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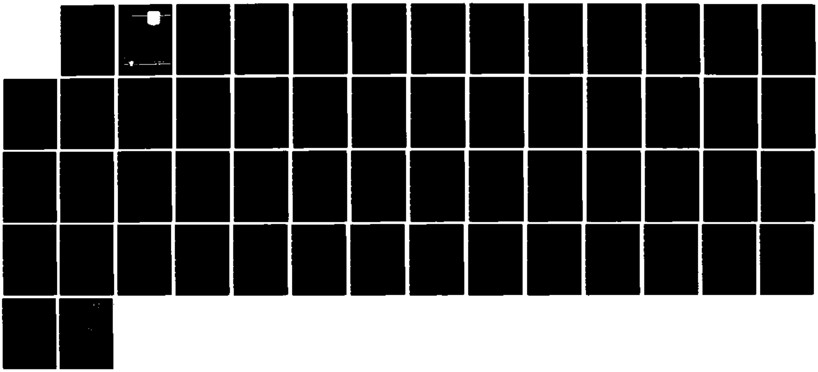

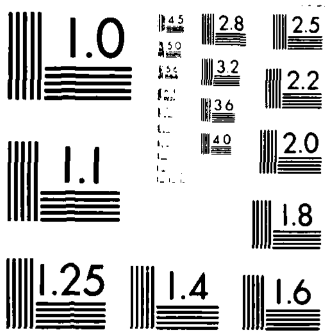

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STUDENT ESSAY

UNITED STATES FOREIGN POLICY RE: THE THIRD WORLD
THE ECONOMIC DIMENSION

BY

LIEUTENANT COLONEL STAN CHERRIE

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ITEM 20 CONT.

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USAWC Military Studies Program Paper

UNITED STATES FOREIGN POLICY RE: THE THIRD WORLD

THE ECONOMIC DIMENSION

by

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6 May 1985

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ABSTRACT

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PREFACE

This individual study project was produced under the aegis of he U.S. Army War College Department of National Security. The scope and general methodology were formulated in agreement with the Chairman of the department, the project adviser, Professor Thad Smith, and the student's faculty adviser Dr. Reed Probst. The paper attempts to crystallize information pertaining to US-Third World economic relations gained in personal research, USAWC lectures, Shippensburg University MPA courses, and the USAWC advanced course programs. Recommendations for foreign policy formulation embody little original thought as a result of an initial lack of knowledge on the topic, however the study offers sound factual (documented) bases for all recommendations.

INTRODUCTION

We as citizens of the United States of America like it or not have been honored or saddled, depending on the point of view, with the mantel of world leadership. Thrust into international prominence after the old World order had been destroyed by two World Wars,[1] the US could no longer afford to adopt a position of isolationism and still ensure that the vital interests of its citizens were met. The World Wars as well as the post war political expansionist threats posed by the Soviet Union left no doubt that the security and welfare of America were greatly affected by the economic and political conditions of the continents that surrounded her.[2]

The realization that as a global power America's security and economic well being were vitally linked and mutually dependent on that of other nations required the US government to formulate a comprehensive foreign policy designed to protect and advance the interests of the United States and its people in international affairs.

As the preeminent world power, America's leadership responsibilities required policies much broader in scope than ever before which affected internal as well as world order affairs. These new, globally oriented policies were shaped by strategic, economic, and humanitarian objectives which would facilitate the attainment of a world wherein all could enjoy peace, prosperity as well as economic and political freedom.[3]

Post war foreign policy formulators soon realized however, that there would be no global "free lunch" in this arena. To enlist the assistance of both developed and developing countries required commitments to a broad band of mutual assistance and security assistance programs designed to assist the lesser developed countries. As a result of the impact of foreign diplomatic, military and especially economic support played in America's struggle for independence,[4] early policy formulators designed policies which provided enormous outpourings of wealth, technology and economic assistance to countries whose mutual friendship we sought.

The roots of our foreign policy development are found in the Lend Lease program. Prior to our entry into WWII the US used its wealth and national resources to support the allies in the fight to defeat Hitler. The emphasis then was primarily aid in the form of money and manufactured goods as opposed to direct (military) security assistance.

The post WWII era spawned the Marshall Plan which again provided economic aid to rebuild the economy of war-torn Europe. Our provision of this mass of economic aid was a direct response to the stimulus provided by the Soviet's threat to exploit Europe's post war economic weaknesses.

In the ensuing years of prosperity, many underdeveloped countries began to voice their acute needs on the International scene.[5] In response to this stimulus, President Truman proposed the Point Four Program, a combination of economic aid and (for the first time) technical assistance, in order to provide for the "improvement and growth of underdeveloped nations."[6]

Shortly after the inception of the Point Four Program, again in response to international stimuli, the policy of granting assistance (foreign aid) again shifted emphasis, this time toward military assistance[7] tailored more toward containing the Soviet Union's expansion along the "rim"[8] of Southwestern Europe than for internal economic development.

During the late 1950's, to ensure the proper balance was stuck between basic military, versus economic assistance, special Congressional committees were formed to study our relations with other countries and how best to support them. These studies concluded that the US had a basic responsibility to continue aid to developing countries,[9] however, it would be "desirable to shift emphasis in the direction of economic assistance whenever and to the maximum extent possible."[10]

Although the recommendations were predominantly in favor of providing economic aid, there was the overriding perception that foreign aid expenditures would continue to be shaped solely by our security goals particularly in Western Europe in response to the threat the Soviet Union posed. As such, the Mutual Security Program, a program which synthesized critical facets of prior aid programs was developed.

Numerous studies, increased publicity of economic theory, and the huge sums of money allocated for foreign aid caused increased public awareness in the programs instituted during this period. For the first time the competing demands of a complimentary economic versus security based aid plan emerged.

On the one hand economists preached the value of foreign capital in assisting countries to reach a "take off" point[11] toward self sustaining growth. This thinking greatly influenced increased allocations of money in the form of aid and grants to developing countries.[12] Later in this same decade with the Vietnam war in full operation, the pendulum then swung toward military assistance as opposed to economic aid.

This brief historical examination of our early foreign policy development demonstrates that it is a dynamic process which is formed in response to international stimuli. This policy must be capable of changing its application or emphasis as deemed necessary to meet the nations security and economic objectives.

Although many stimuli act as bases for foreign policy development the nitude of the Soviet threat causes most Americans to more closely monitor : security aspects of foreign policy particularly as they pertain to the e developed countries. Few people fully understand and even fewer cognize the important economic factors which must be considered in policy velopments.

This dimension of policy formulation was reiterated by the President en he stated:

> "U.S. foreign policy proceeds from two important premises: the need to revitalize the United States and world economy as a basis for the social and economic progress of our own and other nations, and the need to remain strong and safe."[13]

This statement succinctly reaffirms the two primary world interests to hich our policy must be geared and highlights the economic linkages between ations which interact in the worlds economic system.

In order to formulate viable policy options then, it is necessary to nderstand the value of these forces and to determine from whence they ome. Our relationships with other developed industrial countries is well nown, however in the last decade the most rapidly expanding economic links ave been with countries of the Third World.

II. The Third World

In the wake of the worst recession in over forty years, the US has ecovered nicely. Globally however, this recovery has been extremely neven. The well developed, industrialized nations have for the most part eathered the storm rather well. The developing countries however, ustained severe setbacks which may take years to repair.

Many developing countries that had been progressing nicely along the path to economic self-sustainment experienced acute economic problems

It is imperative therefore that we convey to the leaders of these Third ·ld countries we choose to assist that the economic development and social ›gress their countries experience depends totally on the internal official licies they themselves institute with respect to motivating their manpower l their resource utilization.

Our developmental assistance track record has substantially improved er the last decade primarily as a result of increased attention to and alysis of the factors listed above. An examination of the countries that llowed this prescription indicates that they succeeded purely and simply cause they put their developmental goals first and as a result of breaking .to the international market continue to achieve a positive economic growth ıte.[61] Those governments that did not prioritize in this manner however, ıiled in spite of sometime massive transfers of resources from both the ›vernmental and private sectors.

An additional area of concern as regards to Third World domestic :onomic policies lies with those governments which have become economically ɛpressive, that is those who have advocated against free trade, those who ɛek to impose rigid state controls on their economies, and those who impose ɛstrictions to personal choice which are counter producers to economic ɛvelopment.[62]

An example of the dramatic effect restrictive state public policy can ıve on development lies in the area of investment. Although there is but :ant reliable data on private investment for developing countries on which › base an empirical analysis of investment's relationship to economic ɛvelopment, one such study[63] analyzed the interaction of private is-a-vis governmental investment from 1971-1979 and found that:

The most concise analysis that I have found was authored by Peter T. Bauer and Basil Yamey as Chapter 6 in "The Third World: Premises of U.S. Policy." They postulate that natural resources and capital are the primary determinants of economic performance. The Third World as a whole although rich in many strategic raw materials, are relatively poor in both prerequisites. Additionally many Third World countries possess fixed land assets which limits expansion. Thirdly the investment of capital (which most do not have) in long range economic development is a difficult choice to make when faced with the mass poverty that exists. These problems are further exacerbated by an inordinately rapid population growth in most Third World countries.

A cursory glance at these problems might cause one to conclude that the injection of capital into this equation would cure the problem. It was discovered early on in the foreign aid appropriation process however that transferring huge sums of money to struggling economies was not a panacea for development problems.

On the other hand, some hypothesize that economic development is not a solitary economic process[59] but rather one which requires modernization of the entire social structure as the base step. Many sub processes which are "social, ideational, economic and political in nature" requiring total reorganization of thought, changes in patterns of life, etc, must proceed attempts to instantly improve the economy.

The citizens of these countries themselves must be convinced and committed to the developmental process. They must willingly be amenable to trade leisure for work, clear land beyond that needed for their own existence, channel their money or a portion thereof to instruments of production not solely towards durable consumer goods.[60]

Finally, requiring the recipient government to reach agreement on overall development goals before aid is extended[56] improves the fiscal accountability of funds and increases the probability of attaining reasonable goals.

The Third World Domestic Economic Policy Issue

Earlier in this essay I recommended that countries receiving aid meet certain conditions. These were not merely arbitrary but based on past history. They were designed to ensure that developing countries were from the very start on the proper path to development. To date, however, the current Administration has not formulated such conditions into an economic strategy for dealing with the Third World. The real world exigencies of budgetary restraint has caused a serious disconnect between the vital economic interests the U.S. has in these countries and the priority policymakers put on them.[57]

In the absence of such a strategy I have examined the literature and extracted those conditions which I feel Third World countries must meet, the actions they must take and the part we must play in order for full scale development to take place.

The goal that we as an assisting nation desire in developing countries is to generate an expanding economy that is capable of entering the world market. Developing such an economy fosters external commercial contacts which in turn expands worker's choices and opportunities. Simultaneously it provides increased outlets for their goods as well as improved access to sources of materials for their production.[58] How then do we best assist these countries in attaining this level of economic synergism? In order to prescribe a solution we first must have an understanding of the problem.

commitment (re. GNP) more than any industrialized nation.[49] Refusal to accept the United Nations target of .7 has caused serious doubt of our concern and resolve for aiding developing countries.[50]

The existing political climate which is generally unfavorable to unconditional aid, caused a reduction in IDA support of 25 percent. The $250 million wasn't the core issue. The fact that the other 33 nations (by agreement) followed suit completely ruined a planned $16 billion IDA proposed budget (reduced to $9 billion) throwing their economics into a tailspin.[51] Negative support of the International Fund for Agriculture Development has the potential for a similarly disastrous effects of causing other nations to follow suit.[52]

In an age of enormous deficits and public outrage over severely restrained spending for domestic social programs, it would be unwise and politically unsound to recommend, a full scale return to programs expanding as they existed in the 1960's and 70's, however on the other hand our aid policy must not stagnate either.

In order to maximize the benefits that accrue to a strong economic aid and financial assistance package immediate improvement must be made in the areas of aid administration, public awareness and participative management with the aided country in developing realistic aid goals.

We must minimize favors to appease special friends[53] on order to increase the aid based on the economic merit of its need. Aid must be tailored country by country with only the most important projects with the greatest financial impact to be funded.[54]

Encouraging public officials and business personnel to provide input to Congress on the importance of economic aid to the economic welfare of the U.S.[55] is critically necessary if aid levels are to be met.

foreign countries to meet debt payments due to reduced IDA funding has reduced their imports from the U.S. thereby causing a negative impact on our economy; reduced manufacturing for export has likewise exacerbated the unemployment situation in the U.S.

These policies have had a much more pronounced global effect, since reduced participation in the lending banks has all but arrested growth in many countries that had been progressing at an acceptable rate.[46] This arrest of growth rate deprives basic needs leading to political unrest, and mistrust of the system that heretofore had been amenable to supporting the public.

Perhaps the most serious effect of our reduced participation in economic aid programs is the potential disruption of the world's trade and monetary system. President Reagan echoed a fear of the effects of reduced participation in the International Monetary Fund when he imparted:

> "At the end of this road could be a major disruption of the entire world trading and financial systems -- an economic nightmare that could plague generations to come."[47]

Reduced lending also prohibits foreign debt repayment, reduces the creditworthiness of developing countries and reduces their productive capacity (exports) and ability to buy (imports) lending to a total imbalance in world trade.[48]

Added to these serious effects are the loss of international prestige and faith in America as a world leader. Although the U.S. is still the world's leading aid supplier in total dollar amount, it has continued to give less and less of its GNP to aid. Since 1976 the U.S. has decreased its aid

Despite the Vietnam war the recommendations for and allocations of economic aid and financial funds continued at a reasonable level until 1982. During that year the pendulum swung toward security assistance as congressional leaders recanted and in an attempt to rejuvenate the Foreign Aid program voted to increase security assistance funding[37] at the expense, however, of funding for economic aid and financial assistance appropriations.

Recent indicators of decreased support for economic aid abound. Reductions in contributions to multilateral lending institutions such as IDA (by extending the number of years payments are to be made),[38] an inconsistent support of the IMF by the U.S.;[39] the drastic negative trend in economic aid as a function of GDP since 1976;[40] a 25 percent decrease in contributions to IDA (commitment $1 billion);[41] negative response to the U.N. resolution to provide .7 percent of GNP as aid;[42] and the refusal to honor the pledge of $180 million dollars in aid to International fund for Agriculture Development[43] are but a few indicators.

Was this trend in the best interest of our country? The preponderance of opinion barometers indicate that the increased emphasis being placed on security assistance was and is unwarranted, unwise and unpopular. Polls of public opinion taken in April of 1984 indicate that only 30 percent of the population favors military assistance in foreign affairs.[44]

Although there are cogent domestic fiscal needs that account for the reduced Congressional support of our economic aid programs, this reduction is not without serious consequences. For example reduced participation in the multilateral lending institutions has had an indirect impact on the U.S. economy. As a result of reduced support to foreign countries, multi-national corporation development has been arrested;[45] inability of

Security Interests

Although the security aspects of our foreign policy are met primarily as a result of support rendered under the auspices of the Security Assistance Program, economic aid programs are also important and in the words of President Reagan are "complimentary, natural, and necessary allies" of security assistance which afford the opportunity for internal development while meeting the basic needs of the population.[33]

An analysis published by the National Chamber of Commerce of the U.S. on foreign aid describes this bond between security assistance and economic aid programs extremely well. The analysis hypothesizes that the less developed areas of the world may, in fact, hold the balance of world power between democracy and communism.[34] As such, the millions who are struggling with poverty and undesirable living conditions have become a political issue of global importance. Offering supplication to these emerging nations in the form of U.S. economic aid (PL 480 Food, IDA loans, etc.) has the enormous potential to illustrate to them that they can achieve economic improvement through free institutions rathern than through communist methods.

Current Trends

An examination of the budgetary trends during the 1960's and 70's reveals a U.S. budgeting program skewed toward economic aid and financial assistance (Vietnam discounted) with aid granted in the form of country specific as opposed to earlier classifications of loans.[35]

The 1970's brought much criticism to our economic aid program. The inability to win quickly in Vietnam despite billions of dollars of aid caused a wave of skepticism in the U.S. Studies such as the Peterson Report which were commissioned to examine our aid programs, concentrated more on aid disbursing mechanisms rather than on the merits of economic aid.[36]

agricultural or commercial products. These transactions also adjust the demands for agricultural products to farm production, which is also of economic benefit. Thirdly, as we supply capital and facilities to developing countries in the form of aid, we are providing the means for their increased productivity allowing them to enter the global market.[30] The economic advantage that accrues to the U.S. as a result of developing countries entering the global market place are two fold. This advantage is described by A.W. Clausen, president of the World Bank as follows:

> "trade with developing countries is not only important because of their significant contribution to demand ... (but also) because industrial and developing countries have such different comparative advantages trade between them yields large gains"[31]

The international trade issue and its importance will be discussed in further detail in subsequent sections of this essay.

Yet, another economic benefit to U.S. economic interests accrues when aid and assistance is applied to countries who possess raw materials in which the U.S. is not self-sufficient. Conditional economic aid[32] to these mineral rich countries which facilitates construction of facilities designed to produce and or process these materials more efficiently, significantly bolsters their ability to meet U.S. resource needs while enhancing their economy through increased trade on the world market.

Fifth and perhaps most importantly, by providing our pro-rata share of economic aid to the multilateral development banks (World Bank Group) long term loans and technical assistance which Third world countries buy enables these countries to institute sound economic policies and leads to the expanded economy activities cited earlier (global trade, production of raw materials, etc).

developing nations. It is therefore critically important that we not change our pattern and become less "humanitarian" in our foreign policy goal setting. Failure to honor this leadership role would have drastic consequences for the United States.

Economic Interests

Returning to a more mundane level, it can be shown that foreign economic aid and financial assistance programs are positively linked to internal U.S. economic interests. These programs are designed to "meet the development and financial needs of developing countries and to encourage the expansion of a market oriented economy" which, it will be shown, has a dramatic effect on our economy is levelopment in several ways.

First, since the bulk of U.S. dollars sent abroad as part of financial assistance packages comes back to the United States as payment for American goods and services this provides a substantial subsidy for U.S. industry and labor.[28]

Secondly, in addition to the humanitarian goals served by feeding starving people, economic benefits are also realized by Americans as a result of grants and sales of agricultural surplusses under the provisions PL 480 (The Food for Peace Program). This legislation hailed as one of he most important foreign policy instruments the U.S has, particularly in relation to Third World countries,[29] serves the economic interests of the U.S. in several ways. First, since farm surplusses are sold to nations, it means an improved economic posture for our farmers. Secondly, since the surpluses are paid for in the local currency, this currency can be pumped directly back into the country receiving the surplus thereby bolstering their economic strength and developing additional markets for the sale of

3. That extending economic assistance will lead to politically more stable societies in the underdeveloped countries.

4. That successful application of economic aid is likely to lead to a substantial lessening of Soviet political success in that area."[24]

With these basic assumptions on the potential, application, and effects of aid in mind, it becomes easy to link foreign economic aid with the three basic interests it serves for the American people.

Social and Humanitarian Interests.

As a nation we consistently have had the proclivity to set and serve universal goals through our foreign policy. President Kennedy's speech proclaiming that the U.S. would "pay any price, bear any burden, meet any hardship, support any friend, oppose any foe, in order to assume the survival and the success of liberty"[25] is perhaps the best indicator of the sense of Americans relating to the humanitarian needs of other less fortunate peoples of the world.

An examination of Secretary of State Schultz' speech to the Trilateral Commission wherein he cites one of the four interests served by the foreign aid bill as "our humanitarian interest in alleviating suffering and easing the immediate consequences of catastrophe on the very poor"[26] is a second example of the universality of our foreign policy goals.

In a discussion of current objectives of foreign aid assistance programs, then U.S. Ambassador to the U.N., Jeane Kilpatrick remarked that "U.S. policy orientations are today ... committed to universalistic goals including the well being and development of remote people."[27]

As a result of our wealth and position as a world leader we are consistently looked to as a pace setter in he international arena in the fight to eliminate, through economic assistance, the basic problems of

b. Third World internal economic policies as a precondition to U.S. support.

c. International trade and its effect on LDC development (Employment, economic growth, etc.)

d. Third World debt and its effect on US/Global economic conditions.

These issues will be analyzed in the context of our foreign policy. And where necessary immediate actions to limit damage/maximize U.S. and global advantages will be prescribed.

III. Economic Issues and Their Influence on US Foreign Policy

The Foreign Aid Issue

The critical importance of US foreign aid to LDC development was reiterated by President Reagan in his address to twenty-two heads of state at the October '81 economic summit held at Cancun, Mexico wherein he cited the "commitment America has made for development -- and will continue to make -- is enormous."[23] Just why do we continue year after year to support this program so fully...? Is it because our President thinks it is needed or does it serve the needs of the American people. In order to justify continued support of these programs which appear to many critics as "global give a ways" certain assumptions relative to our economic future and the foreign policy which ensures that future must be made. These assumptions are:

"1. That we are a country of enormous and increasing wealth and can transfer substantial amounts of our resources to foreign countries without significant sacrifice to domestic living.

2. That if we provide economic assistance and sustained support it can and will lead to economic growth and perhaps economic self sufficiency in developing countries.

In addition to these industrial giants scores of rapidly developing LDC's who possess the preponderance of the worlds critically needed raw materials (Appendix III),[21] extremely labor intensive societies, and the potential to manufacture cheap quality imports have also challenged the economic dependence of the U.S. making America extremely vulnerable to "external economic shock."[22]

As a result of the vulnerability to external economic pressures and the extreme complexity of the international economic system it is therefore imperative that our government continuously analyze the myriad, economic as well as security facets of this process and address each in a manner that maximizes the advantages to the U.S. without hampering the developmental goals or political relations with other countries.

What are these economic forces... these stimuli exerted by Third world countries that must be addressed? What have our responses been to these stimuli? What are the issues involved? Are immediate changes required? The remainder of this paper will attempt to identify and evaluate selected important issues that are relevant to US foreign policy formulation strictly from an economic perspective.

As a result of the limited scope of this paper I will crystallize this multitude of stimuli into four major economic areas which impact on our policy formulation with the Third World. The forces (stimuli) which affect the global scene are inextricably interwoven with a direct cause-effect relationship on each other and therefore are difficult and at times virtually impossible to discuss separately. The issues I feel are most important are:

a. U.S. assistance to developing countries (foreign economic aid and Financial Assistance and Security Assistance).

In addition, 930 million LDC inhabitants live in seventy-two countries that have only the most rudimentary ingredients necessary to attain a self sustaining stage of economic growth and development. Thailand, India, Peru, Jordan and Liberia are prime examples of this class of Third World nations.

The remaining 200 million with whose plight thanks to telecommunications we are intimately familiar, live in extreme poverty (Ethiopia, Bangladesh, etc.), possess none of the tools necessary for growth, and depend almost totally on the outside world for their daily existence.[20] These sheer numbers of people along with the vast amounts of strategic minerals they possess make the Third world bloc of countries a potent global force.

The strategic importance many LDC's have to the U.S. is well documented. The requirement for basing and staging rights on the horn of Africa, the proximity to critical nodes astride SLOC's (sea lines of communication), and possession of minerals critical to sustaining our war fighting capability are but a few of these factors. The LDC's interaction with and effect on the international economic system, although not as well documented has made these countries equally as important economically as they are strategically.

America, although still sharing the top rung of the global ladder in the military and power projection arenas, economically no longer dominate one half of a strictly bi-polar world. As a result of a decade of internal focus supplanted with external assistance from organizations such as OECD (Organization for Economic Cooperation and Development) heretofore moderately producing industrialized countries such as Japan and Germany have burst onto the international economic scene and challenged the U.S. with a new wave of competitiveness.

manifested as arrested per capita income growth, increased poverty, and postponements of critically needed investments[14] ... all vital needs for economic development.

The countries which incurred the preponderance of these economic ills are frequently referred to as the Third World or South vis-a-vis the more advanced First World market economies and Second World (centrally planned communist) economies of the North.[15]

The Third world as defined in the New America Political dictionary consists of:

> "Those nations, constituting a majority of the international state system, that are-with the exception of the oil-exporting countries-relatively poor, "have not," and underdeveloped in contrast with the capitalist (first) and communist (second) "worlds."[16]

It is difficult to definitively list which countries comprise the Third World since different sources use widely variant indicators to measure factors associated with development Gross National Product, annual per-capita income and Physical Quality of life Index (Appendix 1)[17] are frequently used. A list of those countries generally regarded as Third World is found at (Appendix 2).[18]

Regardless of the exactness of the list, suffice it to say that Third World countries comprise a substantial portion of the world. Approximately three quarters of a billion people live in these LDC's (Lesser Developing Countries). One third of this number live in twenty four states that are rich in resources (the OPEC states, Zaire, Zambia, Jamaica, Morocco, Malasia) or have reached a state of development that is amenable to and attracts foreign investment, Taiwan, Singapore, and South Korea for example.[19]

-"countries with a higher investment-income ratio in general experienced higher average levels of growth" (Appendix IV)

Furthermore the study concluded that:

-"countries with higher shares of private investment in total investment also tend to have higher growth rates (Appendix V).

These conclusions indicate that developing governmental regimes must resist such economic practices as state controlled investment and encourage both investment foreign investment and internal development of private sector funds. It is imperative that countries desiring U.S. assistance allow and encourage private investment in their future. Furthermore we should also insist on internal reforms to ensure that:

- the people are the recipients of the aid
- that private entrepreneurs can produce, sell and acquire materials from outside (imports) so they can continue to produce.[64]

Even in the non-repressive nations of the Third World it is essential that an outward oriented economy still be allowed to function. Until 1981 this trend was proceeding nicely, however many nations faced with serious balance of payments problems chose to institute import restrictions in order to cope with this problem.[65] These import restrictions, though well meaning have all but totally arrested growth in many countries.

Thus far I have discussed the issue of Third World domestic economic policy from two perspectives: the effect internal policies have on full scale economic development and the requirements for economic growth that the US should demand as preconditions for our assistance. As with every issue however there are two sides and I would be remiss in my analysis of this issue if I did not attempt to also view it from the Third World's perspective.

There are many staunch critics of foreign aid of any kind who view the entire process as one of a gigantic, no return on investment handout to a multitude of poverty stricken have-not nations, all anxiously queuing for Uncle Sams dollar! This is not the case in today's world. There has been a demonstrable reticence exhibited by many LDC's to accept certain classes of foreign aid since many of the preconditions I have heretofore mentioned are seen as infringements on their internal national development. Numerous examples abound, however two of the more commonly cited are U.S. set priorities that conflict with their internally developed national priorities and U.S. attempts to closely link aid to prohibitive conditional demands.[66]

Many developing governments who have done extremely well during the early stages of economic development decry the current methods the U.S. and multilaterial institutions use to transfer resources. As it stands now these contributions are to a large extent voluntary and totally tied to the economic conditions of the world. Additionally other aid associated with the fluctuating political will (as evidenced by the heated yearly appropriations battles in Congress) make Third World dependence on funds such as these extremely risky.

The developing countries accept (for the most part) the fact that we must have some influence as a result of granting aid, however in many cases this influence is felt to be repressive; nor is the aid guaranteed for their year to year development of economic systems.

As a fix to this problem I would propose the development of a foreign policy that would completely revamp the mechanism for international resource transfer. Given that there must be some year to year automaticity in assistance if economies are to become self sustaining, I would propose a guarantee of a minimum level, a resource floor, if you will, that could be negotiated with and used as a basic minimum by the LDC's in their economic development planning. Resourcing above this minimum would require detailed justification to compete for additional resources and would similarly be linked to internal preconditions as with the basic aid package.

I might here add a caveat to my recommendation. This policy must be a transient one which as has been proposed[67] might be linked to a predetermined level of "international liquidity." As the ability to continue economic growth becomes more and more dependent on internal financing, aid could be proportionally reduced.

In the wake of such changes it has likewise been proposed that if the above changes were instituted it should follow that the multilateral lending institutions could assume a more functional, larger scale part in the process. Many feel that these institutions mask where aid comes from thereby diluting a prime function of aid dollars; that they make it difficult to monitor an audit trail; and that as such cause difficulties in justifying continued support. Nevertheless, have the potential to improve aid burden sharing and can "better channel assistance to the areas of real need"[68] rather than those preferential areas brought about by special relationships.

Up to this point in this essay I have attempted to illustrate the critical need for a foreign policy that addresses our economic linkages with the Third World. In sequence I have outlined our need for foreign policy, the importance foreign aid plays in this policy and the conditions under which this aid's impact can be maximized. Although these forces are closely interrelated none are as inextricably linked and have a greater effect on the economic well being of the U.S. than my last two issues: Third World trade and Third World debt. As a result of the effects each of these issues has on the other I shall discuss them as one, however I will attempt to prescribe separate policy recommendations for each issue.

The Issue of Trade & Debt

The importance of trade with the Third World can not be understated. Taken as a whole it represents better than 25 percent of the West's cumulative trade. In the case of the U.S. and Japan the figures are even more dramatic wherein it dominates 40% and 50% of the total trade respectively.[69]

In addition to the magnitude of this industry which accounts for hundreds of thousands of jobs in Western society,[70] Third World trade continues to provide numerous commodities which are vital to the U.S. existence. Furthermore as a result of the comparative advantage associated with this trade, the U.S. garners a much higher economic gain trading with the Third World than in trade with other developed countries.[71]

These significant economic advantages not withstanding, the most critical facet of the entire trade issue is its impact on our ability to move from our present recovery status into one of economic expansion. As a condition for continued U.S. economic growth we must, economists postulate, initiate improved technologically based productivity measures and be willing to adapt to patterns of comparative advantage demands.[72]

Moreover these internal changes alone will not ensure sustained and rapid growth. To regain this momentum requires that we further liberalize our international trade by reducing trade barriers. This is especially the case in our interaction with Third World economies.[73]

In order to prescribe courses of action which would assist our return to a more liberalized trade status one should have a thorough knowledge of the etiology of these barriers. To do this requires that we examine the conditions in the U.S. and her sister developed market economies prior to the mid 1970's recession.

In the decades that preceeded the mid 1970's trade had been seen as the single most important prerequisite for economic growth. Produce and sell on the international market was deemed the key to success. The world's critical dependence on Arab petroleum and the OPEC oil initiatives of the 70's however drastically changed that perception.

The recession caused by this act changed the positive perception of international trade to one of instability, imbalance, and harm to domestic economies.[74] Our society had once again become rather content with what it had. This led to an extreme unwillingness to incur risk of any type in aiming for a higher standard of life (i.e. economic growth). Concurrent with this complacency came an extreme unwillingness to change.

This new mindset which developed in most of the leading market economies coupled with several external shocks (inflationary surge, oil price rise, balance of payments problems, etc.) set the stage for economic disaster.

Faced with this situation the U.S. and similar economies were left only two choices: adjust to change or insulate from the threat by adopting protectionist policies to preserve lagging national economies from external threats. Many international traders opted for the latter.

The adoption of protectionist policies in the form of the high import taxes, subsidies to domestic (U.S.) producers, and unpredictable import quotas[75] caused a ripple effect on the world market system and drastically slowed growth in many of the LDC's.

Perhaps the major impact these policies have had on the LDC's is in the form of balance of payments problems. The developing economies of these nations are critically dependent on the earnings they receive from exports. As a result of the inability to penetrate the trade barriers their export earnings were curtailed which in turn led to increased borrowing to service their debts while simultaneously requiring a contraction of importing which brought their economic growth to a standstill.

Regardless of our stated commitment to 1) assisting developing economies and 2) an open free international trading system, protectionist measures have accelerated in the U.S. Some advocate that this has occurred as a matter of visibility, that is, since the benefits of an operating system such as the international trading system are not as visible as are the jobs which might be lost by foreign competition, people react (and cause their representative law makers to do likewise) more forcefully to the latter. As a matter of course however Congressional Budget Office studies show that "for every job saved by trade barriers, three are lost somewhere else in our economy."[76]

Although it may be easy to emotionally justify a rationale for instituting protectionist policies, especially if one's livelihood is threatened, too often these barriers have been erected to protect sectors of our economy that have lagged in change, not adapted technology to improve their productivity and as a result cannot effectively compete on the world market. As a result of the larger economic significance these policies have on the U.S. and trading partner's economies however, they cannot be allowed to continue.

Although this global economic problem is of serious importance to all internationally trading nations, little if anything international in scope has been done to alleviate its cause. Any action in my opinion must be multilateral in nature in order to be effective. There are several forums (UNCTAD, GATT, etc.) already in existence that possess the mechanisms to discuss strategies which could solve these problems, however they do not receive the requisite attention or support to function internationally.

Current rules, regulations, and informal agreements are in existence which could control and stabilize the international trade problem, however as an independent blue ribbon advisory group recently reported:

> "The critical problem today is that the trade rules are no longer seen as being fully effective or generally obeyed."[77]

This group's report advocated (and I fully concur) that any pronouncement of protectionist measures require open and explicit analysis of the policy in the form of a cost-benefits statement. (Appendix VI) Utilization of a system such as this would eliminate subsidy to internal producers not capable of improving productivity. It would force policymakers to "think the problem through" prior to execution and by discouraging protectionism due to the publicity involved, cut to a minimum the trade barriers which choke off international trade so vital to economic growth.

I would further recommend an international panel of advisers that in coordination with GATT, UNCTAD, and the other mechanisms which have the potential to influence international trade, would closely monitor trade problems and make recommendations for policy based on sound economics not volatile politics.

The Third World Debt Issue

Regardless of the magnitude of the global economic issues heretofore addressed, none are more pressing, have a more potentially disastrous effect on the global economy, nor will require more international cooperation to rectify than the Third World debt problem. The roots of this problem are a combined result of normal developmental borrowing and severe external economic shocks.

The effects of the OPEC nation's drastic price increases in 1973-74 caused a global economic chain reaction which began in the developed economies and "rippled downward," gaining in magnitude until it reached the Third World nations. Even the most developed economies dependent on this Mid East oil struggled to maintain economic balance, however the requirement to adjust to such massive change led to production problems, increased unemployment and deepened inflation. The overall effect was a contraction of the economy to offset the effects of the externally imposed economic stimuli.

The deleterious effects on the developing countries were even more harmful. The increase in oil prices placed a more onerous financial burden on their economies as a result of their oil dependence. More importantly was the effect the price increase had on the developed world (who themselves were economizing) which all but terminated the growth in Third World export markets which are critical to their economic survival.[78]

At a time when these developing countries most needed to maximize exports the industrialized countries desired to reduce or at least stabilize these cheaper imports via protectionist measures thereby frustrating the international market (Appendix VII). These compounding actions culminated in a negative economic synergism which severely hampered both developed and developing country growth.

As a result of a complex set of economic processes a large portion of the money made by the Arab nations found its way into Western banks who, anxious to make money using this Arab money, found a wide open market at prudent risk in the form of developing Third World countries. These countries, though hard pressed, desired to keep their economic wheels turning while simultaneously servicing debts they had already accrued in their developmental process.

It is important here to note two significant points. Although many voiceferous critics view the Third World debt problem as one of bumbling mismanagement and indeed some such as Peru, Zaire and Jamaica fit this category, most of the developing countries when granted the loans, instituted sound policies which enabled them to service their loan payments while still producing.[79] Secondly, the criticality of borrowing to develop is not seemingly understood by the American public. The axiom "To be developing is to be in debt"[80] is certainly true. An examination of today's most developed economies indicates that when struggling to improve productivity and attract markets they had an inordinately high usage of capital which not unlike the Third World countries was financed by borrowing.

Throughout this period of global recession the developing countries managed to grow, albeit at a slower pace but sill faster than the developed market economies until they received yet another economic shock, (79-80 oil price increase). This second increase all but terminated world economic growth, seriously hampering world trade and inflicting drastic economic pressures on the Third World. The falling export market and the jolt of steeply rising interest rates placed many of the Third World nations with already huge debts on the brink of default.

The criticality of this financial crisis is easily understated. Suffice it to say that had it been allowed to proceed without the intervention of the cooperative effects of the LDC's, the creditors, and the multilateral lending institutions, it could have easily precipitated the total collapse of the world monetary and economic structure. Furthermore as a result of the deepened involvement of US commercial banks (major as well as smaller banks) the American public soon found they had a stake in this global financial mess.

The doomsdayers continue to predict that there is no way out of this mess short of allowing the largest debtors to default and accepting the consequences of such actions. Default however is not the answer. Neither the creditors nor the debtors desire default since default means the end of credit, seizure of all assets abroad, to include goods and ships in transit. Governments that deal on the international economic market cannot endure these setbacks and survive. Alternative solutions must therefore be sought.

Fortunately many who are in a position to influence solutions to these debt problems do not subscribe to this doomsday philosophy. For example the heads of the multilateral lending institutions realize the magnitude of the problem and its effect on the global economy and on the development of LDC economies. They assess this problem as critical but manageable.

One such executive, A.W. Clausen, President of the World bank, stated such views while addressing the Center For International Affairs at Harvard University. He feels the problem is manageable for three reasons:

> "First expanding international investment is a normal aspect of healthy global development.
>
> Secondly, most of the developing countries coped well with the economic stress of the 1970's.
>
> Thirdly, the international lending system is strong and resilient."[81]

Although as a banker one might assume these reasons rather parochial he caveats his rationale with the statement that the problem cannot be solved and in fact "will only become more severe until we achieve global economic recovery.[82]

Following his advice how can the U.S. influence such economic recovery? First and foremost we must continue to pump capital into the developing economies. One method to achieve this is through increased multinational corporation development. The direct investment of multinational corporations is a prime method for injecting capital. However, as a result of the perceived investment risk associated with such ventures capital investment in this area has decreased from $14 billion dollars in 1981 to less than $10 billion today.[83]

Increased lending and developmental assistance especially under U.S. leadership would also assist by serving two main purposes. First it would provide more dollars to help the Third World economies back to full production capability and secondly reduce the perceived risks that inhibit lending by commercial investors.

These actions which can be influenced by U.S. policymakers in a variety of ways must also be accomplished by individual actions in the form of negotiations between debtors and creditors to reschedule loans thereby affording internally generated capital to be channeled to the more essential economic production capability rather than solely to service debt.

Although not without critics, I feel, that as the most productive nation on Earth we still have the largest leadership role to play, in rectifying the world's debt problem. Actions taken in 1983 to increase the U.S. share of the quota to the IMF by $5.8 billion dollars to help tackle this problem demonstrates an understanding of our stake in the international market place and the role that solving the Third World debt problem plays in this equation. Although the IMF has had its successes and failures it is our demonstrated willingness to assist in solving the problem that is critical.

In addition to the leadership role taken by the United States and other developed economies to solve the debt problem, there are other strategies that Third World countries could adapt to better their position which must be influenced by U.S. policy action.

First each country should institute a forum wherein more equitable prices for exported raw materials can be bargained in exchange for a more positive long term assurance that these raw materials will be available. A forum such as this could likewise stimulate trust in the government's desire to produce and as mentioned previously perhaps reduce the appearance of financial risk to multinational investors.

Secondly some form of control or oversight must be effected by the U.S. to ensure that MNC's contracts are not exploitive. A more favorable sharing of the profits will stimulate trust on both parts, attract more outside

:ivate investment and afford more internal capital to be used for debt ervicing or productivity improvement at the discretion of the developing overnment.

IV. Summary

In this paper I have attempted to identify the most salient economic ssues which are relevant to U.S.-Third World relations. As a result of the cope of this paper I have had to limit discussion to only four issues which n my opinion after reviewing the literature are most critical to our oreign policy makers. I realize that even in these four rather broad opics there are numerous subissues that must be addressed.

It was not my purpose to prescribe detailed solutions to each of these ssues but to highlight certain paths or central tendencies that olicymakers should pursue. In some instances however, as with the nternational Trade issue, solutions to problems lie in the support we, the J.S., give to already existing mechanisms that will help to solve the roblem.

In conclusion I might only remark that daily the United States becomes more economically linked to the Third World. To retain credibility as a world leader therefore we cannot not play "fast and loose with our commitment to the market economy justifying exceptions in our case while refuting Third World claims for equal access."[84] Our increasing dependence on the Third World both strategically and economically requires us to be aware of Third World needs for assistance. The critical importance of our recognition of these needs are captured eloquantly in the words of Malcolm Fraser, Prime Minister of Australia, when he stated "The needs of the Third World are such that, in the last resort, it will turn for assistance wherever it is available, rather than go without ... The west must ensure that the last resort is not the Soviet Union."[85]

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APPENDIX VI

GATT RECOMMENDED "Anti-Protectionist"
Cost Benefits balance sheet

Protection Budget for the . . . Industry—Fiscal Year 19 . .

...sures	1. Rationale, Goals, and Time Horizon of the Specific Measures	2. Exact Description of the Measures	3. Estimated Income Redistribution Effects in 19..	4. Quantifiable Costs and Benefits to the Country as a Whole (Efficiency Effects)			5. Ratio of Cost Per Job Protected to Average Annual Wage in Protected Industry in 19..	6. Nonquantifiable Costs and Benefits to the Country as a Whole	
				a. Estimated costs in 19..	b. Estimated benefits in 19..	c. Ratio of costs to benefits		a. Costs	b. Benefits
...her charges									
...estrictions									
...VERs and MAs)'									
...ls made									
...rough state trading									
...overnment									
...nt									
...y)									
...s									
...es and tax									
...scal exemptions)									
...exemptions									
...guarantees									
...y)									
...c production									
...ies and tax									
...scal exemptions)									
...xemptions									
...ntees									
...y)									
. Industry									

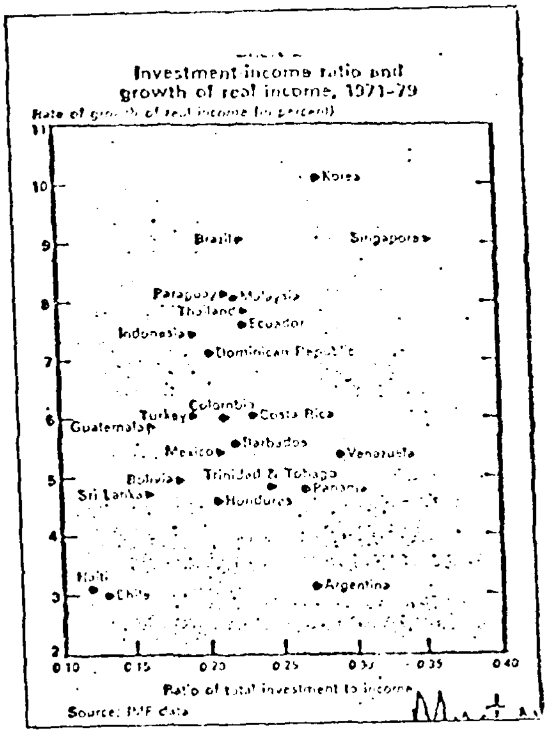
Prototype of Protection Balance Sheet

...of
...ystem of protection granted in the ... industry.
...rotection has already been granted, and which existing nontariff protection is expected to be phased out, and
...sistance is being continued

SOURCE: IMF Newsletter (April 85)

APPENDIX IV

INVESTMENT-INCOME RATIO AND
GROWTH OF REAL INCOME, 1971-79

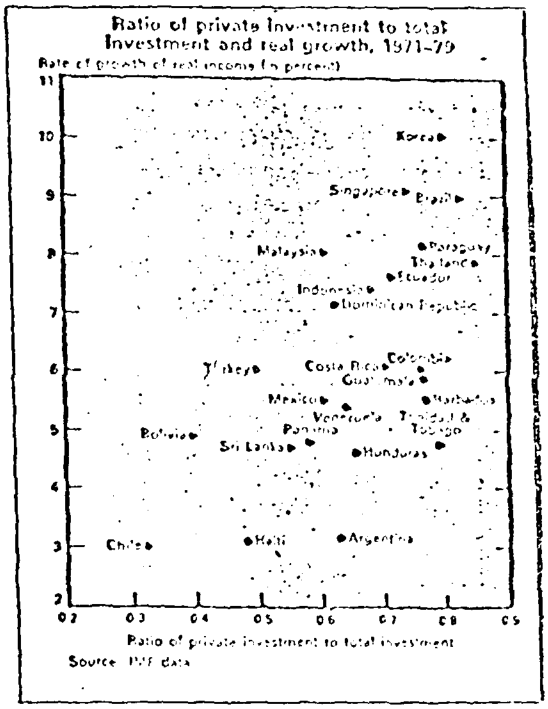


Bleizer, Mario I. and Mohsin S. Khan. "Private Investment in Developing Countries." Finance and Development, 20: pp. 26-29 June, 1984.

RATIO OF TOTAL INVESTMENT TO INCOME
SOUCE: IMF Data

APPENDIX V

RATIO OF PRIVATE INVESTMENT TO TOTAL INVESTMENT AND REAL GROWTH 1971-79



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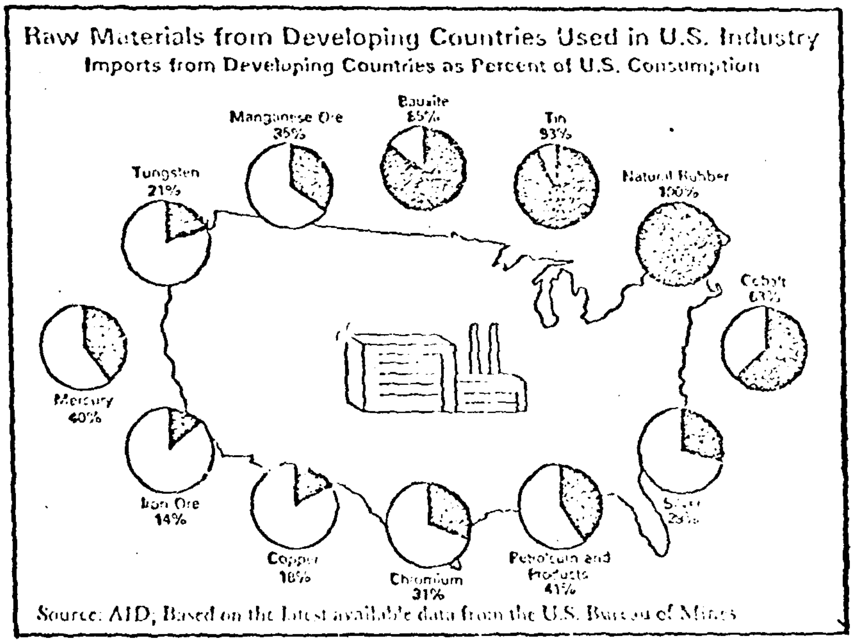
RATIO OF PRIVATE INVESTMENT TO TOTAL INVESTMENT

SOURCE: IMF Data

APPENDIX III



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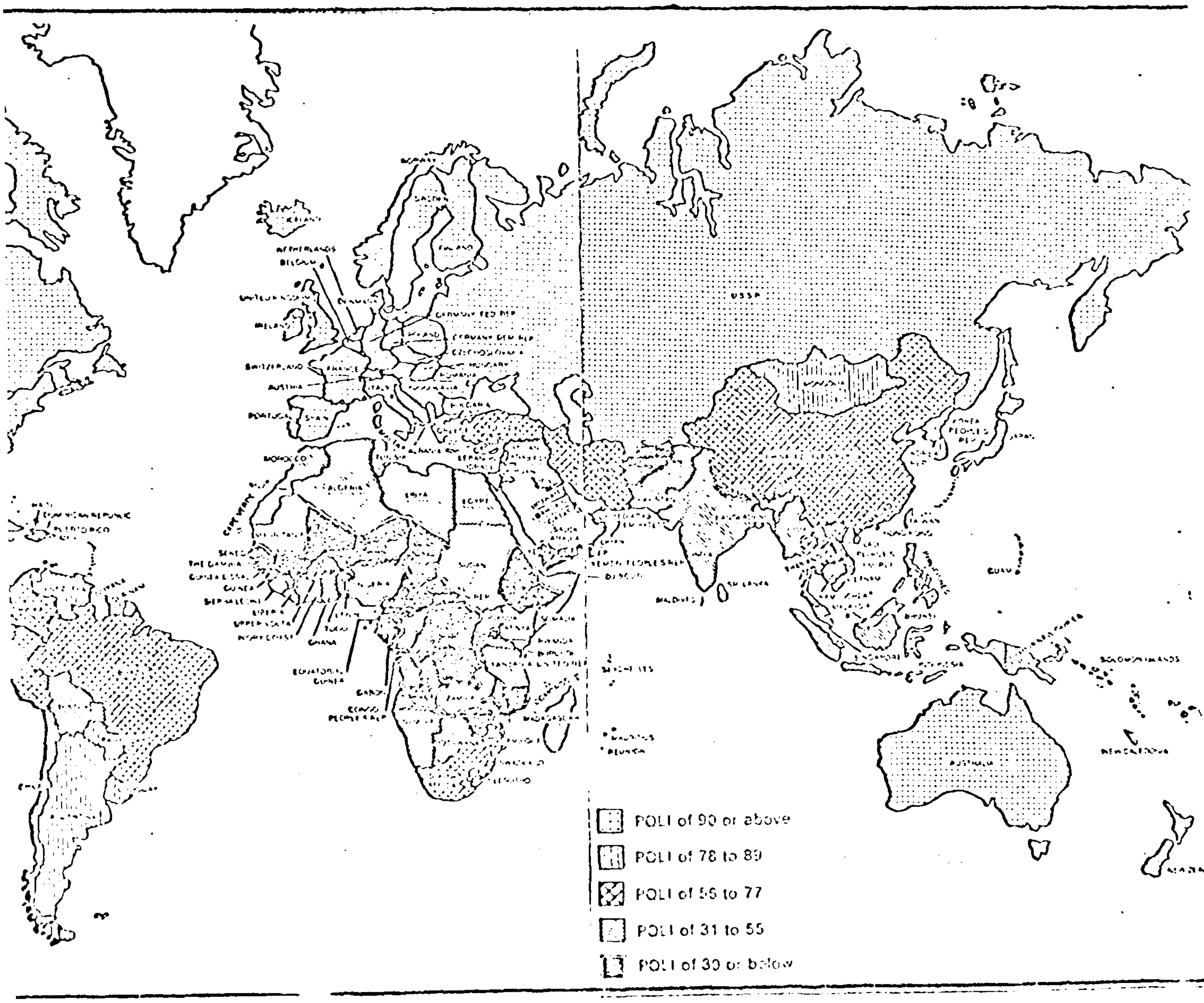
APPENDIX II

THIRD WORLD COUNTRIES

Afghanistan
Algeria
Angola
Argentina
Bahamas
Bahrain
Bangladesh
Barbados
Benin
Bhutan
Bolivia
Botswana
Brazil
Burna
Burundi
Cambodia
Cameroon
Cape Verde
Central African Empire
Chad
Chile
Colombia
Comoro Islands
Congo
Costa Rica
Cuba
Dominican Republic
Ecuador
Egypt
El Salvador
Equatorial Guinea
Ethiopia
Fiji
Gabon
Gambia
Ghana
Grenada
Guatemala
Guinea
Guinea-Bissau
Guyana
Haiti
Honduras
India
Indonesia
Iran
Iraq
Ivory Coast
Jamaica
Jordan
kenya
Kuwait
Laos
Lebanon
Lesotho
Liberia
libya
madagascar
Malawi
Malaysia
Maldives
Mali
Mauritania
Mauritius
Mexico
Mongolia
Morocco
Mozambique
Nepal
Nicaragua
Niger
Nigeria
Oman
Pakistan
Panama
Papua New Guinea
Paraguay
Peru
Philippines
Qatar
Ruanda
Samoa
Sao Tome' and Principe'
Saudi Arabia
Senegal
Seychelles
Sierra Leone
Singapore
Somalia
Sri Lanka
Sudan
Surinam
Swaziland
Syria
Tanzania
Thailand
Togo
Trinidad and Tobago
Tunisia
Uganda
United Arab Emirates
Upper Volta
Uruguay
Venezuela
Vietnam
Yemen
Yemen (South)
Zaire
Zambia
Zimbabwe

APPENDIX I

PQLI Map of the World



NOTE; Each country's PQLI (Physical Quality of Life Index) is based on an average of life expectancy at age one, infant mortality, and literacy.

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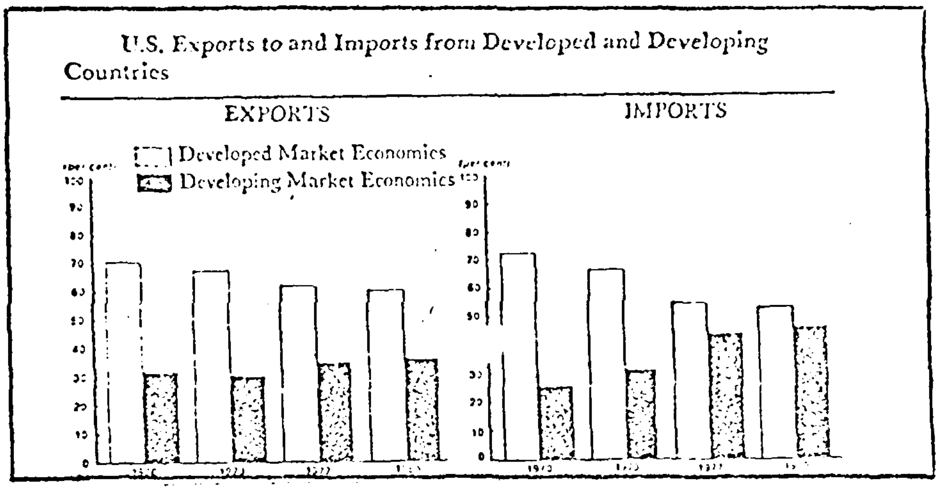
APPENDIX VII

1979 Oil Price Rise and Its Effect on Third World Imports to United States.



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