

REPORT DOCUMENTATION PAGE				Form Approved OMB No. 0704-0188	
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1. REPORT DATE (DD-MM-YYYY) 20-02-2018		2. REPORT TYPE Levy Award Submission		3. DATES COVERED (From - To)	
4. TITLE AND SUBTITLE An Aid Policy for the United States: Increase Connectedness of Democratic States				5a. CONTRACT NUMBER	
				5b. GRANT NUMBER	
				5c. PROGRAM ELEMENT NUMBER	
6. AUTHOR(S) CDR Torrence B. Wilson US Coast Guard				5d. PROJECT NUMBER	
				5e. TASK NUMBER	
				5f. WORK UNIT NUMBER	
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES)				8. PERFORMING ORGANIZATION REPORT NUMBER	
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)				10. SPONSOR/MONITOR'S ACRONYM(S)	
				11. SPONSOR/MONITOR'S REPORT NUMBER(S)	
12. DISTRIBUTION/AVAILABILITY STATEMENT Distribution Statement A: Approved for Public Release					
13. SUPPLEMENTARY NOTES					
14. ABSTRACT US aid could be more carefully spent in the interest of the nation by focusing on the World Economic Forum's (WEF) Twelve Pillars of Competitiveness. This paper examines the pillars with a bias toward connecting developing nations to world trade. Several nations will be briefly examined for possible development aid that would accelerate their economies, driving them up the WEF's development stages. This proposal would focus on nations that are compatible with democratic values in an effort to develop trading partners with fewer ideological conflicts. This essay argues that US foreign aid policy should be solely focused on developing trade infrastructure in nations that are democratic, opening those markets to world trade and developing a worldwide democratic trading bloc.					
15. SUBJECT TERMS World Economic Forum, Connectedness, Foreign Aid Policy					
16. SECURITY CLASSIFICATION OF:			17. LIMITATION OF ABSTRACT	18. NUMBER OF PAGES 13	19a. NAME OF RESPONSIBLE PERSON Torrence B. Wilson
a. REPORT	b. ABSTRACT	c. THIS PAGE			19b. TELEPHONE NUMBER (Include area code) (415) 994-3753

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Adobe Professional 7.0

An Aid Policy for the United States:
Increase Connectedness of Democratic States

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February 20, 2018

Introduction

The United States spends an outsized amount of foreign aid on developing nations that are riddled with corruption. A cursory comparison of the State Department's Foreign Assistance website with the World Economic Forum's (WEF) Global Competitiveness Index reveals a pattern of aid spent on security in nations that divert public funds.¹ Noting that correlation does not imply causation—it could be that these nations need help with security because of their corruption, not necessarily that they are corrupt because of the inflow of foreign aid. Regardless, the result is that public money is getting diverted to private interests at the same time that little progress is made toward security in these developing nations. The American taxpayer may well wonder: where has the money gone?

A focus should be brought to foreign aid in terms of how nations are selected as well as a strict reinterpretation of aid as it relates to national interest. Although national interests admittedly vary with each National Security Strategy (NSS), every NSS places some form of security and economic prosperity near the top of its priorities. This is where foreign aid should be focused. This approach is not meant to return any short-term savings; on the contrary, developing a foreign economy will be more expensive than shoring up their security. However, the long-term return will be in terms of improved trading partners, increased labor depth, and US soft power.

Foreign aid is surprisingly bipartisan. The answer to the taxpayer's question is often simply that foreign aid is cheaper than allowing terrorism to take hold in a developing nation. While this almost certainly true on its face, the developing nations remain "developing" indefinitely, seemingly not lifting themselves out of this cycle. US aid could be more carefully

¹ Klaus Schwab, *Global Competitiveness Report 2017-2018*, Geneva: World Economic Forum, 2017. "Explore Map," Foreign Assistance, <https://www.foreignassistance.gov/explore>.

spent in the interest of the nation by focusing on the WEF's Twelve Pillars of Competitiveness. This paper will examine the pillars with a bias toward connecting developing nations to world trade. Several nations will be briefly examined for possible development aid that would accelerate their economies, driving them up the WEF's development stages. This proposal would focus on nations that are compatible with democratic values in an effort to develop trading partners with fewer ideological conflicts. The United States foreign aid policy should be solely focused on developing trade infrastructure in nations that are democratic, opening those markets to world trade and developing a worldwide democratic trading bloc.

The Competitiveness-Connectivity Nexus

International trade enriches all its parties in aggregate,² but the efficiencies that enable that enrichment create “losers” within one or both nations.³ Erecting barriers to trade will protect jobs in the near term but the inefficiencies created by those barriers will stunt growth for all nations involved.⁴ Nations that choose to break down such barriers face a short-term redistribution of internal wealth. This is one of the primary political hurdles to free trade. Conversely, improving a nation's ability to compete on the world market can ease this burden in the long run. Trade infrastructure achieves this improvement by connecting nations.⁵

The World Economic Forum defines competitiveness as “the set of institutions, policies, and factors that determine the level of productivity of a country.”⁶ This productivity is a predictor of potential prosperity and returns on investment for inflows, ultimately determining the

² Charles J. Wheelan, *Naked Economics*, New York: Norton, 2010, 273.

³ Ibid, 275.

⁴ Ibid, 278.

⁵ Klaus Schwab, *Global Competitiveness Report 2017-2018*, Geneva: World Economic Forum, 2017.

⁶ Ibid.

potential growth for the nation's economy. In order to measure the competitiveness of a nation on the world stage, the WEF has developed Twelve Pillars of Competitiveness, each a composite of several measures, most of which are outside the scope of this paper.

Zeroing in on the second pillar, infrastructure, reveals a series of measures meant to determine the ability of the nation to get goods to market. This pillar is a composite of nine distinct measures including quality of roads, railroads, ports, electricity supply, and telephone lines, among others. This pillar is one of four in the first "subindex" labeled "basic requirements." It is important to note that the infrastructure pillar, as it is meant by the WEF, is more about *trade* infrastructure than clinics and schools, for example. Although buildings are sometimes thought of as infrastructure, these in particular are covered by the health and primary education pillar. A nation that does well in basic requirements may transition out of being a "factor-driven" economy to being "efficiency-driven" wherein there are six more pillars. Competing well in those six pillars may transition a nation into being an "innovation-driven" economy. Here we find the wealthiest nations.

A different, but resonant, perspective on a nation's development is covered by Parag Khanna's book *Connectography*. In it he describes the effect of infrastructure spending as an investment, as opposed to consumption. This, he says, is exactly the type of investment that led to the United States eclipsing Great Britain as a world power in the early twentieth century, the "economic miracle" of Germany in the 1950s, and the rise of the Asian Tigers in the 1970s and 1980s. In each case, infrastructure spending was sustained at 20 to 30 percent of the nation's gross domestic product.⁷ This figure is the proposed target for infrastructure spending for a

⁷ Khanna, Parag. *Connectography*, New York: Random House, 2016, 9.

developing nation. The proposed aid strategy lies at the nexus of global competitiveness, connectedness, and US national interest.

Targeted Aid: Connecting a Nation's Well-being to US Interests

Before making specific aid policy recommendations, it is important to note the importance of US soft power in the context of foreign assistance. Reducing aid to a nation risks losing influence not just in the nation itself, but potentially in the region. It is proposed, however, that the relationship between aid and US influence is complicated. Aid does not directly translate to influence. In fact, Angus Deaton has shown that humanitarian aid, specifically, puts the donor government between the recipient government and their populace.⁸ Conversely, halting aid could be used to rally anti-US sentiment. However, it is difficult to develop and maintain a popular backlash if an economy is improving, which is why a nation's well-being must be an integral part of any investment or change in aid.

Transitioning a nation from being a factor-driven economy to an efficiency-driven economy will have a lasting effect that humanitarian aid alone cannot achieve. Providing temporary relief from poverty is not enough to keep misguided nationalism from being leveraged against US interests. Long term satisfaction of the populace must be established or else popular backlash will return to protectionism,⁹ reducing, if not eliminating, the return on aid investment and harming US interests.

Satisfaction here is a loose construct that Deaton argues to be a composite of many things. He argues that "happiness," a vague notion of well-being, might be a combination of

⁸ Angus Deaton, *The Great Escape: Health, Wealth, and the Origins of Inequality*, Princeton and Oxford: Princeton University Press, 2013.

⁹ Wheelan, *Naked Economics*.

relative equality, health, and education, and is tied closely to a nation's wealth.¹⁰ The relationship between connectedness, competitiveness, and happiness is established through the development of trade infrastructure that leads to improved competitiveness on the global market, improving the GDP and national happiness. No US policy, even foreign aid, should be altruistic. However, developing a nation that is a fruitful trading partner for the US, maintains a positive opinion of the US, and generally rejects US security competitors will serve the Nation's interests.

Policy Recommendation

Having established the link between trade, wealth, happiness, and US interests, certain policy recommendations can be made. Seven principles are proposed:

- Reduce humanitarian aid to democratic nations
- Restrict aid in authoritarian nations to humanitarian aid only
- Develop democratic nations' connectedness
- Restrict USG disaster relief to ad hoc development of logistical network and security
- Eliminate aid to efficiency- and innovation-driven economies
- Focus on trade infrastructure that opens markets to the US and world
- Target infrastructure spending to 20-30 percent of recipient nations' GDP, through a combination of aid, FDI, and a nation's own investments

The foremost recommendation is to reconsider the distribution of foreign aid. Accepting that helping a nation build out its trade infrastructure will accelerate its economy, while humanitarian aid drives a wedge between a nation and its government, a framework for aid distribution becomes clear: help democratic nations build infrastructure and provide

¹⁰ Deaton, *Great Escape*.

humanitarian aid to autocratic nations. That is not to say the United States should turn away from democratic nations in need of humanitarian assistance, especially in the wake of disaster. On the contrary, aid is fungible. Helping a democratic nation build its infrastructure will free up funds for them to provide humanitarian aid themselves.

Many democratic nations will be unable to recover from disaster and US soft power would be diminished through a cold-hearted non-reaction. Fortunately, US non-government organizations are the most charitable on the planet. The fact that they are not tied to the US government is a bonus as they can relieve distress without driving that anti-democratic wedge. The USG's role in disaster should be infrastructure-related. The distribution of food, water, and other supplies after a disaster is a logistical problem at which no NGO excels to the degree the US military does. The USG will still be a player in disaster relief as it opens ports, repairs airstrips, and provides the large platforms required for distribution such as cargo ships, aircraft, and trucks, as well as providing security.

Many nations currently receiving US aid are well developed. These efficiency-driven and innovation-driven economies are capable of competing on the world market without US assistance. The WEF considers them to be upper-tier competitors on the world market precisely because they have met the basic requirements. Aid for them creates competition for the US innovation sectors and undercuts their democratic institutions.

Even after these reductions, a great deal of focus is still required. The final two principles should be coupled. An infrastructure development plan should be developed for nations that are capable of absorbing a supplemental loan, grant, or direct investment equal to 20-30 percent of their GDP. Nations should be also selected for markets that are amenable to US exports and have something the US needs.

Examples

Three examples follow, chosen to show a variety of potential applications. One is chosen as a nation with an innovation-driven economy that would no longer receive aid; another is chosen as a nation in need of, and appears capable of absorbing, external investment; and a final that is a security nightmare that has enough market potential that it might be incentivized to return to democratic norms.

Estonia is an innovation-driven economy according to the WEF. US aid to Estonia has been on the order of \$3.5M over the last several years, reduced most recently to \$1M.¹¹ Despite being the only NATO nation to meet the 2% GDP security requirement, US aid is earmarked to ensure technical compatibility with NATO.¹² Estonia's security situation is notably precarious with Russia violating their "electronic borders." Estonia surely wants nothing more than to remain compatible with NATO and maintain their borders. Cutting Estonia loose from US aid will likely not hurt their security but could harm US-Estonia relations. However, their natural gas market reveals their internal conflict and opportunity. Russia is one of only two trading partners for this significant market.¹³ It is recommended that US aid be replaced with a license to import US natural gas in their extant natural gas infrastructure. They may not choose to use it due to the increased premium, but establishing the ability will increase their connectedness, open the market to the US, and provide them an alternative to buying from their adversary.

Peru is a democratic nation whose economy is currently not capable of completely underwriting its security. Their infrastructure plan was recently announced to increase from 4-5

¹¹ "Estonia," Foreign Assistance, <https://www.foreignassistance.gov/>.

¹² Ibid.

¹³ "Gas Market," *Republic of Estonia Ministry of Economic Affairs and Communications*, <https://www.mkm.ee/en/objectives-activities/energy-sector/gas-market>.

percent of GDP to 6-7 percent.¹⁴ This is a far cry short of the investment that saw the world's richest nations rise to their current status but shows the proper focus. The Peruvian infrastructure gap is estimated to be \$160B but the current plan is only \$60B over four years.¹⁵ For a nation with a GDP of \$192B, spending will need to be closer to \$38B per year. Naturally, the United States cannot, and should not, foot the bill. Opening the Peruvian market to United States investment would not compensate that large of an investment. However, this is a nation with a plan and, despite recent setbacks due to corruption, they are capable of accepting more than the \$50M currently offered in US security aid. Enabling their economy to underwrite their security could one day end the need for any US aid.

Mauritania presents a case where the promise of aid could be used to return a government to democratic norms. Their infrastructure seems purpose-built to support a trade imbalance. The Chinese-built port of Nouakchott serves mostly for imports—driving the trade balance out of Mauritania's favor. The nearby port of Nouadhibou is used for exports, notably of iron and fish, but has not been modernized and interior roads connecting it to the rest of the country are dilapidated.¹⁶ Deaton shows that African incomes are generally tied to commodity prices¹⁷ and it is known that Mauritania has extensive gold and iron reserves.¹⁸ All humanitarian aid is proposed to be cut this year with the remaining \$1.5M going to security.¹⁹ A sole focus on security is to

¹⁴ Jacopo Dettoni, "Afin Chief Draws Up Plan to Close Peru's Infrastructure Gap," <https://www.fdiintelligence.com/Locations/Americas/Peru/Afin-chief-draws-up-plan-to-close-Peru-s-infrastructure-gap>.

¹⁵ "Peru Gov't to Invest US\$60 Bn in Infrastructure Thru 2021," *Andina* (September 7, 2017), <http://andina.pe/ingles/noticia-peru-govt-to-invest-60-bn-in-infrastructure-thru-2021-681320.aspx>.

¹⁶ "Mauritania - Infrastructure, Power, and Communications," *Nations Encyclopedia*, <http://www.nationsencyclopedia.com/economies/Africa/Mauritania-INFRASTRUCTURE-POWER-AND-COMMUNICATIONS.html>.

¹⁷ Deaton, *Great Escape*, 343.

¹⁸ "Mauritania Country Brief." *International Trade Centre*, <http://www.intracen.org/country/mauritania/>.

¹⁹ "Mauritania," Foreign Assistance, <http://www.foreignassistance.gov/>.

treat the symptoms and ignore the disease; indeed, violent extremism is taking root in the Sahel.²⁰ An interim policy of developing the port of Nouakchott and roads connecting it to the mining sites could invigorate the economy and quell the growing inequality. A Public-Private Partnership (PPP) could invite development of the mines. Competing with China's foreign direct investments in Africa as a whole may be politically impossible for the United States, but establishing a profitable foothold seems plausible—especially on the west coast of Africa where China is not currently developing. The United States is the world's largest steel importer. Most steel comes from friendly nations, but a full 9 percent comes from Russia.²¹ Developing a replacement for that, especially as a PPP with US ownership, could be in the Nation's interests. Unfortunately, Mauritania has failed to remain democratic, recently disbanding their high court and senate. Diplomatic outreach could potentially use the promise of foreign direct investment to convince them to return democratic institutions. Short of that, however, and even aid meant for security could be threatened.

Counterarguments

Focusing aid on infrastructure has been tried before. In his seminal work, *The Great Escape*, Angus Deaton builds a comprehensive and thoroughly convincing case against foreign aid. In it he describes foreign aid as a wedge driven between a populace and their government. When a government cannot address the grievances of the people, they will turn to whoever can. Deaton goes so far as to call foreign aid anti-democratic due to the peoples' loss of faith in their

²⁰ Jennifer G. Cooke and Thomas M. Sanderson, "Militancy and the Arc of Instability: Violent Extremism in the Sahel, CSIS Transnational Threats Project and the CSIS Africa Program," Center for Strategic & International Studies, September 2016.

²¹ "Steel Imports Report: United States," *Department of Commerce International Trade Administration* (December, 2017), <https://www.trade.gov/steel/countries/pdfs/imports-us.pdf>.

government when another swoops in to address grievances. Further, he argues that aid is fungible—funds meant for one purpose, even if used for that purpose, free up funds to be used for other purposes. This enables the diversion of funds that is often the foundation of corruption.²²

Included in the examples of foreign aid leading to faltering democracies, he includes an example of infrastructure aid.²³ The infrastructure Deaton is referring to is schools and clinics. As noted previously, the WEF's definition of infrastructure is narrower. Trade infrastructure is fundamentally different in that it accelerates an economy and is more business-facing than public-facing. A business that is globally connected seems more likely to accept improvements to the ports, railways, roads, and communications equipment they use for transactions regardless of the source of aid. Businesses require stability. Any backlash from businesses toward their home government could be ameliorated through improved tax structures, eased bureaucratic regulations, and the reduction of other barriers to trade. In short, businesses are more easily incentivized than the public.

Another counterargument is that aid works the way it is. It only accounts for one percent of US spending, is popular with Americans, satisfies a moral imperative, and is cheaper than fighting terrorists in failed states.²⁴ The most common rebuttal to this argument is known as aid dependency.²⁵ Relatedly, it places the US government between a state and its populace,²⁶ or as

²² Deaton, *Great Escape*, 328.

²³ Ibid.

²⁴ Molli Ferrarello, "What 'America First' Means for US Foreign Aid," *Brookings* (July 27, 2017), <https://www.brookings.edu/blog/brookings-now/2017/07/27/what-america-first-means-for-us-foreign-aid/>.

²⁵ Angelle B. Kwemo, "Making Africa Great again: Reducing Aid Dependency," *Brookings* (April 20, 2017), <https://www.brookings.edu/blog/africa-in-focus/2017/04/20/making-africa-great-again-reducing-aid-dependency/>.

²⁶ Laurence Chandy, Brina Seidel, and Christine Zhang, "Aid Effectiveness in Fragile States: How Bad is it and how can it Improve?" *Brookings* (December 16, 2016), <https://www.brookings.edu/research/aid-effectiveness-in-fragile-states/>.

Deaton puts it, “aid undermines democracy and civic participation.”²⁷ In short, claiming that aid works is simply a status quo argument. Aid does not work the way it is. What works focusing on a nation’s economic engine, but only in nations that are ready to join a rules-based world trade system.²⁸

A final and obvious counterargument is that the Millennium Challenge Corporation seeks to achieve the same ends. This is, in fact, not the case. The MCC does use similar selection criteria by focusing on a range of essentially democratic norms, but the end result is that they intend to develop nations through “country-led implementation” toward a range of ends such as health, water supply, anti-corruptions, and agriculture.²⁹ The proposal here is far more narrowly focused on the kind of connectedness that leads to improved competitiveness on the global markets.

Conclusion

Official aid from the United States should be more closely tied to a narrow definition of vital national interests. Aid is being spent inefficiently. A better, more holistic plan would be to increase connectedness of nations, with a special focus on those nations whose markets are of interest to US businesses and whose governments are compatible with US interests. Focusing efforts on nations who are ready to accept trade-infrastructure development aid and absorb foreign direct investments meant to increase their competitiveness on the world market will do more to lift these nations out of poverty than granting humanitarian aid over the long run.

²⁷ Deaton, *Great Escape*, 352.

²⁸ Souleymane Coulibaly, "Six Steps to Start Changing how Africa does Development," *Brookings* (July 19, 2017), <https://www.brookings.edu/blog/future-development/2017/07/19/six-steps-to-start-changing-how-africa-does-development/>.

²⁹ "About MCC," *Millennium Challenge Corporation*, <https://www.mcc.gov/about>.

Creating democratic, innovation-driven economies for the US to trade with will create a US-aligned economic counterbalance to rising world powers.