Foreign Aid in the National Interest

Promoting Freedom, Security, and Opportunity

FREEDOM
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OVERVIEW

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Overview

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THE WORLD HAS CHANGED DRAMATICALLY OVER THE past two decades. Of the world's 200 countries in 2001, 124 were democracies—the highest number ever. Nearly 6.0 billion people live in market economies, up from 1.5 billion in 1980. Globalization has integrated the world's markets for goods, services, finance, and ideas. Population growth rates are down, and in most parts of the world health and education have surpassed where the U.S. stood 50 years ago. And remarkable advances in biotechnology are bringing the promise of new cures for the sick and new seeds for the hungry.

But these bright prospects also have dark sides. Many new democracies are fragile, others fake. Many market advances are reversing in stupendous losses of confidence—as with Enron and Argentina. Several billion people remain mired in poverty—and stranded across a gaping digital divide, blind to what could be free for all. Weapons of mass destruction using modern technology could unleash irreversible disasters on people and the planet. And for many people, especially Americans, the terrorist attacks of September 11, 2001, breached the sense of security offered by geography.

In September 2002 President Bush introduced his National Security Strategy. For the first time development has been elevated as the third pillar of U.S. national security, along with defense and diplomacy. Under the leadership of Secretary of State Powell, the U.S. development community is redefining its own strategic priorities to meet this challenge.

These changes have altered the landscape for global development. Within this new landscape U.S. foreign assistance must move in new directions. To inform the debate on future assistance, the U.S. Agency for International Development (USAID) commissioned this analysis of the main trends—and the related challenges—now unfolding. This follows in the tradition established more than a decade ago by then USAID Administrator Alan Woods, whose similar report on development trends changed USAID and the debate on foreign assistance.

The main message of this report: foreign assistance will be a key instrument of foreign policy in the coming decades. The report does not address all the issues of development assistance. Instead, it focuses on six:

- Promoting democratic governance.
- Driving economic growth.
- Improving people's health.
- Mitigating conflict.
- Providing humanitarian aid.
- Accounting for private foreign aid.

Of these six issues, four articulate key development concepts driving the President's proposed Millennium Challenge Account, a major new initiative announced by President Bush in March 2002, just the third major foreign aid policy statement since the second world war. The Millennium Challenge Account is based on the proposition that countries ruling justly, investing in their people, and encouraging economic freedom will receive more U.S. aid.

Around the world one of the most pressing needs is to advance democratic governance—no small task. At a superficial level the state of global democracy appears highly encouraging. Over the past quarter-century democracy has become the world's most common regime. But swirling beneath this expansion is growing disenchantment with political leaders seen by their people as corrupt, self-serving, and unable or unwilling to address economic and social problems. In many developing and postcommunist countries, people are losing confidence not just in elected officials but also in democratic institutions. So, promoting democratic governance must become a higher priority in U.S. foreign aid. Democracy and good governance are required to spur development and reduce poverty in poorly performing countries. It is also vital to U.S. security.

Also essential is boosting economic growth in developing countries. The United States can get global agriculture moving by restoring the budgets of global agricultural research centers, training scientists in basic biology and applied agriculture, and pressing to reduce the damage from industrial countries' agriculture policies. The United States can also promote trade and investment in developing countries by better coordinating its policies and programs. And it can help countries develop their microeconomic agendas, improving the climate for business.

Fundamental to this growth is improving people's health and education. Because of changing demographics, most developing countries will have larger workforces over the next two decades. As a result more resources will be available to invest in economic endeavors. But for that to happen, workers must be productive—and to be productive, they must be healthy. Diseases that cause illness and premature death must be identified, prevented, and

managed—including future health problems, which will be more diverse. If foreign assistance continues to rely on long-standing definitions of public health priorities, it may be unable to address this diversity. Responding to changing health challenges will require different budget allocations and more flexible programs.

Global markets are also changing as developing countries shift from low-cost labor to higher-end manufacturing. That change requires new types of workers, able to learn new skills and use new technologies. A primary school education is no longer enough for workers to take part in the global economy. Moreover, higher degrees—academic and technical—are needed to adapt global technology to local settings and to keep up with new advances. So education systems in developing countries must broaden their sights—and U.S. foreign assistance must offer more support for secondary education for the global marketplace.

Given the devastation caused by conflict, the United States needs to do much more to mitigate it—and when that is not possible, to help manage it. Conflict is the product of deep grievances, political and economic competition, irresponsible political leaders, and weak and unaccountable institutions. It does not occur simply because people are unhappy or greedy, or because a country has the resources to sustain violence. Nor does it happen where all state and social institutions are weak. It happens when causes at multiple levels come together and reinforce each other.

Preventing conflict requires long-term interventions that make states and societies better able to manage tensions. Whatever the causes, a crucial part of the solution is encouraging innovative institutions that can deal with problems—local, regional, and national. The most important principle when designing country programs is to apply a conflict lens to each major area of foreign assistance—from agriculture to economic growth to democracy and governance—and to have each area work in concert.

In the aftermaths of conflict and natural disaster, the United States must continue to provide humanitarian assistance—but much more effectively. The need for humanitarian assistance shows no signs of abating, and new dimensions of disasters will create new demands. Trends indicate a larger, more complex role for humanitarian assistance in the coming decades. The United States, the only national power with truly global reach, has a critical role in addressing current and future trends in disaster assistance. It must project a clear, consistent message about addressing humanitarian needs in conflict settings and reducing vulnerabilities that transform natural and technological events into disasters.

U.S. assistance can do much to shape the 21st century. And as the Millennium Challenge Account ramps up, U.S. official aid is set to rise from $10 billion a year today to $15 billion in 2006 and thereafter. U.S. assistance is generally measured solely as the official development assistance that the government provides through USAID, the Peace Corps, multilateral institutions, and programs sponsored by the State Department and Department of Defense. But many nongovernment sources also provide foreign aid: foundations, corporations, private and voluntary organizations, colleges and universities, religious organizations, and individuals.

All these sources—providing nearly $60 billion a year, or six times the official assistance—must be taken into account to plan aid more effectively. With private assistance predominating, U.S. official assistance will have to develop stronger partnerships with the full array of private sources.

The dominant themes, then, are for foreign assistance to focus on political leadership, on policy, on people, and on partnership. Unless a country's leaders make smart choices for national priorities and show their political will to work with outside donors, development—and development assistance—cannot succeed. Unless sensible policies are put in place, with the rule of law to promote good governance and individual freedom, development cannot be sustained, particularly for agriculture, the engine of growth for most poor countries. Unless countries invest in health and education, people cannot take on the demands of today's competitive workplace, and development cannot even start. And unless the official development community works better with partners, both traditional and new, many development opportunities will be wasted. Too much is at stake in all this. We have to ensure that these themes suffuse the future of foreign assistance—all in the national interest.

Andrew S. Natsios

Andrew S. Natsios
Administrator, USAID

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Promoting Freedom, Security, and Opportunity

Overview

The new century has brought new threats to U.S. security and new challenges and opportunities for the national interest. The terrorist attacks of September 11 tragically demonstrated the character of today's world. Globalization has sent unprecedented flows of people, ideas, goods, and services across borders, fostering growth and expanding democracy. More than ever, U.S. security is bound up with the outside world. And as the world has become more connected, it has become more hazardous. Weapons, germs, drugs, envy, and hate cross borders at accelerating rates. Just as the tools, ideas, and resources for progress can quickly move from industrial to developing countries, many forms of risk and instability can travel in the opposite direction.

When development and governance fail in a country, the consequences engulf entire regions and leap around the world. Terrorism, political violence, civil wars, organized crime, drug trafficking, human trafficking, infectious diseases, environmental crises, refugee flows, and mass migration cascade across the borders of weak states more destructively than ever before. They endanger the security and well-being of all Americans, not just those traveling abroad. Indeed, these unconventional threats may pose the greatest challenge to the national interest in coming decades.

Conventional military force, intelligence gathering and operations, law enforcement, and diplomacy play important roles in containing threats to U.S. security. But these mainly deal with the manifestations of trouble, not the root causes. In countries where government does not advance the common good, ordinary people do not realize the promise of development. Corruption is rampant. The state's capacity is weak. Social services are inadequate. And economic growth is stunted. Economic policies hinder growth while benefiting privileged groups. Investment is scant because property rights are insecure, government is predatory, infrastructure is poor, freedom is compromised, human capital is underdeveloped, and there is little confidence in the future. So, economic development is hard to get going—and impossible to sustain.

These circumstances entrench poverty, nurture injustice, and fuel anger and alienation. People give up on the possibility of collective progress. In different countries and among different types of

Development has densely overlapping economic, social, technological, and political dimensions

people, hopes for development are surrendered in different ways. The surrender may be in crime toward other individuals or in hate and violence toward other ethnic groups. It may be toward the state, in insurgency or revolution, or toward the world's successful countries, in terrorism. The response may simply be to emigrate or flee. Most often, the powerless and suffering simply withdraw from the state and survive as best they can from one day to the next. But surviving on the edge of existence only exposes people to catastrophe when nature or politics takes a downward turn. Even when failing states do not directly threaten the United States, they are humanitarian disasters waiting to happen. Only when countries achieve sustained development can they move beyond a chronic vulnerability to crisis.

Preempting threats and disasters is not the only reason that fostering development is in the U.S. interest. Successful development abroad generates diffuse benefits. It opens new, more dynamic markets for U.S. goods and services. It generates more secure, promising environments for U.S. investment. It creates zones of order and peace where Americans can travel, study, exchange, and do business safely. And it produces allies—countries that share U.S. commitments to economic openness, political freedom, and the rule of law.

Almost all countries with high levels of economic and social development are democracies. Why? Because lawful, accountable, participatory government fosters development—and because prosperous, well-educated people demand political freedom. No two full democracies have ever fought a war with one another. The spread of prosperity and democracy is an important foundation for peace. A free, open, prosperous, lawful world is the kind of world Americans want to live in.

A world where all countries are becoming more prosperous would also be a profound affirmation of U.S. values and ideals. The United States is a nation of immigrants who believe that with energy, ideas, and initiative, anyone can succeed. Americans want to believe that for countries as well as people, progress should not be limited by region or culture, and that the country's founding principles affirming life, liberty, and the pursuit of happiness are universal. For the United States to prosper and be secure, the world must prosper and be secure. Thus the United States must foster development around the world.

What is development? Freedom, security, and opportunity

Freedoms are not only the primary ends of development, they are among its principal means.

—Amartya Sen

Freedom, security, and opportunity are the essence of development. Development gives people freedom to choose. Though few people ever have the luxury of perfect choices, development expands choices for individuals—and for the broadest possible range of individuals in society. Development increases people's opportunities to prosper—to educate themselves, to work and produce, to consume, to travel, to enjoy leisure, and to enhance their health and well-being as they wish, as much as they wish. A truly developed society offers equal opportunity to all its members regardless of their background. And development offers people security—from threats of violence that might come from the state, from conflict, or from other people.

Development has densely overlapping economic, social, technological, and political dimensions. Economically, it involves growth—through increasing productivity—and the capacity to sustain it independently of foreign aid or nonrenewable natural resources. Genuine development requires autonomous engines of growth—market expansion and technological innovation—supported by government but led by private initiative. Since World War II some countries have experienced economic growth that has far outstripped their real level of development. Swimming in waves of income from oil or other natural resources, they have absorbed windfalls of national income without transforming their productive capacities. In most cases these waves of greater income do not last. And when they recede, the country plunges backward. Frequently this unnatural wealth is grossly misused by autocratic, corrupt, or fanatical leaders.

Real development involves accumulating physical and human capital and implementing governance rules and institutions that foster lasting increases in investment, output, and income. The process requires economic freedom, with people able to work, save, invest, and produce based on their own choices rather than government mandates.

Improvements in plants, equipment, and infrastructure raise productive capacity by promoting efficiency and cutting transaction costs. In addition to technology for agricultural and industrial production, these improvements involve roads, bridges, ports, markets, schools, industrial parks, communications, and water and power grids. Without these public goods, bottlenecks raise production and exchange costs and so discourage investment. Building and maintaining public infrastructure is often hugely expensive and vulnerable to corruption. Thus the quality of governance strongly influences the potential for sustainable infrastructure development.

Investments in people—essential for sustainable development—are well suited to the humanitarian imperatives of foreign assistance. Lasting improvements in a country's income-generating capacity require healthy, well-educated, well-trained workforces, with the broadest possible inclusion of people in the full scope of economic opportunity. Poverty—with its links to illiteracy, chronic illness, and shorter life expectancy—is not simply a profound humanitarian concern. It is also an obstacle to economic growth. Yet vigorous, sustained economic growth is required to reduce poverty.

Socially, development improves human capabilities and well-being by reducing poverty, improving health, and expanding education. Absolute poverty—with little or no access to nutrition, sanitation, clothing, and shelter—degrades the human spirit and becomes a vicious circle, blocking acquisition of the physical, social, and cultural attributes needed for a viable income and more dignified life. Robust physical health and vigorous support for public health—as reflected in declining infant and child mortality, control of deadly and disabling diseases, and increasing life expectancy—are ends in themselves. But they are also important for raising productivity, reducing poverty, and sustaining economic growth. Better education also enhances people's income opportunities and raises society's productive capacity and entrepreneurial potential. This is why it is so vital that girls enjoy the same education opportunities as boys—that half of society not be left behind. Educating girls reduces birth rates, results in higher education levels for their children, increases agricultural productivity, and boosts family incomes—four big pluses.

Development affects groups as much as individuals. A crucial dimension of development is the accumulation of social capital—the networks and associations that bring individuals together based on trust, reciprocity, and cooperation for common ends. The deeper are a country's reservoirs of social capital, and the more these are based on equitable relations, the more vigorous is coordination for—and commitment to—the public good. Social capital does more than expand investment and commerce based on trust and predictability. It also stimulates the participation, civic spirit, and respect for law required for political development and good governance.

Politically, a society develops as it institutionalizes choices for its citizens. Among the most important is electoral choice—the ability of citizens to choose and replace their leaders and representatives in regular, free, fair elections. Another is the ability of citizens to choose their political beliefs and interests, express them, and organize around them. These and related dimensions of political freedom and civil liberty complement economic competition and stimulate and deepen political accountability.

50 years of development gains

The development progress in the past half-century has been extraordinary. Developing countries now have an average infant mortality rate (69 for every 1,000 live births) equivalent to what industrial countries had in 1950 (see feature overleaf). In 1951, 40 percent of people in industrial countries had a secondary education; today 50 percent of people in developing countries do.[1] Back then almost 1.8 billion people lived in countries with an average daily intake of less than 2,200 calories; today only 432 million do.[2] Life expectancy and literacy have increased almost everywhere.

Some countries have achieved even more dramatic grains. In the late 1950s the Republic of Korea, Taiwan, and Singapore were all considered economic basket cases. Yet all three have moved from low to high incomes as a result of sustained, rapid economic growth. Malaysia, Thailand, and more recently Indonesia have also made impressive progress. And Mauritius used foreign aid and development assistance to achieve rapid economic and social development,

Better education enhances people's income opportunities and raising society's productive capacity and entrepreneurial potential

Over the past half-century most of the world's people, including the poorest, have seen continual and substantial improvement in their basic living conditions. Developing countries are catching up with industrial countries—particularly in life expectancy, nutrition, and literacy. And in infant mortality and secondary school enrollments they have already reached or surpassed the levels achieved by industrial countries in the early 1950s, when the era of foreign aid began.

Incomes are rising almost everywhere

Per capita GDP is the most widely used measure of well-being in a country (box table 1). But it is an incomplete proxy, because it takes into account only the aspects of life captured by market transactions. So it is inadequate for such aspects as education and life expectancy, which also contribute to welfare. Indeed, most people would probably agree that health, life expectancy, access to learning, and freedom to make one's own choices are more fundamental than income.

Another way to measure well-being (though one that still focuses on income) is to find out how many people live on less than a given income. The World Bank uses $1 a day per person as a rough benchmark to identify the world's poorest people, but only since 1987. A recent study went back farther in time. Its estimates show a rapid decline in the share of the world population living on less than $1 a day—from 55 percent in 1950 to 20 percent in 1998 (box figure 1). Just as striking is the steady decade-by-decade decline. Moreover, the study estimates that in 1900 the share of the world's people living on less than $1 a day was 66 percent, so the reduction in the second half of the century was much more dramatic than that in the first.

Incomes rising everywhere, except in Africa, and too slowly in the former Soviet bloc, the Arab world, and even Latin America

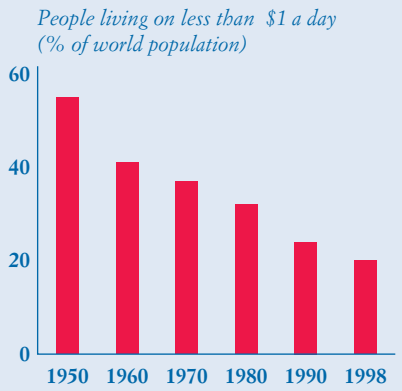
BOX TABLE 1

Growth in real per capita GDP (%)	*Total growth, 1980–2000*
World	29
Industrial countries	52
Developing countries	36
East Asia and Pacific	224
Europe and Central Asia	1
Latin America and the Caribbean	7
Middle East and North Africa	4
South Asia	95
Sub-Saharan Africa	–16

Source: United Nations, Global Population Prospects, 2002.

Steady declines in the proportion of the world's people living on less than $1 a day

BOX FIGURE 1



Source: 1950-80 are from Bourguignon and Morrission 2002 and 1990 and 1998 use the numbers of poor from Ravallion and Chen 2001, and world population from the United Nations World Population estimates.
Note: The main defense for combining the different sources is that the World Bank uses the same combination for a chart (p. 8) in its 2002 publication *Globalization, Growth and Poverty*.

People are living longer—and healthier

Much of the improvement in life expectancy in developing countries comes from the decline in infant mortality, which fell from 158 per 1,000 (meaning that 15.8 percent of babies died within a year of their birth) to 63 between 1970 and 1999. The United Nations projects that infant mortality in these countries will drop to 58 in 2000–05, the same rate prevailing in industrial countries when they began providing assistance to poor countries in 1950–55.

The progress in life expectancy was general. In the early 1950s some 27 percent of the world's people lived in countries where life expectancy averaged less than 40 years. By the end of the century only 0.2 percent lived in the two countries (Rwanda and Sierra Leone) where life expectancy remained that low. And only 4 percent lived in countries where it was less than 50 years—down from 60 percent in 1950–55 (box table 2).

While life expectancy has clearly lengthened, are people healthier? Or has modern medicine simply kept sick people alive longer? Researchers have concluded that health status closely tracks live expectancy. In general, longer lives are healthier lives.

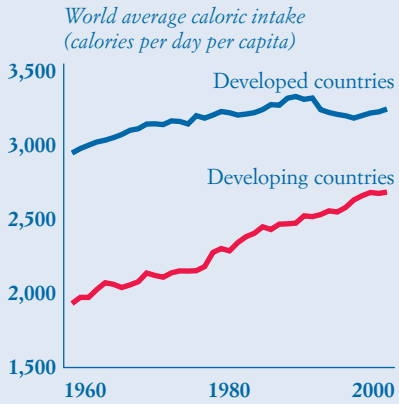
People are eating more—and better

Trends in food and nutrition show a steady improvement since 1961, the earliest year for which comprehensive data are available (box figure 2). Since that year per capita caloric intake has risen worldwide, but much more sharply for developing countries (37 percent) than for industrial (9 percent). Developing countries have clearly been catching up: their average caloric intake rose from 65 percent of industrial countries' in 1961–63 to 83 percent in 1997–99. On past trends, developing countries can be expected to reach the average caloric intake enjoyed by industrial countries in 1961 within a decade—by 2010.

The share of the world's people living in countries where average caloric intake probably falls short of general nutritional

Caloric intake on the rise

BOX FIGURE 2



Source: FAO Agristat database.

adequacy—less than 2,200 calories per person a day—has declined from 57 percent to 7 percent in less than four decades. Meanwhile, the share living in countries where average intake exceeds 2,600 calories a day has risen from 30 percent to 62 percent. But 36 countries still had a per capita intake of less than 2,200 calories in 1997–99—with 24 in Africa, 11 in Asia, and one (Haiti) in Latin America.

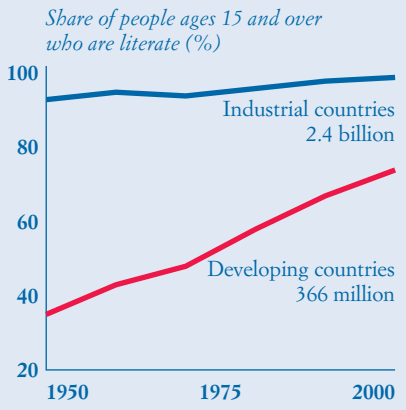
Many more boys and girls are in school

Perhaps the most dramatic change has been the spread of literacy from the elite to the majority. In 1950 only 35 percent of people ages 15 and over in developing countries were literate, but by 2000 this share had more than doubled to 74 percent (box figure 3). The raw numbers are even starker: in 1950, 366 million people in the developing world could read—in 2000, 2.4 billion.

Educating children, not adults, has made most of the difference. Between 1950 and 2000 the number of enrolled students in developing countries jumped from about 100 million to about 1 billion. The growth occurred first at the primary level, where enrollment rose from 38 percent of primary-school-age children in 1950 to 100 percent in 1997. (This does not mean that all children were in school in 1997; in poor education systems older children commonly swell enrollment ratios.)

Many more people can read

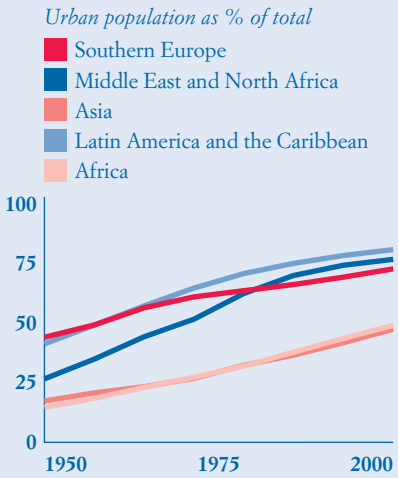
BOX FIGURE 3



Source: UNESCO, Statistical Yearbook (various years) and July 2002 Assessment.

The march into cities continues

BOX FIGURE 4



Source: UNESCO, Statistical Yearbook (various years) and July 2002 Assessment.

Even more dramatic has been the growth in access to secondary education in developing countries. In 1950 high school was the province of a small elite—5 percent of the relevant age group. By 1997, 52 percent of that age group was enrolled—a much higher share than the 40 percent in industrial countries in 1950. Looked at another way, developing countries lag about 40 years behind industrial countries in providing access to secondary education. They reached a secondary enrollment ratio of 50 percent in 1995—industrial countries, in 1955.

More than half the world's people are urban

The world is becoming more urban (box figure 4). By 2000 almost 40 percent of Sub-Saharan Africa's people lived in cities, and about 75 percent of Latin America's. Large nations such as India and China, long considered overwhelmingly rural, have joined the march into cities. In 1950 India had only 17 percent of its people in cities, and China only 12 percent. By 2000 those shares had increased to 28 percent and 32 percent.

Urbanization brings other changes that influence health status. Greater access to education, closer proximity to services, and higher family income can all encourage more—and more informed—use of health care services. But changes in diet and the more sedentary urban lifestyle can lead to new health risks and an increase in non-communicable disease.

Women have many more opportunities

In 1950 women had a lower status and fewer rights than men in most developing countries—because of laws and cultural traditions. By century's end, substantial progress had been made across the board.

- Life expectancy for women, already 2.7 years longer than that for men in 1950, has since increased faster than that for men, with the gap reaching 4.2 years in 1995–2000.
- The gross primary enrollment ratio for girls rose from 56 percent to 95 percent, substantially narrowing the gap with boys' enrollment. Girls' enrollments have risen particularly rapidly (from a low base) in Arab countries. But South Asia lags behind. While in South Asia female secondary enrollments were only 65 percent of male enrollments in 1997, in all other regions they had reached at least 80 percent of male enrollments. At the tertiary level, China and India both lag behind all other developing countries.

And many more people enjoy freedom

Another area of important progress is human freedom. Recall what conditions were like at the beginning of the aid era in 1950. Stalin ruled the Soviet Union and a third of Europe, and Mao ruled China, both maintaining totalitarian governments that rejected individual sovereignty.

Much progress has also been made in the ability of individuals and families to live and work without undue control by government—in large part because representative democracy has become widely accepted as the only legitimate form of political organization.

Source: Fox 2002.

more than tripling its real per capita income between 1970 and 1998.[3]

But many countries remain mired in poverty, and in many African countries per capita incomes have declined since the 1970s. In the 1980s and 1990s economic growth in Sub-Saharan Africa averaged about 2 percent a year—while populations grew by 3–4 percent a year. In 1998 the region's real per capita income was 9 percent lower than in 1970—and in Ghana 16 percent lower, Zambia 41 percent, and Zaire (now the Democratic Republic of Congo) 68 percent.[4]

Free, fair, and competitive elections encourage leaders to govern more effectively, in the public interest

HIV/AIDS is reversing gains in many countries and deepening poverty in others. Around the world some 40 million people are infected—and nearly three-quarters are in Sub-Saharan Africa, which contains just one-tenth of the world's population. In seven Southern African countries—Botswana, Lesotho, Namibia, South Africa, Swaziland, Zambia, and Zimbabwe—more than 20 percent of the population is infected.[5] But the disease is also advancing elsewhere, and is poised to wreak havoc in high-population countries such as China, India, Indonesia, and Russia. The spread of the disease, and the usefulness of technologies and strategies to combat it, will turn on leadership, innovation, and integrated prevention and treatment.

There are many reasons some countries have not made more development progress. But common to almost all of them is bad governance. Rather than being invested in public goods, public resources have been siphoned off by corruption. Kleptocratic leaders have distorted economic incentives, misdirected public investment, and discouraged domestic and foreign investment. Without secure property rights and the rule of law, individuals, communities, and corporations have not had the confidence to risk substantial capital to create wealth. Instead individuals and ruling parties have used their positions to enrich themselves and their families and cronies. Power has been used to distribute opportunities and accumulate personal wealth—not to govern for the common good—creating a zero-sum game in which control of the state means everything. It is easy to see why such societies do not develop—and are prone to violent conflict over control of the state.

Promoting democratic governance

Good governance is perhaps the single most important factor in eradicating poverty and promoting development.

—UN Secretary-General Kofi Annan

Governance is a broad concept, encompassing the capacity of the state, the commitment to the public good, the rule of law, the degree of transparency and accountability, the level of popular participation, and the stock of social capital. Without good governance, it is impossible to foster development. No amount of resources transferred or infrastructure built can compensate for—or survive—bad governance.

Democracy is good for governance

The last quarter of the 20th century witnessed the greatest expansion of democracy in history. If democracy is defined in the minimal sense—as a system of government in which the principal positions of political power are filled through free, fair, and regular elections—about three of every five independent states are democracies today (figures 1, 2, and 3).

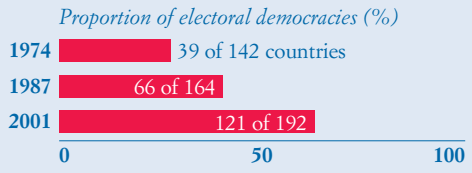
Political parties are among the core elements of democracy. They are the only tested vehicles to structure electoral competition, organize government, and recruit leaders. Yet, almost universally, they stand in disrepute. Their client electorates do not believe they truly represent interests or work for the common good. Instead, parties are often seen as internally authoritarian, corrupt, even venal. Donors often agree—and prefer to work with "purer" actors in civil society. This would be a mistake. Donors need to help reform parties, no less than governmental institutions or NGOs.

Democracy is not strictly essential for good governance. Moreover, bad governance is quite possible under formal democratic structures. But free, fair, and competitive elections do make it possible to remove bad or corrupt political leaders. Thus they encourage leaders to govern more effectively, in the public interest.

Democracy also gives citizens nonelectoral means—associations, movements, the media—to

Electoral democracies more prevalent

FIGURE 1



Note: Data for 2001 are for the end of the calendar year, from the Freedom House survey for that year. Data for 1974 reflect Larry Diamond's estimate of the number of democracies in April 1974, at the inception of the third wave. Data for 1987 are also his estimate.

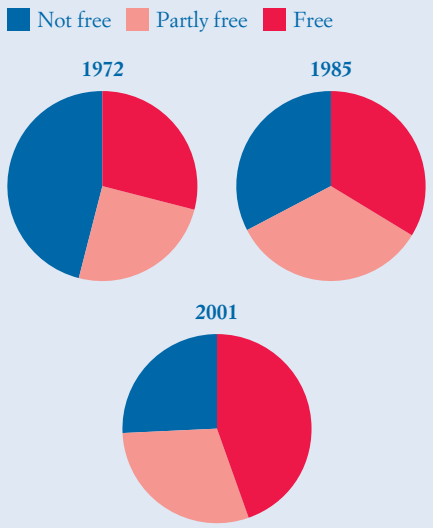
Source: Freedom House 2002.

monitor officials and participate in policymaking. In addition, leaders in democracies have stronger incentives (and more institutional means and obligations) to explain and justify their decisions and to consult a broad range of constituencies before making decisions. Such participation and debate give the public a stronger sense of policy ownership. As a result policies are more sustainable and government is more legitimate.

For these and other reasons it is strongly in the U.S. interest to promote both democracy and good governance. The two are mutually reinforcing: when they develop together, resources are used to advance the public good. Public institutions perform their designated roles. Social consensus supports and stabilizes the system of government. Disputes are settled peacefully. And investment flows into the country, attracted by the

Independent states becoming free

FIGURE 2

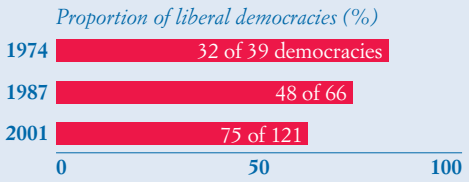


Note: Ratings refer to the status of the countries at the end of the calendar year. See text for an explanation of the basis of the ratings.

Source: Freedom House 2002.

Liberal democracies less prevalent

FIGURE 3



Source: Freedom House 2002.

low transaction costs associated with government transparency and legitimacy and the rule of law. In these circumstances economies grow, human welfare improves, trade expands, political stability and capacity deepen, and countries become more responsible and resourceful members of the international community.

By contrast, when governance is bad and undemocratic—or only superficially democratic—the pathologies of development inevitably have regional and global consequences. Poverty becomes entrenched, reflecting the resources wasted by corruption and distorted investment. Chronic fiscal deficits drain and ultimately drive away international resources. The absence of the rule of law permits—and poverty drives—wanton destruction of the environment and depletion of biodiversity, threatening the global ecological balance (and robbing the world of new medical and agricultural breakthroughs) in ways not fully fathomed.

In the absence of state capacity and will to address public health problems, HIV/AIDS, tuberculosis, and new viruses proliferate, mutate, and cross borders. Venal, unjust regimes fuel antimodernist and religious fundamentalist movements of rage against the West, especially the United States. In the fertile soil of a weak state and feckless legal system, organized crime networks take root, threatening the rule of law internationally through terrorism, piracy, fraud, counterfeiting, kidnapping, money laundering, and trafficking in weapons, drugs, and people.

How can the United States encourage stable, effective democracies? First, the objective must be clear. The goal is not simply to advance democracy around the world. As the collapse of democracy in Pakistan showed in 1999, a country can have competitive national elections and still have governance that fails to generate development and loses public confidence. Nor is the goal simply to promote more capable and transparent

Few leaders can deliver good governance without the institutional accountability to other branches of government and to the people that democracy provides

government. Few leaders can deliver and sustain good governance—with its commitment to promoting the public good and restraining the abuse of power—without the institutional accountability to other branches of government and to the people that democracy provides. Even when nondemocratic leaders are sincerely committed to reform, the absence of institutional mechanisms to monitor and restrain power eventually degrades the quality and legitimacy of governance.

The pursuit of stable, effective democratic governance will involve different sequences of political reform in different countries

These mechanisms include an independent judiciary that enforces clear and predictable laws, an elected parliament that can check the power of the executive, and a civil society that can participate in making and implementing policy. When governance is open to the scrutiny and involvement of a wide range of nongovernmental organizations (NGOs), interest groups, think tanks, and mass media, it is more likely to be transparent, public-spirited, and thus legitimate.

There is no guarantee that electoral democracy will deliver such transparency and inclusion. But it is an illusion to imagine that "liberal autocracy" is a development option in today's world. There are precious few well-governed autocracies, and those that exist (such as Singapore) have sustained good governance for highly idiosyncratic reasons that are not broadly transferable. To develop truly good governance, the typical recipient of U.S. foreign aid needs the openness, competition, and broad and free public participation of democracy.

Different reform sequences for different countries

The pursuit of stable, effective democratic governance will involve different sequences of political reform in different countries (figure 4). In some cases the basic framework for multiparty democracy is in place but needs to be deepened and made more effective and accountable. Some emerging democracies suffer from more specific obstacles, such as institutionalization of the rule of law. And in repressive, corrupt, and closed regimes, multiparty competition—if it exists—is largely a façade. In such countries reforming the economy and strengthening civil society might be more viable in the short term than making an immediate transition to electoral democracy. Another possibility for repressive regimes is to start with elections for local office, the training ground for national politicians.

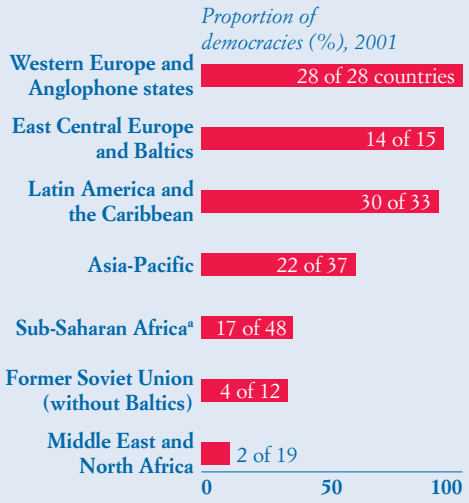
Such variation makes it impossible to offer a general sequence of political reform. Thus democracy and governance must be carefully assessed in each country slated for reform—especially when resources are limited and strategic choices are needed. Moreover, assistance for democracy and governance should be provided with patience and an open mind. No single sector holds the key to fostering democracy and good governance. There is no universal approach, and there are no shortcuts. In most countries lacking stable and effective governance, the United States must be prepared to work on many fronts over long periods.

Strategic priorities

That said, countries that need assistance for democracy and governance tend to share a few priorities. These involve ensuring that democracy advances development and responds to the needs of society—generating capacity for and commitment to using public resources to promote the public good. Such efforts are not new. The foreign assistance community has worked on most of them, particularly over the past decade. What is needed is not invention but innovation, adaptation, refinement, elaboration, deeper commitment, and expansion of activity in some areas.

Democracy is regional

FIGURE 4



a. Excludes Djibouti, Gambia, and Sierra Leone even though Freedom House rates these countries as electoral democracies at the end of 2001. In each case the absence of a free and fair climate for elections—because of fraud, intimidation, or civil war—renders the system less than minimally democratic.

Source: Karatnycky 2002.

Strategic priorities for assistance include:

- Controlling corruption and increasing accountability.
- Strengthening the rule of law and the way it affects individual citizens—not only through the judiciary but also through more professional, vigorous, democratic policing.
- Strengthening and democratizing political parties and deepening their roots in society.
- Helping NGOs committed to democracy and good governance increase their constituencies while using more traditional interest groups to strengthen democracy.
- Developing stronger, more professional states better able to respond to growing public demands for better governance.

Pursuing these priorities requires strengthening links:

- *Across government agencies.* U.S. efforts to strengthen democracy and governance most often fall short because they lack unified support from the entire U.S. government. Such programs cannot succeed if they are inconsistent with U.S. objectives and priorities. It is always difficult to persuade corrupt, undemocratic, or partly democratic regimes to adopt serious governance reforms. But there is no chance of doing so if a regime perceives mixed messages from the U.S. government, whether across agencies or over time. Inconsistency within a region can also generate resentment, confusion, and ambiguity about U.S. aims.
- *Across sectors.* Among the most important lessons of the past decade is that establishing cross-sectoral links—connecting program activities intended to achieve two or more goals—enhances development and amplifies the impact of a given investment. For example, supporting the development of small and medium-size enterprises does more than stimulate and diffuse economic growth. It creates a middle class. And in building up a large class of entrepreneurs independent of the state, it crystallizes interests in better governance, provides new bases for political parties to reach out to these productive interests, and generates new resources to support autonomous interest groups and NGOs. Linking programs for democracy and governance with other programs can thus produce a triple effect. It advances specific aspects of democratic governance. It achieves a more traditional development objective (such as better health care). And it generates additional benefits that neither program could have achieved alone.
- *Over time.* Successful work on democracy and governance requires patience, dedication, and a long-term perspective. The more intractable a country—in the sense of a long history of poverty and weak governance—the longer it will take to turn things around. Development assistance cannot succeed unless it remains engaged in pressing for democratic reforms and assisting forces of reform over an extended period, possibly decades. Significant improvements in governance also require political will. In intractable cases this will take time to generate—and even as it accumulates, it is liable to erode. So, democracy and governance assistance requires engaging the key actors in state and society to develop and sustain the will to reform.

Such assistance also demands tailoring programs to different countries. Some electoral democracies have problems of democratic performance: widespread corruption, judicial inefficacy, weak political parties, human rights abuses, an incompetent state, and in a few cases one-party dominance. The main challenge in these countries is strengthening governance and political representation. About half the countries in which USAID conducts democracy and governance programs fall into this category.

Other countries are quasi-democratic, with ambiguous regimes. In these countries it is not clear if elections are free and fair, or if elected authorities have full power to govern. Competitive, multiparty elections are held, but the contests involve significant fraud or insecurity. And though all the formal institutions of democracy are in place, most function poorly or with constraints. These countries share the program priorities of the first group but also require electoral assistance.

A third group of countries, electoral authoritarian regimes, hold multiparty elections that can even be quite competitive. But the elections are so tainted with fraud and biased toward the ruling party (and typically the incumbent president) that they cannot be considered free or fair. Some of these countries allow serious competition and pluralism not only in elections but also in legislative and judicial systems—which, along with the media, may take steps to erode constraints and induce

Connecting program activities intended to achieve two or more goals enhances development and amplifies the impact of a given investment

accountability. Electoral assistance is a top priority for these more competitive regimes, as is assistance to civil society to intensify demand for reform.

Other electoral authoritarian regimes maintain the façade of multiparty elections but allow little real pluralism or freedom. And when challenged, some of these countries can become brutally repressive. In some cases it may be possible (or strategically wise) to push for genuinely free elections only after other improvements in governance. But in many of these regimes, making elections more credible and fair is vital to preventing violent conflict and securing progress in other areas of governance. In other words, without the uncertainty and incentives generated by true democratic competition, political will for reform is unlikely to emerge.

Levels of foreign assistance must be more clearly tied to development performance

The final group of countries, closed authoritarian regimes, do not hold multiparty elections and generally exhibit extreme political repression and closure. There is little space for opposition or dissent in civil society or the political system. The executive branch and the security apparatus are thoroughly dominant. These regimes fall into two categories: failed states struggling to restore political order and repressive regimes that ban political opposition. In failed states, rebuilding state capacity is essential for improving governance. But without any type of political accountability, participation, consultation, and power sharing, the state is unlikely to gain the legitimacy needed to consolidate peace and establish effective governance. That same is true for states still plagued by civil war or violent conflict.

Among the most urgent challenges for U.S. foreign assistance is how to engage such poor performers. Where political will for reform is lacking, the main thing assistance can do is work with civil society—including NGOs, religious institutions, interest groups, think tanks, and the media—to strengthen constituencies for reform. There may also be reform-minded elements within government who recognize the need for reform but are reluctant to act in isolation. Over the past decade U.S. assistance has helped both groups in several countries. Assistance can enhance actors' understanding of reform issues, knowledge of experiences in other countries, coordination with one another, capacity to analyze and advocate institutional and policy reforms, and mobilization of support and understanding in society. Other external actors can also help tip the balance toward reform through persuasive engagement with a country's rulers and society.

Guiding principles for foreign assistance

The following principles should guide U.S. and other donor efforts to generate home-grown political will for better governance:

- *Levels of foreign assistance must be more clearly tied to development performance* and to demonstrations of political will for reform and good governance.
- *Good performers must be tangibly rewarded.* Reform should be encouraged through predictable and meaningful rewards. When leaders demonstrate respect for democratic procedures and freedoms, and willingness to undertake and follow through on difficult political and economic reforms, they should receive steady increases in aid from the United States and other donors. In addition, good performers—democracies getting serious about controlling corruption and strengthening the rule of law—should be rewarded in other tangible ways: with debt relief, with incentives for foreign investment (including publicity about their good governance), and with trade liberalization—such as the bilateral free trade agreement recently granted to Jordan. It is crucial, though, that increases in development assistance and other economic rewards be contingent on what governments actually do—and keep doing—not what they say they will do.
- *If there is no political commitment to democratic and governance reforms, the United States should suspend government assistance and work only with nongovernmental actors.* USAID has often used such selective suspensions, which can have important symbolic and practical effects. The only exceptions should be for humanitarian relief and responses to global public health threats, and even then minimal reliance should be placed on poorly performing states.
- *The United States should use its voice, vote, and full influence within the World Bank and other multilateral development banks to terminate development assistance to bad governments and to focus on countries with reasonably good governance.* The principles of U.S. foreign policy should extend into international development—meaning that international financial institutions should stop

financing grossly corrupt, wasteful, and oppressive governments. Considerable progress has been made on this front over the past decade, and the United States should continue to press for greater accountability and logic in international lending.

- *The United States must work closer with other bilateral donors to coordinate pressure on bad, recalcitrant governments.* Reductions in U.S. assistance will not do much to change the behavior of political leaders if their governments continue to receive significant aid from other donors. Leaders will be most likely to change if they perceive a consistent message from international donors.

A larger portion of U.S. assistance should be devoted to democracy and governance efforts. In intractable cases the most important thing the United States can do to advance development is help generate the demand for democracy and better governance—by strengthening the capacity of NGOs, interest groups, religious institutions, social movements, the media, universities, and think tanks. Probably no other type of foreign assistance yields such value per dollar.

Driving economic growth

Success in the global economy comes to countries that maintain fiscal discipline, open their borders to trade, privatize inefficient state enterprises, deregulate their domestic markets and invest in the health and education of their people.

—U.S. President George W. Bush

U.S. economic growth has been moderate, averaging only about 1.7 percent a year per person since 1776. But despite a civil war and periodic recessions, it has been continual. Over 225 years, average annual growth of 1.7 percent means a 44-fold increase in per capita income.[6] So the miracle of high U.S. living standards has been persistence, not speed. And it has been the result of strong institutions and sound economic governance that permit individuals to become a bit more productive and a bit wealthier each year, and to be confident that the fruits of their efforts will not be arbitrarily taken from them.

One of the biggest challenges facing developing countries is to sustain growth-promoting conditions over a long period, because a growing economy offers the only long-run hope for reducing poverty. There is scope for implementing growth policies that benefit poor people. But most developing countries have trouble achieving any type of sustainable growth. At least for the next generation, U.S. strategy for reducing poverty in developing countries must focus on economic growth.

Self-sustaining growth is difficult for developing countries because generating knowledge and developing sophisticated human capital depend at least as much on institutions that protect property rights and ensure low transaction costs as on specialization and trade. No simple alternative has been found to the gradual evolution of such institutions. For many developing countries, the quest for growth remains elusive.[7]

Growth is good for the poor

The importance of market exchange illuminates the role of governance in both causing and alleviating poverty. Bad governance results in poorly defined property rights, high transaction costs, large economic risks, and outright theft. Markets disappear in such environments—and with them poor people's hopes for an escape from poverty.

Other factors affecting poverty are visible but hard to incorporate in general models of development. Cultural and religious values are often high on the list: attitudes, mistrust, traditions, religious outlooks, preferences for leisure, and viewing economic success negatively can impede rapid change. Important research, now under way, will define more precisely the relationship between a country's value system and its level of development. The research suggests how and why value systems evolve—and the measures countries might take to strengthen values that encourage development and alter those that undermine it.[8]

Agricultural growth is even better

In recent years many economists have ignored agriculture, arguing that market forces will favor whatever sectors are appropriate. In addition, agriculture plays a shrinking role as economies make the structural transformation to urban-based activities and to industry and services. But in many economies agriculture connects poor people to economic growth. Most of the world's poor people live in or come from rural areas.

One of the biggest challenges facing developing countries is to sustain growth-promoting conditions over a long period, because a growing economy offers the only long-run hope for reducing poverty

Pursuing agricultural strategies in line with market realities and institutional capabilities would provide many benefits to developing countries

Rising agricultural productivity offers economy-wide benefits, such as making food cheaper for urban residents. Pursuing agricultural strategies in line with market realities and institutional capabilities would provide many benefits to developing countries, including:

- *Access to technology.* For many countries agricultural exports provide the foreign exchange needed to buy foreign technology, mostly machines.
- *Increased capital formation.* Public revenues can be highly productive when invested in public goods and infrastructure that make private investment in agriculture more profitable. If agriculture is more easily taxed than nonagriculture in early stages of development, perhaps through border taxes on exports, it may provide revenue for this important initial stage of public investment.
- *Better social outcomes.* Rural education improves with growth in agricultural productivity and rural incomes. Better education, in turn, can directly increase farm productivity. It can also make moving to cities more economically rewarding for children who leave the farm.

The requirements for agricultural development are well known. Better agricultural technology and adequate prices for farmers lead to profitable farm investments and higher incomes that increase commodity output and lift rural residents out of poverty. As noted, rural education speeds up the process, as does assistance in developing new technology. Successful agriculture requires supportive macroeconomic policies, with low inflation, a stable exchange rate, positive real interest rates, and perhaps some monitoring of short-term capital flows. Extending these policies to trade, getting prices right is important: an open economy with low barriers to internal and external trade should create a level playing field for producers and consumers alike. Improving the rural financial system—so farmers can make long-term investments and to handle savings and remittances—is also essential to successful structural transformation.

But it has to be sustainable

The world's agriculture produces $1.3 trillion a year in food and fiber. Agriculture, forestry, and fishing account for one of every two jobs worldwide and seven of 10 jobs in Sub-Saharan Africa, East Asia, and the Pacific.[9] Maintaining the natural resource base that sustains these jobs is critical in the coming decades.

Environmental degradation of these resources affects both human welfare and the economy. Urban water shortages in China—aggravated by overextraction and pollution of nearby rivers and groundwater sources—cost $11 billion a year in reduced industrial output and afflict nearly half the country's major cities.[10] Commercial cutting of India's forests and their conversion to agriculture have undermined the traditional system of village management of local forests—causing shortages of fuelwood and building materials for many of the 275 million rural Indians who rely on local forest reserves.[11]

As global population and income grow, the demand for food, fuel, fiber, and water will increase. To keep up, agriculture must be put on a sustainable footing. Some 2 billion hectares of arable land have been rendered irreversibly unproductive by soil erosion, salinization, compaction, and depletion of organic matter.[12] An estimated 430 million hectares have been destroyed by erosion alone—nearly a third of currently cultivated cropland.[13] Without conservation, more than 500 million hectares of rainfed cropland may become unproductive over the long term in Asia, Africa, and Latin America.[14]

Government prices and policies are key determinants of how ecosystems are treated. They direct many choices on what to consume and how to manage lands and resources. A farmer deciding what crops to plant and what chemicals to use, or whether to increase cultivated area by clearing adjacent forests, is guided by calculating commodity and pesticide prices as well as other farm costs. Similarly, economic factors drive a developer's choice on where to locate housing or a factory or a fisherman's decision on where to fish.

Good economic governance boosts economic growth

Institutions and rules have to be in place to sustain growth once it starts. To encourage competitive markets, governments must overcome the vestiges of protectionism that stifle market activity and block new entrants into the economy. Good

economic governance, founded on predictable and fair laws, is one way to solve this problem. Since the times of John Locke, economic development has been linked to the protection of individual rights and especially of property.

Good economic governance is the result of strong public institutions, with important roles for individuals, civil society organizations, and business and interest groups. The possibility of developing policies for the public good increases when fairness and equity exist to a reasonable degree and when an open society allows for healthy competition among multiple interests. In many developing countries special interests impede economic activity by marginalizing large and potentially productive segments of society that lack the legal and political means to affect public policy. A lack of transparency in government and absence of equal treatment before the law continue to prevent people from participating constructively in the economy. Democratic processes—with equitable, broad popular participation and transparent laws and regulations—contribute to good governance and sound economic policies, resulting in higher levels of development.

Sound economic governance helps create an environment that encourages private groups and individuals to take risks, invest capital, and export. To encourage exports, governments must, at the very least, provide supportive and predictable laws and regulations. Brazil, the Republic of Korea, and Taiwan show how government policies can support low-cost trade in the transition to export-led growth. The same environment that enables private sector–led growth also encourages foreign direct investment.

More trade and investment mean faster growth

Globalization provides an unprecedented opportunity to direct resources toward development. Over the past 10 years developing countries' trade (exports and imports) has grown from less than $1.9 trillion a year to nearly $4.6 trillion.[15] Private capital flows to these countries have grown even more dramatically: net foreign direct investment rose from $30 billion in 1990 to $188 billion in 1999.[16] Countries that have experienced growth in trade and investment have also achieved faster economic growth.

Globalization and regional integration have benefited countries regardless of their stage of development—but developing countries that have changed conditions and mindsets have gained the most. Among countries that have integrated with global markets, income gaps have shrunk and equality has improved. Countries resistant to globalization or lacking the capacity to foster investment and trade have not fared as well.[17] Countries are better able to enter markets when democracy and the rule of law provide freedom and constrain corruption and monopolistic policies (figure 5).

Institutions and rules have to be in place to sustain growth once it starts

Which countries are the slow integrators—and which, the normal?

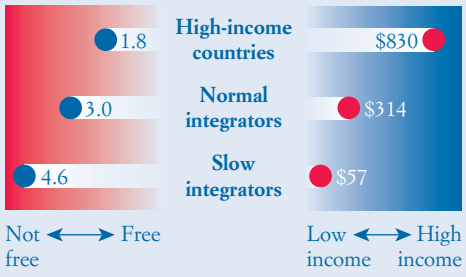
Two indicators show how well countries are integrating:

- The change since 1980 in the share of a country's merchandise trade in GDP indicates the speed of trade integration.
- The share of manufactured exports in a country's merchandise exports in 2000 indicates the depth of trade integration.

Of 111 developing countries, 46 are considered normal integrators and 65 slow integrators.[18] About 90 percent of the least developed countries and 87 percent of low-income countries are slow integrator. In 1999 these countries contained 22 percent of the world's population but accounted for just 9 percent of global GDP and 5 percent of merchandise trade.[19] In Sub-Saharan African 37 countries were slow integrators, with 10 percent of the world's population but only 1 percent of

Freedom means greater integration with global markets

FIGURE 5



Note: Countries classified by USAID. GDP adjusted for purchasing power parity (PPP).
Source: For Freedom House scores, Freedom Foundation; for GDP, World Bank. Hannon and Rhee 2002.

Foreign direct investment is a valuable form of capital because it also transfers production technology, marketing, and management

global GDP. The Middle East, North Africa, and Central Asia also contain many slow integrators.

Among normal integrators annual growth in per capita GDP rose from less than 2 percent in the 1980s to more than 3 percent in the 1990s. But among slow integrators per capita GDP shrank, from –0.5 percent a year in the 1980s to almost –3.0 percent in the 1990s.[20] Differences in global trade and in financial and technological integration are the main reasons for these dramatic gaps.

Most slow integrators desperately need export-oriented foreign direct investment and other types of collaboration with foreign companies. Slow integrators are trying to improve their enabling environments, but potential investors and lenders lack confidence in these countries' capacity to earn foreign exchange and pay back loans. Innovative U.S. assistance could break this vicious cycle, inducing export-oriented foreign investment and other types of foreign collaboration needed to jumpstart nontraditional or manufactured exports.

Improving the climate for foreign investment

Foreign direct investment is a valuable form of capital because it also transfers production technology, marketing, and management. Just as important, that investment is much less vulnerable to investor runs and cross-border contagion than are portfolio investments and bank loans, providing a valuable source of financial stability.

Foreign direct investment has also been a harbinger of globalization. During 1970–86 direct foreign investment flows to developing countries were essentially flat, fluctuating around $11 billion (in 2000 dollars).[21] These figures were small relative to development assistance and other official flows. But by 1999 net foreign direct investment had rocketed to $188 billion, more than three times the official flows (about 20 percent of that foreign direct investment went to China).

Still, in many countries the investment climate continues to be clouded by trade barriers, corruption, and market distortions. Evidence from a large sample of countries suggests that corruption significantly reduces domestic and foreign investment. Leveling the playing field with transparent regulations, predictable laws, and lower trade barriers is necessary to establish a favorable investment climate (figure 6). The environment for foreign direct investment is also directly related to that for private sector development.

U.S. foreign assistance can speed economic growth by providing better access to U.S. markets, encouraging foreign direct investment, and facilitating worker remittances. It can also speed economic growth by:

- Engaging governments in policy dialogues, often with the explicit or implicit promise of greater aid if policy actions are taken. Meaningful policy dialogue requires extensive knowledge of a country's political economy and local capacity for pragmatic policy analysis.
- Producing new knowledge about development through research and project activities. Policy dialogue and knowledge generation should be seen as mirror images that require coordinated, integrated support over long periods.
- Bringing the United States to the table, often in multilateral settings, for diplomatic and trade negotiations. Connecting developing countries to the $10 trillion U.S. economy through trade and investment offers a crucial driver for faster economic growth in developing countries. Because the U.S. government has many agencies with many agendas, an overall policy direction has been missing. Clear guidelines on responsibilities for different aspects of foreign assistance—even narrowly in assistance for economic growth—would be welcomed both in the government and by outside participants.

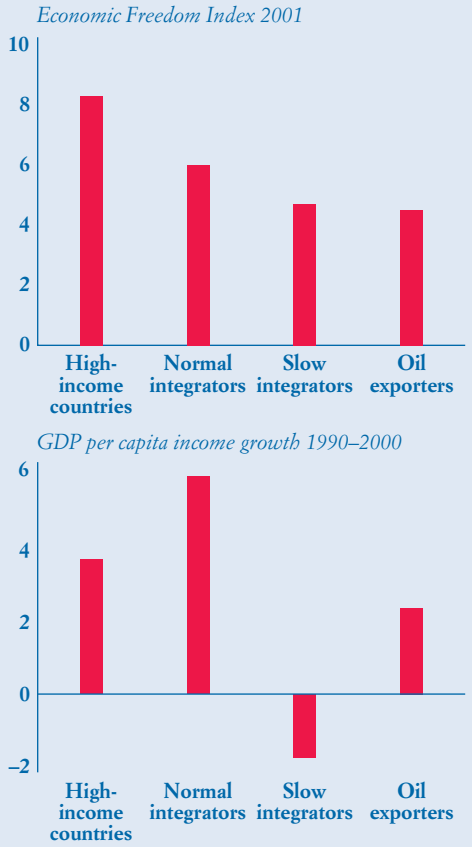
Getting agriculture moving

For decades, there has been no great secret to agricultural development. Better agricultural technology and adequate prices for what farmers produce will lead to profitable farm investments and income streams that simultaneously increase commodity output and lift the rural economy out of poverty. Education of rural inhabitants will speed up the process, as will assistance in the development of new agricultural technology.

Neither the agricultural technology nor the prices in rural markets have been reliable in Sub-Saharan Africa. In Asia success in linking the nontradable sector in rural areas to urban markets

Good investment climate, good growth

FIGURE 6



Source: Heritage Foundation, World Bank, USAID country classifications. Hannon and Rhee 2002.

and labor-intensive export growth has been mixed at best. And in Latin America many of the rural poor have migrated to urban areas—which now account for two-thirds of the population there. Central America and Mexico continue to face acute rural poverty, however, and rural strategies will be needed to reduce it.

The mechanisms for developing technology and providing rural price incentives are no longer as clear as they were in the 1960s. The global agricultural research system has a laudable record of important breakthroughs for many of the world's staple foodcrops. But funding for the system has been threatened as the market prices of these crops dropped to historic lows, under the weight of productivity gains in developing countries and publicly subsidized crop surpluses in rich countries. Biotechnology holds out great promise—largely a product of scientific enterprise, public and private, in rich countries. Already, pest resistance and drought tolerance are being incorporated, using biotechnology, into crops of great importance to poor farmers—cotton, maize, and sweet potatoes. Cost reductions and greater productivity are results that will help keep agriculture moving. Still, few countries have the scientific resources to conduct basic crop research on their own, so a large question looms. Where will agricultural technology come from to feed the additional 3 billion people expected in the next 50 years?

There is an obvious role for the United States in answering this question. First, U.S. leadership can help in restoring budgets of the agricultural research system—and can bring other donors back to the table. Second, our university system is the best in the world at training scientists in basic biology and applied agricultural fields. We have an opportunity to provide the next generation of these scientists for the entire world. Third, we can press for reducing the destructive effect on poor countries of agricultural policies of the industrial countries.

Better agricultural technology and adequate prices for what farmers produce will lead to profitable farm investments

Some place high hopes for solving world market problems in agriculture negotiations at the WTO. But this is likely to be very difficult, as both Europe and Japan are still extremely reluctant to expose their farmers to free markets. But the U.S. Department of Agriculture has taken a clear stance in favor of reduced subsidies and freer trade in agriculture. Its research concludes that removing all forms of agricultural protection and support could raise world prices 12 percent, mostly from removing tariffs. In such a free market U.S. agricultural exports would grow by 19 percent. And removing such distortions would increase global economic welfare by $56 billion annually—about the same amount as all official foreign aid provided by the industrial countries.[22]

Part of the challenge may involve getting U.S. acceptance of agriculture's "multifunctionality" as the basis for domestic policies that have clear social, environmental, or security rationales. The United States joined with other WTO members to launch the Doha Development Agenda that solidified the importance of liberalizing agricultural trade. To be designed are rules that explicitly recognize what functions might be reasonable for agriculture in different countries and at different stages of development. For example, environmental protection would be acceptable for domestic agricultural policies in all countries, whereas policies to stimulate basic grain production to enhance domestic food security would be restricted to countries with limited access to world markets or with poorly developed internal marketing systems.

Wealth is actually created in the microeconomic foundations of the economy, rooted in company operating practices and strategies

Beyond improving the external climate for agriculture, what are the main components of an agricultural strategy and how can the United States help countries develop one? First is a supportive macroeconomic policy, one that yields low inflation, a reasonably stable exchange rate, positive real interest rates, and perhaps some monitoring of short-run capital flows. Second, "getting prices right" extends good macro policy to the trade arena, where an open economy with low barriers to internal and external trade should generate a level playing field for producers and consumers alike. Third, improving the rural financial system will take time but is essential.

None of this is intrinsically difficult, but all of it requires talented policy analysts and government administrators. Training them in U.S. universities and empowering them when they return home is a powerful form of U.S. foreign assistance.

Defining the microeconomic agenda

Much discussion of competitiveness has focused on the macroeconomic, political, and legal circumstances that underpin a successful economy. A stable set of political institutions, a trusted legal context, and sound fiscal and monetary policies contribute greatly to a healthy economy. Macroeconomic conditions provide the opportunity to create wealth but do not by themselves create wealth. Wealth is actually created in the microeconomic foundations of the economy, rooted in company operating practices and strategies as well as in the quality of the inputs, infrastructure, institutions, and array of regulatory and other policies that constitute the business environment in which a nation's firms compete.

Developing countries, again and again, are slowed or paralyzed by microeconomic failures. With global capital markets, countries can engineer spurts of growth through macroeconomic and financial reforms that bring floods of capital and cause the illusion of progress as construction cranes dot the skyline. Such reforms allow countries to exploit current comparative advantages. But unless firms are fundamentally improving their operations and strategies and competition is moving to a higher level, growth through productivity gains will be snuffed out as jobs fail to materialize, wages stagnate, and returns to investment prove disappointing. Capital flows and attention then shift elsewhere. The austerity that results from such cycles is at the core of the backlash against globalization.

The microeconomic foundations of productivity rest on two interrelated areas: the sophistication with which companies or subsidiaries based in the country compete, and the quality of the microeconomic business environment. National productivity is ultimately set by the productivity of a nation's companies. An economy cannot be competitive unless companies operating in it are competitive, whether domestic or subsidiaries of foreign companies. The sophistication of these companies is intertwined with the quality of the national business environment. More sophisticated business strategies require highly skilled people, more information, better infrastructure, advanced institutions, and stronger competitive pressure.

Foreign aid organizations, both public and private, have a distinct role in developing and implementing a developing country's microeconomic agenda. They can bring unique assets to bear that the developing country otherwise would not have access to. Traditionally, foreign donors have provided capital to finance development projects. Often more important, however, is a new type of technical assistance in assessing a country's current competitiveness, in developing the key elements of its microeconomic agenda, in creating measurement tools to track performance, and in setting up institutions for implementation and continuing research on the microeconomic agenda.

This new technical assistance differs from macroeconomic, legal, and financial assistance in a number of crucial ways. The time line between providing the technical assistance and actual changes in behavior and later outcomes is usually much longer than when stabilizing a government's budget or fixing the exchange rate by government fiat. Microeconomic reform requires permanent, stable changes of many interrelated policies. These policy changes filter through to changes in companies' behavior and expectations. Over time, they finally show up in the outcomes if policy makers have kept course. Microeconomic reform is a marathon, not a sprint.

The new technical assistance also requires the cooperation of a large number of participants. It has to include private companies, both domestic and foreign-owned, in assessing the current competitiveness of a location and in implementing changes to upgrade. It has to include non-profit, educational, research and trade organizations to

organize the collective action of individuals and companies and to implement measures to change the business environment. It has to include many different functional and regional parts of government, stretching beyond the traditional focus on the leadership of national ministries.

Finally, the new technical assistance needs to define clusters and regions within a country as their primary unit of action rather than industries and nations. Clusters go beyond individual industries, which on their own control only a subset of the factors that drive their economic performance. And clusters are narrower than large sectors like manufacturing, which are too diverse to allow the development of policies that can make a material difference. Regions control many of the microeconomic business environment conditions that determine the ability of companies to operate productively. And regions differ significantly in their current competitiveness and thus require unique efforts to address their weaknesses. The national level, however, continues to be critical to provide the basic macroeconomic, legal, political, and social conditions that set the stage for microeconomic competitiveness.

On a very basic level, U.S. policies for foreign assistance should meet two practical tests:

- Does the activity upgrade elements of the business environment most critical to development in a particular country?
- What is the distinct advantage to the U.S. in performing this specific activity to upgrade the business environment?

Jump-starting the slow integrators

Most slow integrators desperately need export-oriented foreign direct investment and other types of collaboration with foreign enterprises. These slow integrators are making efforts to improve their enabling environment. Yet potential investors and lenders lack confidence in these countries' capacity to earn foreign exchange and pay back foreign loans, stemming from slow integration into the global economy.

Innovative approaches to U.S. assistance strategies can break this vicious cycle. Foreign economic assistance could play a catalytic role in inducing export-oriented FDI and other types of foreign enterprise collaboration needed to jump-start nontraditional or manufactured exports.

As many now agree, globalization is good for development: the countries that have benefited have been the poorer ones, the ones with the most to gain. What can U.S. foreign economic assistance supply? Much, but only with more effective coordination of policy and program development by U.S. government agencies, and departments. The private sector, which has already done so much to promote development, must also be treated as a partner in the difficult task of building the capacity of countries seeking to globalize. Alleviating poverty and creating opportunities for countries "left out" of globalization's benefits are critical for international security and long-term stability. Only by approaching the process of assistance in this larger and more creative framework of coordination can U.S. foreign economic assistance ensure long-term gains in the process of development.

Foreign economic assistance could play a catalytic role in inducing export-oriented FDI and other types of foreign enterprise collaboration

Investing in people

Investing in people improves the distribution of assets in the early stages of economic growth. For growth to benefit poor people, these investments must include rural schools, primary health clinics, and household food security. In addition, policies that encourage efficient rural financial markets increase poor people's access to capital.

At later stages equitable growth requires providing unskilled and semiskilled workers with opportunities for high school education and on-the-job training (box 2). If such investments are broadly based and of adequate quality, they will keep the distribution of income from becoming highly skewed until well into the development process—leading to the near elimination of absolute poverty. The Republic of Korea and Taiwan managed such investments quite well as they moved into middle-income status. Brazil, the Philippines, and Thailand did not.

Even the poorest countries can set themselves on a fiscally manageable growth path that includes the poor. But that may not occur. Political forces and governance averse to investing in poor people are more likely in countries where poor people's lack of assets keeps them apart from the growth process. But such obstacles provide U.S. assistance with a rationale for investing in the people who those countries' leaders might choose or be forced to ignore. The resulting policy dialogue, and the resources mobilized behind it, could have dramatic effects.

Investing in people improves the distribution of assets in the early stages of economic growth

Box 2. Making education meet the needs of a modern economy

Gross enrollment trends spotlight the education revolution that took place in developing countries after 1960. The World Bank's *World Development Indicators 2002* shows a 104 percent enrollment ratio in low- and middle-income countries in 1998. The gains of the past decades are even more remarkable given the massive increases in population.

But the numbers mask great differences across regions and within countries. Many industrial countries enjoy near universal literacy. But in the Balochistan region of northern Pakistan only 3 percent of women, and only 8 percent of men, were literate in 1990. And in the developing world an estimated 113 million children—one in every five ages 6–11—are not in school, 60 percent of them girls. Girls' enrollments are lowest in Sub-Saharan Africa and South Asia.

The numbers also mask system inefficiencies, such as grade repetition, overage and underage enrollment, and children who enroll but never attend. One in four school-age children drops out of school before completing five years of basic education—but international research suggests that countries may be trapped in low returns to education unless children complete at least five to six years of school.

Masked most by the enrollment numbers: educational quality is often deficient. Education must also be linked to a productive economy. It must provide learning on demand so that workers and citizens can meet the needs of a rapidly changing global economy. Primary education, while providing the basics for lifelong learning, is no longer enough to prepare young people for employment. Secondary education and skills-based learning must now be considered as essential elements in tapping into the global economy—and in building democratic institutions.

Source: USAID staff.

Improving people's health

When it comes to health, developing countries are separating into two groups. In the first, larger group, health care has improved dramatically in recent decades—raising life expectancies, expanding workforces, and reducing deaths from communicable diseases. As a result, by 2020 these countries will have achieved international objectives for basic health indicators. They will have smaller populations under 5, and their median ages will approach those in industrial countries today. Moreover, noncommunicable diseases will be the leading cause of death.[23] But these countries will still have subpopulations with health profiles similar to those in least developed economies. Further, there may be unexpected shocks that could cause countries to regress, such as the HIV/AIDS epidemic, social upheaval, and natural disasters.

In a second, smaller group of developing countries—which includes badly managed economies that have seen little or no growth in recent years—health indicators have stagnated or worsened. Fertility and infant mortality rates are high. Life expectancies are low. And infectious diseases, including HIV/AIDS, are widespread. Though some of these countries are seeing slight improvements in demographics and mortality rates, they will not approach the levels of today's industrial countries by 2020.[24]

These features offer opportunities—and create challenges. In addition to maintaining basic public health services, the first group of countries must decide how to invest in new approaches and technologies. Global health programs can shift their focus from women of reproductive age and children under 5 to entire families, including income earners and elderly dependents. Better health outcomes will require better management of chronic diseases, from prevention through treatment. Sustainable progress in health will require health care institutions with both capital and recurrent financing. And systems will need to respond to rising expectations for health care and to the dominance of private flows in its funding.

In the second group of countries public health interventions will have to remain focused on reproductive and maternal and child health—but, given serious quality problems, must radically revise the strategies used to do so. By 2020 nearly nine of 10 people in this group of countries will be African.[25] New thinking is needed to generate more effective results from global health programs. In addition, consideration must be given to external concerns that affect health outcomes—including income growth, education, water, sanitation, and good governance.

What do these changes mean for foreign assistance?

- Health interventions must encompass a wide range of new approaches and actors. Dealing with local financing institutions, employer benefit plans, and telecommunication networks may be just as important as ministries of health. Increasing both the availability and quality of food will remain critical, but new approaches, such as biofortification of staple crops to enhance their micronutrient content, need to be examined.
- The increase in noncommunicable diseases will be permanent, making health care more expensive. Donors and developing countries must make complementary investments involving all parties—public and private—with vested interests in a country's long-term health status, ultimately aiming for self-reliance.
- Given the rapid and diverse changes in many developing countries, donors must be flexible. Efforts to accelerate the progress of countries suffering from traditional health and disease problems must be combined with programs to help other countries address new challenges.
- Despite 40 years of effort, many countries have extremely high infant mortality and low life expectancy, now affected by high HIV/AIDS rates—suggesting a need to carefully evaluate past public health investments, develop new approaches, and better define the role of the private sector.

Why act on these changes? The impact of the changing disease profile on the economies of these countries, the rising expectations of newly democratic populations for better health care, the expertise and experience of U.S. medical and management organizations to help solve these problems—all argue for transforming U.S. global health portfolios into dynamic investments benefiting everyone.

For both old problems and new, the central concern will be self-reliance—so that economic progress can be tied to progress in public health. A central concern of self-reliance will be financial diversity—including private financing, which already accounts for more than half of health resources in developing countries. Political commitment is also key. For many developing countries, self-reliance in traditional areas such as immunizations is not a matter of inadequate resources but of political will, commitment, and management.

New opportunities—and challenges

New opportunities in global health are a direct result of the changing demographics, epidemiology, and diversity in developing country populations. These opportunities do not imply that humanitarian programs should be eliminated where such needs continue to dominate national landscapes. Nor do they imply that core public health functions dealing with conventional problems are not needed. Indeed, the combination of public and private services is a prerequisite for health progress. But in coming years, where economic progress and democratic governance advance alongside epidemiological change, countries can assume the burden of managing these services.

New opportunities in global health are a direct result of the changing demographics, epidemiology, and diversity in developing country populations

Keeping breadwinners healthy and taking care of parents. With changing age structures, there is opportunity for widening the focus of global health efforts from women of reproductive age and children under 5 to the family—a unit that encompasses both traditional and emerging health concerns.

The number of children under 5 is falling in many developing regions. And at least until 2020, the number of youth will rise. In addition, grandparents and great aunts and uncles will survive middle age.[26] Whether they live independently or with their adult children, their health problems will become a concern for family breadwinners. Thus the health issues of working-age populations will affect family life and economic viability. If both aging dependents and productive breadwinners are chronically ill, a family's future is bleak. Hence the importance of health strategies that aid economic growth.

The near-term challenge is to learn more about families—their problems, their aspirations, and how they are adapting to changing living patterns and health status. How are they allocating their resources to meet changing demands, and how can foreign assistance help that process?

Reexamining financing. The past decade of experimentation with health care financing in developing countries, and equally painful but longer experimentation in the United States, provide a base for exploring new approaches to rising health care costs. Choices will have to be made about public spending, and fresh approaches will be needed to create revenue streams. In young democracies the balance struck between young and old and

Efforts to accelerate the progress of countries suffering from traditional health and disease problems must be combined with programs to help other countries address new challenges

between productive and dependent populations will be a function of what health experts advocate and what people want for themselves. Expectations of health care quality, safety, and service will drive public decisionmaking on health resources. To meet these new demands, governments will have to explore private outsourcing and insurance, as well as pursue greater transparency and better management of service delivery and financing.

One largely unaddressed element is the need for investment in the health industry, for both goods and services. The new epidemiology will require investing in management systems, information systems, technology, provider training, and public education. The public and private capital available for investing in provision—not necessarily bricks and mortar, but start-up costs of new service combinations and organizations—will determine the viability of health sectors in developing countries.

Ensuring quality. Poor-quality health care results in illness and death. It is also a tremendous waste of resources. Higher quality means lower costs. Quality can reduce waste by shortening hospital stays, lowering laboratory test and operating costs, and shifting personnel allocations.[27] For even the poorest countries, such assessments of quality argue for new approaches. And especially for the poorest, they highlight levels of waste that are unsupportable under constrained budgets.

The need to ensure quality is becoming more compelling as epidemiology in most developing countries shifts to chronic and noncommunicable diseases—with longer treatment periods and higher unit costs in both private and public systems. The United States is the world leader in disease management and quality assurance, largely because of national debates over cost containment and health outcomes.[28] These techniques are becoming increasingly refined and practical to transmit to other settings.

Reexamining management systems. Changing disease patterns, broadening demand among aging populations, and rising expectations will make the management of health services more complex. The decentralization of responsibility that often accompanies democratization and economic liberalization also creates new challenges for public health care.

With the increase in private providers and more diverse financing schemes, the role of public health ministries will change from providing services to setting standards and overseeing operations. How well these roles are developed will affect the quality and sustainability of national health systems, public and private. Deeper capacity will be required to manage dispersed health care networks rather than centrally controlled systems.

With the demographic and epidemiological transition, one big management change may be in pharmaceuticals. For many noncommunicable diseases, prevention and treatment are combined. Indeed, many of these diseases entail lifelong pharmaceutical use, unlike communicable ones, with the exception of HIV/AIDS therapies. Rising literacy, education, access to information, and globalization will also spur demand for pharmaceuticals. Given the effectiveness of modern medications, greater access to therapeutics can contribute to a more productive workforce at all ages.

Educating the public. Changing demography, rising urbanization, and spreading literacy may provide opportunities for pursuing more comprehensive approaches to public health education, using new communications technologies. Indeed, such strategies may be essential. Many noncommunicable diseases, especially cardiovascular conditions and cancer, have deep roots in behavior. Encouraging prevention through health-promoting behaviors brings prevention to the forefront for these diseases and can be incorporated into existing primary health care initiatives for infectious diseases.

Research in industrial countries shows that as people age, they begin to be more attentive to health problems and their consequences. The absorptive capacity of the population for health information deepens. Technological innovation will make reaching people easier. Even now, solar-powered, satellite-based internet connectivity is spreading to rural areas in many developing countries.[29] Cell phone penetration is greater than in some areas of the United States.[30] Distance learning methods and technologies are becoming widespread. The evolution of bottom-up wireless mesh routing (Wi-Fi) is rapidly becoming a low-cost method for weaving networks of wireless telecommunications capacity without major investments.[31] The expected extension of such networks into the developing world will significantly increase the capacity to deliver health care messages and consultation to larger populations for lower costs than ever.

Implications for the philosophy and pursuit of foreign assistance

After more than four decades, foreign assistance programs in health—focused largely on public health endeavors aimed at women of reproductive age and children under five—look out on a changed health landscape. Decisions about how to allocate and manage "aid" on that landscape can be guided by various considerations.

First, resources have to confront a growing diversity of complex problems many of which will be more serious. The world is very different from what it was even 20 years ago; it will be even more different 20 years hence. What is striking is the progress, albeit with serious lags in the least developed countries. Entirely new generations of public health problems require entirely new portfolios. Health conditions not previously considered part of a "foreign assistance" portfolio are now worthy of attention. New skills, such as those in health finance and management, become as important as public health credentials.

Second, progress in health will come not just from health programs. Health portfolios must be interdisciplinary, combining the best of health and medical innovation with simultaneous attention to problems as diverse as capital investment capacity, biofortification in agricultural systems to correct micronutrient deficiencies, wireless communication distribution systems, and women's education. This means that portfolios will need to be fairly slim; one cannot undertake multiple complex partnerships in one place (let alone many places) at once. Having limited resources means being selective about investments with an eye to their economic contributions, staying rigorous and brutally honest about measuring impact, and being insistent on the long-term self-reliance of partners.

Third, public health challenges of tomorrow argue for flexibility. There certainly are no longer simple categories of health challenges, if there ever were. Nor are the challenges defined by narrow age categories or by gender. Achieving equality in partnerships means that the United States must have the flexibility to adapt the discussion to priorities as defined by the emerging health conditions. Accelerating the progress of some countries still in the grip of conventional global health and disease problems must be combined with the ability to help other nations address new challenges not conforming to old categories.

Fourth, despite 40 years of effort, health progress in some nations continues to lag behind, with only slow progress projected for the future. Quality, impact, and sustainability have remained elusive. Given the continuing need for future investment in conventional problems, there should be frank and open discussion on new approaches to achieve results. In other quarters, this has been cast as a matter of inadequate international funding.[32] But money is not at the heart of the matter. The partnership dialogue with nations still struggling to make health progress requires exploring and developing entirely new strategies.

The future may thus see major opportunities for a new wave of financing alternatives in the private sector—and for the emergence of service-based commercial lending in health. In the more advanced developing countries, there can be a future in which the health industry is a dynamic force in the economy, creating jobs and accumulating capital.

Health conditions not previously considered part of a "foreign assistance" portfolio are now worthy of attention

Mitigating and managing conflict

Understanding what, if anything, the foreign assistance community can do to help stop a nation's slide to self-destruction is critical. By one count, there were 111 armed conflicts in 74 locations in the 1990s. Of these, 56 were counted as major, armed conflicts, meaning that military casualties exceeded 1,000 battle deaths, either in a year or over the course of the conflict. Although the number of new conflicts has been steadily declining since reaching a peak between 1992 and 1993, many of those that remain—in Afghanistan, Colombia, and Sudan—have become increasingly lethal and durable.[33]

The vast majority of recent conflicts have been internal, characterized by brutality, severity, and socially divisiveness. They cause tremendous human suffering, with a disproportionate share of the costs falling on civilian victims. Before the second World War, the ratio of military to civilian casualties was nine to one. By the close of the 20th century, that ratio had reversed, producing massive and protracted humanitarian crises.[34] Hundreds of thousands have died in direct fighting, with many more forced into refugee states. Fueling religious and ethnic intolerance, these conflicts have led to an enduring climate of hate and fear that can take generations to overcome.

Understanding what, if anything, the foreign assistance community can do to help stop a nation's slide to self-destruction is critical

In addition to the human costs, civil conflict has blunted and reversed prospects for growth, destroyed investments, and caused a dramatic deterioration in the quality of life. Not only has violence taken a serious toll on the economies of countries experiencing conflict, new research demonstrates that the economies of neighboring states and regions also take a serious hit. The financial burden of these wars on the international community is also staggering. In the 1990s the donor community pledged more than $60 billion in aid to assist in the recovery of war-torn countries. World Bank lending for post-conflict recovery alone has increased more than 800 percent. Between 1992 and 1997, peacekeeping expenditures rose by $3 billion, and emergency assistance, largely to conflict affected areas, rose by $33 billion.[35]

In these anarchic and lawless settings, a new breed of conflict entrepreneurs have found sanctuary, and the line between criminal violence and political violence has begun to blur. Transnational criminal organizations, terrorist networks, and local warlords have amassed enormous power and wealth through instability and violence. Indeed, many of the activities these groups engage in—smuggling drugs, trafficking in people, counterfeiting currencies, trading chemical, biological, and nuclear weapons—are easier during conflict and with failed states. To move toward enduring solutions for the problem of mass violence, it is important to understand that violence is not the problem for these groups and individuals—it is the solution, a political and financial step up rather than a step down.

Conflict becomes more likely when causes operate at all of these levels. Clearly, the simple existence of poverty isn't enough. Nor are ethnic divisions. Nor is access to the human and financial resources necessary to sustain violence. These grievances and "conflict" resources are likely to remain latent until political elites see a reason to tap into them to advance a political or economic agenda, often one that serves them more than the group they claim to represent.

Similarly, if there are strong institutions in place that can address grievance or check the behavior of "conflict entrepreneurs," then whatever incentives for violence exist in a society can find legitimate channels of expression or be successfully controlled. External pressures—global markets, transnational weapons flows, criminal networks—can also undermine efforts to keep the peace. But these forces are unlikely to lead to widespread violence unless they resonate in some way with internal causes.

What foreign assistance can do

At a very general level, conflict prevention and management entail a continuum of interventions that have as their primary objective strengthening the capacity of states and societies to sustainably manage sources of tension and strain in their own countries. This will require helping key stakeholders locate and rank the most important causes of conflict exist in their own country. In some places, this may be rural-to-urban migration. In others, communal competition over a dwindling water supply or access to arable land. And in others, still, corruption. Whatever the underlying cause, a critical part of the solution is encouraging the growth of institutions that can craft innovative and participatory solutions to these problems at the local, regional, and national levels.

While there are clusters of fairly distinct activities for short-term and long-term interventions, it is important not to compartmentalize them. Even in the period immediately before and after violence, it is critical that the foreign assistance community continue to encourage the creation of institutions that can address underlying grievances and ambitions. It is also vital that short-term assistance, humanitarian or otherwise, be acutely sensitive to how it feeds into or sustains long-term conflict dynamics, particularly the economic dimensions of violence. Some factors critical in the short-term, such as high levels of youth unemployment, require both long-term and short-term interventions.

Determining where a country falls on the continuum from pre-conflict to post-conflict requires much more sophisticated risk-monitoring systems than most foreign donors currently use. Some early-warning models are being developed to assess risks two or more years out. While these models are not perfect, and certainly cannot predict the outbreak of violence with accuracy, they do a reasonably good job of ranking countries by the probability of violence. In combination with regional expertise, they can help donors identify priority countries and guide decisions about what type of intervention is most necessary at a point in time.

Guiding principles

There are clear limits to what U.S. assistance can do to encourage peace and discourage violence. In severely divided societies, it may be possible to reduce or manage tensions. But it is not possible to eliminate them, and policymakers shouldn't pretend that it is. A durable peace cannot be imposed from abroad. Outside actors can attempt to shift the balance of power between conflicting parties at the margin. They can raise issues that internal actors might not be able to. They can monitor events. And they can bring diplomatic, financial, and military pressure to bear against leaders who are walking down a dangerous path. But conflict is ultimately the product of deep grievance and ambition, reckless leadership, zero-sum competition over political and economic power, weak or unaccountable institutions, and regional and global pressures. What is required is a change in attitudes and power inside a country and the will to address these issues. While a range of policy tools can help in this task, it is important to recognize that most of what we are able to do is at the margins—and will take years to accomplish.

Even within these limits, we need to recognize that U.S. assistance matters a great deal. All aid is political, particularly in countries at high risk for conflict. Foreign assistance is a valuable resource in a resource-poor and highly competitive environment. It feeds into complex internal dynamics and often produces explicitly political results. These results can be positive but—intended or not—they can just as easily be negative. We need to accept and manage the heightened risks in these types of environments. To some extent, this means being more aware of the political aspects of any project and understanding how its design, implementation, and aims may interact with underlying conflict dynamics in a society. It also means consciously attempting to minimize the potential negative consequences of any project. But "doing no harm" does not mean avoiding all action. It means adopting a strategic framework that has an understanding of conflict at its core—and then taking considered risks within that framework.

One of the most important things the foreign assistance community can do is develop a deeper, context-specific understanding of what drives conflict. This will entail a significant investment in research and analysis, both the donor community and in countries where conflict programs are being considered. Much of the success that foreign assistance has been able to claim in the field of health and population, for example, stems from close collaboration between practitioners and researchers. But there is still a strong belief among many development practitioners that conflict is inherently random, driven by passion rather than rational calculation, and not amenable to rigorous analysis or subject to outside influence. There is still a long way to go in conflict research, but scholars have made great strides in uncovering many of the forces that cause and sustain widespread violence.

As important as it is for U.S. assistance agencies to use this research, it is even more critical that they invest in strengthening the capacity of local institutions to conduct research on conflict—and support local discussions about these issues. Unless all the major actors in a society can discuss what they believe to be the central causes of conflict are—it will be extremely difficult to set priorities and devise effective solutions. Drawing in all relevant stakeholders, including the government and the military, has the advantage of gaining consensus on the issues that can be tackled first, and those that are too problematic to take up immediately.

The United States needs to focus as much attention on how to engage or contain groups and individuals who have incentives to participate in violence as on those who are committed to peace. Because of the difficulty of working in environments of conflict, there is a tendency to seek out like-minded human rights organizations, religious groups, and women's groups committed to dialogue and peace. These groups have an important role in the search for solutions, but they have been asked to carry too much of the burden in addressing conflict. The United States also needs to focus on institutions and actors actually driving the violence, whether they are political elites and their followers, religious leaders, or the police.

A cross-sectoral, multi-disciplinary perspective is critical when designing programs in environments of conflict. Every major area focus area in foreign assistance—from economic growth, to agriculture, to democracy and governance—has at least some bearing on the causes of conflict. It is important to apply a conflict lens to each area in high-risk countries, rather than assuming that some areas are more relevant to conflict than

Determining where a country falls on the continuum from pre-conflict to post-conflict requires much more sophisticated risk-monitoring systems

others. This is probably the most important principle to keep in mind when designing a country program.

Providing humanitarian assistance

Humanitarian assistance will remain enormously important for the international community and for the United States

More than three million people lost their lives in the disasters of the 1990s. Conflict-related emergencies were by far the most deadly, with civilians nine times more likely to be killed than the combatants.[36] Natural disasters are statistically less lethal (one-third the number killed in conflict-related emergencies), but they affected seven times as many people over the decade as did conflict.[37]

Reflecting this growing disaster problem and increased awareness, the international community has responded. Between 1990 and 2000 (using 1999 prices and exchange rates), official development assistance (ODA) for humanitarian aid programs grew from just over $2 billion to nearly $6 billion. In most years, the United States was the largest donor of humanitarian assistance by a factor of three to four.[38]

There is no reason to believe that the 1990s disaster pattern was exceptional, with natural disasters being more numerous and affecting more people but conflict-related disasters being more deadly. Natural disasters will likely become even more devastating as populations at risk increase, and the post-cold war world shows little sign of becoming less violent, although the conflicts now are often internal or "intrastate." The trends guarantee that humanitarian assistance will remain enormously important for the international community and for the United States. They also guarantee that the controversies will continue.

Natural disasters

While conflict-related disasters have dominated the funding and focus of much international assistance over the last decade, natural disasters still take a tremendous toll worldwide. They are neither simple nor purely nature-induced, and their devastation in global economic terms and in terms of populations affected far outstrips the damage caused by conflict.[39]

Natural disasters killed or affected an average of 211 million people per year during the 1990s—seven times more than the average of 31 million people killed or affected by conflict.[40] The number of deaths due to natural disasters during the decade—estimated at 665,000—is only one-third of the number estimated killed in conflict. For natural disasters, the lower numbers killed reflect the benefits of early warning and disaster preparedness measures as well as advances in such basic services as clean water and sanitation.[41] The vast majority of those killed in natural disasters occur in countries with low incomes and low levels of human development, reflecting the correlation between poverty and vulnerability.

The rise in number of natural disasters has been meteoric. There were three times as many natural disasters in the 1990s as in the 1960s.[42] While geophysical disasters have remained somewhat steady in number, hydrometeorological disasters have increased dramatically. The period 1991-95 saw three El Niño-Southern Oscillation (ENSO) phenomena, associated with the devastating southern Africa droughts of 1991–92, 1993–94, and 1994–95. In 1997–98, the phenomena again affected temperatures and rainfall patterns around the world. South and Central America had devastating floods and landslides in some areas, drought in others. Southeast Asia had droughts and fires, and East Africa heavy rains and floods.[43]

Humanitarian emergencies in failed and failing states

The defining disaster of the 1990s was conflict-related, and the recent growth in humanitarian aid was largely driven by the devastation in failed and failing states. In the late 1980s five manmade humanitarian emergencies were declared on average each year. In 1990 there were 20. And after reaching a high of 26 in 1994, they averaged 22 a year in the last half of the decade.[44] The majority of were directly related to conflict or severe government repression. Countries from every region made up the list, including Angola, Burundi, Eritrea, Ethiopia, Democratic Republic of Congo, Liberia, Rwanda, Sierra Leone, Somalia, Sudan, Uganda, Indonesia, Afghanistan, North Korea, Bosnia-Herzegovina, Serbia-Montenegro, Tajikistan, Colombia, and Haiti.

By the end of 2000, intrastate conflicts and repression had generated some 14.5 million refugees and asylum seekers worldwide and more than 20 million people displaced within their own

countries.[45] The number of refugees was just below 10 million in 1984, peaked at some 16.3 million in 1993–94, and only then began to decline.[46] Significant refugee repatriations from peace settlements in Namibia, Central America, Cambodia, and Mozambique contributed to the decline. Unfortunately, conflicts in Africa, especially the Great Lakes Region, and elsewhere partially offset these gains. At the end of 2000, Palestinians (4 million), Afghans (3.6 million), and Sudanese (460,000) were the largest refugee populations, more than half the total. Six of the top ten refugee-generating countries were in Africa.[47]

The rise in internally displaced persons has been even more dramatic. From an estimated 1.2 million in 11 countries in 1982, the number rose to 11–14 million in 20 countries in 1986 and to more than 20 million in 40 countries in 1997 (where it remains). Sudan and Angola have most internally displaced people, followed by Colombia and the Democratic Republic of the Congo.[48] This trend reflects the increased number of ongoing internal conflicts. It also reflects improved access to some displaced populations (and more accurate counts) and the world's efforts to limit refugee flows through assistance models that attempt to keep people within their national borders.[49]

Looking ahead

As late as the mid-1980s, only a few pessimists—not well-received—were discussing the potential for religious nationalism, ethnic conflict, and intrastate wars that would, with the demise of the Soviet Union, profoundly affect the world for humanitarian assistance. But we have to look ahead as best we can. Consider the following:

- Economic migrants will continue to swell urban ghettos, many ending up in poor quality housing without water or sanitation and subject to criminal gangs. Flood-induced cholera outbreaks will become more common in urban slums and require emergency responses.
- More people will push into "marginal lands" where human activity has led to deforestation, water shortages, and desertification. Population pressures will continue to force migration to these areas.[50]
- Infectious diseases such as AIDS, tuberculosis, and malaria are emergencies in and of themselves, but they are also deepening the impact of natural disasters and conflict-related crises. HIV/AIDS among drought-affected populations, for example, is leaving many more susceptible to health problems associated with food shortages (and infectious disease) than they might otherwise be. Related illnesses (and death) deeply affect food security and will leave many families less able to fully recover from natural or conflict-related disasters.
- Technological accidents and disasters are projected to increase in both number and severity because of spreading industrialization, aging plants and technologies, declining resources for safety and monitoring, and rising vulnerability caused by ill-informed development decisions (and nondecisions). The consequences of such accidents will not be sensitive to borders and entire regions could well be affected.[51]
- A "domino" or compound effect is also possible whereby a natural disaster triggers a technological event in an urban area, creating unforeseen and uncontrolled population movements and generating conditions for conflict.
- The challenges of meeting needs in current intrastate conflicts remain. While expert opinions vary on whether new intrastate conflicts will erupt, there can be little doubt that some are already intractable and lethal, generating ever-larger numbers of civilian casualties and consequences that are increasingly global in nature.
- The war on terrorism may generate additional intra-state wars or non-military strategies (such as sanctions) that will create new humanitarian assistance requirements.
- Chemical, biological, radiological, nuclear, and explosive disasters loom larger than ever in the post-September 11 world, with still unforeseen implications for humanitarian assistance.

In sum, the need for humanitarian assistance shows no signs of abating, and the new dimensions of disasters will create new exigencies. If anything, the trends indicate an even greater and more complex role for humanitarian assistance in the coming decades. The United States, the one power with truly global reach, has a critical role in addressing current challenges and shaping future trends in disaster assistance.

Complex emergencies and the national interest

There is moral imperative for the United States to take a stand when unimaginable human atrocities

The recent growth in humanitarian aid was largely driven by the devastation in failed and failing states

take place—no matter where. And conflict-related emergencies are, by definition, dangerous to the United States and to global security, as they have clearly destabilized entire regions and proven to be recruiting grounds and safe havens for criminals, extremists, and terrorists.

The war on terrorism's long-term effects on U.S. humanitarian policies are not yet clear. But one can hope that it will generate more interest in addressing festering complex emergencies abroad, avoiding the use of humanitarian aid as a "fig leaf" covering the lack of political or military action. There is danger, however, that the war on terrorism will bring the United States even deeper into the "politics over humanitarianism" realm. Sustained vigilance is now required on the part of U.S. humanitarian officials to ensure that aid is based on need and that resources are not diverted from more acute but less visible emergencies to meet political ends elsewhere.

There is moral imperative for the United States to take a stand when unimaginable human atrocities take place

The U.S. government has improved its assistance operations over the past decade. It must now place special emphasis on the difficult question of protecting war-affected populations, especially the internally displaced. Our commitment to improving the security for relief personnel and for relief goods is clear. Less clear, or at least less reliable, is the commitment to protect the people receiving relief. While traditional discomfort lingers in the humanitarian community over mixing human rights with humanitarian assistance programs, and using military and other types of security forces to enforce protection, the problem of the "well-fed dead" must be faced. A necessary part of addressing the broader protection issue will be a far more rigorous and systematic approach to guarding those internally displaced.

Clear directions

The emerging practices and future trends outlined here point to other clear directions:

- The United States should not only support NGO and UN initiatives to improve standards and accountability. It should also insist on such reforms (and link dollar resources to it), especially in light of sexual misconduct by humanitarian assistance staff in West Africa. Such a strategy should be mirrored by an internal review of accountability measures. The extensive review by the Dutch government of its role at the Srebrenica massacre should be taken to heart.
- The United States should take a stronger leadership role in shaping the practices of developmental relief, breaking from its traditional reluctance to embrace the more political aspects of relief operations. At USAID, the recent creation of a transition assistance office and the incipient birth of a conflict management fund give it greater latitude to experiment with some "nontraditional" approaches and, through its programming, shape the evolution of assistance practices in conflict settings. Support for research, case studies, evaluations, and workshops would help to advance the debate around these important new avenues of aid and expedite progress in improving the overall impact of humanitarian assistance.
- On the development side, the United States should initiate a review of all of its development programs with an eye towards creating a culture of "development for disaster prevention." For much too long, development assistance and programming have been blind to the fact that they have often actually increased vulnerability to disaster, either by ignorance or misinformation.

The full measure of U.S. development assistance—official and private

Heroes. The Mexicans living in the U.S. and sending money to relatives back in Mexico are heroes.

—Adapted from Vicente Fox
President
United States of Mexico

At $9.9 billion, official development assistance accounts for just 17 percent of U.S. assistance to developing countries (table 1). Private international assistance, by contrast, is $33.6 billion—60 percent of the U.S. contribution, and projected to grow to 69 percent by 2010. Every year the publication of the OECD's report on development assistance results in press reports and statements by academics and opinion leaders disparaging America's "stinginess."[52] They assert that U.S. foreign policy will be ineffective without more official development assistance.[53] They claim that U.S. foreign aid programs collapsed after the Cold War.[54] But official development assistance is a limited and outdated way of measuring a

country's giving, and donors should reevaluate it, given the enormous growth in the private sector around the world.

In 2000 the international affairs budget totaled $22.6 billion—so at $9.9 billion, official development assistance accounted for less than half. That official assistance consists primarily of allocations to USAID, the Peace Corps, multilateral institutions, and certain programs sponsored by the State Department and Department of Defense (table 2). The other $12.7 billion spent on international affairs represents all other contributions.

Despite reservations about government aid, Americans have a long tradition of domestic and international generosity. Money finds its way from the United States to developing countries through churches, private charities, foundations, and remittances by U.S. workers to their homelands. In 2000 U.S. universities and colleges gave more to developing countries in foreign scholarships than Australia, Belgium, Norway, Spain, and Switzerland each gave in official development assistance. Remittances from U.S. immigrants to their homelands exceeded official development assistance from Japan—the second largest provider (in dollars) of government aid to developing countries in 2001.[55]

Over the past 25 years U.S. private giving has grown significantly. Churches and other religious congregations initially played the largest role in international giving through relief and humanitarian assistance as well as overseas missions. Then colleges, universities, and foundations began responding to international development needs with scholarships and support for foreign universities and research centers. The number and budgets of private voluntary organizations have also grown as Americans have offered their money and time to international causes. With globalization and changing immigration patterns, U.S. corporations have also increased their philanthropy to developing countries. And U.S. immigrants, many from developing countries, have been sending more and more money back to their homelands.

Although this assistance far surpasses official government aid, the data are weak, and the development community knows little about its nature, flow, and the full amounts involved. Donor agencies understand that private international assistance no longer means only relief efforts or missionaries working in isolated villages. Today, this assistance means dollars transferred directly to Salvadoran families from their relatives in America so that they can buy good healthcare and education. It also means dollars starting up indigenous foundations in Kenya that involve community members in creating grants. The size and the impact of private international giving creates new opportunities for development agencies. By learning more and working with this vast private army for assistance, USAID can enhance its effectiveness and define its comparative advantage and role in the 21st century.

More assistance than meets the eye

TABLE 1

Estimated U.S. international assistance to developing countries, 2000

	US$ billions	Share of total (%)
U.S. official development assistance	9.9	18
All other U.S. government assistance	12.7	22
U.S. private assistance	33.6	60
Foundations	1.5	
Corporations	2.8	
Private voluntary organizations[a]	6.6	
Universities and colleges	1.3	
Religious congregations	3.4	
Individual remittances	18.0	
Total U.S. international assistance	56.2	100

a. Including volunteer time.
Source: OECD 2002; OMB 2002; USAID 2002; various private sources.

Table 3 summarizes all U.S. government international assistance and U.S. private international assistance for 2000, 2005, and 2010. The figure for official development assistance in 2005 does not include additional amounts, still to be decided, for the Millennium Challenge Account, which is to increase that official assistance by $5 billion a year in 2006 and thereafter. Private international giving is not well documented and all categories are underestimated. The table therefore provides a range from the lowest estimates supported by the research to reasonable higher estimates suggested by known gaps in the research. This range of numbers provides a starting point for estimating private international giving.

Foundations. In 1998 all foundations gave an estimated $1.6 billion to international activities, a 66 percent increase from 1994. Since the latest surveys are for 1998, they do not reflect the large international grants by the Bill and Melinda Gates

At $9.9 billion, official development assistance accounts for just 17 percent of U.S. assistance to developing countries. Private international assistance is $33.6 billion or 60 percent of the U.S. contribution

Foundation and by Ted Turner's UN foundation between 1999 and 2001. These two foundations alone give at least $350 million a year to international projects.

Assuming a modest international giving growth rate of 25 percent rather than the robust rate of 66 percent it knew in the 1990s, foundation giving could reach $2.5 billion in 2006 and $3.1 billion in 2010. Foundation reporting is underestimated since not all of the smaller foundations report. In addition, corporate foundations have underreported or not reported at all for surveys. With better data collection, projected levels will be even higher.

Corporations. The full scope of international corporate giving is unknown. It may well be that not even a small portion of it has been captured. Because these expenditures are relatively new and because of different tax, management, and accounting systems overseas, they are difficult to track. The two latest and most complete studies cover only a small sample, with just over 200 companies included in each. In one sample of 209 U.S. companies, only 83 reported making international contributions and only 74 provided more details for the analysis.[56]

The latest survey on international corporate contributions forecasts increases in giving of 1 percent a year. A conservative estimate would mean $3.6 billion in 2005 and $4.6 billion in 2010, an estimate that could perhaps double with better tracking and reporting.

Private and voluntary organizations. PVOs work in some 159 countries in almost all areas of development. The majority work in health, nutrition, and population, with a focus on family planning and child survival. This is followed by community development, food security, food aid, and disaster relief.[57] Of the 436 PVOs registered with USAID, the top 20 each receive above $20 million in grants and contracts. The total came to some $854 million in 2000, 67 percent of PVO funding by USAID. Some of the older, traditional PVOs—such as

Remittances from U.S. immigrants to their homelands exceeded official development assistance

Nearly $23 billion in all: U.S. government international assistance

TABLE 2

Total U.S. government international assistance by agency, classification, and selected programs, 2000

Official development assistance—$9.9 billion	Other government assistance—$12.7 billion
USAID	
Operations	Israel
Development assistance	Newly independent states
Child survival, humanitarian	Eastern Europe and Baltic States
Disaster relief, food aid	
State Department	
Refugees, narcotics	Operations
Asia Foundation	Broadcasting (Voice of America, Radio Marti)
International organizations	Peacekeeping
	Educational and cultural exchanges
	International organizations
	National Endowment for Democracy
Department of Defense	
Humanitarian	Military education and training
Peacekeeping development	Foreign military loans
	Antiterrorism, nonproliferation
Other agencies	
Peace Corps	Export-Import Bank
U.S. Trade and Development Agency	Overseas Private Investment Corporation
Multilateral institutions	Inter-American Foundation
Security assistance (Egypt and others)	

Source: U.S. Office of Management and Budget 2002.

CARE, Catholic Relief Services, World Vision, and Save the Children—receive large private contributions for their domestic and international efforts, ranging from $60 million to more than $380 million.[58]

Assuming increases of 25 percent, PVO private contributions abroad would rise to $5.4 billion in 2005 and $6.8 billion in 2010. Adding the $3.3 billion value of international volunteer time to each of these years would give a total PVO international assistance of $8.7 billion in 2005 and $10.1 billion in 2010.[59]

Colleges and universities. American colleges and universities have played a dominant role in the education of students from developing countries. There were 500,000 foreign students in school year 2000/2001, 3.9 percent of all students enrolled in American colleges and universities. The funding of foreign students increased from $83 million in 1980-81 to $1.3 billion in 2000-01. The percentage of foreign students with U.S. university and college scholarships steadily increased as well, to 20 percent. Funding of foreign students by U.S. universities and colleges doubled between 1996 and 2001. Taking just half this increase would result in $1.7 billion of private funding for foreign scholarships in 2005 and $2.6 billion in 2010.[60]

Religious organizations. International programs in disaster relief, healthcare, agriculture, and education play a large role in the non-secular activities of religious organizations. In a survey of religious congregations, some 74 percent engaged in international activities as one of their top three program areas (health and human services are the other two).[61] Along with corporate contributions, religious international giving is probably the most underestimated of all private giving. With a current figure of $3.4 billion, and assuming a 20 percent increase from the previous survey results, religious giving in 2005 would be $4 billion. In 2010 this could rise to $7 billion.[62]

Personal remittances—staggering. Mexican President Vicente Fox calls them "heroes." Their dollars account for 10 percent of GDP in six Latin American countries and 13 percent in El Salvador alone. They are not presidents of foundations. They are American immigrants sending money back to their hometowns and villages.[63] These personal remittances are a fairly new topic in international development circles.

Much more to come

TABLE 3

Estimated U.S. government and private international assistance to developing countries (US$ billions)

	2000	2005	2010
U.S. official development assistance (ODA)	9.9	10.4	10.9
All other U.S. government assistance	12.7	13.3	14.0
Millennium Challenge Account	n.a.	3.3[a]	5.0
U.S. private assistance (low estimates)	33.6	43.5	55.2
Foundations	1.5	2.5	3.1
Corporations	2.8	3.6	4.6
Private voluntary organizations[b]	7.6	8.7	10.1
Universities and colleges	1.3	1.7	2.6
Religious congregations	3.4	4.0	4.8
Individual remittances	18	23.0	30.0
Total U.S. international assistance	56.2	70.5	84.9
U.S. ODA as % of total	17	15	19
Other U.S. government as % of total	22	20	16
Private as % of total	60	65	65

n.a. Not applicable.
a. Provisional. The Millennium Challenge Account is set to increase U.S. official development assistance by $5 billion a year in 2006 and thereafter.
b. Including volunteer time.

Source: U.S. government and private sources.

Worldwide remittances from immigrant workers more than doubled in the 1990s.[64] In 1989 remittances to all regions of the world were $21 billion (excluding Russia, for which data were not available). By 1999 the total had soared to $50 billion. Latin America claimed the highest amount—$14.5 billion—followed by India's $11.5 billion, the Middle East's $10.4 billion, and Eastern Europe's $6.2 billion. The amount sent to Latin America in 1999 by millions of migrant workers exceeded the financing of USAID and all multilateral lending agencies to the region.

Total personal remittances by immigrants in the United States to developing countries were $18 billion in 2000. Assuming that there is no significant decline in immigration in the medium to long term and that the economy continues to recover in 2002, remittances should continue to grow—but at a slower rate than the 1990s. But even assuming more modest growth rate of 5 percent a year, personal remittances could rise to $23 billion in 2005 and almost $30 billion by 2010.

Americans have not given up on foreign aid. They simply have found new channels to express their compassion for those less fortunate abroad. Eclipsing official government aid is a rising tide of

private giving with significantly lower transaction costs, more client-directed services, and a willingness to cede control to recipients.

The Millennium Challenge Account will increase official development assistance by an estimated $5 billion in 2006 and thereafter

Boosting U.S. official development assistance in coming years will be the increased funding through the Millennium Challenge Account. Announced by President Bush at the InterAmerican Development Bank in March 2002—just before the UN Conference on Financing for Development in Monterrey, Mexico—the core assistance to developing countries will rise by $5 billion a year after three years. This was just the third time in more than 50 years that a U.S. president has proposed a major initiative on foreign assistance. The first was President Truman's, before a joint session of Congress, in what led to the Marshall Plan to lay the foundations for a stable, prosperous, and democratic Europe. The second was President Kennedy's, announcing the creation of the Alliance for Progress, to address the basic needs of people in Latin America.

The Millennium Challenge Account will increase official development assistance by an estimated $5 billion in 2006 and thereafter. It will support reformers and reward good performance. Research shows that in good policy environments, a dollar of aid attracts two dollars in private capital—but that in poor environments, aid drives out private capital and perpetuates failed policies. A guiding principle of the Account is to promote the participation of beneficiaries in program design and implementation, for that is known to increase the prospects for success. Another principle is to broaden today's development partnerships by including more private firms, universities, foundations, and private and voluntary organizations, thus leveraging U.S. official assistance.

Notes

1. World Bank 1999.
2. United Nations 2000. FAO 2000.
3. Van de Walle 2001.
4. Van de Walle 2001.
5. Raymond 2002.
6. Timmer 2002.
7. Easterly 2001.
8. Harrison 2000.
9. World Resources Institute 2001.
10. World Resources Institute 2001.
11. World Resources Institute 2001.
12. World Resources Institute 2001.
13. World Resources Institute 2001.
14. World Resources Institute 2001.
15. USAID 2001.
16. USAID 2001.
17. Dollar and Kraay 2002.
18. Hannon and Rhee 2002. All the developing countries with a population of greater than half million and PPP-adjusted GDP data from 1980 or 1990 were included in the analysis. In addition, 27 high-income countries with a population of more than half million and PPP-adjusted GDP data were classified as developed countries. So the global total in the analysis includes 111 developing countries and 27 developed countries.

According to UN (2001), as of 2001, 49 countries (34 in Africa, 9 in Asia, 1 in Caribbean, and 5 Pacific regions) were designated as the Least Developed Countries (LDCs) that are deemed structurally handicapped in their development process, and in need of the highest consideration from the international community in support of their development efforts. Eleven island countries—population of many of these island countries is less than half million—and 15 land-locked countries are included in the LDC group.

19. See the data annex in Hannon and Rhee 2002.
20. See the data annex in Hannon and Rhee 2002.
21. USAID 2001.
22. USDA 2001.
23. Raymond 2002.
24. Raymond 2002.
25. Raymond 2002.
26. Raymond 2002.
27. Lin (in press); Tavrow and others (in press); Abdallah and others (in press); Reinke (in press); Rafeh and El-Tobgi 1995 and A. K. Rowe and others 2001.
28. This is not to say that quality always drives decision making. The Commonwealth fund surveyed U.S. employers and found that 90 percent of employers ranked price above quality in choosing employee health plans, perhaps, of course, because quality is fairly uniform across providers. See J. S. Scott 1998. For a discussion of the strategies for inserting quality deeply into the motivational structure of future health care financing in the United States in the next two decades see K. Davis and others 2000, pp. 3357–62.
29. Mayur and Daviss 1998.
30. Tri-State Trends 2000.
31. Harmon, A. 2002. "Good (or Unwitting) Neighbors Make for Good Internet Access." *New York Times*. 4 March. Also see Markoff, J. 2002. "The Corner Internet Network vs. the Cellular Giants." *New York Times*. 4 March.
32. WHO 2001. A problem with this work is that it fails to examine marginal costs of extending previously sunk investments in public health. These are likely to be less than average costs. Further, the analysis does not distinguish between the local currency and foreign exchange elements of those costs. The international resource is foreign exchange, not local currency. Hence the only aid-relevant cost issue (even at the margin) is that portion of cost structure that requires convertible currencies. Whether inadequacy of resource flows is an issue, and how big an issue, depends on the nature of this financial analysis.
33. Wallensteen and Sollenberg 2001.
34. Semerad and Hawkins 2001.
35. Semerad and Hawkins 2001.
36. Weiss 1999.
37. IFRC 2001.
38. Randel and German 2002. Official ODA is money given by governments of donor countries who are members of the OECD Development Assistance Committee. They include Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, the UK, the US and the Commission for the European Union. ODA for humanitarian aid includes (but is not limited to) food aid, and aid to refugees abroad and in the donor countries for their first year of assistance. This latter piece distorts the statistics somewhat since some of the funds counted are spent in donor countries. See ODI report for fuller discussion of what

is comprised in the humanitarian assistance statistics.

39. IFRC 2001.
40. IFRC 2001.
41. Abramovitz 2001.
42. OFDA 2000.
43. OFDA 1998.
44. NIC (National Intelligence Council) 1999. NIC used a combination of USAID and UN data. USAID assistance is triggered by a formal "declaration of disaster" by the U.S. Ambassador or the U.S. Department of State. Thus, the reference to "declared" emergencies.
45. USCR (U.S. Committee for Refugees) 2001.
46. NIC 1999.
47. USCR 2001.
48. USCR 2001.
49. Deng and Cohen 1998. p. 3. Consider, for example, Iraq and Bosnia-Herzegovina, where the international community created "safe havens" to protect and aid people within their own countries and limit refugee flows.
50. Kent 1997.
51. Kent 1997.
52. Johnson, Tracy. 2000. "America's Stinginess Is a Problem, Carter Says." *Seattle Post-Intelligencer*. 20 January.
53. Gardner 2000.
54. WHO 2001.
55. IMF 1999 and World Bank 2000.
56. Tillman 2000 and Kao 2001.
57. USAID Private and Voluntary Agencies Financial Statistics Database 2002.
58. Adelman 2002.
59. Adelman 2002.
60. Adelman 2002.
61. Independent Sector 2000.
62. Independent Sector 2002.
63. Bate 2001.
64. IMF 1999; World Bank 2000.

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Foreign assistance will be a key instrument of foreign policy in the coming decades. This report, commissioned by USAID Administrator Andrew S. Natsios, makes that argument while focusing foreign assistance on four dominant themes—political leadership, effective policy, investment in people, and commitment to partnership.

- Unless a country's leaders make smart choices for national priorities and show political will to support meaningful reform, development—and development assistance—cannot succeed.
- Unless sensible policies are put into place to defend good governance and the rule of law, development cannot be sustained. Unless countries invest in health and education, their people cannot compete in today's global marketplace, and development cannot even begin.
- Unless everyone in the development arena works better with partners—both traditional and new, public and private—many development opportunities will be wasted.
- Too much is at stake. Political leadership, effective policy, investment in people, and commitment to partnership must guide the future of foreign assistance—all in the national interest.

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