengthen AID's private enterprise initiative; and
7. ► increase training.

These subjects are discussed in greater detail in the action briefs in the appendix of this report.

We have not addressed the basic organizational structure within which foreign assistance programs are carried out. Whatever the structure of operating agencies, however, the same policy considerations would apply. It is those policy considerations that we have addressed.*

*NOTE:
It follows, obviously, that if functions now performed by AID, for example, were eventually reassigned, any comments in this report addressed to AID but related to those functions would be intended for the agency to which the functions were transferred.

FINDINGS AND RECOMMENDATIONS

1.► Policy Change

Finding

The U.S. Government does not sufficiently encourage or assist recipient developing countries in making the policy changes necessary to allow private sector growth.

Overview: Public sector funds can only supplement, not supplant, the resources that must come from the private sector in the form of trade and investment.

Internationally, there has been a tendency over the last 10 or 15 years to put virtually all foreign assistance on a government-to-government basis. In response to congressional mandates and the "Basic Human Needs" doctrine, U.S. foreign assistance programs have placed nearly their entire emphasis on meeting the immediate needs of the poor, rather than on developing their capacity to meet their own needs over the longer term by stimulating private sector growth and employment. Within the U.S. Government, there appears to be a growing recognition of the need for market-oriented policy change. AID, in particular, has made a strong commitment to use its resources to promote appropriate policy changes in developing countries, but such efforts must be greatly intensified and more thoroughly ingrained in U.S. foreign assistance programs.

We believe strongly that primary emphasis must be placed on the long term, and that sustained economic growth depends on the private sector. Without rising levels of economic activity, basic human needs cannot be met.

We owe it not only to ourselves, but to the people of the developing countries, to try to persuade their governments that what we believe to be true is, in fact, true: that the key to development lies in a vigorous private sector. Politically, this has its costs. Some developing country governments are committed ideologically to statist approaches; and many of their political leaders profit, some of them immensely, from statist economies. By pressing them to shift toward market-oriented models, we will irritate some and alienate others. But, while pandering may be good politics in the short run, it is bad politics in the long run.

To the extent that we can achieve it, close cooperation with other donor countries and institutions can buffer the irritation and also achieve more significant policy results. In any case, if we demonstrate that we are steadfastly committed to the principle of economic development through private sector growth, other developed and developing nations will be more willing to join with us. Our own record of economic development gives us a credential that we should use far more boldly. In this important area, we have both an opportunity and a responsibility to lead, not just to follow.

Recommendation

The United States should sharply increase its efforts to guide developing countries toward market-oriented policies; it should reward those countries that adopt strategies that will lead to a positive climate for business and investment.

Discussion: U.S. support for market-oriented policy reform must be clearly articulated, understood, and practiced by all U.S. agencies. There should be a concerted effort to identify the major impediments to private enterprise in each developing country and the steps the U.S. Government can take to help that country remove those impediments, including assistance to ease the burden of adjustment, if necessary. Our assistance programs should, to the extent feasible, reward countries that adopt appropriate market-oriented economic policies.

Our present foreign assistance programs do, to some extent, help developing countries stimulate private enterprise—for example, by trying to persuade developing countries to adopt agricultural policies that will encourage local farmers to increase production. There are other examples. In one country, at AID's urging, retail fertilizer distribution was transferred entirely from the public sector to the private sector; wholesale and import activities are now under joint study for the same shift. In a Caribbean country, more liberal foreign exchange market rules were established to remove a significant disincentive to exports. In an African country, AID and a host of other donors agreed to provide food aid in exchange for a gradual restructuring of cereals marketing, abolishing a public sector monopoly.

The AID African Economic Policy Initiative, a proposed five-year, $500 million program that is specifically directed to those countries that establish a sound and comprehensive policy framework—particularly in agriculture—is a step in the right direction. The U.S. foreign assistance effort will be more effective if this selective effort to identify and support sound policies and actions and enlist other donors in the process is followed by similar initiatives elsewhere.

These examples illustrate what can be done through persuasion. We understand the sensitive nature of sovereignty and the constraints that prevent foreign assistance agencies from publicizing some of their policy successes; however, we believe the U.S. Government needs to do much more in the area of "policy dialogue." The *Private Enterprise Guidebook* describes some AID policy successes that might be replicated.

In its policy dialogue efforts, AID has sometimes found that it could not forcefully and credibly insist on policy reform to support the private sector in exchange for AID funds. There are many reasons for this, ranging from U.S. political considerations to the size of AID's program in countries where limited funds provide little leverage for change. On the other hand, in some countries where AID has a large budget, there is a commonly held belief among officials in both the U.S. mission and in the host government that threats to tie

AID funds to policy reform are only a "bluff." In many cases, the host government believes that the U.S Government's political interests in the country are so strong that it cannot afford to offend that country by reducing AID's activities. There is often a concern among U.S. policymakers that if we cut off our funds, the recipient country will turn to another donor, possibly the Eastern Bloc, which would be counter to U.S. interests.

Even though we recognize the validity of these concerns, we believe that, in planning its foreign assistance budgets and future programs, the U.S. Government should more strongly take into account the policies of recipients and devote a greater portion of its resources to those that actively encourage the development of private enterprise. Such an approach would serve as an incentive and a reward to those countries that are prepared to adopt sound policies and a disincentive to those that are not. It would also place our resources where they would do the most good.

Recommendation

U.S. food assistance should be used to a greater extent as an incentive for developing countries to adopt market-oriented policies that encourage the private sector to increase agricultural production.

Discussion: While most developing countries are capable of significantly expanding their indigenous food production, the task is often hampered either by resource constraints or by misguided policies. Many countries have used government resources to maintain urban consumption, rather than adopt appropriate incentives to encourage agricultural production.

Perhaps the greatest production constraint is the legacy of inconsistent and often misguided agricultural policies. Developing country governments are increasingly involved in performing functions related to food production, processing, and distribution that could be managed more efficiently by the private sector. Furthermore, in too many countries policies aimed at keeping urban food prices low are achieved by paying low prices to producers.

If effectively used, food aid can provide leverage for negotiating changes in policies and can help cushion the impact of the adjustment process. For example, in countries that adopt policies to provide adequate incentives to farmers, appropriately designed food aid programs can allow the gradual phasing in of higher consumer food costs, thus averting major upheavals in the economy.

Recognizing the primary importance of recipient government policies to agricultural development, the U.S. Government has, for many years, required developing countries to agree to certain "self-help" measures as a condition of P.L. 480 Title I agreements. These measures are designed to promote agricultural production, research, and development and create a favorable environment for private enterprise and investment. In negotiating new agreements, the U.S. Government should require firmer commitments to such policy changes.

Adding to the misguided policy burden, the debt burden of many developing countries reduces their ability to import needed food supplies, use available foreign exchange for private enterprise development, or initiate needed policy changes. In recognition of this constraint to economic development, the President should ask Congress to restore the flexibility to permit P.L. 480 sales for local currency, expand the use of the P.L. 480 debt forgiveness authority, and adopt other changes outlined in the P.L. 480 Action Brief (see appendix). This would improve the use of P.L. 480 as a tool to support policy dialogue and lend flexibility to the foreign assistance program.

2.► Long-Term Economic Strategy

Finding

U.S. foreign assistance programs are often required to address problems other than those related to long-term stability and economic growth.

Overview: In FY 1984, foreign assistance resources totaled about $15.3 billion, of which $8.8 billion was described as economic and $6.5 billion as military assistance. Of the economic aid, however, $1.6 billion went to multilateral institutions and $3.3 billion went to Economic Support Funds (ESF), which serve what are essentially security rather than long-term developmental purposes. This left about $3.9 billion for direct economic assistance, both developmental and humanitarian.

Recommendation

The economic component of U.S. foreign assistance programs should have a higher national priority.

Discussion: Secretary of State George P. Shultz identified four U.S. interests served by the foreign assistance program: (1) a growing world economy, (2) protection of America's vital interests; (3) building democracy and the rule of law; and (4) our humanitarian interests. A vigorous free world economy is a necessary support for all of these interests. Whatever level of military aid is required to satisfy U.S. security interests, it should not be at the expense of economic aid. Levels of economic aid should respond to the extent of need and the dimensions of opportunity.

In past years, it was fashionable to dismiss foreign economic aid as a "giveaway," as if we got nothing in return. Nothing could be further from the truth. Whatever waste there may have been in the past, a properly conceived aid program has been and can be even more of an investment in America's future that will pay for itself many times over. With economic aid, we can buy much-needed stability in vital but vulnerable Third World countries. We can open new markets, increase trade, stimulate job growth, spread hope, and create the sort of climate in which freedom can flourish in future generations. The more we invest in economic development now, the less we are likely to have to spend on arms later.

3.► Linking Trade and Aid

Finding

The links between our foreign assistance program and U.S. foreign trade are inadequate.

Overview: In the normal course of designing development assistance programs, the developmental impact of trade is often overlooked. Increased emphasis on the trade-aid linkage will benefit both the United States and the developing countries. The need for a U.S. Government-wide policy to link aid and trade is discussed in the section dealing with the formation of U.S. economic policy (see page 65). We also analyze separately, in part V, the subject of blending aid and official export credits to finance major projects.

Recommendation

The scope and financing of the Trade and Development Program (TDP) should be expanded.

Discussion: The Trade and Development Program is an excellent model for the linking of trade and aid. On the U.S. export side, TDP has proven to be one of the most effective of the government programs that use foreign assistance funds to involve the U.S. private sector in trade and development activities. TDP finances feasibility studies and other planning services in developing countries for projects, such as telecommunication networks and hydropower facilities, which offer potential markets for U.S. exports. TDP-financed feasibility studies involve U.S. firms at an early enough stage to encourage subsequent contract awards to U.S. firms for equipment and services associated with the projects. TDP also provides the developing country with comprehensive access to U.S.development technologies and project planning skills. This can lead, in turn, to participation by U.S. firms in other projects in that country and can give the U.S. business sector increased knowledge about developing country markets and operating environments. In fact, TDP is now the principal link between our foreign assistance program and trade opportunities for U.S. business. The program has generated at least $500 million in U.S. exports by financing a total of approximately $20 million in feasibility studies.

There is fierce competition from other nations for large contracts associated with major projects in developing countries. The Administration recognizes this and has increased TDP's budget fourfold since 1981 to a proposed $21 million for FY 1985. However, our foreign competitors, particularly Japan, France, Canada, Italy, and Australia, finance TDP-type programs that are substantially larger than TDP. The organization's effectiveness would be enhanced if its authority were broadened to include financing the training component of a feasibility study, or conceivably of a project, to be undertaken by a U.S. firm.

Recommendation

TDP techniques should be applied to other foreign assistance programs, specifically those carried out by AID, to the maximum extent possible.

Discussion: The Task Force has been impressed with the efficiency, flexibility, and effectiveness of TDP. TDP's basic approach is to involve primarily business, not government, in delivering assistance. This benefits both the United States and developing countries. Various techniques have been refined by TDP to leverage its resources, such as sharing the cost of feasibility studies that result in projects. These techniques could be adapted to AID's broader development assistance activities, not merely to feasibility study financing, but for integrated project financing as well. For example, in agribusiness, AID and U.S. firms could cooperate in the financing and execution of an agribusiness project in Africa. If the initial, jointly financed study confirmed the feasibility of such an undertaking, the prospect of developing a cofinancing package would be improved as a result of the familiarity of both entities with the project. At that juncture, outside financing could be sought for most of the project, while AID could elect to partly finance some infrastructure aspect of the project—such as improved housing for workers, training programs, or a health care system.

Recommendation

U.S. foreign assistance resources should be used to build up the trading capacity of developing countries.

Discussion: We believe the trade-aid linkage is a two-way street. Just as we recommend using aid funds to increase trade from the United States, we also recommend using aid funds to build up the capacity of developing countries to export goods and services. We elaborate on this recommendation in our action brief on AID's private enterprise thrust.

Recommendation

U.S. foreign assistance resources should be used to assist in China's modernization process.

Discussion: With over a billion people—one third of the population of the entire developing world—China represents a special case. In effect, its size and its history together put it in a category by itself.

Since the Communist takeover, China's political and economic history have been tumultuous. Its economy is now in a dramatic state of transition. The present government is pressing forward with private sector incentives. The Chinese economic system is opening in ways that not only allow but encourage market-oriented operations. Hungary and Yugoslavia have already introduced capitalist incentives into their systems; now China has started on its own market incentive road.

We recognize that there are unique geopolitical issues involved in the development of additional ties with China and that China's recent past clouds forecasts of its future. Nevertheless, we believe it is important to reinforce and encourage the steps toward private enterprise development that China has taken and to help China address some of the problems that have arisen as a result of its increasing reliance on market incentives. Various program options are discussed in the U.S.-China Trade Relations Action Brief.

Recommendation

U.S. foreign assistance agencies—such as AID, OPIC, and TDP—should package their financial and other resources to promote greater two-way trade between the United States and developing countries.

Discussion: The International Development Cooperation Agency (IDCA) is composed of AID, OPIC, and TDP. In addition to the feasibility study financing and other planning services offered by TDP and the insurance, reinsurance, and financing services offered by OPIC, AID has a variety of financing and non-financing resources that can be blended. These resources include training funds, the Housing Investment Guarantee Programs that provide shelter assistance, the Private Enterprise Revolving Fund to encourage private enterprise development, Development Assistance, Economic Support Funds, P.L. 480, and programs for technology transfer/sales to developing countries. The trade potential of such programs should not be an afterthought for program managers. It is an important feature of foreign assistance for developing countries and for the United States.

4. ► Agricultural Assistance

Finding

In implementing its agricultural development policies, AID has not given private agribusiness activities the attention and support they deserve.

Overview: Historically, success in agriculture—both in the United States and in the developing world—has depended upon the efforts of the individual family farmer. With his initiative and energy, the individual agricultural producer offers the most realistic prospect for meeting the challenge of world hunger.

In many countries, agribusiness activities are performed by public bodies (parastatals). In most cases, these have performed unsatisfactorily and they themselves have frequently become serious impediments to development. Private agribusiness firms could perform these functions more efficiently, while, at the same time, expanding markets and creating new jobs.

Recommendation

Private sector efforts to form private sector agribusiness development corporations should be encouraged and supported.

Discussion: No private or public U.S. institution now provides the necessary combination of equity capital, management expertise, and ability to bring together U.S. and developing country agribusiness partners on any substantial scale. The World Bank's International Finance Corporation (IFC) is available to American firms, but it is not solely focused on agribusiness and, as a multilateral organization, it has no particular responsibility to address specific concerns of U.S. companies.

One example the Task Force reviewed was the effort of a U.S. private group to establish an American Agricultural Development Corporation, financed by both the public and private sectors, to provide equity and debt capital to LDC agribusiness and to help in the transition from public to private ownership of agribusiness activities in developing countries. The proposed corporation would be structured as a for-profit venture expected to recover its costs, earn profits, and pay dividends. The equity capital would be subscribed by the private sector, with contributions to operating expenses in the initial years from private not-for-profit organizations (major private foundations). Additional capital would be sought in the form of low-interest loans from AID. Assistance might also be sought from OPIC. Another example is the non-profit World Food Corporation (WFC), which organizes and manages profit-oriented small-farm agricultural development projects financed by U.S. and host country private investors and development assistance agencies.

A successful corporation would facilitate private enterprise development in developing countries, while also enhancing market development and trade objectives. U.S. private business participation through such a mechanism would provide increased direct private investment, with the related transfer of modern technology and management skills, fostering of an entrepreneurial spirit, and opportunities for import or export expansion.

These are the types of private sector initiatives that hold out the greatest hope for success. The foreign assistance agencies should support this kind of private sector initiative with seed money, initial funding, and investment guarantees where appropriate.

Recommendation

Developing country agricultural entrepreneurs should be supported by qualified U.S. executive-managerial and technical personnel "on loan" from the private sector to assure the ongoing progress of companies and individuals being financed with U.S. foreign assistance funds.

Discussion: Greater use should be made of U.S. business skills to help agribusiness in developing countries. Representatives of American business can act as a bridge between U.S. Government and host country officials, providing the perspective of practitioners in matters relating to a broad range of policy options; they can also provide needed technical assistance and continuity in the project and post-financing stage to assure the long-term effectiveness of the assistance being provided. They can raise the host country's level of technical sophistication, identify obstacles to free trade and free markets, and alert U.S. business to opportunities in developing countries.

5. ► Support for Multilateral Institutions

Finding

The international financing institutions play a constructive role in Third World development.

Overview: The multilateral financial institutions, founded shortly after the end of World War II, have assumed a prominent role in the economic history of the LDCs. The IMF concentrates on short-term economic adjustment and balance of payment problems, while the multilateral development banks primarily provide capital and technical assistance for longer term development programs. Their assistance is generally provided within policy guidelines that are consistent with private sector growth objectives.

Recommendation

The United States Government should utilize its resources to support broad economic changes in developing countries and, where appropriate, coordinate its efforts with those of the International Monetary Fund, the World Bank, and the International Finance Corporation.

Discussion: Foreign assistance resources should be used to encourage policy adjustments the United States identifies as necessary to strengthen economies in developing countries. This should be an objective of bilateral programs as well as multilateral efforts.

The IMF has done yeoman service in dealing with problems associated with the debt crisis over the last few years. It has taken the lead in convincing countries to adopt sometimes painful policies that were necessary to put them on sound financial footing. The IMF has also taken the lead in devising international financing packages to tide these countries over until their new adjustment programs become effective.

It is particularly appropriate that these activities be performed by an international (rather than a bilateral) institution. Frequently, the IMF has both developing and developed country confidence, providing a professionalism that is not seen as tainted by national interest. It does a difficult and unpopular job as well as it can be done.

Recommendation

The United States should continue to support the multilateral development banks' efforts to support private enterprise development.

Discussion: Since its founding, the World Bank Group, including the International Development Association (IDA), has provided over $100 billion in financing to the developing world.

The IFC is an affiliate of the World Bank that was established specifically to help promote productive private enterprise in developing countries. In its fiscal year ending June 30, 1984, IFC approved investments totaling $696 million, about half of which was for its own account and the other half for syndication to others. (Only $75 million of this amount represented IFC equity investments.) These commitments supported a total investment of almost $2.5 billion. Many of these, however, had some form of government involvement, reflecting the pervasiveness of government ownership in the developing world and the difficulties development agencies face in promoting private enterprise. As noted in the previous section, one approach to providing greater private sector focus is the establishment of a Private Enterprise Institute. The IFC might be the natural entity to carry out this concept.

The regional development banks—Asian, Inter-American and African—have operated largely along the same lines as the World Bank. The Asian Development Bank recently established a private sector financing facility that began operating early this year. The Inter-American Investment Bank (IDB) recently decided to establish the Inter-American Investment Corporation, which will support private enterprise investment. However, the IDB's facility is not yet funded or in operation.

Too often, these institutions have followed the easy path of supporting state-owned or managed activities. There are signs of change and greater focus on the need to stimulate growth and productive efficiency, which the United States should support. On balance, they have made a major contribution to development.

6.► Strengthening AID's Private Enterprise Initiative

Finding

The breadth and scope of AID's private enterprise activities are too limited. In order to expand them, AID needs a clearer mandate, improved skills, and greater flexibility.

Overview: AID is the principal entity for the programming and disbursement of economic assistance and Economic Support Funds.* In the 1970s AID's main focus shifted from supporting large infrastructure projects, such as hydropower and fertilizer plants, to basic human needs. The BHN approach emphasizes providing help for relatively small scale social projects in the form of technical assistance, modest loans or grants, and commodities—such as seed and fertilizer—related to the project. AID's mandate thus took on more of a social development focus than it had previously; some refer to the shift as moving from a "top-down" to a "bottom-up" approach. With this shift came a change in the expertise of the agency.

In 1981, the Reagan administration placed increased emphasis on the role of the private sector in the development process and in our bilateral assistance programs; in AID it was superimposed on the existing agency structure and mandate. The Bureau for Private Enterprise (PRE) was established within AID to spearhead this effort. It has been given only limited budget and staff. The genesis of what is called the "Private Enterprise Initiative" in AID flows from

*See footnote on page 44.

the basic belief, derived from the American experience, that emphasis on private enterprise is unequivocally the most rapid and efficient economic development approach. Further, a private enterprise, market-oriented economy will lead naturally to, and support, a pluralistic society based on individual political freedom.

In support of this effort, it is important that both business and AID develop mutually reinforcing relationships. This will require greater understanding on both sides than now exists. Through trade and investment, U.S. companies can increase profits and make a greater contribution to development. We include here only a few suggestions as to how AID and the private sector can work together to build additional cooperative relationships. This process can be greatly enhanced by clearer policy guidance to AID, enabling it to make necessary changes in approach, style, and personnel.

Recommendation

AID's congressional mandate, its policies, its programs, and its organization must be revised to reflect greater private sector emphasis.

Discussion: The Agency for International Development has had essentially the same form since it was extensively reorganized in 1961. In the intervening period, the world and AID's mission have both changed dramatically. In the late 1960s, AID had over 18,000 employees; today it has about 5,000. Congress has added requirements that have greatly limited AID's ability to deal with the developing world. Operating procedures established by the agency over the years, partly in response to new congressional mandates, have added rigidities that further inhibit effective action. The BHN mandate drastically altered the character of the agency, its personnel, and its activities. During this Administration, AID has altered its approach to stress policy influence, institutional development, technology transfer, and private sector development.

To reflect these changes, AID's private sector mandate should be strengthened in terms of legislative language, resource availability, and organizational structure. Further, both Congress and the executive branch must recognize that private enterprise is synonymous with risk-taking. Private sector projects do fail; there is no reason to try to disguise this fact. AID must feel free and willing to engage private entrepreneurs in its development work by sharing risks itself.

Private sector project approaches must be integrated more fully into all AID activities. Financing of venture capital, intermediate credit institutions, management training programs, prototype private enterprise projects with replication potential, cofinancing, brokering between U.S. and LDC businesses, and the new Private Enterprise Revolving Fund should have full executive and legislative support.

Because of its past social development orientation, many AID employees were hired for training and skills related to publicly-administered programs, such as population planning, health, nutrition, and agricultural development. Some brought experience in international affairs, as well as area studies, and a large contingent of AID employees were once Peace Corps volunteers. While AID will continue to need experts in such disciplines, a different balance of skills is required to carry out the private enterprise initiative. Without supportive personnel, well-versed and experienced in private enterprise, the effort to design development programs with a private sector orientation will founder. To correct this imbalance, AID hiring practices and personnel training programs must be oriented more heavily toward private enterprise skills.

PRE has not yet gained adequate financial support or influence. We recognize that PRE's separate budget and staff have been deliberately kept small in order not to isolate or "cubbyhole" the private sector initiative. Nevertheless, we believe that PRE's approximately 1 percent share of the AID budget since 1981 hardly indicates a sufficiently strong agency commitment. PRE's resources and its influence within AID need to be expanded. It also needs a greater presence in the field missions; the great majority of AID missions should have at least one private enterprise specialist and, in larger missions, a fully staffed office.

Recommendation

AID should turn to the U.S. business community to assist it in developing practical modes of business-government cooperation.

Discussion: Most AID relationships with the private sector are with universities, private voluntary organizations (PVOs), foundations, and consulting firms rather than with U.S. businesses engaged in manufacturing, trade, and investment. U.S. business has little opportunity to work directly with AID in development programs or for the improvement of commercial relationships between U.S. firms and developing country enterprises. At the program level, placing greater reliance on private business would extend AID's capacity to do more for the same amount of money and energy. By making use of an enterprise already involved in a country or business sector, AID can tap into the local business's technical know-how, management experience, and practical judgment.

By enlisting the strengths of U.S. business, AID can also improve the leverage of its limited development resources for such traditional activities as agriculture, shelter, health, population, and training. The challenge to business is to find ways to work with AID in areas of mutual interest as a way of developing knowledge, markets, and new opportunities.

AID should assess whether various government and nongovernment entities established to promote expanded private sector trade activities, such as the National District Export Councils (DECs) and the advisory committees of the Department of Commerce and the U.S. Trade Representative, might assist in recommending new modes of government-business cooperation.

Recommendation

The U.S. Government, to the maximum extent feasible, should channel its foreign assistance resources through the private sector and not through governments: AID should substantially increase its support of private intermediate credit institutions (ICIs).

Discussion: The provision of credit, technical assistance and, in limited cases, equity to private business ventures in developing countries through intermediate credit institutions is one of AID's more successful activities. By relying on a local or U.S. financial institution that understands the way business is done and the risk inherent in any given undertaking, AID shifts questions of feasibility and administrative management to those who will ultimately be responsible for investment decisions, or who are expert in this field.

AID's experience as a wholesaler of funds and technical assistance—through financial institutions and otherwise—has generally been better than its experience where AID has managed projects directly. The agency has a long history of support to ICIs, with a considerable legacy of new ventures, successful institutions, and improved capital markets. AID can do more to help establish and expand private ICIs that combine local capital and business knowledge with foreign private capital and business development experience. To be effective, AID must be flexible in the type of assistance provided, both to the institutions and through the institutions to their borrowers. We believe that the payoff from moving more AID funds through ICIs will be very large.

Recommendation

AID should increase its equity financing through ICIs.

Discussion: One of the principal shortfalls in financing businesses in developing countries is the lack of sufficient equity capital to provide a solid underpinning for business. In the past, AID has provided funds to such equity-taking institutions as the Latin American Agribusiness Development Corporation (LAAD) and Latin Caribbean Investments (LCI), but these are relatively exceptional cases; in fact, little AID funding has been available to support equity financing in the last ten years.

AID should review its efforts to catalyze private investment, foreign and domestic, in those countries in which it operates and should systematically evaluate the potential for ICI expansion. As AID develops a stronger intermediate credit program, it should establish equity windows in ICIs for local borrowers. U.S. venture capital companies, international banks, and investment banks also need to be enlisted to provide assistance and support to an AID staff inexperienced in these matters.

One of the arguments leveled against AID's financing of business is that economic circumstances in recipient countries are frequently heavily distorted by governmental control, regulation, subsidy, or public sector competition. The argument is that private investment in such countries does not respond to free market signals and, as a result, AID finances ventures that are not economically sound, though they may be profitable. While this argument has merit, it is also true that distortions exist in all economies and the alternative can be worse. Assistance to the public sector, under such conditions, strengthens its control over the economy, and deprives the private sector of resources.

In our view, it is much better to risk erring on the side of support for private enterprise than to do nothing or provide an undue amount of support for the public sector. AID should adopt a clearly stated position that a dollar spent on the private sector is likely to be more beneficial than a dollar spent on the public sector. The burden of proof to the contrary should rest with those who want to finance public sector activities.

Recommendation

AID should serve more as a broker between U.S. businesses and prospective overseas partners by providing inexpensive, current, and easy-to-use information on the investment climate and operating conditions in developing countries.

Discussion: Joint ventures between U.S. and developing country businesses have great potential for contributing to economic development. But someone has to get the interested parties together. Public sector programs undertaken by developing countries to help their businesses acquire new technologies or develop new markets have achieved only limited success. Not only have they come up against bureaucratic obstacles and funding constraints, but frequently they have failed to recognize that most such resources needed by business firms (particularly new technologies and marketing know-how) are developed by, and reside in, other businesses, not research institutes or public programs.

Most small and medium-sized U.S. businesses need help if they are to develop international ventures; by themselves they lack the information and experience needed to reduce the risks to manageable levels. AID could perform a valuable service by assembling the necessary information, much of it publicly available but not easily accessible, and providing it to businesses in useful form.

By working closely with U.S. trade associations and voluntary business associations, AID and the private sector could effectively leverage their expertise in a cooperative relationship. AID should help such organizations become more active in generating and disseminating information and ideas to their members and in facilitating member involvement in international markets.

Recommendation

AID should support the formation of trading companies and other business brokering institutions that have developmental potential.

Discussion: Legislation enacted in 1982 permits the establishment of export trading companies (ETCs) in the United States and opens a new opportunity to foster U.S. trade and develop stronger business ties with developing countries. While large multinational corporations can generally initiate trading ventures on their own, this is not the case for the smaller entrepreneur. Perhaps the most creative technology transfer and development opportunities lie with U.S. small and medium-sized business. Trading companies can help these private enterprises expand into international markets, while accessing the same markets for needed raw materials and finished goods.

There are many avenues of potential cooperation among ETCs, small and medium-sized business, and those primarily concerned with development. For instance, ETCs can assist AID in evaluating, designing, and implementing projects that support private enterprise or assisting with those projects in which procurement or marketing is a prime consideration. AID might provide trading companies with technical assistance, finance, or marketing assistance in cases where the work of the trading company directly benefits the development process. Trading companies in developing countries could serve as the intermediaries for an AID foreign exchange fund for spare parts and input materials for small LDC firms. These are only a few illustrations of ways in which this new concept might be used creatively to mutual advantage. More thinking along these lines is needed.

It is clear to us that there is a great commonality of interest between smaller firms in developed and developing countries. Developing countries need products, technical processes, and support services that meet their capital requirements, production capacity, and social and development goals. However, both officials and business people in developing countries are often unaware of the talents and productive capabilities available in U.S. small businesses, and of how valuable these could be to them. Similarly, many U.S. small businesses fail to recognize investment and trading opportunities in developing countries. The use of specialized entities, such as ETCs, would be a good way for AID to help narrow this communication gap, meet development needs, and greatly expand two-way trade.

Recommendation

AID should encourage joint undertakings between businesses and private voluntary organizations in developing countries.

Discussion: PVOs have made an enormous contribution to development in the Third World. Most are involved in traditional activities such as education, health, shelter, agriculture, food distribution, and disaster assistance. AID deals with PVOs both as intermediaries in conducting AID programs and as independent entities in their own right. Total AID-administered resources to PVOs for overseas programs in FY 1983 exceeded $600 million. (The majority of these funds were for food aid distribution.)

At a time when AID's financial and personnel resources are severely limited, PVOs have been able to extend AID's effectiveness. A number of PVOs, such as the Young President's Organization (YPO), Technoserve, Volunteers in Technical Assistance (VITA), Partnership for Productivity (PFP), and the Overseas Education Fund (OEF), are making significant contributions to private enterprise development. Another PVO, the International Executive Services Corps (IESC), has provided the services of thousands of retired executives to solve problems for indigenous LDC businesses. Because of their nongovernmental standing and credibility, they often serve as a link between the public and profit-making sectors in a developing country. The efforts of most center on training, technical assistance, and resource management for small enterprises and agriculture. Others are active in project planning, project management, and credit assistance. Partnerships between PVOs, government, and private enterprise offer an attractive means of meeting development goals.

Because of their continuity and on-the-ground knowledge of developing countries, some PVOs are uniquely suited to facilitate the movement of U.S. products and services, particularly those of small business and agribusiness. Others can provide various support services, such as training and infrastructure development, that augment U.S. investment. Familiarity with local business customs, market needs, and sources of supply enables PVOs to help U.S. businesses enter into new ventures in developing countries. In effect, PVOs can serve as intermediaries for U.S. business by promoting trade and investment relationships that meet local development objectives.

We support the steps AID has already taken to increase cooperation between PRE and its Office of Private and Voluntary Cooperation and, in particular, the recent transfer of Cooperative Development Organization activities to PRE. Initiatives with U.S. cooperative organizations have great potential for mobilizing private American financial and human resources that assist in the development process and enhance the ability of rural and urban poor to participate in their own country's development process. These initiatives are designed to strengthen their service capabilities, increase U.S. cooperative-to-developing country programs, and funnel additional resources through them. An informal sampling of AID missions found that there is considerable field experience in bringing together the PVOs and business community. AID ought to analyze ways various missions have approached these cooperative efforts and build on the knowledge gained.

Recommendation

AID should streamline its administrative and procurement processes.

Discussion: Procurement and contracting negotiations are normal business requirements. There is a point, however, at which excessive requirements become severe disincentives to those who might otherwise be interested in participating. In our view, this has too often been the case with AID. Unnecessary regulations and bureaucratic procedures choke smaller firms when they deal with AID and dissuade larger firms from engaging in such business.

7. ► Training

Finding

Training, in various forms, is one of the most effective long-range means of promoting development. Fulfilling training needs offers the United States a significant opportunity.

Overview: Many U.S. Government agencies—the Departments of Agriculture (USDA), Defense (DOD), Health and Human Services (HHS), the United States Information Agency (USIA), and others—are involved in the training of people from developing countries.

Since 1943, AID and its predecessor agencies have financed training for over 240,000 developing country participants in the United States or in a third country. As indicated in Figure 2, at the present time the AID Participant Training Program annually sponsors over 9,000 students in the United States. About half engage in formal academic studies. The others are enrolled in technical training and in short courses, observation visits, or internships. Most participants come from the public sector and generally return to predetermined public sector jobs. Individuals from private enterprise have little opportunity to participate in U.S.-based training programs.

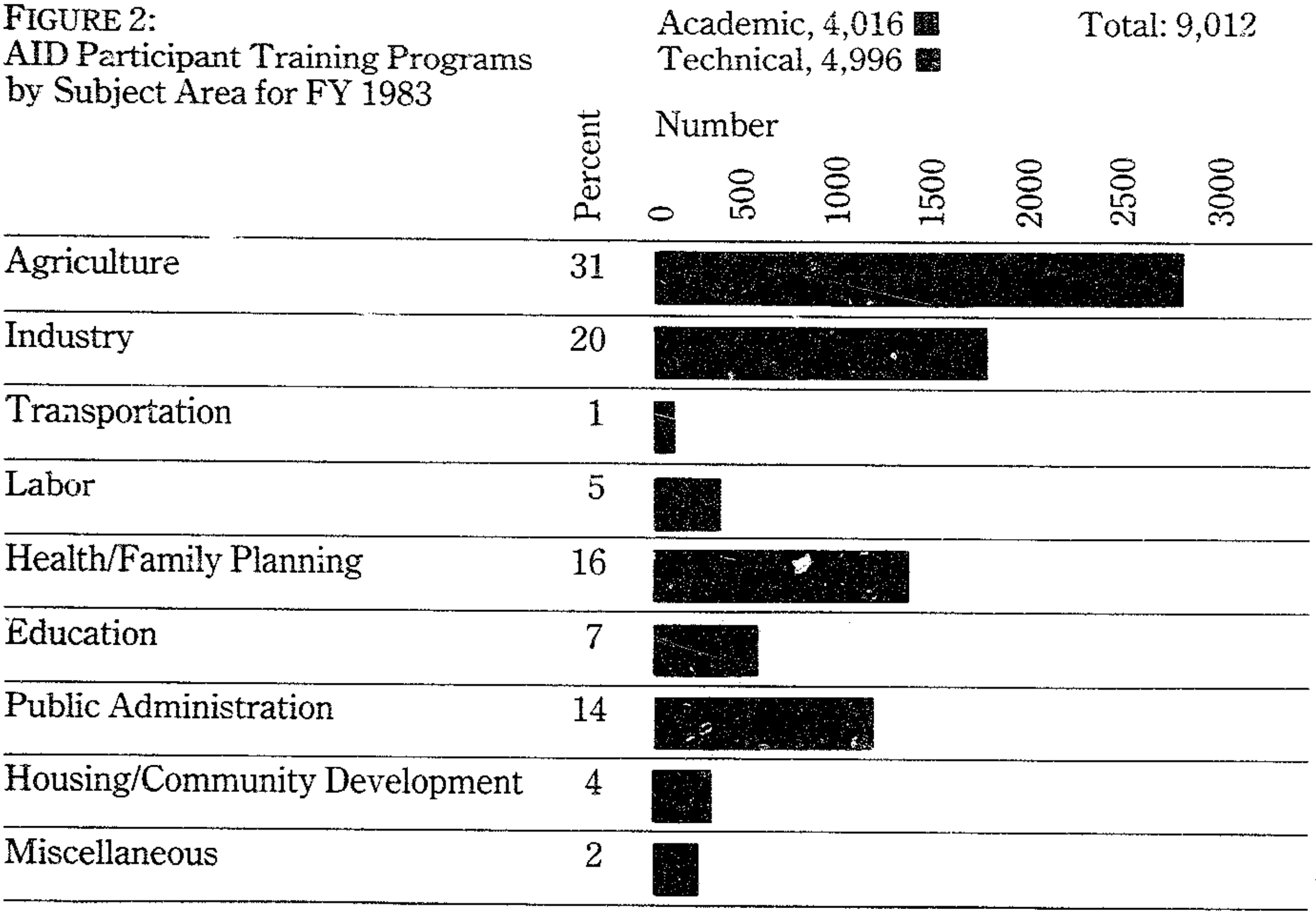
The Task Force was impressed by the number and quality of people who received training in the United States. Developing country businessmen, government officials, and educators felt that it was a positive experience and an opportunity they would otherwise not have had. As a result of such programs, the legacy of good will toward the United States is substantial.

Recommendation

The United States should significantly expand U.S.-based training and place stronger emphasis on private sector participation and needs.

Discussion: Gradually doubling the size of the present program financed by AID to 18,000 participants per year would be feasible if more private sector support were generated to administer the program and share the cost. Based on current costs, such an increase would require approximately $150 million. This amount could be substantially reduced if existing AID resources were spent more on short-term programs and if private sector cost-sharing programs were developed.

FIGURE 2:
AID Participant Training Programs by Subject Area for FY 1983



SOURCE:
Office of International Training, Agency for International Development (1984).

Acquiring the skills needed for available home country jobs is of paramount importance. While some highly sophisticated training is appropriate, lower-level, practical, hands-on training is needed in most cases. This includes managerial, vocational, and technical training. Special emphasis on small and rural enterprises, the source of most economic activity in developing countries, is needed.

More on-the-job training in U.S. business, financial, and manufacturing organizations—including small businesses—is also needed. Programs that supplement institutional and business-related academic programs and place emphasis on work-related practical experience should be increased. Participants brought to the United States under AID auspices would benefit from greater exposure to American business techniques; in turn, they could offer U.S. business expanded contacts with present and future leaders of developing countries. U.S. firms should be aware of the potential trade and investment benefits that can be derived from training developing country personnel.

Various facilitating organizations, such as trade and business associations, educational institutions, PVOs, and international finance and trading firms, could be employed to develop contacts and handle arrangements. Developing country business and professional associations could help with participant selection, along with the indigenous companies that share training costs for their employees. (This is an illustration of the kind of PVO-business community interaction AID could stimulate.)

Public sector officials should also be educated to business and trade techniques so that they develop a greater awareness both of what the private sector needs and of what it can contribute to economic growth.

Because AID has not had extensive experience working with U.S. private enterprise on training activities, an advisory board could provide AID with valuable insights on how to involve the U.S. private sector in developing country training programs.

PART IV

The Formation of U.S. Economic Policy

INTRODUCTION

Private enterprise in development cannot flourish if other U.S. economic policies are askew or out of kilter. In fact, our examination of U.S. economic interaction with the developing world has made it forcefully clear to us that, in the age we are now entering, the entire fabric of our domestic and international economic relationships will become tightly interwoven. This has important implications for development strategy, but it has equally important implications for the machinery of economic policy-making generally.

In this section, we focus on what has been the economic policy formulation process; what we see as the need for a new kind of "process machinery" to address the economic challenges of the near and long-term future; and some specific measures that we believe require immediate attention.

Historically, U.S. economic success has resulted from a strong private sector; government policies that have been, on balance, more supportive than inhibiting; able people making policy decisions; and a policy process that has enabled the government to respond to changing needs in a timely fashion. Today's challenges include those of economic development. But the interconnections between these and broader economic and security concerns are such that neither can be dealt with in isolation.

The security and economy of the United States, other developed nations, and the developing nations will depend on how effectively we design and execute an integrated set of strategies to deal with the linkages between domestic and international economic issues.

One of the basic facts of life in these final decades of the twentieth century is that economically we live in a new world. Rapid changes are taking place all around us: in the patterns of trading activity, in technology development and dissemination, in exchange rate determinations, in the structure of international debt, in the competitive environment, in migration, and in a host of other interrelated activities. To take just one example, the number and diversity of major trading nations has increased dramatically, with such nations as Brazil, South Korea, India, and China joining their ranks. And, at the same time, the volume of world trade has increased enormously, while the patterns of U.S. trade have undergone a dramatic shift. It was not very long ago that total U.S. trade was less than this year's estimated U.S. trade deficit of some $130 billion.

One factor contributing to that deficit has been the strength of the U.S. dollar against other currencies. In turn, this is related to interest rates, capital flows, and budget deficits. Other countries protest that the strong U.S. dollar and high U.S. interest rates are hampering their own recoveries; ironically, five years ago alarms were sounded in international circles about the weakness of the dollar.

This country's own industrial profile has changed radically from that of a goods-producing country 20 years ago to that of a predominantly service economy. The development of the microchip and other technological advances continue to foster rapid change. In turn, this affects such matters as our attitudes toward immigration and our bilateral relations with neighboring developing countries. U.S. banks worry about their foreign loans. U.S. labor unions worry about competition from lower-paid foreign workers. U.S. companies worry about the impact of antitrust laws and tax policies on their ability to compete abroad.

Our point here is not to prescribe specific remedies for all of the world's difficulties, or even to enter the debates about macroeconomic cause and effect, but rather to emphasize the degree to which our own and the world's economic concerns are interrelated and interdependent.

In the years ahead, both the interrelationships and the complexity of our economic challenges will continue to increase. We can no longer view international and domestic economic concerns in isolation, or economic concerns separate from political and security concerns. Therefore, we believe the time has come when there must be a regular, institutionalized mechanism for dealing with these matters in a coordinated way at the highest level. This mechanism must cut across the separate jurisdictions of the various cabinet departments, just as the challenges themselves do.

The Policy Formulation Process

PAST APPROACHES TO WHITE HOUSE ECONOMIC POLICY FORMULATION

Each President organizes the White House and Executive Office of the President to suit his personal management style. With respect to economic policy formulation and implementation, there have been essentially three basic approaches: (1) reliance on the appropriate cabinet departments and agencies, working through interagency committees when necessary; (2) creation of a separate entity, reporting to the President, which deals primarily with international economic policy; and (3) establishment of an entity responsible for both domestic and international policy, also reporting to the President. President Dwight D. Eisenhower chose the second approach, relying on the Council on Foreign Economic Policy (CFEP) to coordinate his foreign economic policy. President John F. Kennedy abolished CFEP, choosing to depend on his Secretary of State and the National Security Council (NSC) for international economic policy advice. (Presidents Lyndon Johnson and Jimmy Carter essentially followed the Kennedy approach.)

President Richard M. Nixon recognized the need for better coordination of international economic policy. In 1971 he established the Council on International Economic Policy (CIEP) to develop and coordinate international economic policy and its relationship to domestic economic policy. In addition, CIEP was to provide top-level focus on a full range of international economic policy issues including trade, investment, balance of payments, and finance; consider international economic aspects of essentially foreign policy issues (e.g., aid and defense) under the general policy guidance of the NSC; and maintain close coordination of those activities with basic foreign policy objectives.

CIEP achieved some successes, as demonstrated by its ability to force agency cooperation on certain issues (such as the exchange rate). It was also able to play a major role in hammering out the necessary Administration and congressional compromises in the Trade Act of 1974 and served as a channel to the President for unreconciled views. However, during this period, real power rested with the Departments of State, Treasury, and the NSC, all of which often sought to override CIEP actions.

Partly because of these problems, President Nixon created the Council on Economic Policy (CEP) in 1973 to better coordinate the formation and execution of all economic policy, domestic and foreign. In 1974, President Gerald Ford absorbed CEP into a newly created Economic Policy Board (EPB). It had a multitude of functions, including advising the President on all aspects of national and international economic policy; overseeing the formulation, coordination, and implementation of U.S. economic policy; and serving as the focal point for economic policy decision making. The idea was not to create an additional staff or entity that would compete with existing departments or agencies, but rather to facilitate the economic policy decision-making process. Many felt it was one of the more effective approaches to economic policy organization.

THE EXISTING POLICY FORMULATION PROCESS

Under the Reagan administration, high-level interagency economic policymaking is carried out through four main institutions: two cabinet councils, the Trade Policy Committee (TPC), and the Senior Interagency Group-International Economic Policy (SIG-IEP).

The cabinet councils are subgroups of the cabinet, designed to review issues requiring presidential decision. The Cabinet Council on Economic Affairs (CCEA), chaired* by the Secretary of the Treasury, considers both domestic and international economic issues. The Cabinet Council on Commerce and Trade (CCCT), chaired by the Secretary of Commerce, has predominant responsibility for trade issues. The activities of the cabinet councils are, in turn, coordinated and supported by the White House Office of Policy Development (OPD). Given the significant impact of international trade actions on the domestic U.S. economy, all of the cabinet councils, to varying degrees, have become involved in trade issues. Nevertheless, the OPD continues to have a predominantly domestic orientation as did its predecessor, the Office of Domestic Policy.

The TPC is the initial high-level route for consideration of most trade issues and resolution of agency disagreements. It is chaired by the ambassador-ranked United States Trade Representative. When agreement cannot be reached on an issue through TPC and a presidential determination is required, the issue is sent for resolution to the CCCT.

Differences within the Administration over international economic issues, such as the U.S. embargo of energy-related equipment to the Soviet Union, highlighted the need for a top-level group to examine the foreign policy, national security, and economic implications of international economic policy questions. To respond to this need, the National Security Council established SIG-IEP in 1982. SIG-IEP has considered a wide range of issues, including grain sales to the Soviet Union, pipeline sanctions, U.S.-India relations, and renewal of the Export Administration Act (EAA).

The Secretary of the Treasury is chairman of the SIG-IEP in addition to his role as chairman of the CCEA. As chairman of CCEA and SIG-IEP, the Treasury Secretary provides leadership in discussions on international issues with major economic implications. The CCEA also provides Treasury with a vehicle for presenting analysis to the cabinet, while SIG-IEP gives Treasury a mechanism for providing analysis to the NSC.

While this arrangement has improved the Administration's capacity to coordinate economic policy in response to international events and crises, more must be done.

Turmoil in international financial

*NOTE:
All cabinet councils are officially chaired by the President. The cabinet member most directly concerned with the issues of each council serves as chairman *pro tempore.*

markets, debilitating effects of the debt crisis, both on developing and developed countries, and rising protectionist pressures at home and abroad are all examples of challenges that demonstrate the need to deal more comprehensively with long-range strategic economic issues. Not only are these issues becoming more critical to our own future, but increasingly, domestic policies have important impacts on the economies of other countries. The U.S. policy on illegal immigrant amnesty not only affects our domestic labor market, but has serious international political implications, as does U.S. farm policy. The economic policies of other countries, designed to address domestic objectives, also have widespread strategic implications. For example, the European Economic Community (EEC) Common Sugar Policy has had a devastating effect on the economies of many developing countries. It raises serious trade subsidy issues and, most important, has national security implications for the United States.

There will, of course, be many situations in which the various interests of the United States conflict with one another or in which domestic considerations conflict with foreign policy considerations. These conflicts may make coordination messy, but they also make it necessary. The greater the conflicts, the greater the need for an institutional structure to manage them.

Establishing an Economic Security Council

During the course of our work it became clear that any efforts by the U.S. Government to specifically encourage the growth of private enterprise for development, particularly through our foreign assistance programs, will be hampered if other U.S. economic policies are askew or contradictory. The interconnection of so many aspects of governmental policy—such as trade, finance, agriculture, foreign relations—as well as the need to enhance the way we organize U.S. Government resources, gave rise to our analysis of the U.S. economic policy formulation process. As a result of these deliberations, we recommend establishment of a new mechanism in the White House, namely the Economic Security Council, and the creation of the position of Assistant to the President for Economic Affairs.

Finding

In order to cope with the new and changing circumstances, a new institutional structure is needed to ensure better formulation and coordination of U.S. international and domestic economic policy.

Overview: High stakes are involved in the integration of U.S. domestic and international economic policies. The executive branch must be structured so that those decisions that are crucial to our economic future are given thorough and fully coordinated consideration.

FIGURE 3:
Membership of Trade and International Economic Policymaking Institutions

	Policymaking Institution			
Member[a]	Cabinet Council on Commerce and Trade (CCCT)	Cabinet Council on Economic Affairs (CCEA)	Trade Policy Committee (TPC)	Senior Interagency Group-International Economic Policy (SIG-IEP)
The President	●	●		
The Vice President	●	●		
Department of Commerce	●	●	●	●
Department of the Treasury	●	●	●	●
United States Trade Representative	●	●	●	●
Department of Agriculture	●	●	●	●
Department of Defense		●	●	●
Department of Energy	●		●	
Housing and Urban Development		●		
Department of the Interior			●	
Department of Justice	●		●	
Department of Labor	●	●	●	
Department of State	●	●	●	
Department of Transportation	●	●	●	
Council of Economic Advisers	●	●	●	●
Central Intelligence Agency				●
International Development Cooperation Agency			●	
National Security Council			●	●
Office of Management and Budget		●	●	●
Counselor to the President	●	●		
White House Chief of Staff	●	●		
Assistant to the President for Policy Development	●	●		●

SOURCES:
A Preface to Trade, USTR, 1982; *Interagency Structure of Economic and Foreign Policy Decision Making*, U.S. General Accounting Office, 1983.

NOTES:
[a] The membership of the interagency units is composed of the heads of the line cabinet departments and agencies. For example, the Secretary of Commerce, as opposed to the Department of Commerce, is a member of the Cabinet Council on Economic Affairs.
[b] The President is chairman of the Cabinet Councils on Commerce and Trade and Economic Affairs (as well as the other cabinet councils).
[c] The Secretary of Commerce and the Secretary of the Treasury serve as chairmen *pro tempore* of their respective cabinet councils. The Secretary of the Treasury also serves as chairman of SIG-IEP, while the United States Trade Representative serves as chairman of the Trade Policy Committee.

Recommendation

The President should establish an Economic Security Council (ESC) to formulate and coordinate domestic and international economic policy.

Discussion: As the world's markets grow more internationalized, other nations increasingly approach international politics as, to paraphrase Clausewitz, an extension of economic policy by other means. Our government institutional arrangements should reflect this new reality.

The increasing complexity of international economic problems, cutting as they do across the jurisdictions of the individual cabinet departments, makes the need for a coordinating point within the Executive Office of the President almost self-evident.

We propose that the President establish, initially by Executive Order, a White House council called the Economic Security Council. This council would be chaired by the President and include those cabinet rank officials needed to fulfill the ESC mandate.

The ESC would parallel the NSC in its advisory and operating capacities, raising economic policy issues to a level comparable to that of international political issues. Ultimately, legislation should be proposed to institutionalize the ESC structure and thus to assure its permanence and the development of an institutional memory and appropriate linkages among various cabinet departments. The ESC would advise the President on all aspects of domestic and international economic policy; oversee the formulation, coordination, and implementation of U.S. economic policy; and serve as the focal point for economic policy decision making.

Among other functions, we would expect the ESC to:

- ☐ examine the domestic, foreign policy, and national security implications of international economic policy issues;
- ☐ identify ways in which the various U.S. Government resources can be used to increase U.S. trade with developing countries and strengthen their economies;
- ☐ develop common priorities and government-wide guidelines for specific agency actions affecting international economic policy;
- ☐ insure that international economic considerations are brought to bear in the development of domestic policy;
- ☐ coordinate preparations for international economic summit conferences; and
- ☐ assure the consideration of developing country issues in the policy deliberation process.

With the Economic Security Council in place, it should be possible to streamline the present cabinet council structure. The ESC would need a minimum staff to provide, within the White House, an interdisciplinary reservoir of those skills and backgrounds necessary to the analysis of economic issues and their wide-ranging impacts. It would maintain close liaison with the various departments and agencies, ensuring that issues needing ESC attention received that attention. It would also provide an institutional memory through which past experience could be readily brought to bear on current issues.

The ESC, thus structured, would be in a position to analyze such questions as, for example, the effect of economic sanctions against another country on U.S. industry and agriculture, the trade implications of U.S. monetary policy, or the impact of pollution or anti-trust regulations on U.S. productivity and international competitiveness. Issues addressed elsewhere in this report, such as those related to the foreign assistance budget, trade policies, and P.L. 480 funding levels would, of course, be within the province of the ESC.

Recommendation

The President should designate an Assistant to the President for Economic Affairs who would participate in the Economic Security Council.

Discussion: An organizational structure, a set of principles, and a system cannot assure the necessary level of attention to a multitude of policy issues. The way in which a policymaking system operates also depends on the people involved. Presidential decisions are often influenced by the personal and professional relationships that exist between the President and his chief advisers and agency heads. A point of contact and coordination in the person of a close, trusted, expert adviser who would have the President's ear is needed to insure that the economic dimensions—both domestic and international—of pending issues are taken fully into account in the presidential decision-making process and that this is done early enough in the process to let the economic considerations work their way through it. The Assistant to the President for Economic Affairs must be such an individual.

The assistant to the President would be unconstrained by departmental jurisdictional boundaries and constituency interests and would have a "presidential" perspective. The assistant could identify for the President points of view that might not otherwise be adequately represented within existing policy coordinating groups. This official could also call attention to emerging issues that might not, at the time, seem important to any single department or agency, but that could offer prospects for positive action or pose serious problems if not dealt with.

Such a senior adviser to the President would insure that linkages between domestic and international economic concerns, including those linkages that deal with developing nations, are adequately factored into presidential decision making.

Not long ago, it was common in government circles for international economics to be consigned, like other arcane matters, to the specialists with the hope that it would intrude as little as possible on the consciousness of those charged with the more "glamorous" work of looking after the nation's political relationships. But economic concerns can no longer be separated from political concerns. Economic welfare can no longer be separated from human welfare. The structure of the executive branch must reflect this interweaving of economic considerations through the whole fabric of domestic and international politics.

In the advanced technological age we are now entering, the changing dynamics of the world's interlocking economies will hold the key to the future for the next generation. This is true of the developing and developed nations alike. We believe that these organizational changes—the creation of an Economic Security Council and designation of an Assistant to the President for Economic Affairs—taken together, will equip the executive branch with the means to give economic issues the quality and degree of attention they will need if we are to master that future.

Major Immediate International Economic Policy Issues

While we believe an Economic Security Council and an Assistant to the President for Economic Affairs are needed for the long-term future, there are also several more immediate policy issues directly related to our particular mandate that we believe need to be resolved now. We treat these policy issues in this section of the report because, were the Economic Security Council now in place, we would look to the ESC to help resolve them. We note that we elaborate on some of these issues in the final section, which concentrates on food and trade. These issues include: strengthening foreign assistance, linking trade and aid, harnessing our tremendous agricultural productivity, and reorienting the government's role in regulating U.S. business.

STRENGTHENING FOREIGN ASSISTANCE

Finding

Both legislatively and administratively, our foreign assistance programs suffer from confused mandates, from divided responsibility, and often from a perception that economic development has a low priority.

Overview: In the past, economic development policy was generally seen as something apart from the U.S. economy itself. There was little examination of the interaction between the two. At the same time, foreign assistance programs frequently focused on social development objectives at the expense of those principles necessary for sound, long-term economic growth. Individual aid programs were often launched with little regard for their relationship to overall aid objectives, and then encumbered with successive layers of specific legislative requirements that further limited their responsiveness and flexibility. The bureaucratic structure that has evolved is a product of historical accident as much as it is of deliberate planning. Economic assistance has frequently been treated as the "poor relation" in both the foreign policy family and the economic policy family.

U.S. economic policy formulators tended to emphasize our relations with other industrialized nations, allowing foreign assistance institutional arrangements to proceed on a separate track. Given the limited impact of the Third World on U.S. economic performance and the fact that foreign assistance programs answered to a different drummer, we tended to overemphasize our social development objectives without applying the key economic principles we had learned in building our own economy. What we have in place today represents an amalgam of sporadic attempts to influence our foreign assistance programs.

Recommendation

There must be greater, more regularized consideration of developing country issues in the policy deliberation process.

Discussion: Over the last four decades, U.S. policymakers have concentrated far more on East-West relations and on Europe and Japan than on developing country matters. The reasons for doing so were legitimate at the time, but times have changed dramatically. The developing countries are now the ones with the greatest potential for economic growth; at the same time, they are the ones whose economic problems are the most likely to jeopardize the international trading and financial systems and world security. These countries have become far more sophisticated in their economic relations and require more thoughtful treatment by U.S. Government policymakers than ever before.

The International Development Cooperation Agency (IDCA) is now the government's focal point for economic matters affecting U.S. relations with developing countries. IDCA's mission is twofold: first, to ensure that development goals are taken fully into account in all executive branch decision making on trade, financing, monetary, and other economic policy matters affecting developing countries; and second, to provide strong direction for U.S. economic policies toward the developing world. Yet, the IDCA director is a member of only the statutory Trade Policy Committee. IDCA should be a full participant in other U.S. policy formulation and coordination units, specifically including the proposed ESC.

Recommendation

Changes must be made in AID's mandate and organization in order to improve the effectiveness of foreign assistance programs.

Discussion: Congress has mandated many requirements for U.S. foreign assistance programs; some are mutually exclusive and many are counterproductive. For instance, so many legislative demands have been placed on AID that the organization is now smothered by review procedures and strangled by red tape. As a result, when it finally does do something, the product is often too late and too "safe" to achieve its intended objective. The extremely complicated and unduly burdensome P.L. 480 approval process is a good example of the kind of obstacles sensible programs encounter. At least six separate agencies with vastly different mandates must all agree on even the most minor aspects of each P.L. 480 project. (The P.L. 480 Action Brief provides additional details on this subject.)

Also, in an effort to respond to perceived congressional priorities, foreign assistance programs have tended to support either nonproductive spending or government involvement in productive activities. Even now, the bulk of development funds go to or through public agencies, public enterprises, and publicly-owned financial institutions. Because public agencies never go bankrupt, they can continue to command resources even though they may be inefficient and may fail to achieve their objectives. Over the last four years, AID's efforts have demonstrated a policy shift away from the public sector to the private sector. It should be commended for that. But much more needs to be done in this respect.

While we agree on the main problems in existing foreign assistance programs, the Task Force is not entirely of one mind as to the solutions. We have considered a variety of alternatives. Some of these would involve major congressional action to rearrange responsibilities and to clarify duties among agencies. Others would require presidential but not legislative action. Still others could be accomplished by different departments and agencies.

The Task Force is in general agreement that: (1) the bulk of aid funds should be routed to the private sector, with particular emphasis within AID on intermediate financial institutions, the PRE revolving fund, and training; (2) AID procedures must be streamlined and action speeded up; and (3) the P.L. 480 program should be managed primarily by USDA. Some members feel that OPIC and TDP should be given new developmental responsibilities and increased funding; that the U.S. and Foreign Commercial Service (U.S. & FCS) should manage the private sector loan program; and that ESF and humanitarian assistance should be managed by the Department of State, using senior AID personnel. Some believe a totally new development institution should be established specifically to support private sector activities. Others would prefer more modest measures, building on the successful beginning steps already taken to increase reliance on private enterprise to achieve development objectives.

We did not attempt a comprehensive management study of the sort that would be needed to chart specific proposals for reorganization of our foreign assistance programs. We did become convinced, however, that changes in the mandate and management structure are needed to improve the impact of U.S. foreign assistance in general, enhance private enterprise development, and improve the ability of the private sector to participate in development assistance efforts. We believe this is an area that needs close examination. Our central focus was on policy approaches and on the policy process; the structure of our aid programs also needs a detailed management survey.

LINKING TRADE AND AID

Finding

Responsibility for the U.S. Government's trade policies and programs is fragmented among several government agencies. Policies and programs do not operate within an overall strategy aimed at benefiting both the United States and developing countries, nor are they designed to address both U.S. trade objectives and broader U.S. economic objectives.

Overview: Despite the growing importance of trade to the health of the U.S. economy, the United States still concentrates its attention on specific import problems rather than on broader strategies of export generation. A particularly troublesome aspect of this lack of an overall strategy is that, unlike our foreign competitors, the United States does not specifically link its aid and trade activities to promote both trade and development except in its relatively small Trade and Development Program (TDP).

Trade is necessary for promoting broad-based sustained economic development. As we have indicated, its importance to the economic well-being of developing countries, the United States, and other industrialized nations has grown considerably over the past decade. It is clearly beneficial for all participants to further increase such trade flows; for, in the long term, trade is the primary source of external resources and the impetus for growth for all countries. However, there is no central point in the executive branch where trade and aid issues can be reviewed, nor is there an opportunity to evaluate trade and aid issues within a broader U.S. economic strategy.

Recommendation

The U.S. Government must develop an aggressive, consistent trade policy that mixes aid and trade resources, enables U.S. firms to be more competitive in world markets, and meets the challenges posed by the growing governmental role in world competition.

Discussion: U.S. Government agencies

rarely follow common trade strategies, except when the White House identifies critical short-term political or security interests in a particular country or group of countries, e.g., the Caribbean Basin. The absence of a consistent American trade strategy and the patterns of stop-go or zig-zag courses of action have discouraged private business efforts to expand exports and to encourage overseas production and research and development. The United States needs a longer term vision of international economic problems and opportunities as well as a greater integration of, and consistency among, trade policy and domestic economic, agricultural, and regulatory policies. The establishment of an Economic Security Council would provide a focal point to develop such a vision as well as a framework in which trade policy could be developed to address these needs.

A coordinated, aggressive, consistent trade policy would enable the United States to respond quickly to opportunities as well as to anticipate its competitors' actions and counter unfair competition. To do so will require an understanding of the changing character of competitive conditions and of the relationship among trade, U.S. long-term strategic interests, and foreign assistance policies. An effective approach must be built around:

☐ a consistent strategy geared to the expansion of trade and private sector activities;

☐ effective coordination of U.S. international economic policies and programs so that agency policies become mutually supportive rather than conflicting;

☐ establishment of long-term economic linkages and increased cooperation with other countries, with particular emphasis on those economies that are guided by market-oriented principles;

☐ common priorities and guidelines for all agencies that provide export financing or influence trade in order to strengthen the competitive position of U.S. industries in international markets, while retaining the flexibility to respond to, or to anticipate, changing market conditions;

☐ pressing bilateral and multilateral institutions to prohibit or at least limit lending or granting funds to parastatals that compete unfairly with private enterprise; and

☐ strong business-labor-government cooperation.

Recommendation

The United States must link its trade and foreign assistance programs.

Discussion: The United States does not now link its trade and foreign assistance programs to enhance long-term economic relationships with the recipient countries. Establishing such a linkage will require the United States to re-evaluate its trading and assistance relationships with those countries. This linkage should focus on designing aid programs that promote two-way trade, while also helping a nation's development, and on continuing long-term private sector ties that are consistent with broad American objectives of trade liberalization. As a corollary, our trade policies should also promote development. For example, using foreign aid funds to finance project components of a major export-generating facility in a developing country could help a country improve its trade balance. The project could also be designed to develop a future market for U.S. construction, engineering, and equipment firms. In terms of trade policies, granting Generalized System of Preferences (GSP) and most favored nation status, or changing tariff and quota levels have a tremendous impact on the ability of a developing country to export. U.S. trade and assistance relationships should have multiple objectives: strengthened recognition of mutual economic, social, and political interests; enhancement of long-term interrelationships in trade, investment, and other economic activities; development of strong economies and markets in developing countries; reorientation of development in directions consistent with market forces; and encouragement of entrepreneurship.

Given the inherently parochial views of independent agencies and departments charged with administering individual trade and aid programs, the United States must have an institutional mechanism with a broader view of U.S. economic relations with Third World countries so that such aid and trade linkages can be formed within a consistent policy framework.

Recommendation

The United States should consider ways to give higher priority to the need for a freer and more open international trading system and continue to press for a new round of multilateral trade negotiations. This new round should include adopting a trade-in-services code; the application of trade rules to middle-income developing countries; and strengthening enforcement procedures against government-subsidized trade.

Discussion: Over more than 36 years, the General Agreement on Tariffs and Trade (GATT) has provided the framework for most of the world's trade. It has adapted to change through a series of multilateral negotiating rounds, each focusing on practices that constrained the growth of world trade. In addition to the negotiation of codes to deal with nontariff barriers, much attention in the last round (the Tokyo round took place between 1973 and 1979) was devoted to defining special rules for developing country participation.

In 1985, the five largest industrial democracies (the United States, Japan, West Germany, the United Kingdom, and France) will all have at least two years before their next elections. This could provide a good opportunity to make progress on a new round of trade talks. Passage of the Trade and Tariff Act of 1984 represents a very positive achievement of the Administration. It gives the President new authority to pursue talks on trade liberalization. And, by strengthening executive branch power to retaliate against unfair trade practices by other nations, it gives us additional negotiating leverage.

Assuming that some satisfactory solution is devised for the debt crisis, a new round of talks could concentrate on such concepts as the application of differential treatment (LDCs would have fewer obligations and receive preferential treatment under GATT), graduation (where preferential treatment is phased out for more advanced LDCs), and the role of government in trade. Also, the dramatic growth in services is changing the structure of trade and transforming the world economy. Banking, insurance, and telecommunications have grown to enormous proportions. A growing number of sophisticated manufactured imports require continued service to keep them operating, and this product servicing (such as user training or maintenance) may not be available in the importing market. For their own benefit, developing countries should encourage trade in services to flourish without excessive barriers. Codification of rules for trading in services is extremely difficult—banking is different from telecommunications—but the effort must be made.

Recommendation

The authority of the United States Trade Representative (USTR) as trade policy negotiator and manager should be strengthened and expanded.

Discussion: As previously discussed, the ESC would be responsible for developing an overall U.S. economic policy as well as the framework for a coordinated strategic trade policy. These responsibilities do not diminish the traditional role of the U.S. Trade Representative. Once U.S. economic objectives have been clearly defined and given appropriate priority, it becomes much easier to attain the objectives of the more narrowly focused agencies and policies.

In our view, the authority of the USTR and the TPC, which he chairs, should be strengthened. The Trade Agreements Act of 1979 and Reorganization Plan No. 3 of 1979 (on international trade reorganization) expanded the role of the USTR and the TPC from providing interagency coordination of U.S. positions in multilateral trade negotiations to include responsibility for negotiating multilateral and bilateral trade agreements, import remedy policy, energy trade issues, East-West trade policy, international investment policy, and international commodity negotiations. In addition, the scope of the work of the present private sector advisory system that advises the USTR on negotiating questions should be widened to deal with other issues that require extensive public-private interaction. In strengthening the role of the USTR, we believe there is a need to clarify the distinction between the USTR's policymaking, coordinating, and negotiating mandate and the Commerce Department's responsibility for implementing trade policy and export promotion.

GETTING THE MOST OUT OF AMERICA'S AGRICULTURAL PRODUCTIVITY

Finding

The United States needs a more coordinated policy to integrate domestic agricultural programs, food assistance programs, and agricultural trade programs.

Overview: The advent of the United States as a major trader in world agricultural markets scarcely more than ten years ago has brought problems not previously encountered. These problems relate to: (1) inconsistencies within, and lack of coordination between, domestic agricultural policies and export strategies; (2) multiple, sometimes conflicting, objectives among our foreign assistance efforts; and (3) differences between the trade practices followed by our competitors and those followed by the United States.

U.S. agricultural export policy has traditionally tended to be reactive and geared more toward disposing commodities that cannot be absorbed in domestic commercial markets than toward an integrated, aggressive export marketing approach. Senator Robert Dole recently said: "To my knowledge, no effort has ever been made to rationalize their differing and, at times, contradictory objectives in order to establish a unified and coherent policy for U.S. agricultural trade and food assistance."

Recommendation

The United States must integrate its agricultural trade, food aid, and domestic farm policies.

Discussion: The impact of domestic agricultural programs on the competitiveness of U.S. commodities in world markets, and the ability of the United States to use its agricultural productivity to address the food needs of developing countries, must be more explicitly recognized in domestic policy formulation. This will be especially important when the Congress considers replacement legislation for the Agriculture and Food Act of 1981, which expires in 1985.

The Federal Government has intervened directly in domestic agricultural production and marketing since the depression days of the 1930s. The focus has been primarily domestically oriented, in pursuit of socially acceptable incomes for the farm population. A complex set of price supports, production controls, direct payments, and related mechanisms was put into place over the years in pursuit of this objective. These measures, however, failed to fully account for changing world market conditions. One unintended result of this domestic focus is that government price supports for many commodities have again been allowed to approach levels that impede the competitiveness of U.S. products in foreign markets and the ability of the United States to use its agricultural productivity to meet critical food needs in LDCs. The domestic farm income orientation has also resulted in the imposition of extensive production constraints at a time when many developing countries are not able to meet the food needs of their people, and many thousands of their poor are suffering from severe malnutrition and hunger. The United States could face a calamitous deterioration of its image and influence around the world if it were to continue its policy of giving billions of dollars to its producers to abort the production of food.

Further, unlike foreign competitors, our food aid policy and programs are not effectively integrated with our commercial agricultural export policies. In addition to its humanitarian objective, one of the original objectives of food aid was to develop markets for U.S. food exports. The U.S. Government needs to establish a policy for using U.S. agricultural productivity to address both objectives. For example, today the United States is the world's largest concessional food exporter. It provides over one-half of the total government-assisted agricultural trade moving in the world market, but its share of commercial agricultural trade is only 15 to 18 percent. By recognizing the benefits of market development efforts to both the U.S. economy and the economies of developing countries and making simple, flexible credit programs available to U.S. exporters in an integrated international agricultural trade policy framework, U.S. exports can make a much larger contribution to economic growth.

Recommendation

The Administration should seek to better relate U.S. responses to LDC food and domestic security requirements.

Discussion: Often what eventually erupts as a security threat has roots in food shortages; this is particularly likely when economic reforms needed for long-term growth bring painful short-term dislocations.

Recent civil disturbances in the Dominican Republic, Tunisia, and Egypt had to be quelled by military action. In these cases, civil strife threatened to seriously undermine governments the United States perceived as taking positive measures necessary for economic growth. Additional food assistance might have succeeded in softening the impact of adjustments and reduced the need for a military solution to resulting problems.

As long as food aid, trade, economic development, and other programs affecting our relations with developing countries are fragmented in different agencies having different objectives with no overriding body to coordinate these objectives, we will continue to forego opportunities to marshall our resources to maximum effect and assure a constructive resolution of conflicting interagency goals.

BUSINESS REGULATION

Finding

Some U.S. Government measures have discouraging or disadvantageous effects on American firms that are involved or might become involved in long-term relationships with private enterprise in developing countries.

Overview: U.S. trade policy has too frequently involved an extraterritorial extension of U.S. policies and laws to other nations, thereby creating conflicts for U.S. businesses and economic tensions with other governments. Although some efforts have been made to reduce the discouraging effects of such laws and administrative measures (especially through recent regulatory reform initiatives of the Reagan administration), the lack of an effective high-level coordinating mechanism has resulted in inconsistencies in policies and mutually conflicting practices.

Historically, one reason so few U.S. businesses participate vigorously in export trade has been the U.S. Government's failure to take international considerations sufficiently into account in setting domestic economic policies. Government policies often raise the cost of producing for export, increase the sales price, critically extend the contract negotiating period, or introduce other uncertainties that discourage U.S firms from voluntarily entering the international marketplace. The United States must have an institutional capability to view trade and domestic economic issues as inseparable components of a coordinated and consistent U.S. economic policy.

Recommendation

The U.S. Government should coordinate more effectively its efforts to assure that U.S. laws and regulations reflect greater sensitivity to structural changes in the international marketplace.

Discussion: State companies, conglomerates of competing firms, and a host of other factors are rapidly rearranging the structure of the international trading system and the terms of trade. Yet the U.S. Government has no institutional ability to assure that the new structure is reflected in its laws and regulations. For example, nearly a century ago the United States enacted stringent antitrust laws to regulate its domestic market. Over the years, changes in U.S. antitrust laws have lagged behind changes in the configuration of our economy. Today, most sectors of our domestic markets are powerfully affected by foreign competition. Measures of domestic concentration and competition that were appropriate to the United States in the 1940s make little sense now. They need reappraisal—not simply by the legal community, but by those who understand commerce and trade. For example, the United States is the only country whose antitrust laws are applied to both its foreign and domestic commerce. Similar observations have been made about the Foreign Corrupt Practices Act, the Internal Revenue

Code, and the taxation of Americans who work overseas. While an extraterritoriality policy can be tailored to fit different legal and regulatory provisions, objective criteria must be established. Our trading partners, as well as American exporters and investors, need clarity and predictability in rules that reflect today's realities. Another example of an originally well-intentioned—but now seriously outmoded—regulation is the cargo preference requirement for U.S. food assistance programs. This requirement will reduce our food aid by more than $100 million this year alone.

There have been recent signs that there is greater awareness of the need to review and revise U.S. laws and regulations related to the international marketplace. Enactment of the Export Trading Company Act of 1982 was a step forward. The response to the law has been limited, partly because of inadequacies with its language, partly because there were disagreements within the Administration as to how the regulations should be written and interpreted, and partly because the business community has been suspicious and cautious in testing this new vehicle. Continuous review of regulations and progress in ironing out differences is required to assure consistency with overall U.S. economic objectives.

PART V

Current Areas of Concern: Trade and Food Assistance

Two key elements of any development strategy are trade and food. Trade nourishes the economy; food nourishes the people. There can be no successful economic development without enough of both to sustain it.

As it happens, trade and agriculture are also both matters of key importance to the economy of the United States. There are a number of specific measures with regard to trade policy and food aid that we believe should be taken for the benefit of both the United States and the developing countries. These proposed measures would serve the cause of international private enterprise. They would serve the cause of economic development. They would also serve the interests of the United States and the people of developing nations.*

Trade

INTRODUCTION

For developing countries, particularly those struggling to accommodate heavy debt burdens and debt service payments, trade offers the only realistic path toward long-term economic growth. For the United States, trade is vastly more important to the economy now than it was over the past century. For both the United States and the developing countries, how the global trading system evolves over the next few years will determine whether we are to share in a future of peace, stability, and prosperity rather than one of hunger, want, and unrest.

*NOTE:
Task Force members George Ferris and Myer Rashish take exception to Part V as not germane to a report on private enterprise and development.

Importance of Trade to Developing Country Economies

For developing countries, the future depends increasingly on expanding trade. This is so because internal markets are limited, foreign assistance programs are declining, and many donor countries face budgetary crises. At the same time, economic difficulties continue to plague industrialized nations, which are the major market for LDC goods and services. (These conditions will not change in the short term.) Not only is expanded trade critical to provide the wherewithal to service massive debts, but trade stimulates more efficient internal production as competition from imports and for exports drives local producers to improve productivity and encourages innovation.

In general, the most effective way for developing countries to participate in the international trading system is to pursue an export-oriented development strategy. Such a strategy places primary emphasis on production processes that generate exports rather than on those that substitute for foreign imports. A successful export-oriented development strategy will also tend to discourage the adoption of nonmarket policies that are inner-oriented and restrictive.

The Newly Industrialized Countries (NICs), such as Hong Kong, Singapore, and South Korea, many of which are former recipients of sizable donor assistance, developed their economies by relying on export-oriented trade policies. These are now vibrant economies, whose value as trading partners far exceeds the funds expended on them by donor nations. The assistance given these NICs during the 1960s is small compared to the sevenfold increase in their imports from the United States between 1972 and 1981.

Importance of Developing Country Trade to the United States

The international trading system and the level of U.S. exports to developing countries have substantial impact on the entire U.S. economy. U.S. exports and imports worldwide represent approximately 25 percent of the $3 trillion value of goods and services generated in the United States in 1982, compared to only 5 to 10 percent 15 years earlier. Developing countries in particular accounted for most of the growth in American exports from 1975-1980 and thus for a significant share of the new jobs created in U.S. manufacturing firms during this period. Thus, the 20 percent decline in U.S. exports to Latin America in 1983 as a result of the debt crisis cost approximately 250,000 Americans their jobs.

Unfortunately, many in the United States have been slow to recognize the importance of international competitiveness to the health of our own economy. The seemingly secure, attractive and growing United States and developed country markets of the past have left a legacy of complacency. Only now are we beginning to recognize that domestic producers are vulnerable in domestic markets to international product improvements or lower prices. Few businesses can continue to ignore the consequences of the fact that often their

FIGURE 4:
Balance of Merchandise Trade,
1970-1982

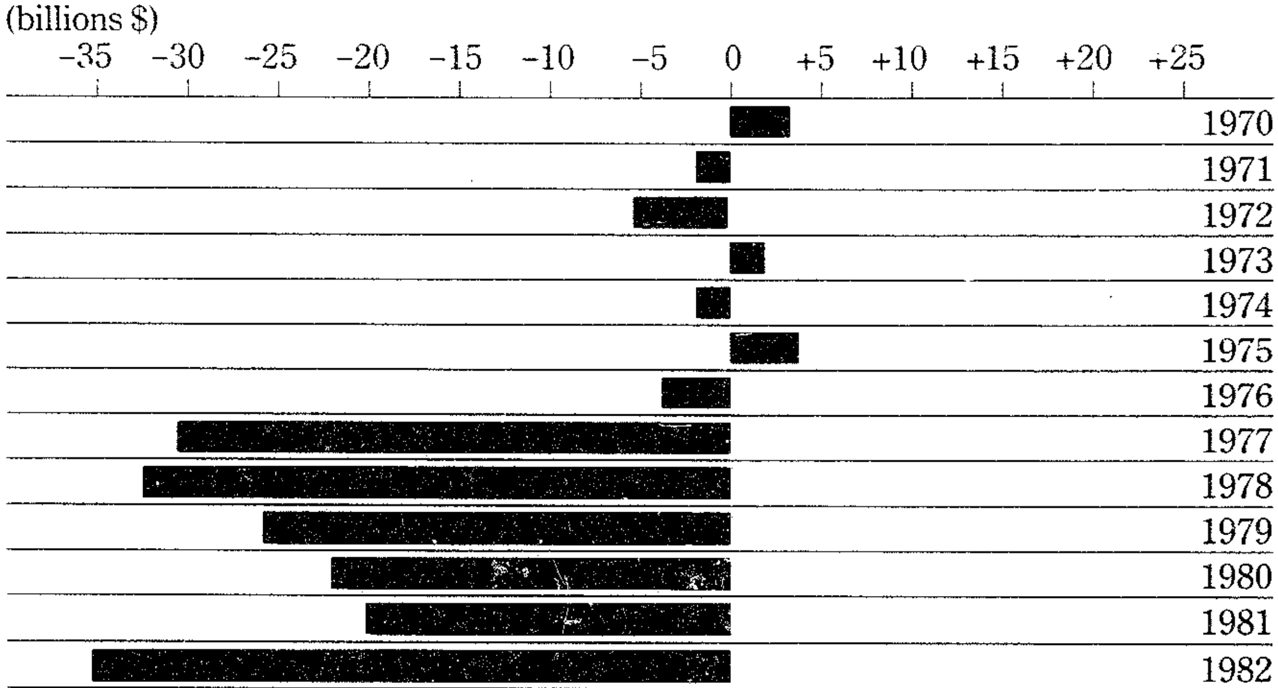
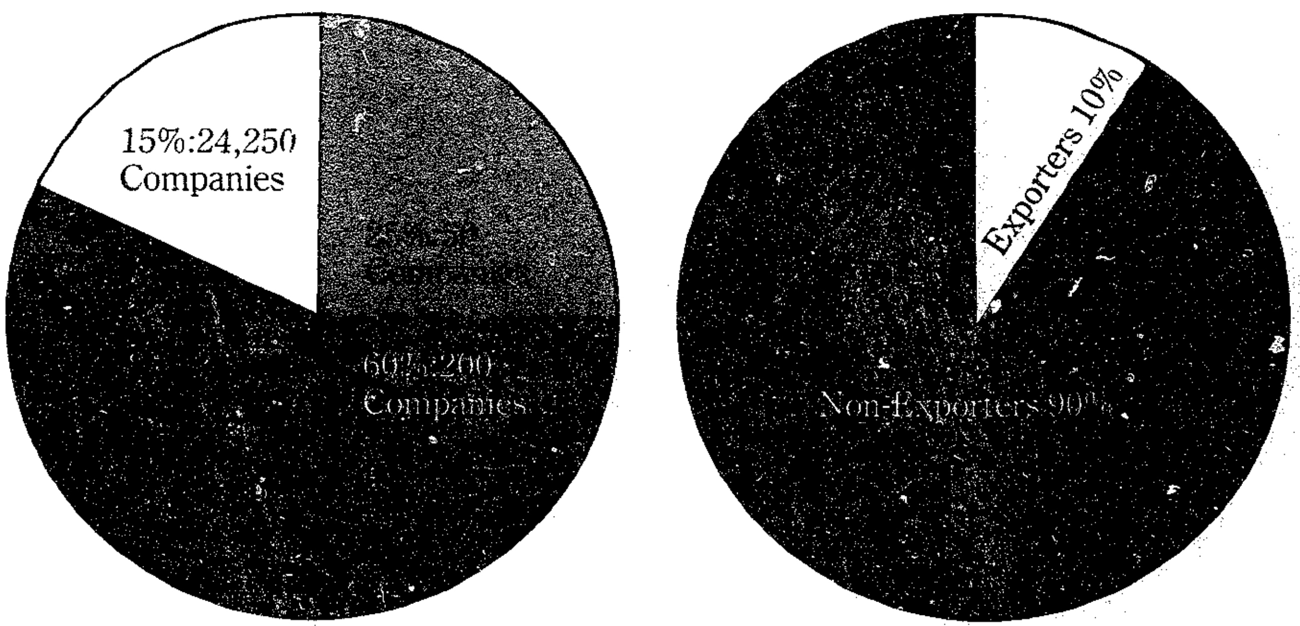


FIGURE 5:
Participants in U.S. Trade, 1984



Total Exports

U.S. Manufacturers:
Estimated at almost 300,000.

SOURCE:
The Export Trading Company Guidebook, U.S. Department of Commerce, International Trade Administration, 1984.

raw materials, component parts, or entire products may originate in the developing world. Competition in the U.S. marketplace is no longer national, but international. American businesses that adapt to changing circumstances and recognize opportunities will prosper; those that do not will, at best, survive temporarily at a cost to themselves, the U.S. consumer, and U.S. relations with friendly nations.

As one advocate put it, "the unmet needs of the developing countries are business opportunities." Attention to the developing world will mean bigger and better markets, a larger manpower pool, and increasing operational flexibility for those businesses engaged in the international arena. It will also mean greater economic security for the United States.

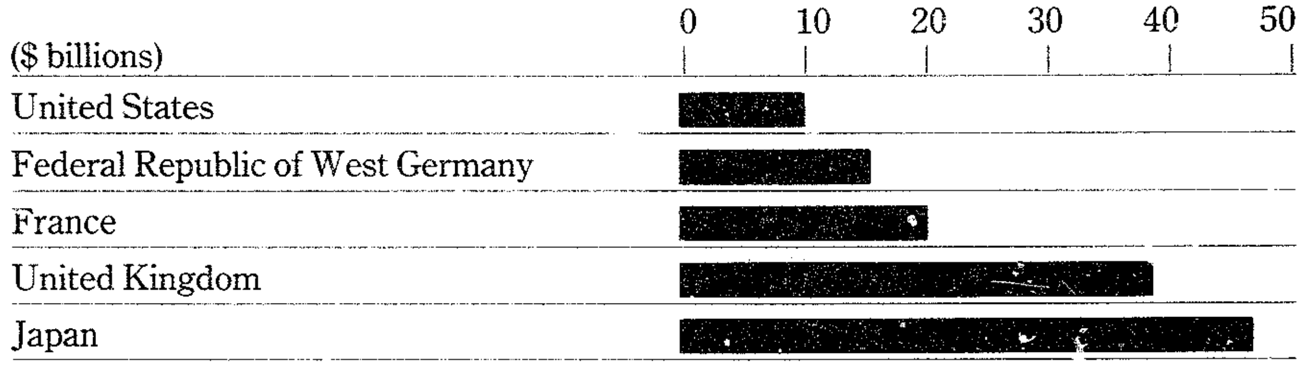
Based on price and other considerations, the Department of Commerce estimates that between 10,000 and 25,000 U.S. business firms could export their products, but do not. It is also estimated that 100 U.S. companies account for 50 percent of U.S. foreign trade and that only 250 U.S. firms account for 85 percent of our foreign trade. (See Figures 4 and 5.)
This is much too narrow a base on which to rely for an economy as large and diverse as ours. American companies need to recognize and understand the opportunities available to them. Through investment and trade, U.S. business can improve long-term profitability and make a greater contribution to LDC development.

The International Marketplace

New technologies are dramatically changing the competitive positions of firms, industries, and nations and may even alter the process of development itself. Technological change is hastening the evolution of local and regional markets into global markets. Sophisticated systems of licensing, communications, coproduction, and finance link firms of various sizes. These networks provide economies of scale previously attainable by only a few large firms. While these developments offer significant opportunities to all participants in the international marketplace, they have also given rise to a variety of trade distorting practices as countries attempt to minimize the internal disruptions that may result from changes in external trading patterns.

The increased use of protectionist trade measures has had a significant impact on world markets. Many Free World governments, including the United States, have increased the subsidies and trade barriers by which they protect old, inefficient industries and agricultural producers from import competition. The new style of developed country protectionism relies on domestic subsidies, voluntary export restraints, and other devices that are more difficult to quantify, rather than on tariffs. The relative invisibility of these tactics, which often operate through administrative discretion, makes it almost impossible to assess precisely either their impact or their value. But the results are just as pernicious as are those of older forms of protection.

FIGURE 6:
A Comparison of Total Exports Supported by Official Finance in the Major Trading Nations in FY 1982



SOURCE:
Export-Import Bank of the United States, 1982.

Similarly, developing countries have taken measures that have a negative effect on the world trading system. Many developing countries rely on stringent government control of every element of a transaction; enact policies that discourage business rather than attract it; and, in essence, favor government resource allocation over economic growth.

Once protectionism has taken root, a prolonged period of prosperity may be necessary before countries are prepared to back away from their protectionist policies. Also, protectionist tactics by the developed countries reinforce the temptation toward inward-looking protectionist policies by the developing countries themselves.

Many foreign governments have been increasing their official efforts to promote exports to developing countries. They enhance standard financing packages with special features to give their exporters a competitive edge in developing country markets. Examples of such enhancements include: financing of local currency costs for turnkey projects; inflation insurance for large contracts requiring long construction periods; exchange risk insurance for foreign currency-denominated loans; mixed credits that combine concessional government funds with commercial funds to produce lower than market-based interest rates and more lenient loan terms for exporters; and tied-aid credits that utilize the government's foreign assistance programs to influence procurement decisions in their exporters' favor. Some sense of the extent of official government assistance is provided in Figure 6.

Thus, increasingly U.S. exporters find themselves having to compete against the national treasuries of mercantilist nations. These mercantilist states are attacking the free enterprise system in the Western world through their use of mixed credits and other subsidies. This kind of competition also raises developing country expectations that U.S. firms will offer similar trade packages. Further, the absence of U.S. Government support of a similar nature deprives developing country businesses of valuable U.S. technical expertise that is critically needed. It also diminishes opportunities for U.S. private companies, especially small and medium-sized, to participate in the LDC development process. To cope with this situation, we are forced to use mixed credits to protect the system of international private enterprise.

The Newly Industrialized Countries have also used export support programs to buy their exporters' way into targeted foreign markets. They provide combinations of below-market interest rates and longer-than-customary repayment terms. The areas of such competition are growing and now include offshore oil drilling rigs from South Korea, compressors from Taiwan, and aircraft and agricultural products from Brazil. Countertrade in lieu of cash is also emerging as a major alternate payment mechanism. Developing countries increasingly require countertrade components in import contracts. Despite the short-term attractiveness of such trade policies, particularly for those developing countries with heavy debt burdens and severe foreign exchange constraints, they ultimately hurt all participants in the international marketplace and inevitably lead to an inefficient and wasteful allocation of resources with serious negative long-term growth implications. Furthermore, the use of such approaches requires greater government interaction in domestic economies and international trade, compounding market distortions and adding even more inefficiencies. The cumulative effect of these interventions is to slow the real, long-term expansion of world markets. Ultimately, this expansion will only occur through opening international competition, guided by liberalized trade rules that are adhered to by all trading nations.

FINDINGS AND RECOMMENDATIONS

Finding

The United States has not adopted a strong enough stance in its negotiations to stop foreign governments from using unfair methods of subsidizing export finance.

Overview: Major exporting nations are employing predatory, mercantilist practices to protect their domestic markets and to exploit foreign markets. These include tariff barriers, a host of new and inventive nontariff barriers, and a potpourri of export subsidies, the purpose of which is not to build the economies of the recipient countries, but merely to pre-empt the markets of their customers. What these practices mean, in effect, is that our farmers no longer compete against foreign farmers; our workers no longer compete against foreign workers; and our corporations and cooperatives no longer compete against foreign corporations and cooperatives. Instead, they must confront foreign governments and their national treasuries. We endorse the Administration's efforts to negotiate an end to the use of mixed credits and other types of predatory concessional export financing for commercial advantage. The United States considers trade-motivated subsidized financing wasteful, costly, and ultimately futile because it causes a budgetary drain on exporting countries and distorts the international trading system. Exported goods and services should be sold under free market conditions on the basis of price, quality, and intrinsic value. Subsidized financing does not contribute to the value of these goods or lead to eventual reduction of production costs.

In OECD negotiations, the United States has attempted to eliminate the use of those mixed credits used primarily for commercial purposes. Little progress has been made. We believe that U.S. negotiators need a more forceful position and more effective bargaining chips to help them achieve their goals. The mixed credits recommendations we make would provide the U.S. Government with more negotiating leverage to end foreign governments' use of unfair or predatory concessional financing and level the playing field for international trade, opening the way to market forces and competition.

Recommendation

The United States should use aggressively the mixed credits authority of the Export-Import Bank (Eximbank) to counter competitors' mixed credit offers.

Discussion: Eximbank should operate up to the full limits of its combined $14 billion in guarantee and loan authority to fight predatory mixed credit practices of our foreign competitors. The use of mixed credits and other concessional financing programs by foreign governments increasingly serves to exclude U.S. exporters from markets in developing countries and elsewhere, and results in substantial long-term business losses without increasing total world trade and without the benefits of expanded trade opportunities for developing countries and their private sector businesses. In the strongest terms, we are clearly of the view that the use of mixed credits is not a policy we desire, but rather a weapon we must use to respond to the policies of others because negotiating an end to the use of mixed credits in the near future is unlikely. In fact, the incidence of mixed credit offers and financing continues to increase. The increased use of mixed credits tends to shift scarce highly concessional funds from the poorest countries to higher income developing countries. Further, mixed credit financing can divert concessional funds from the recipient country's highest priority development projects because mixed credits frequently go to sophisticated, capital-intensive projects that may not be at the top of the recipient country's development agenda.

The United States should use the financing capabilities of the Eximbank to the full extent of its resources as a temporary weapon in a strategy that will provide the U.S. Government with more negotiating leverage to roll back the mixed credit programs of others and enable U.S. exporters to meet this unfair competition. Existing authorities are adequate for Eximbank to maintain an aggressive mixed credits program, as demonstrated by its recent mixed credits offers. Eximbank has substantial unused financing authority and total financing ceilings that are sufficient to accommodate any activity likely to be generated by this program in the near future. Use of Eximbank resources in this manner will serve notice to our competitors that the United States will provide the necessary assistance to U.S. firms that find themselves competing against predatory financing, thereby substantially improving our negotiating position. In FY 1983 and FY 1984, we estimate that the total mixed credit offers by our foreign competitors may have been as much as $7 billion. We believe that, if necessary, the Eximbank should use the full extent of its authority to fight mixed credits. If this requires $7 billion or more on our behalf, that is only half of Eximbank's annual loan and guarantee authority, much of which has been unused in recent years. We endorse such an expenditure to provide short-term protection to American firms and help end the use of predatory trade practices by our foreign competitors as soon as possible for the long-term benefit of all global trade participants.

Recommendation

AID should also use its limited mixed credits authority, although the Export-Import Bank will be the major source of mixed credit financing.

Discussion: Legislation on export financing passed by Congress in 1983 directed Eximbank and AID to establish a mixed credits program. AID would probably not be as effective as Eximbank in carrying out a mixed credits program because of its strong developmental and political mandates, in which trade and export promotion are not key factors. In addition, AID's limited resources are primarily allocated to countries where the mixed credit programs of our competitors are not directed; new legislation would be required for it to expand its mandate to other purposes in other countries. Start-up time would be long, institutional difficulties great, and the benefits not as clear as maintaining the program with Eximbank. AID does have the authority, however, to engage in mixed credit activities under limited circumstances in certain countries, such as its Trade Financing Facility in Egypt. AID should continue and expand these practices under appropriate circumstances.

Finding

The current debt crisis in the developing countries requires close cooperation between the U.S. private and public sectors to assure that adequate trade financing is made available.

Overview: Many middle-income LDCs are in serious debt trouble because of heavy borrowing during the 1970s. This year the U.S. private sector has begun to look at some new methods of export financing. Private sector sources of export financing include banks, exporters, trading companies, commodity companies, countertraders, private insurance companies, and other financial intermediaries. However, the resources available are considerably less than they were three years ago, and U.S. Government trade financing programs do not operate in a manner that adequately addresses the current debt crisis.

Recommendation

U.S. Government foreign credit programs should operate under consistent guidelines.

Discussion: The U.S. Government provides varied export financing and services support through many agencies and programs. A coordinated approach has been impeded by protectiveness toward agency prerogatives and limited interagency cooperation, which has been evident to the users of these programs for a long time. The proposals contained in the Formation of U.S. Economic Policy section should remedy the long-term coordination problem. Meanwhile, general guidelines are necessary.

We suggest that the U.S. Government support financing of U.S. private sector exports and developing country imports when any of the following conditions exist:

- ☐ credit is not available for developing countries in the commercial markets;
- ☐ unfair financing practices are being used by foreign governments to subsidize their exports; or
- ☐ the national security interest of the United States requires the support of a particular export or export activity.

Better coordination among U.S. Government agencies with respect to export support programs should bring more effective diplomatic results regarding U.S. trade and the quality of our foreign assistance. It should also help neutralize the unfair trading practices of our foreign competitors. A clear, overall policy framework should be established within which all these trade financing programs would operate.*

Such a coordinated approach requires explicit, consistent agency-to-agency guidelines on terms and definitions, application and filing procedures, and coverage. These guidelines should reflect developing country and regional priorities and be drafted so as not to disturb established markets for U.S. exports (by offering concessional terms when they are not required). Such guidelines for trade financing would benefit the private sector as well, a first step in effectively blending private and public sector resources.

For example, among the more important shortcomings of the different guarantee programs is the lack of consistency in coverage. Eximbank, OPIC, CCC, and SBA all issue guarantees, but specific coverage varies significantly between each agency and all have different guidelines for submitting claims. Another complicating factor is the different type of coverage provided for past-due interest. While knowledgeable exporters and banks can benefit from the lack of consistency among agency programs, these inconsistencies discourage other exporters or potential exporters.

The new coordinated approach would also allow the innovative blending of seemingly unrelated public and private sector resources. This could be done by dividing a single, large-scale project, turnkey project, or commodity sale into components. Special financing, guarantees, or insurance for some components of the transaction could be pro-

*NOTE:
The primary supplier of official export credit support in the United States is the Export-Import Bank of the United States (Eximbank), in conjunction with the Foreign Credit Insurance Association (FCIA), and the Private Export Funding Corporation (PEFCO). The principal other U.S. Government agencies that support U.S. exports are AID, the Commodity Credit Corporation (CCC) and the Foreign Agricultural Service of USDA, the Overseas Private Investment Corporation (OPIC), the Small Business Administration (SBA), and the Trade and Development Program (TDP).

vided, while leaving other components to be handled by the market or by official export credit support within the OECD guidelines. A second method could entail providing development assistance in a non-earmarked form that is parallel with, but not formally linked to, a project or set of transactions financed with commercial or official export credit support. A third method would be cofinancing, with public funds used to soften the overall credit terms of private funds and leverage greater private financial support at the same time.

Recommendation

As part of an integrated trade policy, the participation of the U.S. private sector in countertrade should be facilitated when it is in the best interest of the United States.

Discussion: Estimates of the volume of countertrade vary widely, but projections suggest that, unless matters change, a significant amount of world trade will involve some form of countertrade by the turn of the century. Due to the scarcity of foreign exchange, developing countries are increasingly employing barter and countertrade, particularly with agricultural products. In part, it has been brought about by increased protectionism in developed countries (which has deprived developing countries of a market for their goods) and the debt crisis. Developing countries use countertrade as a means of bypassing foreign exchange limitations and continuing trade when commodity markets are depressed and financial markets are shrinking.

In a healthy international trade environment, barter and other forms of countertrade may represent market distortions. In the current international trade environment, however, many developing countries believe mandatory countertrade requirements improve their ability to expand much needed trade and to develop export opportunities that would not otherwise exist. While the United States should continue to oppose such countertrade mandates, it should not impede the ability of U.S. private firms to expand trade through countertrade arrangements. Direct U.S. Government involvement in countertrade should be primarily related to acquiring strategic materials.

Food Assistance

INTRODUCTION

Among all the human needs that economic development serves, food is the most basic. In most developing countries, agricultural development is fundamental to economic development. And in the development of the market sector, agriculture frequently leads the way. In developing countries, the overwhelming majority of "entrepreneurs" are small scale family farmers.

American agricultural abundance is one of the wonders of the modern world. Historically, we have used our abundance to respond quickly and generously to the plight of others facing hunger or starvation. It is a tradition that reflects well the basic decency and values of the American people. Not only our agricultural products, but also our knowledge of how to grow, store, transport, process, and distribute them can be of enormous value to the developing nations. As these countries improve their economies, they become increasingly important commercial markets. Thus, expanding world markets for U.S. agricultural resources can, at the same time, be of enormous value to the U.S. economy.

Importance of Agriculture to Developing Country Economies

To an extraordinary degree, economic development in the Third World depends on agriculture. This sector provides sustenance, jobs, and foreign exchange. More than two-thirds of the developing world's people live in rural areas and most of them work at jobs related to agriculture or agribusiness.

Unfortunately, progress in agricultural development in the recent past has been extremely disappointing. In 31 of the least developed countries, agricultural production over the past decade increased only 1.6 percent per year compared to a population increase of 2.6 percent per year. Starvation is thus a constant threat and increased production is a vital and urgent necessity.

The President has proposed two major initiatives in recent months to address the most critical aspects of the poor agricultural performance in developing countries.

The first of these, the establishment of a $50 million Special Presidential Fund, would enable the United States to respond more effectively to acute food crises. It would help avoid delays and clear the way for the United States to take the lead in emergency relief efforts even when annual food aid funds are severely limited.

In the long term, however, indigenous agricultural production must be increased. This requires developing country policies that encourage agricultural production. In too many cases, existing policies fail to provide sufficient incentives to farmers to increase production, and preclude the efficient operation of the market. To help remedy this, the President has also proposed a five-year, $500 million program, referred to as the Economic Policy Initiative (EPI). The EPI is designed to provide additional support to African governments that are either free-market oriented or are taking steps in that direction. In particular, it would provide additional development resources to nations that have changed, or are in the process of changing, their systems to (1) provide greater incentives to farmers and (2) reduce the state's role by eliminating state marketing boards and price controls that artificially skew resource distribution in ways that are harmful to farmers. This initiative will also serve as a catalyst for improvements in other bilateral and multilateral assistance efforts.

Importance of Agriculture to the U.S. Economy

Despite the small percentage of Americans actively engaged in farming, the agriculture sector in the United States—including farmers, agribusiness, and retail food operations—provides over 20 percent of U.S. GNP and 22 percent of U.S. employment.

Before the 1970s, the U.S. was not a major participant in world food markets. Agricultural exports were only 10 percent of farm cash receipts in 1950 and 14 percent in 1960. By 1980, exports provided almost 30 percent of total cash receipts. Today, the production from four acres of every ten is destined for foreign markets. Overall, at least one-third of the total production capacity of U.S. agriculture produces for foreign markets. The growth of agricultural exports has given farmers, labor, and the agribusiness sector a vital stake in U.S. international economic policies.

U.S. agricultural exports consistently set new value and volume records through the 1970s, but peaked in 198[illegible]. They have declined precipitously since then. In FY 1983, exports fell to $34.8 billion, 21 percent below the record high. This resulted primarily from a slackening in demand brought about by the worldwide recession and the debt crisis, strong appreciation of the dollar, which placed our products at a competitive disadvantage, an increased use of export subsidies by our competitors, and abundant harvests elsewhere in the world. While some recovery in exports is expected this year, the decline brought to the surface troublesome, longer term problems for U.S. trade.

Despite the importance of this sector to the U.S. economy, we have adopted agricultural policies in the past that have attempted to reduce farm output rather than use our agricultural potential to benefit U.S. farmers, U.S. and world economies, and the millions of starving and malnourished in the developing world. Under the 1983 Payment-in-Kind (PIK) program, for example, 50 million tons of corn and 16 million tons of wheat (valued at $10 billion) were returned to farmers with corresponding 40 million ton and 16 million ton reductions in production.* This would have been more than enough to supply the 33 million tons of food needed by developing countries to achieve minimally acceptable nutritional levels. (See Table 5 on page 115.) At a time when the international donor community is having difficulty accommodating even emergency food needs of one to two million tons in drought-stricken African countries, a domestic farm program that results in such a massive reduction in production is unacceptable. A better way must be found to harness America's agricultural bounty that will provide an appropriate reward to the labors of our farmers, while addressing the food needs of our fellow men.

Global Competition

Hope of achieving the full potential of expanded markets for agriculture, with resulting benefits for the United States and developing country economies, hinges, in large part, on whether or not we can achieve a truly market-oriented world trading system. As in other trade areas, in recent years we have seen competitors increase agricultural exports while employing predatory trade practices to protect their domestic markets and exploit foreign ones. Many of these countries have artificially stimulated a higher level of production to promote agricultural exports with subsidies greater than their domestic resource base would justify. Thus, our farmers now compete against the national treasuries of other countries. Many developing countries have also attempted to achieve agricultural self-sufficiency, often supported by the import substitution policies of development institutions in the past, in ways that resulted in the inefficient use of increasingly scarce resources.

Most important, other exporting nations with abundant supplies compete fiercely for the available markets, frequently employing practices not available to U.S. exporters. The most direct of these is the use of export subsidies to penetrate markets, a practice used most notably by the European Economic Community (EEC). Such trade distorting practices can have a devastating impact on developing countries. The European Economic Community-Common Sugar Policy (EEC-CSP) provides a striking example.

The EEC-CSP, which subsidizes both production and exports of sugar, has resulted in massive increases in surplus sugar production (EEC production rose from 9 million tons in 1974-1975 to a high of almost 16 million tons in 1981-1982, while consumption fell from 10.6 to 10.1 million tons). Surpluses have been dumped upon the world's sugar markets. Today's low world sugar prices can be attributed to the EEC-CSP, which has contributed about two-thirds of the current price depressing buildup of world sugar stocks. In turn, the low sugar price has had a serious impact on the economies of many developing countries, particularly in Latin America and the Caribbean, stamping out private enterprise. The EEC, through its market-distorting use of Treasury funds, forced prices down to levels sharply below the cost of production. Countries in this region lost about $3.7 billion in foreign exchange earnings over the past three years from sugar sales alone. Millions of dollars of additional income would have been lost each year had the United States not assured a reasonable price for its quota imports from this region.

Not only are the economic impacts of such policies severe, but the close link between economic stability and political

*NOTE:
The reduced production and declines in carryover stocks attributable to the PIK program versus the effects of the drought are difficult to differentiate. This figure represents an informed estimate by USDA.

stability has had major national security ramifications for the United States. At a time when the United States is committing billions of dollars in military assistance to its European allies, the EEC, through its farm policy, has contributed to political and economic instability in Central America and throughout the region. Part or all of the billions of dollars spent by the EEC on export subsidies could be more constructively used to pay for the costs of NATO.

The use of concessional financing and predatory export subsidies accounted for $950 million, or 13 percent, of the drop in U.S. agricultural exports from 1981 to 1983. Such measures are used less when markets are expanding rapidly, but their adverse effect on U.S. agricultural exports becomes pronounced in slow growth periods. Given the outlook for slower market growth in the future, they can be expected to be a persistent concern in such a trade environment. Moreover, the scope of preferential credit is likely to expand to ameliorate the credit constraints imposed by the growing Third World debt pressures. Exporting countries have chosen to compete with predatory trade financing mechanisms rather than increase the availability of food assistance or address the root causes of the inability of importers to purchase food in commercial markets.

FINDINGS AND RECOMMENDATIONS

Finding

Many developing countries face chronic food shortages that will undermine their political stability and economic development.

Overview: At the beginning of this decade, food production for all developing countries was 38 percent greater than in 1970, but population growth was so rapid that production per person was only 8.9 percent greater and, even then, there were large variations between countries. As production expands to marginal land and capital to meet investment needs becomes scarcer, prospects for growth in per capita food production to the end of the century are considerably less favorable than they were in the 1970s.

By the year 2000, the world will have 1.5 billion more people to feed than it does today. This is more than seven times the current population of the United States. Each year the world must feed and clothe 90 million more people. While the absolute number of additional people to be fed is an important determinant of future food needs, so is their geographical distribution. Most of the additional people—93 of every 100—will live in the lower income developing countries, where people are struggling to increase their consumption and upgrade their diets, but many lack the purchasing power to do so.

By the end of the century, the additional global food requirements will be enormous—some 40 percent more in

2000 than in 1980—just to maintain average consumption. An even greater increase would be needed to provide malnourished people in poor countries with an adequate diet. While every region of the world can be expected to expand food production in an attempt to meet the growing demands, large supply/demand imbalances will still exist in more regions. Addressing these imbalances will require significant efforts by both developed and developing countries.

Recommendation

Food aid should be at least doubled to help avert starvation, alleviate poverty and malnutrition, expand developing country agricultural markets, and support private sector growth.

Discussion: In the short term, food aid can help meet emergency food requirements, particularly in lower income countries. In light of serious credit constraints, heavy debt burdens, and potentially higher food prices, there is the strong possibility that the developing world will face a major food shortage within a decade—far greater than even the present shortage in Africa. To help avert this crisis, we should at least double our P.L. 480 program, keying the actual increase to meeting needs and averting starvation, while increasing the flexibility of program terms to meet the individual needs of recipient countries.* Specific recommendations on more flexible terms are outlined in the P.L. 480 Action Brief.

For 1983-1984, USDA estimated that low-income countries would require 12 million tons of food aid just to maintain average food consumption levels. To attain a minimally acceptable level of food consumption, as prescribed by Food and Agriculture Organization (FAO) standards, 33 million tons of food aid (of a total 48 million ton import requirement) would be required (see Table 3) with an additional 2.7 million tons required to rebuild depleted stocks for food security purposes. These figures compare to the current donor country commitment under the international Food Aid Convention to supply 9 million tons of food aid, the originally planned FY 1984 U.S. P.L. 480 program of 5.7 million tons, and an 18 million ton per year U.S. food assistance program in the 1960s. (See Figure 7.)

With our abundant resources and well-deserved image as a humanitarian nation, we should take the lead in increasing relief efforts in Africa and elsewhere in the world. A significant increase in P.L. 480 will (1) help meet critical food needs; (2) signal the intention of the United States to meet these needs through official food aid; and (3) provide significant benefits to the U.S. economy while strengthening the long-term ability of developing countries to meet their own needs. After all, how can we expect private enterprise to possibly flourish and grow in areas where most of the farming and labor forces are in a starvation cycle.

We recognize the concern that large-scale increases in food aid could serve as a disincentive to local production. Therefore, as an important component

*NOTE: Reference to a doubling of the P.L. 480 program is based on the approximately 5 million ton level originally approved for FY 1984 and planned for FY 1985 at the time the Task Force developed this recommendation. Subsequent increases in the program, which are expected to increase FY 1985 shipments to about 8 million tons, were not considered in the Task Force analysis.

TABLE 3:
Cereal Import Requirements and Food Aid Needs to Support Consumption

(in thousand tons)	1983-84 Import Requirement Status Quo[a]	Nutrition[b]	1983-84 Food Aid Needs Status Quo[a]	Nutrition[b]
North Africa	10,153	6,400	3,517	377
West Africa	2,099	3,685	985	2,754
Central Africa	714	1,715	167	1,169
East Africa	1,974	5,613	1,624	5,296
Southern Africa	1,988	2,772	1,314	2,097
Middle Africa	1,378	1,525	277	423
Subtotal	18,306	21,710	7,884	12,116
South Asia	2,164	18,024	1,270	15,647
Southeast Asia	4,981	3,700	1,946	2,688
Subtotal	7,145	21,724	3,216	18,335
Caribbean	998	11,227	227	465
Central America	600	626	144	288
South America	2,770	2,765	963	1,501
Subtotal	4,368	21,618	1,334	2,254
Total	29,819	48,052	12,434	32,705

SOURCE:
World Food Aid Needs and Availabilities, U.S. Department of Agriculture, Economic Research Service, 1983.

NOTES:
a) To maintain current consumption levels based on per capita intake of food staples at levels reported over last four years.
b) To raise per capita intake of staples to levels associated with the Food and Agriculture Organization's recommended mininums.

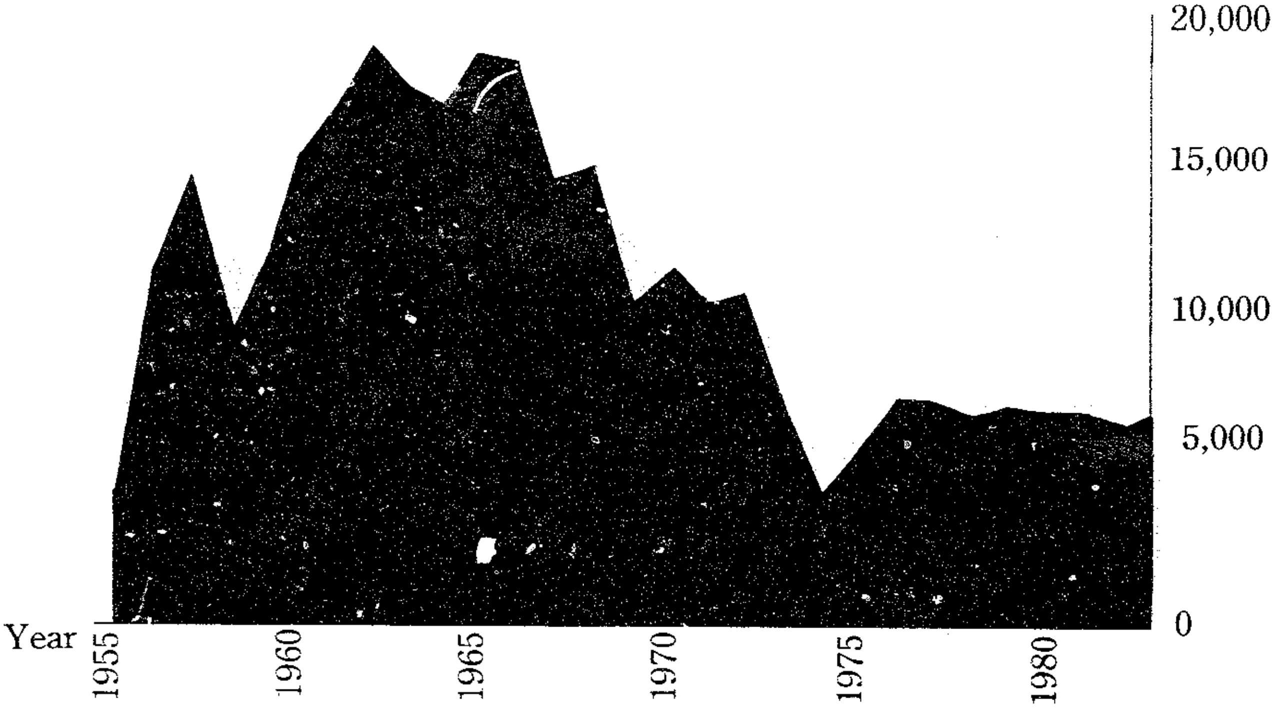
of the expanded program, appropriate assurances should be obtained that recipient countries will adopt policies to maintain their domestic producer prices—where these are adequate—as incentives for domestic production and increase them where they are not adequate. Sufficient safeguards must also be in place to assure that these additional supplies will not disrupt commercial markets or exceed the capacity of the local distribution infrastructure. AID should consider establishing a program to provide short-term financing to help developing countries address these constraints wherever they preclude the programming of additional food aid.

Recommendation

A much larger share of total U.S. foreign assistance should be food assistance.

Discussion: In times of low commodity prices and large U.S. agricultural surpluses, food assistance is one of the most cost effective forms of foreign aid. In fact, rather than adding to government costs, savings in deficiency payments, loans, and storage costs under price support programs from an expanded P.L. 480 program can actually result in a net gain to the U.S. Treasury. For illustrative purposes, the Task

FIGURE 7:
P.L. 480 Shipments 1955-1983



Force examined the impact of doubling the P.L. 480 program for the next five years.* Such an increase would provide approximately six million additional tons of food per year to help meet critical food needs and allow improvement in currently inadequate diets. This would result in a direct benefit-cost ratio of nearly 2:1 to the U.S. Treasury, with nonrecoverable costs totaling only $2.5 billion compared to price support savings of $4 to $5 billion. (See Table 4.)** This does not include additional benefits to be derived from expanded commercial market opportunities for U.S. agricultural exports, the impact of a higher level of exports on general economic activity, or the employment opportunities generated by the increased economic activity. Such a doubling of the program funding would generate approximately $1.6 billion in additional economic activity, with benefits to the U.S. Treasury of approximately $300 million in revenue, $80 million in unemployment savings, and approximately 20,000 additional jobs.

Additional flexibility must also be provided so that critical food aid needs can be met in a timely manner. The establishment of the Special Presidential Fund proposed by President Reagan would be a major step toward meeting this objective. Additional steps must be taken, however, including increased flexibility to use the emergency provisions of the Food Security Wheat Reserve Act and Commodity Credit Corporation (CCC) borrowing authority. (See P.L. 480 Action Brief for further elaboration.)

NOTES:
*See footnote on page 101 and assumption #3 on table 7 (page 104).
**In table 5 on page 104, we calculate the nonrecoverable costs of $2.5 billion as the difference between the total cost of the increase in P.L. 480 ($7.4 billion) and the total P.L. 480 repayments ($4.9 billion).

Recommendation

Agricultural export credit programs should be significantly increased to help lessen the development impact of large food deficits and large debt burdens.

Discussion: U.S. agricultural export-financing mechanisms offer the possibility of using U.S. food productivity to help ameliorate the adverse development impact of large debt burdens and large food deficits. These include direct provision of credit, credit

TABLE 4:
Benefits Achieved from an Increase in P.L. 480

Basic assumptions of this table are: (1) Cost of Title I commodities will be repaid over 40 years; (2) One example assumes target prices are frozen at current levels, the other assumes continued escalation; (3) Costs and savings are based on a maximum FY 1984 increase of $1 billion, a total program level of $3 billion in each of the next five years, and the originally planned FY 1985 program level of approximately 6 million tons.

	FY 84	FY 85	FY 86	FY 87	FY 88	FY 89	Total
Total cost of (in $ millions) Increase in P.L. 480	1,000	1,339	1,306	1,272	1,238	1,203	7,358
Savings—Frozen Targets							
P.L. 480 Repayments	665	884	862	840	817	794	4,862
Price Support	218	382	541	866	1,120	982	4,109
Total Savings[a]	833	1,266	1,403	1,706	1,937	1,776	8,971
Net Benefit (Cost)	(117)	(73)	97	434	699	573	1,613
Savings—Escalated Target							
P.L. 480 Repayments	664	884	862	840	817	794	4,862
Price Support	218	382	666	1,305	1,200	1,422	5,193
Total Savings[a]	833	1,266	1,528	2,145	2,017	2,216	10,055
Net Benefit (Cost)	(117)	(73)	222	873	779	1,013	2,697

SOURCE:
USDA, Office of Budget and Program Analysis, January 1984.
NOTE:
a)Net benefit cost is calculated by subtracting total savings from the total cost of increase in P.L. 480.

guarantees, and the combination of the two (blended credit) as a financial package. The Task Force recommends that these programs be increased significantly to accommodate both U.S. market development objectives and the needs of financially constrained developing country importers.

Another innovative program, the CCC intermediate export credit program,* could be a particularly useful tool to help alleviate debt constraints while facilitating both market development for the United States and agricultural development in developing countries. Local currency generated from the import and sale of U.S. agricultural commodities in the importing country are used to establish facilities to improve the handling, marketing, processing, storage, or distribution of imported commodities. Because this program would use the private sector to identify, plan, and implement intermediate credit-financed projects, it would greatly increase the involvement of U.S. and indigenous private enterprise in the development process. This program has substantial long-term potential to expand two-way trade and is an extremely flexible mechanism both in terms of funding and minimal legislative or administrative constraints.

Finding

Present U.S. food assistance programs do not emphasize private enterprise development and U.S. private sector involvement in development assistance.

Overview: Historically, both in the United States and in the developing world, success in agriculture has depended upon the efforts of the individual family farmer. The individual agricultural producer, with his initiative and creativity, represents the most realistic prospect for meeting the challenge of world hunger.

*NOTE:
This program was established in 1980 but has not been used since the establishment of the export credit guarantee program in 1981. The program allows the Secretary of Agriculture to enter into project agreements with U.S. or foreign private entities, or with foreign governments, under which the CCC may finance the sale and export of U.S. agricultural commodities for periods in excess of three, but not more than ten, years.

Recommendation

The U.S. Government should follow the instructions and intent of the law that most counterpart funds generated by P.L. 480 should be channeled through businesses and not through government.

Discussion: Essential as some public sector projects may be to provide necessary infrastructure, the absence of entrepreneurship, management skills, and enterprise-specific capital accumulation critically limit the development process and seriously inhibit the potential of public sector investment. Therefore, a larger proportion of the local currency generated by U.S. food assistance resources should be channeled to companies to stimulate private business, rather than to government for public projects that are not required to meet the infrastructure needs of the private sector.

A major portion of local currencies generated under P.L. 480 should be used for loans to the private sector and to stimulate private sector development by remedying inefficiencies that prevent the full play of market forces and the establishment of prices based on supply and demand factors. The emphasis should be on agricultural and agribusiness development and on facilities to handle U.S. food, feed, and fiber imports. Loans should be made through local financial institutions that have the business expertise to evaluate private sector projects and can meet the needs of small and medium scale businesses, including farmers.

Similar private enterprise stimulation should be provided by increasing the leeway to generate local currencies for these purposes under U.S. food donation programs.

Additional mechanisms, some already authorized and some requiring new authority, must also be used to significantly increase private sector involvement in P.L. 480 assistance efforts and to enhance the program's impact on the development of self-sustaining private enterprise in developing countries. Specific recommendations to reinstitute P.L. 480 agreements with private trade entities, enhance the role of PVOs under P.L. 480, and use P.L. 480 repayments to establish a private sector loan fund are discussed in the P.L. 480 Action Brief. In addition, we strongly recommend expanding foreign currency funding of the USDA Agricultural Cooperator program as a means of attracting greater private sector participation in trade expansion efforts and in the development of expanded indigenous private enterprise capabilities.

A commitment to private sector promotion and enhancement of market-oriented activities often depends on the continued, predictable availability of resources. If we wish to encourage resource commitment and risk-taking by the private sector in developing countries (in this case primarily rural agricultural producers), multiyear commitments of resources under our food assistance programs become even more necessary.

Training
Action Brief

Developing countries lack sufficient private sector skills; the United States should undertake a major initiative to expand training for private enterprise. AID's U.S.-based training program should be doubled to 18,000 participants per year.

Introduction

A major international economic policy objective of the Reagan administration is to help developing countries rely less on their public sector and more on their private sector. The Agency for International Development (AID) and other government agencies can play a major role in implementing this policy by increasing training related to private enterprise development.

Human resources are at the core of any economy. Misdirected or underutilized, such valuable talent can be as much a drain on an economy as it is potentially an asset. The training of future business leaders, entrepreneurs, managers, and the work force will contribute significantly to economic growth.

Most developing country enterprises are hampered by a lack of adequate business and management skills. The means by which these skills can be acquired range from apprenticeship programs that provide on-the-job training to formal courses, including graduate business degrees. All too often, however, there is little or no access to training progams of any type.

Until recently, U.S. foreign assistance programs did not pay much attention to the importance of training for private enterprise. Yet, one of our most important resources is our technical and managerial business know-how and our tremendous capacity for conducting training and education programs, particularly in areas related to private enterprise.

While considerable progress has been made over the past four years, the Task Force believes that to strengthen private enterprise in many developing countries, training for and by private enterprise should be dramatically increased.

Summary of Major Recommendations

The recommended actions have been divided into two sets: (1) those actions AID can immediately undertake within its existing authority, and (2) those actions that may require outside authorization procedures (i.e., legislative action), or other U.S. Government approval by such entities as the Department of State. Keeping this division in mind, we propose that AID undertake the following actions to support private enterprise training in developing countries.

■ Develop and implement a detailed strategy for private enterprise training and improve institutional capacity to monitor, evaluate, and document training programs.

■ Focus on managerial, vocational, and technical training rather than on academic degree training.

■ Emphasize training that supports the development of business skills.

■ Emphasize the needs and potential of private enterprise through training programs for public sector officials.

■ Double AID's Participant Training Program to 18,000 participants with more opportunities for individuals from the private sector.

■ Develop training relationships between private enterprises in the United States and developing countries.

■ Establish in-country selection panels for participant training that include local and U.S. business leaders along with host government and USAID representatives.

■ Continue to support and expand existing in-country educational institutions and training programs.

■ Expand training approaches that integrate the resources and capabilities of U.S. private enterprise into AID's in-country training activities.

■ Increase AID assistance for in-country training programs that support U.S. investment, trade, and capital development projects.

■ Establish a private enterprise training advisory board composed of leaders from the U.S. private sector.

Background

In 1983, about 334,000 individuals from the developing countries studied in academic programs in the United States: 70 percent were privately funded, 25 percent were funded by their home government and other institutions, and only about 2 percent were funded by the U.S. Government. Thousands more were trained by nonacademic public and private organizations.

AID TRAINING PROGRAMS

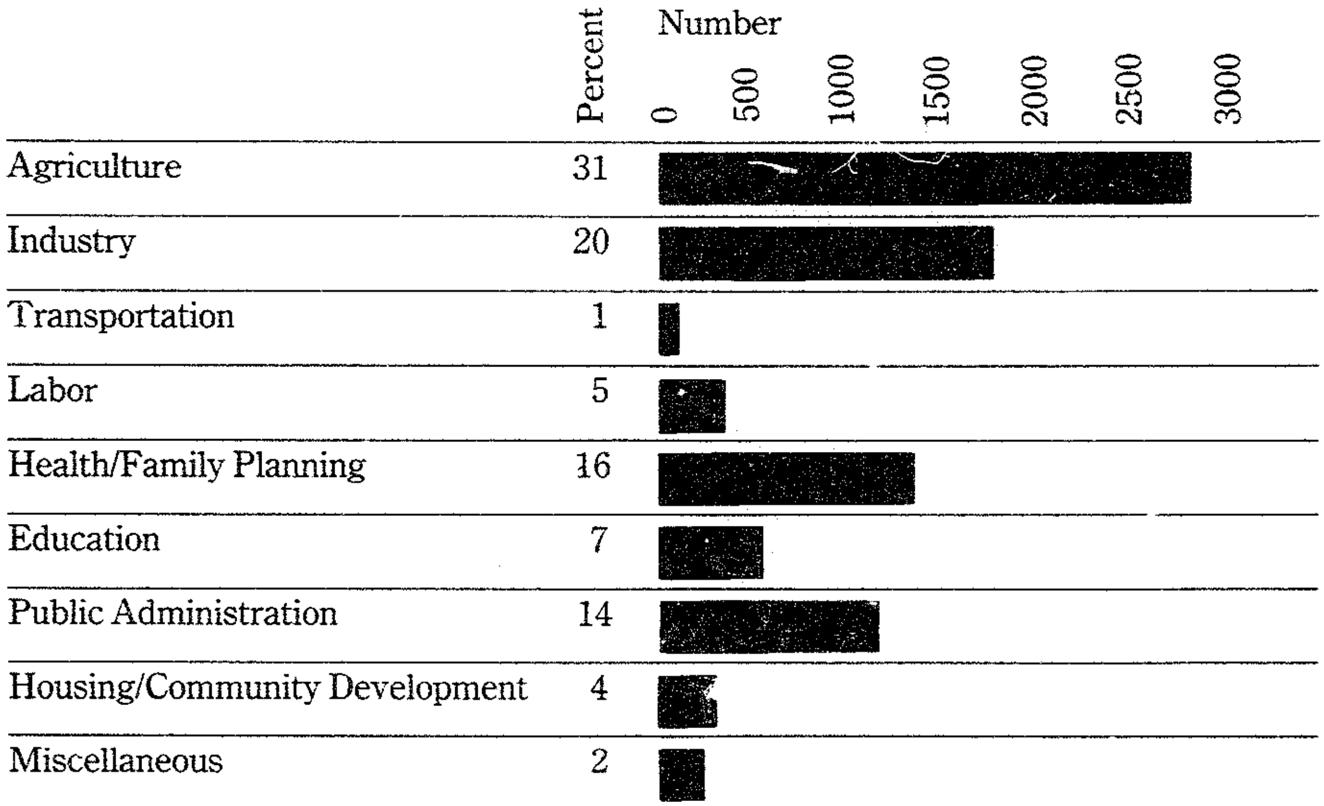
AID is largely responsible for U.S. government-sponsored training of individuals from developing countries. AID policy encourages training for three purposes: (1) developing local staff for AID-assisted projects; (2) strengthening key public and private sector development institutions; (3) developing local training capabilities. AID provides training for individuals from developing countries in order to transfer knowledge and skills, enhance economic cooperation among nations, and to strengthen political ties between recipient countries and the United States. The building of self-reliant and productive societies continues to be a major purpose of U.S. Government training programs.

AID has two broad-based categories of training: participant training, i.e., AID-sponsored training in the United States or in another developing country (third country training), and in-country project-related training. Related programs include the new training activities of AID's Bureau for Private Enterprise (PRE).

NOTE:
■ = no outside authorization needed (in-house changes and/or reallocation of existing funds)
■ = probable outside authority necessary, new funding required

FIGURE A.1:
AID Participant Training Programs by Subject Area for FY 1983

Academic, 4,016
Technical, 4,996
Total, 9,012



SOURCE: Office of International Training, Agency for International Development (1984).

Training begins with Country Development Strategy Statements (CDSS) that are established by each AID mission in conjunction with the host government. Specific projects are identified that meet the country's development priorities. Training needs are then isolated in each project development paper. In the end, almost every development project has a training component, although some projects are designed exclusively for training. The mission determines if training can be done in-country. If not, they look to a third country (for example, a regional facility) or to the United States. In some cases, training for a project may take place in more than one location.

Participant Training

Since the program began 40 years ago, over 240,000 individuals have taken part in AID's participant training program. In FY 1983, over 9,000 AID-sponsored participants received academic or technical training in the United States. This is up from 6,700 participants in 1978, but down from 13,500 participants in 1969. The participant training program costs roughly $150 million annually. AID training programs are decentralized with program and funding decisions made at the bureau or mission level. AID sponsors two general types of participant training: academic and technical.

Academic training is defined as that which takes place in an accredited institution of higher learning and leads to a degree. Of the total participants currently in training, about 45 percent are enrolled in U.S. colleges and universities, with the majority enrolled in graduate degree programs. Many of the programs combine academic study with practical training.

Technical training, which accounts for about 55 percent of all participant training, includes observational visits, on-the-job training, special programs and seminars and, in some cases, training in an academic institution not leading to a degree. Most technical training programs are of less than three months duration.

In spite of a trend toward more technical training, project design determines the appropriate ratio of academic to technical training. Although actual cost estimates vary widely, depending on the length and nature of a program, for planning purposes AID uses estimates of $3,100 per month for technical training and $1,700 per month for academic training. Table A.1 shows the composition of AID's participant training program by subject area.

Private enterprise training, as it is now defined by AID, falls under the "miscellaneous" category and primarily includes training for banking and finance, investment promotion, trade development, and general management. Other categories, such as industry, agriculture, labor, and housing/community development, do contain elements of private enterprise training. AID does not have specific information on the percentage of participants trained in private enterprise-related activities in the United States.

Participants selected for training in the United States are usually educated and at the mid-career level. Most come from the public sector in developing countries and generally return to predetermined public sector jobs. Agreements with AID require participants to return to their home country and to a specific job for a stipulated time. Less than 1 percent of AID-sponsored participants fail to return home.

Due to staff and budget reductions, AID increasingly contracts with private and public institutions for participant training programs, with the Office of International Training (S&T/IT) serving as the overseer and coordinator of training management services. S&T/IT directly manages about 35 percent of all participants. Several federal agencies (The Departments of Agriculture, Labor, Transportation, and Commerce) and about 100 private sector contractors are used to program and manage the participants who come to the United States. These contractors include universities, private training firms, industry, labor, and other organizations. Examples include Partners for International Education and Training (Partners), and the International Marketing Institute (IMI).

Partners, a consortium of international education and exchange organizations, was established in 1982 to manage programs for approximately 2,000 AID-sponsored participants each year. While most placements are in U.S. academic institutions, Partners has found many short-term placements for developing country participants in U.S. businesses. About 20 percent of the participants have direct contact with U.S. industry. A recent program, for example, placed 39 Caribbean participants with a muffler manufacturer, furniture companies, food processors, and other private companies.

A recent program sponsored by AID's Office of Women in Development (WID) brought 33 businesswomen from developing countries to the United States. They spent three weeks in a small enterprise development program conducted by IMI in Boston. An optional observation study tour followed the official program. Visits to many U.S. firms, small and large, were included.

AID uses private enterprise to do specialized technical training as part of the participant training program. Most of the AID training is purchased, but it is occasionally donated or given at a reduced rate by private industry. Generally, these programs, frequently offered as unsolicited proposals by training elements of large corporations, tend to be expensive. Unless off-the-shelf, they are costly in terms of the staff time required by AID and its contractors to design and manage individually tailored programs. Complete data and statistics on AID training provided by U.S. private enterprise are not available.

AID also operates a reimbursable

training program in which all participants are sponsored by their governments, with most placement in U.S. colleges and universities. Outside organizations, under contract to AID, organize and conduct the training. The program is self-sustaining, with all program costs covered by fees from the sponsoring countries. (Reimbursable agreements have generated about $75 million since the program began.)

In-Country Training

Training in recipient countries is limited primarily to on-the-job training of local nationals working under AID development projects—usually in the functional areas of agriculture and nutrition, population and health, and education and human resources. Training ranges from academic degree programs to technical seminars to short on-the-job instruction.

Training in local educational institutions is an AID priority. When possible, AID prefers to upgrade the local institution rather than send the student overseas. However, if the local institution cannot meet project requirements, participants are sent to the United States or a third country.

In-country training generally costs much less than U.S. or third country training, particularly for people at lower skill levels and for those who do not speak English.

Participation levels cannot be accurately estimated, but the numbers vastly surpass those of the participant training program because the majority of AID projects include a training component. Isolating private enterprise training is difficult because the definition of private enterprise used by AID and others is not clear or consistent. For example, it has not been determined whether business skill training for an employee of a state-owned enterprise should be defined as private enterprise training or not. Another reason why there is so little identifiable private enterprise training is that there are so few recognizable AID private sector projects.

In varying degrees, all the AID regional bureaus are involved in private enterprise training projects. The Bureau for Latin America and the Caribbean (LAC) has a number of innovative projects associated with the Caribbean Basin Initiative. For example, the Barbados Institute of Management and Training is receiving AID support to assist the private sector in training and upgrading management and technical skills that are critical for business expansion, new investment, and employment opportunities. In Honduras, the National Training Institute is providing improved skill training for middle managers, i.e., mechanics, carpenters, electricians, and machine operators. An AID grant is helping to establish a graduate training program in business administration at Catholic University in the Dominican Republic. A new institute for executive training and a management research center will also be established.

Bureau for Private Enterprise Training

AID's Bureau for Private Enterprise (PRE) recently began to provide training grants for projects it finances. PRE has also financed innovative programs for technical and management skill development through institution-building and the employment of U.S. firms and business associations, but on a limited experimental scale. A $1 million grant, for example, will help Bangkok's new Institute for Management Education train working business managers using courses based on U.S. models. The Young President's Organization, under PRE sponsorship, is conducting seminars designed to share U.S. business experience with local entrepreneurs.

U.S. PRIVATE ENTERPRISE TRAINING

Universities, other educational institutions, and private training firms account for most of AID's training in the United States and overseas. However, U.S. business and private voluntary organizations (PVOs) have supported AID training programs and have conducted training programs of their own for many years.

U.S. private enterprise contributes to training through educational assistance programs, donations to existing institutions, and investment and trade-related activities.

Many U.S. multinational corporations provide training in conjunction with their overseas operations. Within the scope of company operations, they have established a reputation for the efficient transfer of knowledge to developing country employees, suppliers, and customers. Clearly some of the best long-term training has resulted from direct foreign investment in developing countries. Other sources of training include licensing arrangements, technical assistance agreements, management contracts, engineering and consulting contracts, and training associated with the purchase of equipment and supplies.

U.S. private enterprise sponsors many private sector training activities for developing country participants in the United States and abroad. They include the following.

☐ Several East Coast transportation companies arranged and paid for an observational training program for five urban planners to study mass transit. AID funded only the per diem and the international travel.

☐ A recent AID Latin American Bureau project brought a group of Caribbean business leaders to the United States for on-site training with various U.S. private firms, who provided many in-kind contributions. Nearly 42 percent of the program costs of the project were covered by the private sector. The unplanned "spin-off" results of the project have not been fully realized, but to date they include several U.S.-LDC joint ventures, $250,000 in American equipment purchases, and a contract to manufacture a U.S. firm's product under license.

☐ The U.S. Telecommunications Training Institute, a consortium of major firms, such as AT&T, IBM, GTE, and many others, trains individuals in the application of telecommunications technology. The institute, in conjunction with the Academy for Educational Development in Washington, D.C., trained over 200 people from 65 developing countries in 1983, its first year of operation. Training and administrative costs are donated by the participating firms. Most of the training took place in corporate facilities. International development institutions (including AID) funded 70 percent of the costs of transportation and sustenance. The program is designed to introduce developing country participants to the products, services, and technologies of the U.S. telecommunications industry. The participating firms regard the program as a long-term investment that should lead to commercial benefits. Funding for the program comes out of the marketing rather than the training budgets of many of the firms. Participating firms have benefited from technical assistance relationships, new business contacts, and a better understanding of the developing country markets.

☐ The International Cooperative Education Program of Northeastern University in Boston, Massachusetts recognizes a frequent shortcoming in international training: the reluctance of developing country participants (non-AID sponsored) to return home after completing an academic program in the United States. Northeastern offers a unique solution: home country work assignments. Engineering and business students serve a designated period working for a U.S. multinational in their home country midway during their degree program. The firm benefits from having a trainee on-site with local knowledge, an effective means to screen candidates for permanent employment at an early stage, and a good source of long-term business contacts. The developing country gains a qualified engineer or business manager after completion of the formal education program.

☐ For 35 years, Bechtel Corporation has incorporated specialized construction, engineering design, and decision analysis training programs for local personnel into its normal project operations in developing countries. This on-the-job training, which integrates the trainees into the Bechtel engineering team, eventually transfers leadership of the project to the client, leaving Bechtel as an adviser.

PVOs are also involved in a wide variety of training activities in the less developed countries (LDCs). PVOs are an increasingly important source of training and technology for local firms. They also have assisted U.S. firms with meeting training needs in developing countries. Examples include the following.

☐ The International Executive Services Corps (IESC), utilizes the services of retired U.S. executives to assist host country private enterprise and some government agencies with increasing productivity through management training and technology transfer; and improve the image of U.S. business abroad. Through over 9,000 assistance projects they have provided a variety of training and technical assistance programs that have resulted in increased employment, increased investments, and in about 1,500 cases, enduring relationships with U.S. firms.

☐ The Industry Council for Development offers industrial expertise to governments and enterprises to assist in development projects and programs. Long-term development through practical cooperation between governments, aid organizations, and industry is their prime objective. Advisory services are drawn from the council's primary resource—the expertise of U.S. commercial enterprises.

☐ The Center for International Private Enterprise (CIPE), a nonprofit affiliate of the U.S. Chamber of Commerce, is developing training programs for executives from trade associations and voluntary business groups. Training is designed to strengthen business institutions, improve management skills, and share techniques for increasing business participation in the public policy process. The first program, conducted in the summer of 1984, brought 28 executives from the developing countries to the United States for training at the chamber's Institute for Organization Management.

TRAINING BY OTHER U.S. GOVERNMENT AGENCIES

In addition to AID, U.S. Government agencies with major programs that bring LDC participants to the United States are the Department of Defense (DOD) and the U.S. Information Agency (USIA). DOD provides military training for about 11,000 individuals from developing countries every year. USIA conducts programs and offers scholarships of a general nature for a large number of LDC participants. USIA's International Visitor Program brings about 3,500 individuals to the United States every year for short-term study tours. Another USIA program, the Hubert H. Humphrey North-South Fellowship Program, sponsors about 95 professionals from 56 developing countries at U.S. universities.

The Departments of Education, Energy, and Health and Human Services have sizable training programs, but they are designed around professional needs rather than geographic considerations. The Department of Agriculture has a major training program, but most participants from developing countries are sponsored by AID.

The Peace Corps conducts many training activities in conjunction with their in-country development programs. The Overseas Private Investment Corporation (OPIC) also finances some training associated with its investment and insurance projects. Many other agencies sponsor training programs in areas specially related to their expertise, but programs tend to be on a small scale with only a few LDC participants

The impact of U.S. Government training can be profound. As of 1983, 44 current heads of state and 495 cabinet level ministers around the world had participated in educational and cultural exchange programs sponsored by USIA's International Visitor Program. Many former AID participants are now in high-level policymaking positions in their home countries. Thousands of other foreigners who studied at U.S. military academies have gone on to positions of military and civilan leadership.

TRAINING BY OTHER DONOR COUNTRIES

In 1982, the United States ranked fourth in the number of participants trained on publicly financed fellowships by member countries of the Organization of Economic Cooperation and Development (OECD). The Federal Republic of Germany led with 22,000 followed by the United Kingdom with 12,400, Japan with 11,000, and the United states with 8,800.

Direct comparisons are misleading because U.S. figures apply only to AID, not to other U.S. Government agencies. For instance, the Japan International Cooperation Agency, Japan's equivalent of AID, trains only 4,500 participants—under half of those reported in the OECD figures.

In addition, some OECD countries concentrate on short programs and observation tours, others offer partial scholarships, and some include training outside their borders. The German fellowship program, for example, includes some in-country training.

Program content of other OECD training programs is similar to that of the United States. Emphasis is on training to support traditional development activities. Elements of the Japanese and British training programs place special attention on developing long-term commercial relationships.

The USSR's economic development programs have been accompanied by a comprehensive training effort. During 1983, more than 50,000 LDC students attended Soviet schools. Most of these students were on full scholarships that covered subsistence, living quarters, tuition, and transportation. This training is estimated to cost the USSR the equivalent of $250-$300 million annually. Moscow has viewed its academic program as a low-cost, potentially high-yield effort. Half of all Soviet scholarships have gone to 50 countries in Africa. According to the USIA, the Soviet bloc has increased total exchanges in Central America sevenfold over the past five years. They offer scholarships to 14 students for each one who is invited to study in the United States.

Recommendations

TRAINING FOR PRIVATE ENTERPRISE DEVELOPMENT

AID needs to develop and implement a detailed strategy for private enterprise training and improve its capacity to monitor, evaluate, and document its training programs.

Discussion: Neither AID nor other U.S. Government training entities have a comprehensive strategy for training that incorporates private enterprise development needs and offers a means of facilitating trade and investment between the United States and developing countries.

Principally through PRE, AID has made significant inroads in the area of training as it relates to private enterprise development. However, AID has not raised private enterprise training to a level of priority consistent with the dependency of private enterprise on a trained labor force.

A training strategy should take into consideration the changing needs of developing countries, potential U.S. private sector assistance, and the activities and plans of other U.S. Government agencies and departments. This strategy should include Country Training Plans at the mission level, which would require private enterprise training to be included. Standardized procedures for identifying training projects and for reporting results should be developed.

The lack of readily available data on the extent of training for private enterprise and information on the origin and post-training location of trainees limits AID's ability to develop strong, effective training programs in harmony with the agency's mandate. Training successes and failures are not easy to identify. AID needs to develop management systems that enable the missions and AID/Washington to plan, develop, and implement training programs more effectively. This will permit the monitoring and evaluation of training programs long after they are complete.

AID should produce an annual report that fully documents its training programs and plans. A standard definition for training that encompasses all types of training related to private enterprise—including training in AID's more traditional disciplines—should be adopted in the report.

A larger share of AID's training resources should be devoted to programs that focus on managerial, vocational, and technical training rather than on academic degree training.

Discussion: Acquiring skills that meet local job demands and development needs is of paramount importance. A wide variety of private enterprise training programs need broad support. Highly sophisticated academic training may be appropriate in some cases, but lower level, practical, hands-on training is badly needed. This includes managerial, vocational, and technical skill training. Special emphasis needs to be placed on small and rural enterprises, the source of most economic activity in developing countries.

Training associated with many traditional AID projects could be enhanced by more emphasis on private sector solutions to development problems. Projects with a training component should expose participants to private enterprise approaches to management and development.

AID should place special emphasis on training that supports the development of business skills.

Discussion: An entrepreneurial spirit exists in many developing countries. However, those with the will to start or expand a business frequently lack the necessary management and business skills to do so. AID should continue to support and develop programs that impart business and organizational knowledge to accompany that driving spirit. Training cannot create entrepreneurs, but it can help existing entrepreneurs improve their chances of success by providing start-up information and teaching beginning-level management skills.

In particular, developing country businesses need a better understanding of domestic and international marketing requirements. Many business people understand how to make a product or provide a service in a developing country, but a lack of marketing skills prevents them from expanding their businesses to their full potential. Economic success for many developing countries will depend on the ability of local businesses to export products and services to their regional neighbors and the industrialized countries. The Reagan administration's Caribbean Basin Initiative, for instance, offers handsome export incentives to countries of the region, but only those companies with knowledge of U.S. market requirements will be able to benefit. Marketing education also offers a secondary trade benefit to U.S. businesses; local firms learn how to purchase raw materials, components, capital equipment, and finished goods.

U.S. business leaders along with host government and USAID representatives.

Discussion: Individuals for U.S. participant training programs are presently selected by host government and AID officials or AID contractors. The new emphasis on private enterprise development suggests that representatives from the private sector should be included in the selection process. Selection panels could review applications from the local private sector and help foster a closer working relationship between AID and the local business community. These groups could also help assess private sector training needs and identify and develop in-country institutions to provide appropriate training. Indigenous companies that share the cost of training should obviously have a voice in who is selected.

AID should consider new ways to utilize the reimbursable training program to support developing country private enterprise.

Discussion: AID's reimbursable training program offers a means of expanding AID training programs on a virtually cost-free basis. A modest increase for promotional activities could spark interest from many more countries than now participate. Private enterprises in developing countries, including U.S. companies, could be encouraged to send their local employees to work and study in the United States under a modified reimbursement program. Middle-income developing countries represent a potentially sizeable market for this service, but other traditional AID recipient countries should also be considered.

IN-COUNTRY TRAINING

AID should continue to support and expand existing in-country educational institutions and training programs.

Discussion: Many local educational institutions have failed to provide practical programs to meet local market requirements and immediate student and business needs. New educational and training programs need to be established that meet private enterprise needs. Once programs are established, AID should encourage these institutions to develop outreach mechanisms to the local business community. Local business must perceive training and manpower development as a valuable resource for growth and profitability. The benefits of investing in training are an essential component of business development, not a low priority expense to be ignored.

Local educational institutions also need to develop follow-up mechanisms that enable the participants to have continued access to new information. This should include seminars and workshops, continuing education, in-service training, and access to training materials and outside experts. Business groups and trade associations could serve as a bridge between the institutions and private enterprise.

Training approaches that integrate the resources and capabilities of U.S. private enterprise into AID's in-country training activities should be expanded.

Discussion: AID should facilitate the placement of U.S. business executives and corporate technical experts in local training projects and encourage multinationals to offer their training services and facilities free of charge or on a marginal cost basis to nonemployees. In particular, the training of customers, suppliers, and personnel from other support enterprises offers obvious benefits to multinational corporations. Companies like Sears International and The Singer Company have been doing this successfully for years. AID can help facilitate the identification of host country needs and assist with the implementation of training programs utilizing private sector resources.

AID assistance for in-country training programs that support U.S. investment, trade, and capital develop-

when facing the need for quick action to meet a competitive offer. Guidelines for the program need to be established so that exporters and bankers have a clear understanding of when, and under what circumstances, Eximbank funds can be drawn upon.

Although they need further definition and refinement, the following criteria provide an initial framework.

☐ Eximbank should offer financing to U.S. exporters that will enable the exporters to compete on equivalent terms with exporters from other countries who benefit from commercially oriented concessional credit (mixed credits). In some cases, Eximbank may provide identical financing packages; in other cases it might include some other combination of down payment, rate, term, and grace period concessions that would be equal, but not superior, to the competing financing.

☐ Eximbank should aggressively counter competing offers. For instance, in qualified cases in which Eximbank believes there will be mixed credit competition, it should use the prior notification procedures under the OECD Arrangement to query the country in question about its intent. If the country involved uses mixed credits extensively and does not provide a clear negative response to the query, Eximbank should be directed to operate on the assumption that a mixed credit package will be offered and it should provide appropriate financing to the U.S. exporter. In other cases, Eximbank may have to make judgments about the intent behind competing offers—whether the principal motivation is commercial or developmental.

☐ All operations undertaken should be consistent with U.S. responsibilities under the OECD Arrangement, which permits matching of competing offers, and with other U.S. international commitments.

☐ Eximbank should pay particular attention to those products of competing countries that have benefited most from mixed credits, such as telecommunications, power, and transport equipment firms. However, it should not exclude any products in which U.S. exporters can be price-competitive.

☐ Eximbank should not exclude products that are in world oversupply, such as copper or steel processing equipment, because to do so would be tantamount to announcing that the United States is leaving the field to others. However, it is current U.S. policy not to finance such exports. We do not quarrel with the policy. Our clear preference would be to avoid these areas, but given the needs of the program, flexibility may be required.

Summary

The Eximbank program can be implemented now. It is needed to make U.S. exports competitive with the subsidized commercial exports of our competitors. It will improve the U.S. negotiating position by trying to eliminate commercial export subsidies. It will serve U.S. exporters and the national interest. The President should direct the Export-Import Bank to undertake such a program immediately and continue it until our competitors stop using these predatory and expensive practices.

ment projects should be expanded.

Discussion: While low labor costs and other incentives are attractive, one of the reasons many U.S. firms shy away from investments or major projects is because the cost of bringing the labor pool up to required skill levels is prohibitive. AID support for U.S. small businesses that want to invest or export products requiring technical skill training is particularly encouraged. For example, if a small U.S. firm wants to export equipment to a developing country that will help development, such as a solar-powered windmill or water pump, AID could share in the cost of training local workers to operate and maintain the equipment.

This is particularly relevant for U.S. construction and engineering firms competing for major overseas contracts in developing countries who are often expected to finance training costs associated with the project. This is principally because many other donor nations support training costs through aid programs or other government-financed programs. AID should provide grants on a selective basis to projects that contribute to development and where U.S. firms risk losing the contract because of their inability to offer a competitive financing package. Training benefits can accrue long after the project is completed.

ORGANIZING AID FOR TRAINING

AID senior management should examine whether the agency is now adequately organized to manage a major initiative in private enterprise training.

Discussion: Our recommendations call for a substantial increase in, and a redirection of, training for private enterprise. This will require different approaches, resources, and possible modification of AID's organizational structure to effectively respond to the new training mandate. It is essential that AID senior management review AID capabilities to decide if existing mechanisms can be readily adopted and, if not, what new aproaches should be proposed.

A Private Enterprise Training Advisory Board in AID, composed of leaders from the U.S. private sector, should be established.

Discussion: AID has not had extensive experience working with private enterprise on training activities. An advisory board would provide AID with the valuable insight it needs from the U.S. private sector. Experts would assist AID in determining how to involve U.S. private enterprise in training LDC participants in the United States and overseas. The board would also help AID develop, apply, and evaluate a consistent set of training principles and objectives.

APPENDIX B

Mixed Credits

Mixed Credits Action Brief

The United States must strengthen its position in negotiations to end unfair trade finance competition. The Export-Import Bank should operate up to its $4 billion lending authority and $10 billion guarantee authority to counter predatory trade practices and provide equivalent support to U.S. exporters.

Introduction

Exports are increasingly important to the United States economy. One tenth of our national income stems from trade; 20 percent of our work force depends on trade for its livelihood. Forty percent of our agricultural production is sold abroad; one third of our corporate profits are generated by international operations.

Every major trading country except the United States has undertaken serious efforts to achieve international competitive dominance in one or more industrial export sectors. These efforts are also evident in the agricultural sector, an increasingly important segment of U.S. trade. U.S. markets at home and abroad have been major casualties. Costs to U.S. industry have been severe in terms of employment and profits. Industries in which the United States was totally dominant only a few years ago are increasingly threatened by carefully targeted, subsidized foreign competition. These industries include commercial aircraft and other transportation equipment, machine tools, computer chips, electric and nuclear power, and a growing list of high technology industries.

Various countries have targeted different industries in which to become competitive. Common to them all, however, is a governmental effort that is both well-funded and well-coordinated. Their efforts are based on three important realizations: (1) that new international markets are becoming increasingly scarce; (2) that some form of price break or other financial inducement may tip the balance toward a particular seller for Third World buyers; and (3) that the key to future sales is market penetration today—a toehold in a new market today may be parlayed into a captive market tomorrow.

Each of the governments that has joined this competition has developed and is actively implementing aggressive commercial strategies to insure its success: specific domestic industries such as steel, telecommunications, and energy have been targeted for the export push; direct subsidies have been applied to research and development activities; and preferential financing subsidies have been undertaken to spur the private sector to concentrate its effort on penetrating, pre-empting, and capturing new markets. In many cases, initial successes in winning bids provide suppliers with substantial advantages in future competition for expansion or new projects in the same sector because the exports targeted for support are large capital projects. Increasingly, the victims of these predatory, trade-distorting practices have been U.S. suppliers who have been unable to match the officially supported financial terms offered by foreign competitors.

We now stand at a crossroads in trade and finance policy. The concessional export financing practices of other governments for commercial advantage continue to increase, despite more than a decade of multilateral negotiations to bring the growing export credit struggle to a halt.

The international competitiveness of U.S. industries with true comparative advantage—industries in the energy and high technology areas, for example—is declining, in large measure because the United States has refrained from meeting and neutralizing the aggressive promotional practices of other countries. Without the ability to sell abroad, remain on the cutting edge of vital technologies, and maintain economic prosperity at home, U.S. industry will continue to falter, thereby imperiling not only our growth, employment levels, and profits, but our national security as well. In the final analysis, a sound and thriving economy will have as much to do with our world position as will the state of the arms balance.

The most damaging subsidy scheme in recent years, from the perspective of its harm to U.S. producers and exporters, has proven to be "mixed credits." Initially, mixed credits were defined as a blend of concessional government resources with public and/or private commercial credits that had the effect of reducing the real cost of an export to the buyer—often to a point where the price was below the cost of production. Recently, the term has been generally expanded to encompass official export financing subsidies for commercial purposes rather than development purposes, whether by a single source or combination of sources. These government subsidies for commercial gain are costly. They distort trade patterns and reduce competition.

The United States can and must adopt a program that enables U.S. exporters to finance the sale of U.S. goods and services on terms that are competitive with the subsidized terms offered by the governments of our aggressive trade competitors. This assistance should be carefully targeted against predatory official efforts to capture existing U.S. markets and to pre-empt and lock up new markets. The assistance should be focused on sectors of the U.S. economy in which American industry is clearly competitive with nonsubsidized foreign competition.

To meet the mixed credits challenge, the U.S. must: increase its efforts to negotiate an end to these widespread trade finance subsidies for commercial advantage; and, in support of this negotiating position, provide funding and formulate clear policy guidelines to counter and neutralize the predatory official activities of competitors.

The basis of a program to meet this unfair competition is laid out on the following pages. The program can be undertaken immediately without need for additional funding or increased authority and can be built on existing institutional arrangements. It should be continued as long as necessary to convince U.S. competitors that reliance on market forces, without the use of government subsidy, is a better way to increase trade and achieve worldwide growth and prosperity.

Background

DEFINITION AND CONTEXT

Official export promotion efforts consist of a wide array of governmental programs in financing, insurance, guarantees, taxation, commercial reporting, and market development. All exporting countries, including the United States, provide various forms of export promotion to expand markets and increase sales. They also provide concessional export financing for developing countries that require imports to meet critical development needs. In recent years, however, the distinction between acceptable export promotion practices and development assistance efforts has been blurred, particularly in the use of mixed credits.

Current international conventions provide for commonly accepted and agreed upon financial practices and terms for official export financing. They also provide methods for defining concessionality as applied to interest rates and terms. Unfortunately, however, they only narrowly define the range of unacceptable financing techniques used by countries to subsidize exports for commercial purposes. A wide range of commercially oriented subsidized financing activities escapes official notice because of this narrow approach.

Various types of mixed credits have come under some international scrutiny, but, as with other extraordinary export support measures, not enough effort has been expended to carefully define, monitor, and regulate their use. Consequently, there is some confusion in official and business circles concerning both the nature and extent of the mixed credits practice.

Mixed credits, taken broadly, include all of the following types of credit practices.

(1) *Cofinancing:* a mix of public capital (sourced from different public entities) or public and private capital in a single export transaction.

(2) *Joint financing:* a cofinancing arrangement for which there is a common list of goods and services and where financing of all or certain items are shared between colenders in agreed proportions.

(3) *Parallel financing:* a cofinancing arrangement in which each colender finances different goods and services or distinct parts of a project.

(4) *Associated financing* (as defined by the Development Assistance Committee of the Organization for Economic Cooperation and Development): transactions that associate, in law or in fact, some combination of Official Development Assistance (ODA), other official finance with a grant element of at least 20 percent, and official private export credits or other official flows at or near market terms.

(5) *Tied aid credits:* a credit that is provided for development aid purposes and is financed either exclusively from public funds or partly from public and partly from private funds.

Most official international mixed credits attention is focused on combinations of financing rather than a single export credit. In any event, whatever term is used, the use of these or any other concessional export financing techniques, principally for commercial rather than for development purposes, distorts international trade and is detrimental to the development process and the world's trading system. Other countries are using a wide variety of these techniques.

Countries offer numerous reasons for

using mixed credits: to help their trade balance; to support the growth and development of specific domestic industries; to relieve domestic unemployment; to improve efficiency in specific industries through increased economies of scale; to increase the availability of cheap credit for the developing world; to leverage greater financial flows to the developing countries without undue restrictions on their use; and to provide aid at concessional rates to advanced developing countries (ADCs), like Colombia and Brazil.

Whatever the reasons, available evidence shows that an increased use of mixed credits tends to shift scarce ODA funds from the poorest countries to higher income developing countries. Further, mixed credit financing can divert ODA from the recipient country's highest priority development projects because mixed credits frequently go to sophisticated, capital-intensive projects that may not be at the top of the recipient country's development agenda.

Where legitimate development needs are served, use of concessional mixed credits may be appropriate. However, the record indicates that the domestic economic considerations of donors are usually the controlling factors in these decisions. The direct costs to the donor countries—and to the world's trading system—are great. For these reasons, the United States must continue to press for the elimination of all forms of government export subsidies for commercial purposes.

THE ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT ARRANGEMENT ON MIXED CREDITS

In February 1978, the United States and 21 other OECD countries reached agreement on principles to govern the use of export credits, including tied aid credits. Under that agreement—the OECD Guidelines for Officially Supported Export Credits (Arrangement)—the 22 signators agreed to apply common credit terms to various classes of importing countries. The Arrangement is a "gentleman's agreement" that is applicable to officially supported export credits with repayment terms of two years or more.

The principal purpose of the Arrangement is the reduction and eventual elimination of trade-distorting export credit subsidies as well as the promotion of international trade on the basis of price competition and quality considerations.

Tied aid credits usage is permitted by the Arrangement in accordance with specific guidelines. Moreover, the participants have agreed to terms for reporting derogations and for matching the nonconforming credits of both derogating participants and nonparticipants.

The guidelines include:

☐ considering credits with a grant element above 25 percent as Official Development Assistance (ODA) rather than as commercially oriented trade credits;

☐ notifying other participants promptly after commitment when a tied aid credit with a grant element above 25 percent has been offered;

☐ refraining from offering tied aid credits with a grant element of less than 20 percent; and

☐ notifying other participants 10 days before commitment, when planning to offer a tied aid credit with a grant element of at least 20 percent, but less than 25 percent.

Once notification of such an offer is given, other participants have the right to match, identically or through other means, the terms of the credit. If matching results in new derogations, further time extension for discussion and action by participants also apply.

The Arrangement definition of mixed credits is far too narrow and the Arrangement reporting guidelines are far too incomplete to capture the true nature and extent of the mixed credits problem. Many types of mixed credit transactions escape proper reporting and scrutiny. Thus, parallel financing undertakings between a government entity and a private capital source, in which a package of exports are disaggregated and financed separately by each colender, would escape the Arrangement's reach and probably go unreported. This technique is commonly practiced by various countries. Moreover, many of the reports do not include enough information to be of use, either for matching by other participants or for gauging the extent of the problem. The United States has been trying to tighten up the agreement by increasing the grant element subject to prior notification, by increasing the size of the grant element necessary to be considered ODA, improving the amount and quality of reporting, and various other means. Some progress has been made, but many subsidy practices are not covered by the Arrangement and the incidence of mixed credit offers and financing continues to increase.

EXTENT OF THE PROBLEM

Hard data are not available covering the broad spectrum of activities we consider concessional mixed credits. Some countries, such as Sweden, use mixed credits as an integral part of their aid program. Some tied credits are offered in such a way that the subsidy is not directly linked to the commercial credit, others are not reported for various reasons. Countries are extremely clever in finding ways to meet the letter of international obligations while continuing to engage, for practical purposes, in what they have agreed not to do. In 1983, less than 20 percent of offers reported by Arrangement participants were in the agreed guideline range of a 20-25 percent grant element, 30 percent of the offers were in the 25-30 percent grant element range, 20 percent had a grant element "greater than 25 percent," and most of the remainder had a grant element in excess of 30 percent. This high concentration just outside the agreed upon range is a clear indication that some countries are using the definition of ODA as a disguise for commercially oriented trade practices. These unfair trade practices are hurting U.S. exporters.

Data assembled by the Export-Import Bank show that the number of mixed credits agreements offered by industrialized countries has continued to rise rapidly since 1980. The number of offering countries has also risen. Mexico, South Korea, and other Advanced Developing Countries, in addition to the traditional donor community, have begun to offer mixed credit financing. The dollar value of mixed credits offered rose significantly until 1980, remained constant at just over $2 billion annually through 1982, and increased to $3.5 billion in 1983. Mixed credit use continued at that pace into 1984.

Because of definitional limitations, these figures probably understate the incidence of mixed credits. Additionally, however, many experts believe that countries underreport either deliberately or through administrative carelessness. It is highly probable that the amount reported would increase significantly if our broader definition of mixed credits were used. Of importance, too, is the fact that mixed credits are often concentrated in certain heavily subsidized industrial sectors. Thus, the trade-distorting effects of the credits may be far greater than published data indicate. While OECD reports are not complete on this point, the data suggest this may be particularly true in the power and transportation sectors.

France has offered over 50 percent by value of all reported mixed credits. The adoption of "defensive" mixed credit programs by Canada, Japan, Germany, and others has not led France to reduce its activity. While France has cut the size (in dollars) of its mixed credit offers since 1980, the number of offers in 1983 was almost triple the 1980 level.

Most of the countries that are the principal recipients of mixed credit offers are actual or potential Eximbank customers. Six of these countries stand out in terms of dollar volume: Mexico, Brazil, Egypt, Morocco, Indonesia, and India. All except Morocco are significant U.S. export markets.

U.S. Response to Date

[redacted]

NEGOTIATING POSITION

The U.S. Treasury Department considers trade-motivated subsidized export financing wasteful, costly, and ultimately futile because it causes a budgetary drain on exporting countries, with no real trade or development advantage to show for it. U.S. Government policy is that exported goods and services should be sold on the basis of price, quality, and other intrinsic merit. To do otherwise is to neglect the marketplace and distort international trade patterns.

Consistent with this position, the United States has attempted to negotiate an end to the use of those mixed credits used primarily for export promotion. In December 1983, for the first time, mixed credits were the highest priority item on the agenda in negotiations on the OECD Arrangement on Export Credits. The United States made a number of proposals, as it has over the years, designed to expand the definiton of mixed credits, to make their use more evident and to further restrict their use. The United States has taken positions consistent with this in other international negotiations as well. Progress has been limited and prospects for an early or even medium-term breakthrough do not appear to be good.

At the OECD Ministerial meeting in May 1984, the United States attempted to secure agreement to prohibit grant elements below 50 percent, a hefty increase above the current limit of 25 percent. This would have made mixed credits for commercial purposes much more expensive for the offering government. However, the United States received virtually no support for this position from the other members.

There are reports that the United States was preparing a new series of proposals to present to the export credit group of the OECD at a September 1984 meeting that was postponed. Reportedly, the proposals could limit the provision of mixed credits only to countries with lower income levels, apply the proposed 50 percent grant element only to selected high technology industries and perhaps others. We support this U.S. position and believe the United States should continue to press for adoption of these and other proposals that will reduce or eliminate these unfair practices. However, we are not optimistic about the chances for successful negotiations on these points; furthermore, we are not convinced that, even if successful, a new Agreement will stop the practice. The high incidence of offers outside the limits of the agreement in recent years is discouraging to us. The United States needs to underscore its negotiating strategy with an aggressive mixed credits program that will demonstrate the futility of continuing these predatory trade tactics.

PAST ACTIVITIES OF THE EXPORT-IMPORT BANK AND AID

Before 1981, Eximbank selectively matched the interest rate subsidy on mixed credits offered by others, winning some deals for U.S. business. However, the U.S. Government did not find this approach to be effective in developing negotiating leverage and the practice ceased. In October 1982, the Eximbank introduced a medium-term credit program to provide fixed rate support for those medium-term export sales up to $5 million that are facing subsidized, officially supported export credit competition from abroad. With evidence of the competition, Eximbank can provide fixed rate financing to the U.S. bank financing the export sale. Eximbank has, in some cases, offered to extend grace periods and repayment terms as a way to counter interest rate subsidies offered by competitors. This is considered to be an effective negotiating tactic because of the superiority of U.S. capital markets as a source of long-term capital. However, Eximbank has not aggressively sought out opportunities to counter subsidized credits.

In 1982, AID adopted a policy on mixed credits that delineated their use for export financing. The policy recognizes that other donors actively use mixed credits. AID agreed to consider financing mixed credits using ESF funds, but only to counter specific offers and only in specific cases in which the project has a high priority in the recipient country's development. AID also adopted a program to meet mixed credit competition in Egypt, specifically allocating funds for that purpose. However, restrictions placed on the use of funds, including the requirement for evidence of concessional competing offers, are very tight.

Shortly before the OECD Ministerial meeting in May 1984 the Export-Import Bank made two mixed credit offers in response to competing mixed credit offers from France. One was to finance the sale of machine tools to Indonesia, the other to finance the sale of telephone switching equipment in Cyprus. Since that time, Eximbank has made a small number of additional offers of mixed credit financing in response to offers made by other countries.

The Indonesia sale demonstrates the high cost of this type of activity. It was a $15 million contract by a U.S. manufacturer. Over the life of the contract, Eximbank income will be reduced by $16 million compared to the income that would have been generated by its normal rates. The Eximbank subsidy amounted to 40 percent of the contract price; cost per job created was $47,500. This subsidy cost is in line with estimates of the Congressional Budget Office on the overall cost of mixed credits.

CURRENT LEGISLATIVE GUIDANCE

In November 1983, Congress passed legislation that extended the financing authority of the Export-Import Bank and provided guidance on mixed credits and Eximbank's operating policy. The legislation emphasized Eximbank's mandate to provide export financing that is fully competitive with that offered by other countries. It directed the executive branch to take two specific actions. First, the legislation directed the President to pursue vigorously international negotiations to limit and set rules for the use of tied aid for exports. Specified negotiating objectives were in line with already existing government positions. Second, the legislation directed AID and the Export-Import Bank to establish mixed credit programs competitive with those of other exporting nations. Mixed credit offers under these programs are to be coordinated by an interagency committee and require the unanimous consent of its members.

Congress made it clear that it wants the United States to be more aggressive in meeting unfair financing competition from other exporting countries.

Eximbank and AID have developed standards and guidelines for the programs called for by Congress. AID's program is proposed to extend to a limited number of countries because of other legislative requirements. The Eximbank plans to act on a case by case basis, using both interest rate concessions and improved terms as necessary to meet competition. By terms of the legislation, the National Advisory Council must pass on each transaction. Substantially increased activity from either Eximbank or AID in support of U.S. exports is unlikely, however, for the following reasons.

☐ Concessional terms are very expensive to the Eximbank and it wants to maintain its commercial standing.

☐ AID's primary interest is in carrying out its development mandate in those countries in which it operates and in assuring that any use of its Economic

Support Funds be consistent with the economic, security, and political criteria used to establish ESF country allocations.

☐ The principal recipients of mixed credit offers are countries in which AID has little or no activity.

☐ AID believes that the unqualified use of mixed credits could divert its assistance from the neediest countries and from a recipient's highest priority projects.

☐ The interagency coordination process is bureaucratic, time-consuming, and not suited to the pressing needs of timely action.

Findings

☐ The United States and its exporters are losing markets to countries that provide concessional credit to their exporters for commercial purposes.

☐ Past U.S. Government actions to meet commercially motivated subsidized financing competition have been limited and ineffective.

☐ The U.S. negotiating posture in regard to mixed credits is essentially right, but it is not likely to be effective in the short to medium term.

☐ U.S. Government agency responses to the initiatives directed by Congress have not resulted in a significantly more aggressive stance by the United States.

☐ A new approach is needed in order to support U.S. negotiating efforts and permit U.S. exporters to compete on equal financing terms with exporters from other countries who benefit from officially subsidized financing.

If recent history is any measure, progress in negotiations in the near future is likely to continue to be slow and indecisive. Recent steps taken by the DAC to broaden the range of mixed credit activities proscribed by international agreement are welcome. Welcome, too, is France's recent decision to withdraw a line of credit to Algiers for subway construction. But we must maintain the effort to negotiate an end to this expensive and wasteful practice.

Recommendations

The United States should assign the highest priority to negotiations directed at stopping the practice of governments using various methods of subsidizing export finance to commercial advantage.

We strongly endorse the Administration's policy to put an end to these subsidies, which are costly, wasteful, and ultimately gain nothing for those nations that engage in the practice. Goods and services should move in international commerce according to their intrinsic value and the marketing effort behind their sale; subsidized financing does not contribute to their value, nor does it lead to the eventual reduction of production costs. To the contrary, it enables the movement of goods that might otherwise find no market. This does not promote the best interests of either buyer or seller; in the long run, continued use of mixed credits will have an adverse effect on the growth of trade, the world's economy, and prospects for improved living standards.

The United States should actively discourage the use of mixed credits and other forms of commercially motivated subsidized financing in the appropriate multilateral fora and in bilateral discussions with those nations that engage in the practice.

The United States should be prepared, up to the limit of Eximbank's lending and guarantee authority, to fund an aggressive program of subsidized export financing to meet the competition of other countries. The program should remain in effect until other countries discontinue their mixed credit programs.

The Export-Import Bank is the principal official financing arm of United States trade policy and is specifically charged with promoting U.S. exports "at rates and on terms and conditions that are fully competitive with other countries and consistent with international agreements." Eximbank finances exports to many countries that are recipients of mixed credit offers. A program to compete directly against a broad range of unfair mixed credits would be consistent with the bank's mandate to be competitive, but it would be inconsistent with its mandate to remain financially sound, as large amounts of concessional financing would lead to losses on the bank's portfolio. However, existing authority is adequate for Eximbank to undertake such a program immediately; new legislation would not be required.

Eximbank has substantial unused financing authority and total financing ceilings that should be sufficient to accommodate any activity that is likely to be generated by this program. In FY 1983 it used less than $1.5 billion of its nearly $4 billion lending authority and less than $7 billion of its $10 billion guarantee and insurance authority. Lending, guarantee and insurance authority for 1985 are expected to be in the same order of magnitude. A similar shortfall is likely in 1984. Unused ceilings on Eximbank's lending authority totaled several billion dollars.

Other U.S. institutions such as AID would not be as effective in a mixed credits program. AID has strong developmental mandates in which trade and export promotion are not key factors. In addition, AID has limited resources that are primarily devoted to countries to which mixed credits are not directed. Legislation would be required to thrust AID into a strong trade promotion role. Not only would start-up time be longer with AID, but the institutional difficulties would be extensive.

EXPORT-IMPORT BANK

Amount Required

Available data do not provide a solid basis for estimating the funds that might be required. Eximbank believes that 13 export transactions valued at $576 million may have been lost to foreign mixed credits (narrow definition) over the four-year period from August 1979 to August 1983, an average of almost $150 million per year. Documentation for lost sales is very difficult to produce because there is no effective way to collect the necessary data. In recent years, the amount of mixed credit offers by other countries has averaged about $2 billion per year. It increased to $3.5 billion in 1983 and will be at least that amount in 1984. Estimates of lost exports and mixed credit activity generally would probably be much higher if they were based on a broader definition of mixed credits—one that reflects the full range of commercially oriented subsidized financing techniques used by our foreign competitors. This, in addition to underreporting, might well double the reported $3.5 billion.

COST TO THE UNITED STATES

According to estimates of the Congressional Budget Office, the cost to the Eximbank in lost interest over the life of a credit, when used to match a competing mixed credit with a 25 percent grant element, would be about 40 percent of the face amount of the loan. As an example, the use of $1 billion a year for mixed credit financing would therefore reduce Eximbank income by approximately $400 million over the life of the loans or about $40 million per year. These losses would not be recovered.

This $40 million annual loss of income to Eximbank would be a small fraction of its annual interest income, which amounted to more than $1.4 billion in FY 1983. However, its net losses of $247 million in FY 1983 would increase further if this loss of interest from a mixed credit program had also been reflected in the bottom line.

Criteria for Use

The purpose of this more aggressive stance would be to counter the use of subsidized mixed credit financing (in its broad meaning) by export competitors. The difficulties with data collection already enumerated will be much worse when facing the need for quick action to meet a competitive offer. Guidelines for the program need to be established so that exporters and bankers have a clear understanding of when, and under what circumstances, Eximbank funds can be drawn upon.

Although they need further definition and refinement, the following criteria provide an initial framework.

☐ Eximbank should offer financing to U.S. exporters that will enable the exporters to compete on equivalent terms with exporters from other countries who benefit from commercially oriented concessional credit (mixed credits). In some cases, Eximbank may provide identical financing packages; in other cases it might include some other combination of down payment, rate, term, and grace period concessions that would be equal, but not superior, to the competing financing.

☐ Eximbank should aggressively counter competing offers. For instance, in qualified cases in which Eximbank believes there will be mixed credit competition, it should use the prior notification procedures under the OECD Arrangement to query the country in question about its intent. If the country involved uses mixed credits extensively and does not provide a clear negative response to the query, Eximbank should be directed to operate on the assumption that a mixed credit package will be offered and it should provide appropriate financing to the U.S. exporter. In other cases, Eximbank may have to make judgments about the intent behind competing offers—whether the principal motivation is commercial or developmental.

☐ All operations undertaken should be consistent with U.S. responsibilities under the OECD Arrangement, which permits matching of competing offers, and with other U.S. international commitments.

☐ Eximbank should pay particular attention to those products of competing countries that have benefited most from mixed credits, such as telecommunications, power, and transport equipment firms. However, it should not exclude any products in which U.S. exporters can be price-competitive.

☐ Eximbank should not exclude products that are in world oversupply, such as copper or steel processing equipment, because to do so would be tantamount to announcing that the United States is leaving the field to others. However, it is current U.S. policy not to finance such exports. We do not quarrel with the policy. Our clear preference would be to avoid these areas, but given the needs of the program, flexibility may be required.

Summary

The Eximbank program can be implemented now. It is needed to make U.S. exports competitive with the subsidized commercial exports of our competitors. It will improve the U.S. negotiating position by trying to eliminate commercial export subsidies. It will serve U.S. exporters and the national interest. The President should direct the Export-Import Bank to undertake such a program immediately and continue it until our competitors stop using these predatory and expensive practices.

U.S.-China Trade Relations

U.S.-China Trade Relations Action Brief

The United States should actively support the emergence of the People's Republic of China as a major participant in the international trade arena and realize its importance to U.S.-developing country relations.

Introduction

CHINA'S AGRICULTURAL SECTOR MODERNIZATION

The People's Republic of China (PRC) today manages to feed almost one quarter of the world's people from just 13 percent of its total land area. Although the Chinese have succeeded in slowing the population growth rate in recent years, the absolute number of people that will have to be fed and clothed in the future is staggering. This will exert tremendous pressure on its agricultural resource base. While its agricultural system managed to successfully provide minimally adequate diets for the vastly expanding population of the last three decades, reform was necessary if agriculture was to meet future needs and contribute to the overall development of the Chinese economy.

China is attempting to rationalize its economic structure by introduction of management and organizational reforms, material incentives, market forces, and liberalized agricultural policies. Through these reforms, the Chinese leadership apparently envisages an economy that combines state ownership and central planning of its key elements with greater individual incentives and a small, but growing, individual enterprise sector. The long-standing policy of self-reliance has been supplemented with an "open door" policy to promote development through interaction with the world economy and increased utilization of imported technology.

The most effective and far-reaching reforms have been in agriculture, involving the gradual dismantling of the commune system and a shifting to household production units. These reforms have provided incentives to boost production, latitude for greater individual decision making, and allowed free markets for over-quota production. In addition, the agriculture sector reforms and loosened state control over rural market activity have allowed significant price increases to producers and achieved the desired diversification of production in cash crops and livestock. The success, thus far, suggests that such reforms will be continued.

Of major concern is the increase in rural unemployment, which is now estimated at 30 to 40 percent of the total agricultural labor force, or about 100 million people. To address this problem, the Chinese are encouraging a shift of the rural labor force into nonagricultural enterprises, such as small food processing factories and other small rural industry and the service trade, especially in the commerce and transportation sectors. The new freer markets and private service establishments are beginning to offer alternatives to state employment.

Agriculture sector success has been attributed, in part, to the reorientation of consumer and producer prices, but at great cost in terms of state subsidies. Agricultural grants now account for more than 70 percent of total government subsidies, which consume nearly 45 percent of government revenues.

PRIVATE ENTERPRISE AND INVESTMENT

Total U.S. investment in China is estimated at about $500 million, including about $85 million in 20 joint ventures. The recently signed Industrial and Technological Cooperation Accord is likely to result in additional investment opportunities as protocols are established over the next few months, especially in the energy and transportation sectors. China's interest in acquiring needed technology to spur its modernization efforts has been well-established and has resulted in 130 contracts for technology transfer between 1973 and 1981, primarily for energy and power generating equipment, electrical machinery, and precision instruments.

There has already been an extensive commitment of private American capital to the development of China's energy sector, including an April 1984 agreement by Occidental Petroleum Corporation to jointly develop the world's largest open-pit coal mine involving an investment of approximately $640 million. Offshore oil exploration alone is expected to require somewhere in the range of $20 billion over the next five to ten years. In 1980, the first wholly-owned foreign enterprise was established. The 3M Company of St. Paul, Minnesota is currently planning to establish such a wholly-owned enterprise in Shanghai to manufacture products for the telecommunications industry.

China now considers foreign investment an attractive alternative to commercial borrowing. Considerable progress has been made in establishing a legal and regulatory framework that is attractive to foreign investors. The Bilateral Tax Treaty, signed during President Reagan's April trip to China, represents a significant commitment by both countries to increased commercial ties despite their vastly different social, political, and economic systems. The agreement prevents double taxation, reduces taxes on income from interest and royalties--particularly important in light of the liberalized U.S. rules on technology transfer and the resulting licensing fees for U.S. firms—and gives U.S. investors knowledge of the tax consequences of doing business in China.

In addition to the agreement on taxes, President Reagan also initialed a Nuclear Cooperation Agreement which, when ratified by Congress, will open the way for U.S. sales of nuclear technology and equipment to China. Progress is also being made on a Bilateral Investment Treaty (BIT) that would assure non-discrimination against foreign investments* and establish arbitration procedures and rules for compensation in the event of expropriation as well as terms for repatriation of earnings. Trademark regulations were promulgated in 1982 that included a new definition of infringement and established mechanisms for dispute settlement. China has also promulgated a new patent law that affords protection to foreign-owned technology. Further patent protection is expected to be included in the BIT.

In terms of stimulating private enterprise, China has made much progress in increasing the autonomy of enterprise managers to enter purchase and sales agreements and take personnel actions and has increased the reliance on profits and taxes to improve the efficiency of enterprises and boost state revenues. China is currently putting in place a system that will reward efficiency by allowing enterprises to keep more profits and by denying state subsidies to perennial money losers. The increased opportunities for individuals and collectives to engage in competitive activities can be seen, for example, in the construction industry, which is increasing its reliance on competitive bids, and increasing the number of participants in the bidding process.

Beginning in 1979, China experimented with the concept of "special trade zones" or "special economic zones" (SEZs) in southern coastal areas. In order to attract foreign investment and spur economic development, businesses in these SEZs were given special incentives, such as a reduced tax rate, exemptions from import duties on raw materials, and more flexibility in management decisions, particularly regarding employees. The success of the SEZs, which attracted $2.8 billion in foreign investment by the end of 1983 (almost half the national total), has resulted in extending the concept to most coastal cities. The SEZs have also proven to be a key factor in technology transfer. Following the introduction of overseas technology into large coastal factories, it has been quickly transmitted to the interior and then used to assist in the development of rural industries. The relaxation of government controls in an attempt to increase economic efficiency has allowed the emergence of a new class of entrepreneurs, approximately 2.3 million out of an urban work force of 110 million, and the "enlivenment" of the economy.

*NOTE:
In the past there has been strict control over remittances and requirements concerning local hiring and the export of production financed by U.S investors. Current difficulties in negotiating the BIT stem from disagreement over arbitration of disputes by third parties.

TWO-WAY TRADE

For a market economy to survive and grow, it needs external markets for its goods and services. The Task Force is concerned that protectionist pressures in the United States, such as those that recently surfaced in the textile industry, can serve not only as a disincentive to China's efforts to expand trade with the United States, but might also slow down internal reliance on market forces.

As they attempt to increase the time available to make needed structural adjustments in their own economies, the imposition of trade curbs by developed countries can have devastating effects on the economies of developing countries struggling to recover from the current recession. For example, in 1982 China had a trade surplus of $3 billion. During the first nine months of 1983, this surplus shrank to only $900 million, mostly because of textile import restrictions imposed by Western nations.

In our attempt to increase our own and developing countries' participation in the expanded international markets that result from increased economic development, we must take care that our markets offer corresponding opportunities for developing country exports. This is particularly relevant in our relationship with China, a country that tends to view trade relations from a much broader perspective than we do and consequently links actions taken in one sector to actions in others. This has been particularly visible in the Chinese failure to comply with the existing U.S.-PRC long-term grain agreement. It is clear that China's performance under this agreement and willingness to enter future agreements is contingent upon the openness of U.S. markets.

This linkage between agreements is likely to surface again in the area of technology transfer. We are encouraged by the Reagan administration's commitment to provide increasingly sophisticated forms of technology to China and by recent actions taken to implement this commitment. However, given the strong PRC interest in acquiring the technology necessary to speed its development process, future difficulties in this area could have significant ramifications in all U.S.-PRC trade areas.

U.S. AGRICULTURAL ACTIVITIES IN CHINA

Present U.S. trade with China is already considerable, some market development activity is underway, and other cooperative programs are in place. In 1982, 32 percent of the total $5 billion in trade with China was for agricultural products. The agricultural trade balance was $1.3 billion in favor of the United States. However, due to friction over a variety of issues, particularly U.S. restrictions on textile imports, and exceptionally good harvests, agricultural trade dropped 64 percent in 1983 to only 12.4 percent of the total $4.4 billion in trade. The U.S. agricultural trade balance was only $370 million.

The United States now operates an agricultural trade office in Beijing under the authority of the Agricultural Trade Act of 1979. This office services U.S. agribusiness through such activities as appraising local market conditions and cultural and trading practices, providing trade leads and opportunities, arranging appointments, and assisting with product exhibits and promotions.

There are also three Foreign Agricultural Cooperator offices in China under the auspices of the U.S. Feed Grains Council and the U.S. Wheat and Soybean Associations. Activities of these groups have included establishing a model bakery and noodle plant and constructing a model wheat milling facility with U.S. technology and Chinese land, building materials, and labor. Plans are underway for a model feed additive manufacturing plant that will also act as a training facility for ration balancing, livestock nutrition, and the use of U.S. technology in producing feed additives.

The U.S. Department of Agriculture's Office of International Cooperation and Development (OICD) also operates an extensive program with China for science and technology exchange under a specific agriculture protocol, as do several other agencies under a variety of implementing protocols for the overall U.S.-PRC Science and Technology Agreement. These protocols cover such diverse areas as earthquake studies, surface water hydrology, and biomedical science. The OICD program was of particular interest to the Task Force because it has received high praise as a model program for strengthening cooperation and extending mutual benefits on a cost-sharing basis. Exciting work has been done in plant and animal germ plasm exchange, which will benefit the agricultural economies of both countries and ultimately lead to increased feed, livestock, and poultry trade. While this type of cooperative effort appears to offer considerable promise, this initiative has been put on hold, pending resolution of long-term grain agreement difficulties.

In addition to the specific exchange of scientific and technology information, the agreements provide a forum for both sides to review issues and concerns of a broader nature than pure science and research. The interchange that takes place under such agreements is usually directed to the need to understand and interpret data and to relate the impact the new technology has on improving output in each country. Under the agreements, both sides are able to discuss how the shared information affects the viability of competing or complementary farm interests.

Another highly successful program operated under these protocols is the National Center for Industrial Science and Technology Management Development at Dalian. The national center is the first management development center in China to be organized in cooperation with a foreign government. Its program is modeled on the curricula of U.S. graduate schools of business administration. Not only does this program provide management training and skills to Chinese managers, it also affords substantial contact with industry, government, and academic professionals from all over China. It is an ideal mechanism to promote the adoption of an appropriate business environment to attract U.S. business investment.

While these activities are extremely useful beginnings, a more extensive effort will be required to develop the cooperative environment and full range of agribusiness relations necessary to realize the potential of the Chinese market.

AGRICULTURAL EXPORT FINANCING PROGRAMS

China has not participated in any of the Commodity Credit Corporation (CCC) export financing programs, although there are no restrictions to its doing so. For example, it has been eligible for the Export Credit Guarantee Program since 1979. This program provides CCC guarantees of U.S. bank financing of foreign purchases for up to three years. The Chinese failure to use this program is presumed to be because of its high interest rates and their ability to obtain more favorable terms for cash purchases.

However, the tremendous demands that China's development plans will place on available resources in the next few years may force a reversal of the financial retrenchment of the recent past, which allowed the accumulation of large foreign exchange reserves ($14 to $17 billion at the end of 1983). As a result, the Chinese may begin looking for financing now while their credit is particularly good to cover their expected import requirements, especially for grains. China has had to import large quantities of grain to meet the needs of urban consumers due, in large part, to internal infrastructure constraints that have precluded efficient distribution of record grain crops. These food imports continue to place severe strains on the existing port capacity. Such infrastructure constraints can have a severe impact on China's ability to import goods and services necessary to continue its modernization process and the expansion of two-way trade with the United States.

Recommendations

A concerted effort should be made by the Administration to ensure removal of the existing restrictions on foreign assistance to China.

PRC eligibility for U.S. assistance is governed by Section 620(f) of the Foreign Assistance Act of 1961, which prohibits any assistance under the Act to Communist countries, defined to include 18 specifically named nations, one of which is China. The President may waive this prohibition, but only if he determines that aid is "vital to the security of the United States," that the recipient nation is not "controlled by the international Communist conspiracy," and that such aid will help the recipient attain independence from Communist control. The Administration has submitted a proposal to eliminate this prohibition on aid to China, which includes nearly all bilateral aid and some military assistance. It is part of the foreign assistance authorizing legislation that is currently held up in the Congress.

Because China is a major and important Third World country, the Task Force urges that innovative means of developing closer ties between the United States and China continue to be sought. While efforts to remove the current prohibition on foreign assistance to China should be continued, these existing strictures should not be allowed to become insurmountable obstacles.

Increased technical assistance, especially in agriculture, should be provided through an expanded Trade and Development Program.

The U.S. Trade and Development Program (TDP) has made significant progress in the area of technical assistance through the financing of feasibility studies in high priority development areas. Like the science and technology exchange programs, the TDP cost-sharing and reimbursable features make it particularly attractive to the Chinese, while providing significant opportunities for U.S. business to participate in the modernization and development process.

During President Reagan's April 1984 trip to China, two TDP agreements were signed and four more were signed by Secretary Malcolm Baldridge during the Joint Committee on Commerce and Trade meetings held shortly after the President's return from China. These six projects involve approximately $1.4 million in TDP financing in the areas of energy resources (oil and gas), silicon materials and fiber optics plants, and wheel and tire manufacturing. In FY 1983, TDP supported, on a cost-sharing reimbursable basis, a feasibility study for a dairy project joint venture in Guangdong Province.

Such TDP-financed feasibility studies can have a significant impact on increasing the participation of U.S. firms in China's modernization efforts and in providing the technology to make these efforts successful.

Steps should be taken to highlight China's eligibility to participate in the P.L. 480 program.

The P.L. 480 legislation permits the sale of agricultural commodities under Title I and donations for economic and community development under Title II only to countries that the President has determined to be "friendly" to the United States, i.e., any country not "dominated or controlled by a foreign government or organization controlling a world Communist movement." The only exception to this prohibition is for famine or disaster relief under Title II.

Because this restriction did not specify any country by name, there was uncertainty over whether it applied to China. In 1982, the Administration successfully obtained congressional clarification of the provision that would permit the President to declare China eligible for P.L. 480 assistance. To obtain this clarification, assurances were provided at the time that no bilateral program was being considered under P.L. 480 and that the clarification was being sought solely to ensure that, in principle, we were treating China in the same way we were treating other friendly, nonallied countries.

The Task Force believes a carefully structured program, focused on the promotion of private enterprise, could effectively demonstrate the U.S. commitment to its economic principles and support the steps taken so far by the Chinese to encourage reliance on individual initiative and market forces. By targeting joint ventures in China's urban areas, even a limited program could provide some assistance to the Chinese in their attempt to rationalize agricultural producer and urban consumer food prices.

For example, a program to finance tallow sales for use in feed rations could be effectively used to assist in the development and expansion of China's feedgrain industry. P.L. 480 Title I agreements could be entered with U.S. private trade entities who agreed to undertake joint venture feed mill or feed additive production projects. This would encourage increased cooperation between the U.S. private agribusiness sector already participating in the Chinese economy through the Agricultural Cooperator program and the agricultural sector in China. It would also result in mutual benefits as U.S. feedgrain, seed, and technology exports increased and the Chinese economy acquired needed technical expertise, production facilities, and marketing know-how. Because the industry is in its infant stage, there would be inherent limits to the magnitude of such a program, and a funding level of $5 to $10 million could have a significant impact.

Efforts should be redoubled to secure funding for the CCC Intermediate Credit Program and the development of appropriate agricultural infrastructure.

The United States could specifically assist in China's attempts to address agricultural infrastructure problems through the CCC Intermediate Export Credit Program. This program provides three to ten-year export financing for U.S. agricultural commodities. Funds generated from the local sale of those commodities in the importing country must then be used to fund agriculture sector infrastructure projects (storage and port facilities, roads, processing plants, etc.) designed to improve the handling, marketing, processing, storage, or distribution of imported commodities. This program could, therefore, provide additional food supplies while the Chinese agriculture sector adjusts to the demands of newly adopted market mechanisms and the funds needed to build critical infrastructure facilities.

Greater private sector involvement in promoting agricultural development in China could be attained by involving the private sector Agricultural Cooperators in the identification, planning, and implementation of intermediate credit-financed projects.

P.L. 480
Action Brief

The P.L. 480 Food for Peace Program should be at least doubled to help avert starvation and alleviate poverty, expand developing country agricultural markets, and support private sector growth.

Introduction

WORLD FOOD NEEDS AND AVAILABILITIES

The developing world today faces an economic crisis of major proportions and will continue to experience serious difficulties throughout this century. Rapid population growth and the need to improve the diets of millions of people create rising demands for the most basic human need—food. Most developing countries will have difficulty expanding their food production fast enough to keep pace with increased needs. Natural resources are being depleted at alarming rates as agriculture expands onto marginal lands of low and unreliable productivity. Agricultural productivity increases are desperately needed, but depend on substantial investment in land development, infrastructure, and such production inputs as fertilizer and seeds. Capital to meet these needs is scarce, especially in the present world financial crisis. Business and technical skills and a suitable technology base continue to be critical constraints. In addition, government policies in many countries discourage agricultural production. The combination of these factors suggests that food deficits will continue to grow.

Unfortunately, progress in agricultural development in the recent past has been extremely disappointing. Asia, Africa, and Latin America have all turned from food exporters to food importers. Their overall rate of growth in agricultural production has decreased due to soil erosion and reduced return on the use of various production inputs. Further, there have been only relatively modest advances in agricultural technology, especially as related to the needs of developing countries. For example, in 31 of the least developed countries, agricultural production over the past decade increased only 1.6 percent per year compared to a population increase of 2.6 percent per year. Starvation is thus a constant threat. Increased production is a vital and urgent necessity.

Estimates by the Department of Agriculture (USDA) support the notion that significant amounts of food aid will be required in the coming years to sustain even the current inadequate diets in many developing countries. In 1983-1984, USDA estimated that at least 12 million tons of food aid would be required to maintain average per capita consumption levels. This quantity would have to be increased to at least 33 million tons were per capita consumption to rise sufficiently to meet minimally acceptable nutritional levels. (See Table D.1.) This grim picture masks additional problems that call for even higher levels of food imports. These figures do not take into account either uneven distribution across or within countries or allow for unforeseen natural disasters that can demand significant quantities of food to meet dire human needs. For example, the United Nations estimates that 150 million Africans are chronically hungry and tens of millions suffer from thirst or contaminated water supplies as a result of the current drought situation.

Against the 12 million metric ton need projection for 1983-1984, total planned food aid in cereals from donor countries was approximately 9 million tons. Of this total, the United States expected to contribute approximately 6 million tons.* (See Table D. 2 for the level of P.L. 480 assistance.) To sustain current consumption levels or improve diets, donor countries must greatly increase the quantity of food assistance in the short term and heighten efforts to assist developing countries in improving their own agricultural production efforts over the long term. Furthermore, where population growth increases at a faster rate than agricultural production growth, and food import foreign exchange requirements increase to meet the higher demand, the effect is to reduce imports of other goods—including investment goods for development.

Abundant global cereal stocks and low world prices should set the stage for a reversal of declining per capita consumption in medium and low-income importing countries. But, because of severe limitations on the ability of developing regions to finance needed purchases, record high cereal supplies remained out of the reach of many of the poorest countries.

U.S. AGRICULTURE

The productivity of the U.S. farm sector has been phenomenal. For various reasons, however, it has resulted in billions of dollars of government outlays, large surpluses, and low farm incomes. To accept expensive production controls, low farm income, and reduced competitiveness of U.S. agricultural commodities in world markets, rather than use our agricultural abundance to help meet the needs of the world's hungry, is ironic for a country with a long established tradition of humanitarian concern for those less fortunate and a philosophy of rewarding personal efforts and productivity gains rather than penalizing success.

Before the 1970s, the U.S. farm sector was not a major participant in world food markets. Agricultural exports were only 10 percent of farm cash receipts in 1950 and 14 percent in 1960. By 1980, however, exports amounted to 30 percent of total cash receipts. Today, the production from four acres of every ten is destined for foreign markets. Overall, at least one-third of the total production capacity of U.S. agriculture produces for foreign markets.

*NOTE: Increases in P.L. 480 funding during FY 1984 permitted total shipments of about 6.5 million tons.

TABLE D.1:
Cereal Import Requirements and Food Aid Needs to Support Consumption for 1983-1984

	(in thousand tons)	Import Requirements Status Quo[a]	Import Requirements Nutrition Based[b]	Food Aid Needs Status Quo[a]	Food Aid Needs Nutrtion Based[b]
Africa and Middle East	Angola	311	302	71	62
	Benin	86	0	46	0
	Burundi	0	8	0	8
	Cameroon	183	302	0	119
	Cape Verde	53	45	28	22
	Central African Republic	30	103	26	99
	Chad	80	395	75	390
	Comoros	30	62	18	50
	Congo	81	83	16	18
	Djibouti	36	NA	0	NA
	Egypt	7,714	4,019	3,317	0
	Equatorial Guinea	4	NA	3	NA
	Ethiopia	532	2,354	450	2,272
	Gambia	0	0	0	0
	Ghana	247	538	166	458
	Guinea	188	449	77	338
	Guinea-Bissau	36	41	25	30
	Kenya	318	1,080	215	977
	Lebanon	613	769	77	232
	Lesotho	325	263	259	197
	Liberia	137	110	62	35
	Madagascar	400	203	372	175
	Malawi	27	160	0	132
	Mali	165	780	129	743
	Mauritania	162	208	116	162
	Mauritius	148	137	12	1
	Morocco	1,481	1,658	200	377
	Mozambique	669	1,272	484	1,087
	Niger	180	152	143	115
	Rwanda	58	55	58	55
	Senegal	350	477	0	68
	Sierra Leone	77	58	27	7
	Somalia	355	293	284	222
	Sudan	224	501	224	501
	Swaziland	113	105	95	87
	Tanzania	450	816	394	759
	Togo	61	135	44	118

(continued)

SOURCE:
World Food Aid Needs and Availabilities, 1983, USDA, Economic Research Service, July 1983.

NOTES:
a) To maintain current consumption levels based on per capita intake of food staples at levels reported over last four years.
b) To raise per capita intake of staples to levels associated with FAO's recommended minimums.

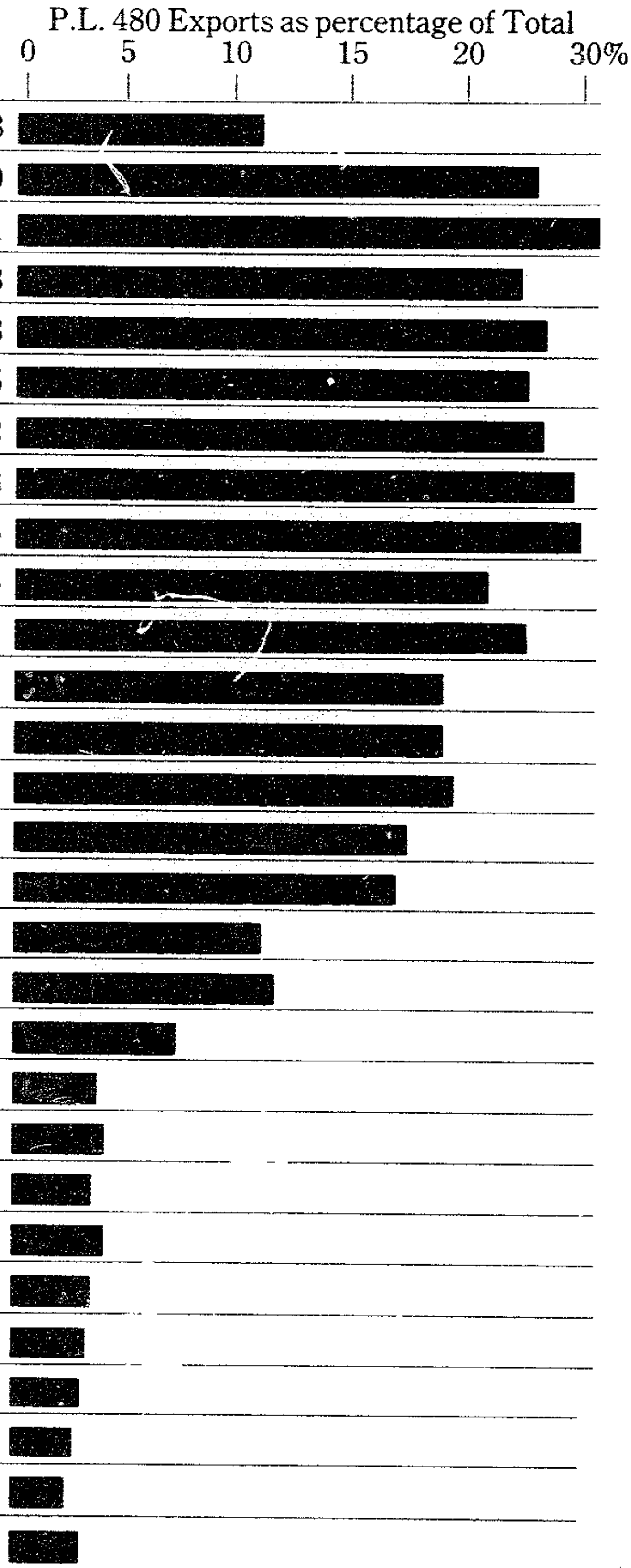
		Import Requirements		Food Aid Needs	
	(in thousand tons)	Status Quo[a]	Nutrition Based[b]	Status Quo[a]	Nutrition Based[b]
Africa and Middle East (continued)	Tunisia	957	723	0	0
	Uganda	0	506	0	502
	Upper Volta	38	300	6	267
	Yemen Arab Republic	544	504	179	139
	Yemen, PDR	221	252	21	52
	Zaire	288	1,227	51	990
	Zambia	275	569	73	368
	Subtotal	18,247	22,014	7,837	12,234
Asia	Afghanistan	125	144	101	121
	Bangladesh	1,256	6,132	1,085	6,045
	India	0	9,805	0	8,239
	Indonesia	2,329	0	297	0
	Kampuchea	123	253	94	224
	Laos	55	63	0	0
	Nepal	0	854	0	854
	Pakistan	0	0	0	0
	Philippines	1,122	1,366	382	626
	Sri Lanka	783	1,090	83	390
	Vietnam	1,352	2,018	1,173	1,838
	Subtotal	7,145	21,725	3,215	18,337
Latin America	Bolivia	590	703	333	445
	Colombia	517	0	0	0
	Costa Rica	107	74	0	0
	Dominican Republic	327	398	0	80
	Ecuador	342	417	72	172
	El Salvador	219	290	138	208
	Guatemala	129	81	0	0
	Haiti	221	449	94	321
	Honduras	103	181	6	80
	Jamaica	450	380	133	64
	Nicaragua	40	0	0	0
	Peru	1,320	1,645	559	884
	Subtotal	4,365	4,618	1,335	2,254
	Total	29,757	48,357	12,387	32,825

It is now widely recognized that for the U.S. agriculture sector to be continuously operated near an acceptable capacity level, the foreign market share must be maintained and expanded. Export growth convinced American farmers that continued expansion of foreign markets is crucial to their economic well-being. It is similarly critical to the agribusiness community, which also expanded its facilities and earnings during the export expansion period of the 1970s. This entire group—farmers, labor, and the agribusiness sector—now has a vital stake in U.S. international policies.

Despite the small percentage of Americans actively engaged in farming, the agriculture sector in the United States, including farmers, agribusiness,

TABLE D.2:
P.L. 480 Exports from 1955-1983

	Total Agricultural Exports (billions of U.S. dollars)	Total P.L. 480 Exports (billions of U.S. dollars)	1,000's Metric Tons
1955	$3.1	$0.4	3,418
1956	3.5	1.0	10,070
1957	4.7	1.5	14,271
1958	4.0	1.0	9,228
1959	3.7	1.0	11,488
1960	4.5	1.1	14,325
1961	4.9	1.3	16,342
1962	5.1	1.5	18,778
1963	5.1	1.5	17,366
1964	6.1	1.4	16,776
1965	6.1	1.6	18,411
1966	6.7	1.3	18,157
1967	6.8	1.3	13,957
1968	6.3	1.3	14,579
1969	5.7	1.0	9,996
1970	6.7	1.1	10,936
1971	7.8	1.0	9,834
1972	8.0	1.1	9,905
1973	12.9	1.0	7,373
1974	21.3	0.9	3,314
1975	21.6	1.1	4,827
1976	22.1	0.9	6,652
1977	24.0	1.1	6,434
1978	27.3	1.1	6,094
1979	32.0	1.2	6,284
1980	40.5	1.3	6,067
1981	43.8	1.3	5,893
1982	39.1	1.1	5,696
1983	34.8	1.2	6,192



SOURCE:
U.S. Department of Agriculture.

and retail food operations, is responsible for over 20 percent of the U.S. GNP and 22 percent of U.S. employment.

In 1982, U.S. farmers contributed over $71 billion to the GNP. By the time this was consumed, other sectors of the industry added $556 billion to its value, in effect generating $8 for every dollar's worth of product from the farming sector. Assets in agriculture amount to nearly $1 trillion, an amount equal to almost 90 percent of the combined assets of all manufacturing corporations in the United States. The value of farm assets, with the economic activity generated by farm products flowing through the economic system, makes the agriculture and food system the nation's largest industry and employer.

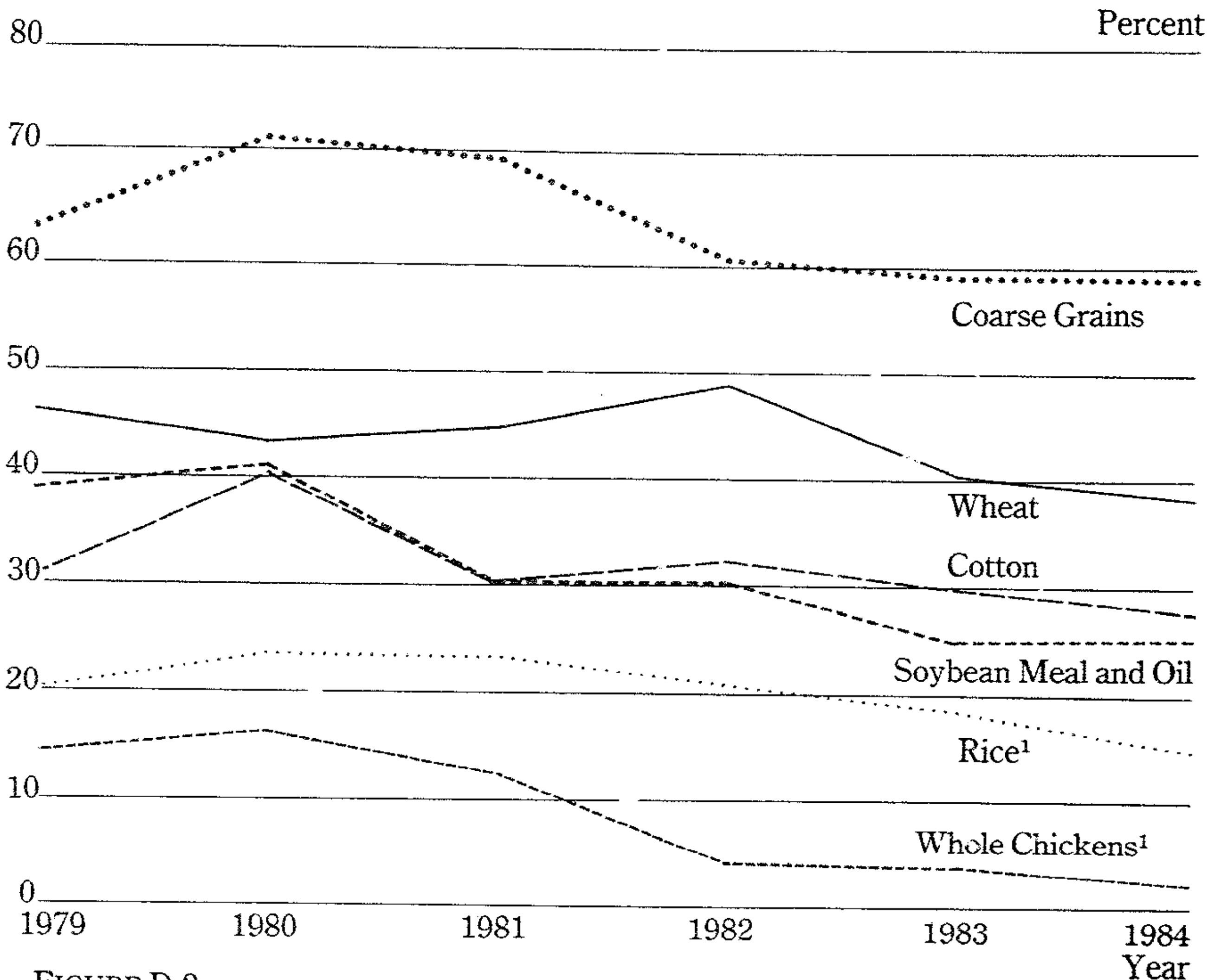
In 1982, American consumers spent over $300 billion for food, about 15 percent of personal disposable income. This share is much less than the share spent for food in the United Kingdom, France, Japan, and virtually all other developed countries. The tremendous growth in productivity of the U.S. agriculture and food system has freed billions of dollars of consumer income for the purchase of other goods and for savings and investment.

U.S. agricultural exports consistently set new value and volume records through the 1970s, but peaked in 1981 and have declined since then. In FY 1983, exports fell to $34.8 billion, 21 percent below the record high. This resulted primarily from a slackening in demand brought about by the worldwide recession, the severe debt crisis, strong appreciation of the dollar placing our products at a competitive disadvantage, the increased use of export subsidies by our competitors, and abundant harvests elsewhere in the world. While some recovery in exports is expected this year, the decline surfaced longer term troublesome problems for U.S. trade.

Hope of achieving the full potential of expanded markets for agriculture, with resulting benefits for the United States and developing country economies, hinges on whether or not we can achieve a truly market-oriented world trading system. In recent years, we have seen competitors increase exports while employing predatory trade practices to protect their domestic markets and exploit foreign ones. Many of these countries have artificially stimulated a higher level of production to promote agricultural exports than their domestic resource base would justify. Many developing countries have also attempted to achieve agricultural self-sufficiency, often supported by import substitution policies of development institutions in the past, which resulted in the inefficient use of increasingly scarce resources.

Most important, other exporting nations with abundant supplies compete fiercely for the available markets, frequently employing practices not available to U.S. exporters. The most direct of these is the use of export subsidies to penetrate markets, most notably by the European Economic Community (EEC). Another is the use of concessional financing, primarily mixed or blended credits which, by reducing interest rates, effectively reduce the cost of products to the importer. (These competitor subsidies accounted for $950 million, or 13 percent of the drop in U.S. agricultural exports from 1981 to 1983.) Our farmers thus now compete against the national treasuries of other countries. Such measures are used less when markets are expanding rapidly, but their adverse effect on U.S. agricultural exports becomes pronounced in slow growth periods. Given the outlook for slower market growth in the future, they can be expected to be a persistent concern in such a trade environment. (See Figures D.1 and D.2.)

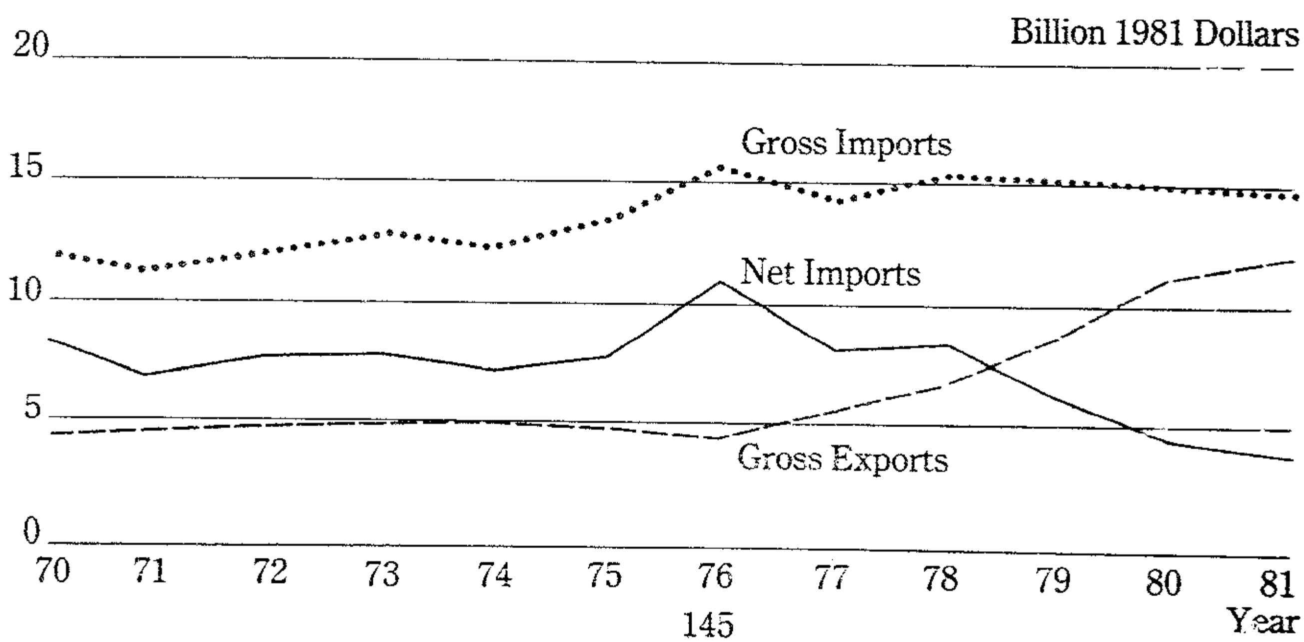
FIGURE D.1:
U.S. Share of World Trade,
Selected Commodities



[1]Calendar Year

SOURCE:
U.S. Department of Agriculture, 1984.

FIGURE D.2:
EC Trade in Major Commodities
Under the Common Agricultural Policy*



*Meat, Dairy, Sugar, Grains, Oil Seeds, and Non-Grain Feed Ingredients.

SOURCE:
U.S. Department of Agriculture, 1984.

ADDRESSING THE THIRD WORLD DEBT CRISIS AND FOOD AID NEEDS

The P.L. 480 Food for Peace program should be at least doubled to help avert starvation, alleviate poverty and malnutrition, expand developing country agricultural markets, and support private sector growth.

Discussion: In the short term, food aid can contribute to meeting the gap between food supplies available in developing countries and unmet food requirements, particularly in lower income countries. There is the strong possibility that the developing world will face a major food shortage within a decade—far greater even than the present shortage in Africa. We need to significantly increase our P.L. 480 program to help avert this crisis.

An economy cannot hope to improve if the vast majority of its people are near starvation or if most of its budget is expended on importing food supplies for subsistence. With our abundant resources and well-deserved image as a humanitarian nation, we should be at the forefront of the relief effort in Africa and elsewhere in the world.

We recommend a significant dollar increase in the P.L. 480 program, to at least double its current level in 1985.* This increase should be keyed to meeting needs and averting starvation. Although the quantity of food provided by a doubling of the funds available for P.L. 480 will depend on the level of prices, it is currently estimated that commodity prices will rise only slightly over the next five years. The additional funds will, therefore, provide approximately 6 million metric tons of commodities each year from FY 1985 to FY 1989, bringing total OECD donor country food aid to approximately 15 million metric tons.

A significant increase in P.L. 480 will help meet critical food needs, signal the intention of the United States to meet these needs through official food aid, and provide significant benefits to the U.S. economy while strengthening the long-term ability of developing countries to meet their own needs.

Provision of substantial food aid would also provide some debt burden relief because large donated food supplies could free up some foreign exchange for debt retirement purposes. This is especially true if other donor countries are encouraged to increase their contributions by a comparable amount.

We recognize the concern that large-scale increases in food aid could serve as a disincentive to local production. Therefore, as an important component of the expanded program, appropriate assurances must be obtained during the agreement negotiation process that policies will be adopted to maintain domestic producer prices where they are adequate and increase producer prices where they are not adequate incentives for domestic production. Sufficient safeguards must also be in place to assure that additional quantities will not disrupt commercial markets or exceed the absorptive capacity of the local distribution infrastructure or of program implementing agents. AID should consider establishing a program to provide short-term financing to help developing countries address these constraints wherever they preclude the programming of additional food aid.

ADDRESSING EMERGENCY FOOD AID NEEDS

Additional mechanisms must be provided to respond quickly to emergency food aid needs.

☐ Flexibility to use the emergency provisions of the Food Security Wheat Reserve Act should be increased.

☐ Flexibility to use Commodity Credit Corporation borrowing authority should be increased.

Discussion: In addition to greatly increasing the size of the U.S. food assistance program, additional flexibility

*NOTE: Reference to a doubling of the P.L. 480 program is based on the approximately 6 million ton level originally approved for FY 1984 and planned for FY 1985 at the time the Task Force developed this recommendation. Subsequent increases in the program, which are expected to raise FY 1985 shipments to about 8 million tons, were not considered in the Task Force analysis.

must be provided to address critical food aid needs in a timely manner. The establishment of the $50 million Special Presidential Fund would be a major step toward meeting this objective. However, more must be done. In particular, we recommend increasing the flexibility to use the emergency provisions of the Food Security Wheat Reserve Act. This Act was designed, in part, to provide additional flexibility under P.L. 480 to meet emergency humanitarian food needs resulting from natural disasters. However, this authority has never been used. Even when substantial emergency food needs exist and P.L. 480 emergency reserve funds are extremely limited, AID is not able to use the Act to provide immediate relief because Congress requires that supplemental funding be sought first. While the Task Force supports the current requests for supplemental funding for P.L. 480 to provide emergency food assistance, we do not believe starving people should have to wait until the U.S. legislative process can be completed. Rather, agreement should be reached between the Administration and Congress on providing additional flexibility to use the wheat reserve whenever extraordinary needs arise, with costs to CCC reimbursed through subsequent appropriations, whether regular or supplemental.

Because the wheat reserve may have limited usefulness when disaster strikes countries that are not traditional wheat consumers, CCC should also have the flexibility to address emergency needs through its borrowing authority. While an unallocated reserve of P.L. 480 funds is maintained for such purposes, too often it is insufficient so that our response to disasters results in shifting commodities away from previous commitments to voluntary agency food donation programs. It is extremely important that the U.S. Government not shift commodities away from voluntary agencies. The United States and the President need the authority to send food to any developing country in the world threatened by drought or famine beyond current budgetary limits on regular P.L. 480 programs. Once disaster strikes and the President declares a state of emergency, food aid should start and be justified in supplemental appropriation requests. Such aid would be temporary, ending when the crisis has been adequately addressed.

AGRICULTURAL PRODUCTIVITY IN DEVELOPING COUNTRIES

U.S. food assistance should be used more effectively as an incentive for developing countries to adopt policies that promote reliance on market forces and the local private sector to increase agricultural production.

☐ The authority to accept local currency payments under Title I should be restored.

☐ Guidelines for invoking the debt-forgiveness provisions of Title III agreements should be liberalized.

☐ A revolving fund to finance private enterprise projects should be established with P.L. 480 repayments.

Discussion: Recognizing the primary importance of recipient government policies to agricultural development, the U.S. Government has for many years required developing countries to take certain "self-help" measures as a condition of P.L. 480 Title I agreements. These include measures to promote agricultural production, research and development, and to create a favorable environment for private enterprise and investment. In negotiating agreements, the U.S. Government should require firmer commitments to adopt policy changes that will facilitate the establishment and development of self-sustaining private enterprise.

To gain greater leverage for policy changes affecting the private agricultural sector, the President should ask Congress to restore the flexibility to make Title I sales for local currency.

Originally, P.L. 480 provided for concessional sales in exchange for local currencies. These U.S.-owned local currencies were then used to finance mutually acceptable development projects. Later, the law was changed to require dollar rather than local currency payment but with concessional credit terms attractive to the recipient country. Local currencies are still generated under such agreements through sale of the food in the marketplace, but they are owned by the recipient government which, in turn, has a dollar obligation to the U.S. Government. How the local currency generations are used depends largely upon the effectiveness of U.S. negotiations at the time of entering into the concessional sales agreement.

To gain more leverage in negotiating policy reforms, Title III was later added to P.L. 480. It provides a "debt-forgiveness" incentive for all or part of the P.L. 480 agreement. The debt-forgiveness provision under Title III is to be exercised only where LDCs accept and carry through on significant policy initiatives. When the debt-forgiveness provision is activated, the recipient government is not required to repay the U.S. loan either in dollars or in local currency. Because Title III programs may offer a greater incentive to host governments to negotiate policy initiatives, additional flexibility to invoke the debt forgiveness provisions of this title should also be established. The availability of alternative financing arrangements under P.L. 480, from Title I local currency to longer term Title III agreements, provides a "shopping basket" flexibility for considering the needs and terms most suitable to a developing country at any given time.

A program to use some of the Title I, P.L. 480 dollar repayments for private enterprise development would provide needed foreign exchange to the economies of recipient countries as well as additional supplies of capital for investment in private sector agricultural development projects. (These repayments total about $400 million per year.)

Although the authority to establish a revolving fund already exists, legislation to use P.L. 480 receipts for such a fund is needed. Such a revolving fund could complement the recently formed PRE Private Sector Revolving Fund and could be linked to the proposals for the establishment of an American Agricultural Development Corporation (ADC) and increased aid to other ICIs discussed elsewhere in this report.

PRIVATE ENTERPRISE DEVELOPMENT

The private sector provisions of P.L. 480 must receive much more emphasis than is currently the case.

- ☐ A major portion of local currencies generated by the P.L. 480 program should be used for direct investment in private enterprise projects.
- ☐ The USDA Agricultural Cooperator Program should receive increased local currency funding under P.L. 480 authority.
- ☐ Private Trade Entity agreements should be reinstituted.
- ☐ The role of private voluntary agencies should be strengthened.

—Administrative procedures should be relaxed.
—Multiyear commitments should be made.
—Additional authority to generate local currencies under Title II should be granted.
—Participation of PVOs in Title III programs should be encouraged.

- ☐ Lead responsibility for Title I should rest with USDA's Foreign Agricultural Service.
- ☐ Program implementation should be freed from many of the current legislative constraints and administrative encumbrances.

—Extend Title III authority to all U.S. foreign aid recipient countries.
—Maintain availability of Title I to needy countries regardless of whether or not they meet the poverty criteria of the International Development Association (IDA).

—Distribute funds to the private sector in a timely manner.
—Keep prescribed activities to a minimum.
—Promote the eligibility of activities further along in the farm-to-market chain for P.L. 480 support.

☐ The cost of cargo preference requirements should be removed from the P.L. 480 budget.

Discussion: Essential as some public sector projects may be to provide necessary infrastructure, the absence of entrepreneurship, management skills, and enterprise-specific capital accumulation critically limit the development process and seriously inhibit the potential of public sector investment. Therefore, most U.S. food assistance resources should be channeled to private companies to stimulate private business, rather than to government for public projects. Recipient country governments need to understand it is in their own self-interest to channel this assistance into the private sector directly or through indigenous relending institutions.

Entirely aside from improved food availability, perhaps the greatest contribution P.L. 480 has made to economic development has been the generation of local currencies from sales in the marketplace that were reinvested in order to stimulate the country's own agricultural economy. To the extent that such local currencies are effectively used in the agricultural sector, they lessen future needs for foreign aid. To the extent that they are utilized through the country's private sector, they offer greater hope of sustainable progress in their own agribusiness economy.

A major portion of the recipient-owned local currencies generated from local sales of P.L. 480 commodities and local currencies acquired by the U.S. Government through Title I sales under the restored local currency authority should be used for loans to the private sector. The emphasis should be on agricultural and agribusiness development and on facilities to handle U.S. food, feed, and fiber imports. These loans should be made through local financial intermediaries that have the business expertise to effectively evaluate private sector projects and to meet the needs of small and medium scale businesses, expecially in rural areas.

The Task Force notes, in particular, the valuable contribution the USDA Agricultural Cooperator Program has made in stimulating private enterprise in developing countries. Local currencies generated under P.L. 480 were originally available for this joint U.S. Government-private-sector-funded market development effort. The government portion of funding is currently provided through dollar appropriations that have constituted a decreasing proportion of total program costs over the past 15 years. Substantially increasing the use of P.L. 480 local currencies to support Agricultural Cooperator program activities, such as those designed to improve livestock feeding and feed and food processing capabilities, is precisely the type of private sector activity for which a larger proportion of U.S. food assistance resources should be used.

P.L. 480 legislation specifically authorizes direct negotiation of Title I agreements with U.S. and foreign private trade entities (PTEs). Due to the program's multiple objectives, increases in commodity prices, and limited funding availability, the authority for PTEs has not been used in recent years. Reinstituting the PTE program could significantly increase private sector involvement in P.L. 480 assistance efforts and greatly enhance the program's impact on the development of self-sustaining private enterprise in developing countries. In the past, the PTE program effectively stimulated private enterprise activities in developing countries and increased the participation of the private sector in U.S. development assistance efforts. For example, the 1967-1972 PTE agreement with the Korea Silo Company resulted in the construction and equipping of the grain terminal facility at the port of Inchon, Korea. The agreement with Purina-Korea, Inc. established facilities for the production of animal feeds. The PTE program has also been effectively used to increase the funding capabilities of intermediate credit institutions lending to agricultural cooperatives.

A timely advantage of the PTE program is its ability to cut across national boundaries. This program could be very useful in addressing regional problems in light of the success of the Administration's Caribbean Basin Initiative and the need to develop additional tools for such regional approaches to development.

One segment of the U.S. private sector that has played a critical role in promoting agricultural development and meeting humanitarian needs in developing countries is the Private Voluntary Organizations (PVOs). The role of PVOs in U.S. Government food assistance programs, however, is often restricted by the extensive program review process, restrictive administrative procedures, and lack of multiyear program commitments.

Further, the ability of PVOs to identify agricultural development opportunities independently, within the context of a particular country's development priorities and needs, has been restricted by the overall program priorities established by AID in Washington. When a PVO program can be designed to address a high priority problem in the recipient country, it is often easier to both reach amiable working arrangements with host country institutions and gather additional resources for the development effort. This is particularly relevant to the promotion of private enterprise, which has traditionally received scant attention due to the overriding relief or emergency assistance orientation of Title II programs. A private sector emphasis will provide not only today's sustenance but also the wherewithal to meet humanitarian needs over the longer term by promoting market economies and self-sustaining private enterprise activities.

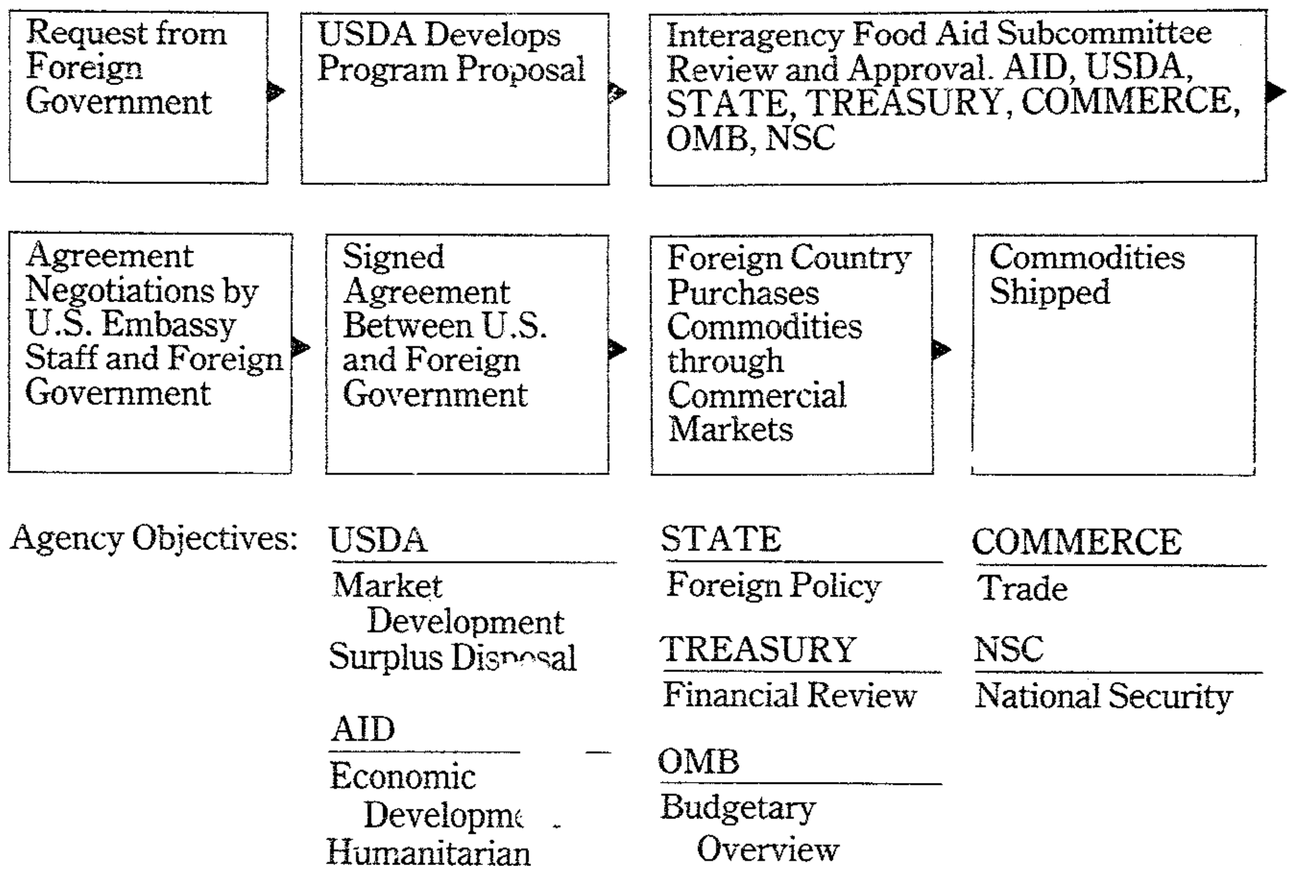
The wealth of experience among PVOs in rural areas could also be effectively used in Title III programs. To date, there has been considerable difficulty in identifying the appropriate mechanisms to achieve the intended objectives of Title III programs. Encouraging the PVOs to take an active role in implementing Title III programs could reduce many of the difficulties currently experienced by the program.

However, a commitment to private sector promotion and enhancement of market-oriented activities often depends on the continued availability of resources. If we wish to encourage the commitment of resources and risk-taking by the private sector in developing countries (in this case primarily rural agricultural producers), multiyear commitments of resources under our food assistance programs become even more necessary than under traditional food assistance programs.

U.S. food donation programs should have more leeway to generate local currencies to implement projects and increase the participation of indigenous private enterprise in development efforts. Under Title II of P.L. 480, authority to generate local currencies is severely limited. Restrictions on the ability to generate development funds under this program, however, in many cases preclude the implementation of extremely effective programs involving the participation of both the United States and developing country private sector entities and the development of self-sustaining private enterprises in the local economy. Such funds are particularly critical to those least developed countries that have undertaken significant reforms in the agriculture sector, but lack the funds to carry out specific programs and projects to implement the new policies.

Interdepartmental procedures for P.L. 480 program implementation are extremely complicated and unduly burdensome and need to be streamlined. (See Figures D.3 and D.4.) In part, the current situation stems from the long list

FIGURE D.3:
P.L. 480—Title I/III Program Flowchart



SOURCE:
USDA, 1984.

of conditions mandated by Congress that each project must satisfy. The list has grown over the years with the annual process of authorizations and appropriations. This is further aggravated by operating procedures established within the implementing agencies, which often includes a committee system for project review and approval as well as for other administrative decisions. This approach is also employed at the field level, putting additional time-consuming burdens on those responsible for operating the program.

USDA should be made the primary U.S. Government entity responsible for implementing the private enterprise development objectives of U.S. food assistance programs. This is because of its greater experience with private enterprise programs and requirements, its ability to identify projects likely to improve the recipient country's ability to meet food needs through increased agricultural production, knowledge of more efficient farm-to-consumer distribution systems, and appreciation of the benefits of expanded private enterprise participation in the agricultural sector. With lead responsibility at USDA, the program would be used less for short-term political objectives and more for sound agricultural policy change and productive agribusiness activities.

In addition to a change in overall administrative responsibility, several legislative constraints need to be relaxed. For example, the Title III program is currently limited by law to the poorest developing countries. Frequently, these countries are not the best ones in terms of potential gains from policy reform. Extension of the Title III authority to all recipients of U.S. foreign aid would provide wider latitude to deal with policy initiatives for strengthening international private enterprise where

FIGURE D.4.
Title II Program Development and Implementation

Program Sponsor Request
- Voluntary agencies
- World Food Program
- Recipient country

▶

Washington Review
- AID
- USDA
- OMB

▶

Interagency Food Aid Subcommittee Approval

– AID	– Treasury
– USDA	– Commerce
– OMB	– NSC
– State	

▶

Approval Notification

Sponsor	*Implementing Agent*
– PVO	– Headquarters and recipient country
– WFP	– Rome and recipient country
– Country	– Recipient country

▶

Commodity Procurement
- USDA

▶

Commodity Shipment Booking

Sponsor	*Implementing Agent*
– PVO	– Private booking agent
– WFP	– USDA and private booking agent
– Country	– USDA

▶

Commodity Arrival in Country supervised by:
- PVO
- WFP
- Country

▶

Direct Distribution of Commodities to Individual Recipients
- PVO
- Country

▶

Compliance Reporting to AID (commodity use and number of recipients)
- PVO
- WFP
- Country

Agency Responsibility:

Primary program responsibility rests with AID. Operational responsibilities for Title II activities are carried out by three types of program sponsors: private voluntary agencies (PVOs); intergovernmental organizations, primarily the UN/FAO World Food Program (WFP); and recipient governments (Country).

TABLE D.3: Benefits Achieved from an Increase in P.L. 480

SOURCE:
U.S. Department of Agriculture, Office of Budget and Program Analysis, 1984.
NOTES:
[a]Additional funds required to increase P.L. 480 by $1 billion in FY 1984 and to bring total funding level to $3 billion in each of next five years.
[b]Cost of Title I commodities will be repaid over 40 years.
[c]Cost of Title II commodities and shipping plus Title I Ocean Freight Differential. The Title I OFD is the additional cost of using U.S. bottoms in compliance with U.S. cargo preference requirements, which are not repaid by the recipient country.
[d]Projections were made assuming that target prices were frozen at current levels and assuming target prices continued to escalate. Savings in price support programs result from the additional U.S. exports under P.L. 480 that reduce the cost of loans, deficiency payments, storage, and other expenses associated with the programs.
[e]A $1 billion increase in P.L. 480 in FY 1984 was the maximum possible at the time the analysis was performed.
[f]Based on the planned FY 1985 program level of approximately six million tons at the time of the analysis. Does not include subsequent increases raising FY 1985 shipments to an estimated eight million tons.

(in $ millions)	FY 84[e]	FY 85[f]	FY 86	FY 87	FY 88	FY 89	Total
Cost of Increase in P.L. 480							
Total Cost[a]	1,000	1,339	1,306	1,272	1,238	1,203	7,358
Less recoverable[b]	665	884	862	840	817	794	4,862
Net Cost[c]	335	455	444	432	421	409	2,496
Title I OFD	85	120	118	114	111	108	656
Title II	250	335	326	318	310	301	1,840
Savings in price support program[d]							
Frozen targets	218	382	541	866	1,120	982	4,109
Escalated targets	218	382	666	1,305	1,200	1,422	5,193
Net Benefit (Cost)							
Nonrecoverable P.L. 480 less frozen targets	(117)	(73)	97	434	699	573	1,613
Nonrecoverable P.L. 480 less escalated targets	(117)	(73)	222	873	779	1,013	2,697

the payout would be greater.

The Title I program is also subject to the current restriction on the proportion of funds (only 25 percent) that can be allocated to countries with per capita incomes above the IDA poverty level. Removal of this restriction would meet several objectives.

In the first place, the conditions required for effective private enterprise development are more likely to exist in middle-income developing countries. Thus, the majority of potentially successful projects will be found in middle-income countries with more established commercial markets. Furthermore, the opportunities for expanding markets for agricultural commodities, both indigenously produced and imported, are likely to be greater in middle-income countries.

The second important objective is providing some relief from excessive debt burdens during the current foreign exchange liquidity crisis. In recent years, many of the lower income countries were not viewed as good credit risks and, therefore, much of the development assistance provided was in the form of grants. Middle-income countries, on the other hand, were extended significant amounts of financing based on their growth potential and perceived creditworthiness. It is primarily the middle-income countries that could benefit from the debt relief aspects of the increased P.L. 480 funding levels.

Finally, many of the operational procedures required for P.L. 480 program implementation should be streamlined, from those pertaining to project approval to those dealing with the mechanics of commodity shipment.

In particular, the current cargo preference requirements of P.L. 480 significantly complicate the administration of the program and greatly diminish the funding available to finance commodity purchases (by more than $100 million this year alone). The additional P.L. 480 funding could provide significant additional quantities of food if cargo preference costs were not paid with P.L. 480 funds. Merchant marine support should be funded separately based on the merits of such support. It should not reduce funds available for U.S. foreign assistance efforts or complicate other program operations. At the very least, the cost of cargo preference compliance should be identified and paid for as a separate line item in the budget, rather than through the budgets of other programs. At best, cargo preference requirements should be eliminated entirely, particularly under P.L. 480, and replaced with a more cost-effective direct subsidy program for the merchant marine.

Summary

Certain forms of foreign assistance and some programs designed to stimulate trade are extremely cost-effective. They achieve their objectives at little net cost, while providing significant benefits to the U.S. economy. The best foreign assistance programs, not only leverage resources to the maximum extent possible, but also provide maximum benefits at minimum cost.

In times when commodity prices are low and large quantities of U.S. agricultural commodities cannot be absorbed in commercial markets, food assistance is one of the most cost-effective forms of foreign assistance. For illustrative purposes, the Task Force examined the impact of doubling the P.L. 480 funding level over the next five years.* Such an increase would provide approximately 6 million tons of food to help meet critical food needs and allow some improvement in the currently inadequate diets of millions of people. Furthermore, this would result in a benefit-cost ratio of nearly 2:1, nonrecoverable costs totaling only $2.5 billion compared to projected price support program savings of $4 to $5 billion. (See Table D.3.) Such a favorable benefit-cost ratio does not include additional benefits to be derived from expanded commercial market opportunities for U.S. agricultural exports, the impact of a higher level of exports on general economic activity, or the employment opportunities generated by the increased economic activity.

For example, doubling program funding would generate approximately $1.6 billion in additional economic activity, with benefits to the U.S. Treasury of approximately $300 million in revenue, $80 million in unemployment savings. It would also create approximately 20,000 additional jobs.

Given the importance of agriculture to the United States and the developing world and the multitude of benefits the program offers to both the U.S. and developing country economies, a much larger share of total U.S. foreign assistance should be in the form of food assistance. Rather than paying our farmers to idle productive land, our agricultural abundance should be used to meet the critical food and development needs of less developed countries.

*NOTE:
See footnote on page 146 and note #a on page 153.

AID and Its Private Sector Initiative

AID and Its Private Sector Initiative Action Brief

AID's private enterprise initiative needs to be strengthened and more fully integrated into the mainstream of the agency. While some actions may require legislative or wider executive branch approval, there is much that AID, within its existing authorities, can do.

The President's Task Force on International Private Enterprise addressed a broad spectrum of U.S. foreign assistance programs and agencies. This action brief consolidates and expands upon those recommendations that relate directly to AID, and focuses on those actions that can be taken without addressing the broader question of U.S. foreign assistance structural reorganization. This brief does not deal with the Overseas Private Investment Corporation (OPIC) or the Trade and Development Program (TDP) which, along with AID, are components of the International Development and Cooperation Agency (IDCA). While AID presently carries out many of the activities dealt with below, in our view there are substantial qualitative and quantitative differences between what is presently done and what should be done.

Summary of Recommendations Relevant to AID

The recommended actions have been divided into two sets: (1) those actions which AID can immediately undertake within its existing authority, and (2) those actions that may require outside authorization procedures (i.e., legislative action), or other U.S. Government approval such as the Department of State. Keeping this division in mind, we propose that AID undertake the following actions to support private enterprise in developing countries.

POLICY ORIENTATION

■ Strengthen and fully integrate the private enterprise initiative into the mainstream of AID.

■ Emphasize private enterprise in policy dialogues with developing countries. Target more assistance to and through efficient private entities rather than governments.

■ Devote a larger share of AID's resources to countries that adopt a policy framework conducive to private enterprise, investment, and trade.

■ Instruct AID missions to submit realistic and viable private sector strategies as part of the AID Country Development Strategy Statements (CDSS) and identify ways to expand LDC private sector participation in AID projects.

■ Promote greater U.S. business community participation in AID-financed projects in developing countries.

■ Emphasize trade considerations to a greater degree in designing assistance programs.

■ Prepare detailed country-specific plans to support U.S. and indigenous private sector efforts as part of a comprehensive strategy developed by ambassadors and country teams in LDCs.

PROGRAM DEVELOPMENT

■ Support the full and continuous cataloguing of all past and present AID activities dealing with private enterprise.

■ Increase substantially financial support to developing country businesses, particularly through the funding of intermediate credit institutions (ICIs), and encourage ICIs to provide equity funding as well as loans.

■ Increase the involvement of PVOs in private enterprise development.

■ Consider the advantages of entering into a major service(s) contract with an international commercial or investment bank to help design financial plans for projects and to train AID employees.

■ Develop mechanisms by which AID missions can facilitate relationships between U.S. and developing country businesses, with special emphasis on small businesses.

■ Allocate funds to support specific, problem-solving technical research with potential commercial application in developing countries.

■ Broaden ties with the international financial community and with venture capital organizations.

■ Explore the feasibility of, and coordinate within the U.S. Government and other participants, the establishment of a Private Enterprise Institute.

■ Increase substantially the training of LDC citizens in the United States and overseas with particular emphasis on fields related to private enterprise development. Establish a private enterprise training advisory board to assist AID in this regard.

■ Support the private sector's initiative to establish an American Agricultural Development Corporation with AID and U.S. private sector cofinancing.

AID ORGANIZATION AND PERSONNEL

■ Channel a larger proportion of AID financial resources to private enterprise development.

■ Improve private enterprise skills in AID through in-house and academic training of AID personnel, as well as private sector exchange programs, and recruit skilled business people.

■ Detail AID personnel to other U.S. Government agencies that deal with investment, trade, and commerce such as OPIC, Eximbank, the U.S. Trade Representative's Office, and the Commerce Department.

■ Improve AID's ability to communicate and work with business in the United States and in developing countries.

■ Increase the budget and personnel of the Bureau for Private Enterprise and give it more approval and coordination authority over all mission and bureau private enterprise projects.

■ Establish private sector adviser positions in AID missions overseas.

NOTE:
■ = no outside authorization needed (in-house changes and/or reallocation of existing funds)
■ = probable outside authority necessary, new funding required

The Task Force believes that actions that adhere as closely as possible to the intent of the recommendations that follow will improve AID's performance in carrying out the private enterprise intiative. We believe these recommendations are reasonable; many draw from and expand upon past AID experience. All will ultimately serve to help AID to address more effectively the basic human needs of the people of the Third World.

POLICY

Strengthen and fully integrate the private enterprise initiative into the mainstream of the agency.

In terms of linking private enterprise to development efforts, the Task Force considered the fact that foreign assistance programs authorized under the Foreign Assistance Act of 1961 are driven, in large part, by the desire to meet basic human needs (BHN). The Task Force believes that much good has come from this objective, such as AID's concentration on the small farmer and its attention to developing country education and basic health care. We believe that these needs can be met on a sustainable basis only when there are ample opportunities for employment and the full utilization and development of human resources. Rather than competing with AID's BHN focus, reorienting foreign assistance programs toward the dynamism of the private sector will actually support and reinforce BHN goals.

While the BHN concept complements a private enterprise thrust, neither Congress nor AID has moved toward full integration or balance of the two in the foreign assistance program. One reason this may be the case is that traditional foreign assistance groups have not recognized this complementarity and have not brought this message to Congress. AID must actively strive to correct this. Congress must go on record regarding AID's involvement in private enterprise. We believe Congress would endorse a strong commitment, particularly because it could result in expanded trade and increased employment for both the United States and the developing world.

While AID has done much to foster private enterprise, much more needs to be accomplished. For example, AID's mandate and approach to private sector development needs to be strengthened in terms of legislative language and resource availability. PRE's approximately 1 percent share of the entire AID budget hardly bespeaks strong support and commitment to the initiative. Congress and the executive branch also need to recognize that private enterprise is synonymous with risk-taking. Venture capital financing, ICIs, prototype projects with replication potential, cofinancing, brokering projects, and the new PRE Revolving Fund are all measures that should have full executive and legislative support.

Emphasize private enterprise in policy dialogues with developing countries. Target more assistance to and through efficient private entities rather than governments.

AID presently channels most of its funds through developing country government agencies. As a U.S. Government assistance program, we understand the need for AID to work with developing country governments in reaching agreement on programs. However, in many cases it is not necessary for developing country government agencies to actually implement the programs. Once the government has given general concurrence to a program concept, AID should increasingly look to the United States and developing country businesses as vehicles to implement the programs. In this regard, we commend AID's Bureau for Private Enterprise (PRE) for its imaginative use of venture capital, insurance, and leasing companies to undertake AID-financed activities. This is an effective way to leverage scarce foreign assistance funds. In addition, we note the imaginative work undertaken by AID's Bureau for Latin America and the Caribbean (LAC) in support of the Caribbean Basin Initiative. For example, they have explored ways to help develop trading companies by financing commercial banks and development banks that, in turn, provide the necessary capital to trading companies.

Devote a larger share of AID's resources to countries that adopt policies conducive to investment, private enterprise development, and trade.

Many AID missions and regional bureaus have taken the initiative to involve private enterprise in their development efforts. However, AID has a long way to go before it is effectively organized and committed to investment, private enterprise, and trade as key to development so that these areas will command a significant portion of AID resources. AID has made an impressive start in certain areas, such as the projects undertaken by the Caribbean Basin Initiative (CBI), and those developed by PRE.

Generally, in its "policy dialogue" efforts, AID has not felt it could forcefully and credibly insist on policy reform to support the private sector in exchange for AID funds. There are many reasons for this, ranging from U.S. political considerations to the small size of AID's program in a given country so that the funds provide little leverage for change. Even in some countries where AID has a large budget, both the U.S. mission and the host government implicitly operate under the assumption that threats to tie AID funds to policy reform are only a "bluff." This is because the host government believes that U.S. political interests in the country are so strong that the United States cannot afford to offend that country. Also, there is often a feeling among U.S. policymakers that if we were to follow through, the recipient country might turn to another donor, possibly the Eastern Bloc.

While recognizing the dilemma, AID should concentrate its resources in countries that adopt a policy framework conducive to investment, private enterprise, and trade. AID funding should be responsive to a recipient country's willingness to develop its private enterprise system, particularly when actions are taken to remove disincentives. Proposed by the Reagan administration, the new Economic Policy Initiative for Africa, wherein $500 million would be available to African countries that pursue positive market-oriented policies, is very much a step in the right direction.

Develop detailed plans to support U.S. and indigenous private sector efforts. These plans should be part of the comprehensive strategy developed by the U.S. ambassador and his country team.

AID operates within the framework of overall U.S. policy toward each country. The State Department and the National Security Council (NSC) develop an agenda and a budget for each country with which the United States maintains diplomatic relations. Currently, private sector issues do not have the position in most country team plans in keeping with their importance, particularly in LDCs.

Discussion of policy approaches provides frequent opportunities for key officials in the host government to talk things over informally with the American ambassador, the AID mission director, and others. To guide these discussions and pinpoint targets of opportunity, each embassy should incorporate into its planning a strategy for support to the United States and LDC private sectors as well as identify particular policy changes to be encouraged. This strategy should then serve the entire staff of the U.S. country team—from the ambassador down—as the framework for their efforts.

Instruct AID missions to submit realistic and viable private sector strategies in their Country Develop-

ment Strategy Statements, and explore ways to better ensure greater private sector project implementation in the field.

AID instructed its missions to develop private sector strategies in their CDSS. The initial response from many of the missions was perfunctory. AID project designers and managers and AID directors must make a commitment to the initiative in order for it to work. One way to institutionalize the initiative is by shifting the burden of proof so that the CDSS must contain an explicit justification for funding a public sector project rather than a private enterprise project.

There has been some indication of wider attention to private sector development in the foreign affairs community. The State Department, in conjunction with AID and the Commerce Department, has taken an important step in identifying the private enterprise climate and constraints through its recent Investment Climate Statement publications. These publications should set the stage for American ambassadors in developing countries to draw up an action plan that identifies the constraints to investment, trade, and private enterprise, as well as a strategy to remove those constraints, including the use of AID resources. AID missions should utilize the information from the Investment Climate Statements as well as other sources in their CDSS planning of private enterprise projects.

PROGRAMS

Fully catalogue past and present AID activities dealing with private enterprise.

AID must fully and continuously catalogue what has and has not worked in its private enterprise development activities. AID possesses a state-of-the-art system of evaluation that allows it to closely monitor selected development projects from the proposal stage through the afterlife of the project stage. However, AID has not sufficiently catalogued "success" or "failure" in projects. This has led to gaps in AID's memory of what works and does not work. The Task Force commissioned a special study to catalogue AID's past and present private sector activities designed to foster trade, development, and private enterprise. We recommend AID build on this study.

New private sector-related projects undertaken during this Administration have not yet reached a point where they can be fully evaluated. Also, we recognize that developing a track record for this type of initiative requires several years before results are available. We believe that private enterprise development efforts are seriously impeded by the lack of readily accessible information on completed or in-process projects.

Nor does AID know exactly how much of its budget is devoted to private enterprise development. In large part, this is due to differing interpretations throughout AID as to what constitutes private enterprise. Private enterprise is a broad and complicated concept and circumstances differ from country to country. AID must establish a working definition to provide guidance to its field missions. Included in this definition should be development projects that directly foster market-oriented policies and the growth of trade; attract private domestic and foreign investment; and build up profit-making, nongovernment organizations that generate employment. Until AID clarifies its working definition, it will continue having difficulty institutionalizing its private sector intiative and rewarding those who have made major efforts to carry it out.

AID projects must take into account their positive contribution to the economies of both the recipient LDC and the United States. The impact of AID projects upon both the U.S. and LDC economies is an important yardstick in determining their viability. Important factors, such as employment generation, two-way trade stimulation, and market expansion, are an integral part of, and not separate from, a project's developmental impact.

Substantially increase financial support to developing country businesses, particularly through the funding of intermediate credit institutions (ICIs) and encourage ICIs to provide equity funding as well as loans.

Along with managerial talent, equity is one of the scarcest resources for private sector activities in AID-assisted countries. AID is currently permitted to accept debentures with equity features in financing projects. Present legislative authorities are sufficient for those special situations in which AID might want to have a direct profit participation in one of its projects. As a general rule, however, we do not believe it appropriate for a sovereign government to own equity of a business in another sovereign country.

There are various alternatives by which equity financing can be offered without direct U.S. Government participation. AID does make loans to financial institutions that, in turn, can offer equity financing. The Task Force strongly recommends an increase in this kind of activity. ICIs should be encouraged to provide capital funds to their borrowers, when appropriate, and undertake limited venture capital types of financing.

Increase the involvement of PVOs in private enterprise development.

AID should increase its support and utilization of PVOs that assist private enterprise development, particularly those that facilitate the involvement of U.S. private enterprise in developing country activities. Emphasis should be on U.S. small business and the promotion of investment and trade relationships.

AID should also encourage the formation of partnerships between AID, the PVOs, and U.S. business in order to link U.S. firms with developing country private enterprises. New means and fora should be developed in which the U.S. business community can join forces with the PVO community to develop new approaches to stimulate international business relationships. Corporate support for private enterprise-oriented PVOs is essential.

U.S. trade associations and voluntary business associations should be encouraged to form nonprofit subsidiaries or to work with existing PVOs to help bring their industry's resources to bear in meeting developing country needs.

Through its Bureau for Private Enterprise, Office of Small and Disadvantaged Business Utilization, Bureau for Food and Voluntary Assistance, and the Advisory Committee on Voluntary Foreign Aid, AID should promote the in-country capabilities of PVOs to the U.S. business community, as well as to other government agencies, and should encourage PVOs to join forces with U.S. business to help meet development needs.

Examine the possibility of a major services contract with an international commercial or investment bank to help design financial plans for projects and to train AID employees.

AID should consider signing a services contract with an international (U.S.) commercial or investment bank to help AID design financial schemes for projects and upgrade AID banking skills. Under such an arrangement the bank would provide AID with experts in this field, train present AID employees and imbue in AID a "commercial" or "private enterprise" attitude toward financing.

Facilitate relationships between U.S. and developing country businesses with special emphasis on small businesses.

The role presently played by the larger, multinational firms is indispensable to international trade and development. The U.S. Government and its overseas representatives should support the efforts of these firms. Yet we particularly believe the United States should actively support the efforts of small and medium-sized U.S. and developing country businesses.

Small and medium-sized businesses are the heart of the private sector in most of the countries in which AID operates. They are the primary source of employment. AID needs to do more in the catalytic role of bringing local and U.S. small and medium-sized businesses together, particularly because local businesses can learn from U.S. businesses and because they face similar challenges. AID can provide information, ideas, and money to provide linkages through trade associations and voluntary business associations where appropriate.

AID must develop credit, training, and technical assistance packages that are responsive to small business in developing countries. While recognizing that it does require considerable administrative work to develop such packages (i.e., it often takes as much time and cost to process a $10,000 loan as a $1,000,000 loan), the objective of helping small business is well worth the effort. AID should also help small businesses in developing countries join together to export their products.

Export trading companies can be enlisted by AID to help design, implement, and evaluate projects that support private enterprise.

Allocate funds to support specific, problem-solving technical research with commercial application in developing countries.

An educated guess places at least some degree of technical transfer in over 90 percent of all AID projects. However, AID does not fully recognize (or utilize) the real magnitude and potential of the technology transfer aspect of its activities. AID needs to find imaginative ways to adapt and apply new and existing technologies to developing country needs. This can be done through support for joint ventures with U.S. firms, and through licensing arrangements and similar means of commercializing the process, while involving private enterprise in development. AID should make a concerted effort to understand the process of technology transfer between private enterprises and consider setting aside funds to support specific, problem-solving technological research that has clear, commercial application in the developing world. It should also assure that the benefits of that research be made available to LDCs at a reasonable price. The BIRD Foundation model, which involves joint participation by recipient and donor countries and entrepreneurs, is worthy of replication elsewhere.

Broaden ties with the international financial community and with venture capital organizations.

International institutions such as the World Bank, the International Finance Corporation (IFC), the International Monetary Fund (IMF), and the regional development banks play a crucial role in pressing for structural adjustments of developing country economies, promoting private sector initiatives, and addressing those conditions necessary to attract trade and investment. In pursuing policy reform, they have the advantage of bringing extensive resources and the approval of the international community to bear on private sector development matters. They combine assistance specifically targeted at policy reform with project loans, credit, training, technical assistance, and direct investment in private enterprise in order to strengthen conditions for self-financed private sector growth.

AID should support those multilateral development institutions that foster private sector growth. In particular, the IMF, World Bank, and IFC merit the full support of the U.S. Government. They have, in many cases, been supportive of the "market-oriented" philosophy and have had a substantial impact on developing country leadership decisions. We must generously support such institutions, particularly those programs and projects that are directed at and are conducive to creating the conditions for private sector growth. In general, the multilateral development banks need to give much greater emphasis, as the World Bank is presently attempting to do, to building up private enterprises in developing countries.

Further, we should support the concept of the Multilateral Investment Guarantee Agency, which has been proposed by the World Bank, as a means to attract private investment to developing countries.

Coordinate the establishment of a Private Enterprise Institute.

While there are many institutions worldwide that address developing country issues, none we uncovered focus primarily on the private sector and its role in development. Therefore, we recommend the United States, in conjunction with other donor nations, developing countries, and business establish a Private Enterprise Institute (Institute).

There is presently no central clearinghouse for information and statistics that relate to private sector research. As the research center for private enterprise development, one of the Institute's primary functions would be the collection, analysis, and dispersal of data pertaining to the role of the private sector in economic development. Specifically, there is need for solid economic analysis that will convince developing country policymakers to rely more on the private sector and less on the public sector. The IMF, the Development Assistance Committee of the Organization of Economic Cooperation and Development (OECD), and the World Bank are all very good sources of data, but because their focus is not directed toward the private sector, there are significant gaps in available information. (For instance, recently major private banks involved in loans to developing countries felt compelled to create an institution to monitor the indebtedness of the borrowing nations.)

The Institute would also collect and catalogue case studies on how developing countries have successfully used the private sector to bring about economic growth. Special attention would be directed to projects funded by Official Development Assistance (ODA) that encourage private sector development in a country. Dissemination of the catalogued information will also be important to the Institute's successful operation. The analysis must be undertaken so as to be useful to governments seeking to foster private enterprise as well as businesses interested in understanding the private sector climate of a particular country.

Fundamentally, the Institute should be a collaborative project of countries that recognize that their own well-being is dependent upon the dynamism of the private sector. Developed and developing countries that join together to form the Institute, will be tangible proof of the importance of free enterprise. The Institute would be structured so that every country benefiting from its counsel and services would be required to have some financial stake in it. One institutional approach to achieving these objectives would be to relate the Institute to the IFC in some fashion.

The private sector should also participate in the Institute. Much of the data collected and analyzed by the Institute should be of value to enterprises operating in the international marketplace. By instituting a fee for services and advice, the Institute would in time become self-financing.

Substantially increase the number of developing country representatives trained in private enterprise development specialties both in the United States and in developing countries. Establish a private enterprise training advisory board.

We recommend that there be a substantial increase in AID's training that is directed to subjects related to private enterprise development. Training should also be available to participants from the private sector. Further, U.S. and developing country private sectors should be used, whenever possible, to provide business-related training. This will require much more coordination of effort than presently exists.

In conjunction with U.S. firms, we recommend that AID finance on-site training in the United States. AID training should strike a better balance between academic training and practical, hands-on training with U.S. companies. Training in production processes, business management, finance, international business procedures, marketing, and other skills will have a higher value in most countries than degree-granting programs. As much of this training as possible should be conducted through and by U.S. business, to transfer the skills they have and to build long-term, mutually beneficial relationships.

Two other areas are worthy of greater attention: AID should provide assistance for in-country training programs that support the development of trade expertise and directly relate portions of its training efforts to U.S. private sector investment and construction projects. AID might consider training assistance in conjunction with those projects for which American architecture, engineering, and construction firms may be submitting contract bids.

Support the private sector's initiative to establish an American Agricultural Development Corporation with AID and U.S. private sector cofinancing.

The U.S. comparative advantage in agriculture and the major importance of agriculture to developing countries make it particularly appropriate to focus on private enterprise initiatives in agribusiness. Currently, there is no private or public U.S. institution that can provide the necessary combination of equity capital and management expertise to facilitate the participation of private business needed to support agricultural development. (Although the World Bank's International Finance Corporation is available to American firms, it is a multilateral organization with no particular responsibility to address the specific concerns of American firms.)

Furthermore, many agribusiness activities in LDCs continue to be performed by public bodies (parastatals). Parastatal performance has proved unsatisfactory and, in many cases, they have become impediments to development. Private agribusiness firms could perform many of these intermediate functions more efficiently, given the opportunity, resulting in market expansion and the creation of new jobs. An American Agricultural Development Corporation (ADC), financed by both the public and private sector, could help in the transition of agribusiness activities in developing countries from public to private ownership.

Other industrialized countries have successfully utilized the private sector through officially supported organizations. These countries have harnessed their own private sectors to provide both capital and technical and managerial know-how to private enterprises in developing countries. They not only use investment banking and venture capital approaches to satisfy directly the financial requirements of the indigenous private sector, but these officially supported corporations also play a catalytic role in assembling financial packages and facilitating transfer of technical and managerial expertise. While the format differs somewhat from country to country, they have a common purpose: to bring market discipline to development projects and expand self-sustaining economic activity. Their basic objective is to practice good development while making money.

The proposed ADC would be structured as a for-profit venture, expected to recover its fees, earn profits, and pay dividends. In short, business would be the vehicle to achieve other purposes. Equity capital would be subscribed by the private sector, with contributions to operating expenses in the initial years from private not-for-profit organizations (major private foundations). Additional capital would be obtained from AID, possibly through a convertible debenture.

A successful corporation would not only serve to facilitate private enterprise development in developing countries, but would also enhance market development and trade objectives as well. Through such a mechanism, the participation of U.S. private business in the development process would provide a much-needed supplement to public aid in the form of increased direct private investment. It would also provide the related transfer of modern technology and management skills, foster an entrepreneurial spirit, and provide opportunities for import or export expansion.

AID ORGANIZATION AND PERSONNEL

Channel a larger proportion of AID financial resources to private enterprise development.

AID should significantly expand the amount of financial resources—both operational and programmatic—devoted to private enterprise development. Specifically, AID should devote a much larger share of its Development Assistance and Economic Support Funds (ESF) to private enterprise activities. Redirection of the resource flow in due course would translate into a substantially higher proportion of AID staff and time devoted to private enterprise development.

Improve private enterprise skills in AID through training of AID personnel and recruitment of skilled business people.

AID's BHN thrust in recent years has meant that most permanent AID professionals have skills that relate mainly to publicly-administered social programs such as population control, health, nutrition, as well as agricultural development. Many have degrees and backgrounds in such fields as anthropology, agriculture, agronomy, economics, health systems, sociology, public administration, and the developmental sciences. Some also bring experience in international affairs, as well as area studies. A large contingent of AID employees were once Peace Corps volunteers.

AID will continue to need experts in the areas mentioned above; however, it is the Task Force's belief that a greater balance in AID staff skills is required to adequately support the private sector initiative. Without AID personnel who are well-versed and experienced in private enterprise activities, and are actively seeking opportunities to utilize private sector approaches to development problems, the prospects that the initiative will take hold are not great. AID needs to emphasize the skills that will be required to support the private initiative in years to come. AID hiring practices and personnel training programs should be more heavily skewed toward private enterprise background and skills.

Present AID personnel should be afforded the opportunity and encouraged to study in after-hours training programs in fields dealing with international business, trade, markets, and finance. Such subjects as international-developing country business, trade, marketing, and finance should be among those receiving the highest priority. AID-sponsored in-house seminars should focus on private enterprise development subjects, and could be conducted by professionals in the fields of international finance, trade, banking, and marketing. Conceivably, this could be supplemented with on-the-job training programs for AID personnel.

AID should set up an active recruiting program for private sector skills. In its university recruiting program, AID should look carefully at graduates from business schools. It must also step up its recruitment of people at mid-levels with significant business experience.

AID should develop the capabilities of its local country staffs so that they are familiar with the needs of private enterprise.

Detail AID personnel to other U.S. Government agencies that deal with investment, trade, and commerce, such as OPIC, Eximbank, the U.S. Trade Representative's Office, and the Commerce Department.

While AID and the other government entities involved in some aspect of U.S.-developing country economic relations meet relatively frequently in interagency settings, the Task Force did not sense that there is much understanding from one organization to another of how the other agencies function, what their precise mandate is, what special skills they have, or how various programs might be better integrated to achieve broad U.S. policy objectives.

Assigning middle and senior-level AID personnel to the major U.S. agencies involved in some aspect of U.S. relations with developing countries should prove mutually beneficial to both agencies and participants. AID personnel will have a broader perspective on how entities more directly involved in trade and investment operate, how programs might be made more complementary, and how cofinancing might work. At the same time, AID personnel so assigned will provide these agencies with a developmental perspective and expose them to the wide range of programs and techniques applied in AID recipient countries around the world. We envision that this AID personnel secondment program would operate in a manner similar to the way AID personnel are now assigned in certain areas to the Department of State.

Improve AID's ability to communicate and work with business in the United States and in developing countries.

AID should support organizations and programs that serve as brokers between the U.S. private sector and the LDC private sector. Information on the variety of services, approaches, and institutional arrangements to provide brokering services should be readily available to businesses. Services such as the International Executive Services Corps (IESC) and the Joint Agricultural Consultative Corporation (JACC) should receive continued and expanded support from AID.

In addition, AID must greatly modify and simplify its administrative operations (such as procurement and contracting procedures) to deal with the private sector on a businesslike basis if it expects to work successfully with private enterprises. Businesses have criticized the government for not acting more like a business. While procurement and contracting rules are normal requirements of business, the extent to which AID carries them is excessive. Simple, understandable procedures are key for someone starting a business; smaller firms simply do not have the skills, patience or resources to effectively deal with the plethora of AID regulations and make a profit.

Lacking sufficient information about international markets, many U.S. firms ignore opportunities to go overseas because of what appears to them to be unknown, high-risk markets, too undefined and "unattainable" to be worth the effort. AID's familiarity with developing nations qualifies it to coordinate efforts with other government entities, such as the Small Business Administration (SBA) and the Department of Commerce. AID should investigate such organizations as the National District Export Council (DEC) as potential vehicles to assist in disseminating useful information about LDC markets. AID should also explore ways of using the products and services of other U.S. Government entities, such as the U.S. and Foreign Commercial Service (U.S. & FCS) at the Department of Commerce. The U.S.& FCS was established in 1982 to increase the number of American firms engaging in international trade and help small and medium-size firms. It has an invaluable warehouse of information on foreign markets and the nuts and bolts of exporting. It also provides contact services—helping U.S. firms to find agents or distributors for their products. It even offers an advertising service to help gain international exposure for companies with new products. The U.S.& FCS also sponsors trade fairs and missions. With a global network of 1,100 employees in 70 U.S. cities and 120 foreign cities, the U.S.& FCS has both a domestic and foreign outreach capability.

Increase the budget and personnel of the Bureau for Private Enterprise and give it more approval and coordination authority over mission and bureau private enterprise projects.

The role of the Bureau for Private Enterprise should be expanded and given greater senior management support, particularly in areas related to investment, private enterprise development, and trade. PRE is considered by some as an AID appendage, often resisted and even resented by missions and by Washington staff as an organization imposed upon them, an additional unwarranted and unrealistic burden. We recommend that AID significantly increase the PRE budget and staff to increase the momentum of the private sector initiative.

With regard to financial resources, there is a need for a reasonable budgetary target beyond AID's current 1 percent allocation to PRE. (Even with the inclusion of other AID private enterprise projects outside PRE, the total percentage of AID funds allocated to this area is no more than 5 percent.)

With respect to personnel, every AID regional bureau and mission (other than the smallest) should have a private enterprise office, staffed with skilled personnel who develop and manage AID's investment, private enterprise, and trade activities. The great majority of AID missions should have at least one private enterprise specialist and, in the case of the larger missions, a fully staffed office. The importance of private enterprise skills in the work of the mission should be raised to a level equivalent to that of other specialists, such as economists.

Papers Provided to the Task Force

The Hudson Institute
The Changing Worldwide Economic and Political Environment, 1985–2000

The Hudson Institute
The Future of World Economic Development

Daniel Landau
Government and Economic Growth in Lesser Developed Countries

Harald B. Malmgren
Background Paper: Competitive Assessment and Strategic Trade

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Foreign Aid, the Private Sector and Economic Growth

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Agency for International Development Private Enterprise Policy Dialogue: Forms, Experience and Lessons

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Agency for International Development Private Sector Initiatives: Past, Present, and Lessons Learned

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Response to Survey Questionnaire of the President's Task Force on International Private Enterprise

Albert H. Small
The Promotion of International Private Enterprise

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Private Enterprise Development

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Reference Materials

The archives of the President's Task Force on International Private Enterprise consisting of papers, correspondence, meeting transcripts, and summaries are available at:

The Office of Records Management
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A volume of selected papers prepared for the Task Force can be obtained by writing to:

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Index

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