IMPACT OF FOREIGN AID IN DEVELOPING COUNTRIES

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ABSTRACT

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Foreign aid is a post-war phenomenon which was introduced to help the Third World countries to escape from the underdevelopment and poverty. The paper argues that foreign aid programmes originated as part of the ideological confrontation known as the Cold War and that the motives behind aid were always more political than economic. The objective of this paper is to portray foreign aid as the mechanism which explains the relationship between the rich and the poor nations in the world today, in other words, the paper explains the relationship between the Official Development Assistance and the level of development. The research is explanatory in nature. Both social and economic indicators were utilized to investigate the research problem. Because of the limited time factor, the immediate focus of the analysis was on Guatemala and Peru as case study. The study concludes that foreign aid retards and distorts the process of economic development of the recipient countries and results in dependence and exploitation. It also replaces domestic savings and flows of trade. It seems clear that most countries are economically dependent on the rich. Furthermore, in many ways the working of the international capitalist economy clearly intensifies the condition of dependence. Giving aid for development seems almost the exact reverse. Power does play a part in the relations between the rich and the poor. Turning to the future, foreign aid programmes are bound to change to reflect the new realities of global international relations.

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INTRODUCTION

In recent years the gap between rich and poor nations has become wider (Nebudere: 1977). A minority of the world population is using the majority of resources. In this context international aid was introduced to help the Third World countries to escape from the underdevelopment and poverty. Nevertheless, there is evidence indicating that aid works as a mechanism of control and its overall purpose is to preserve a system contrary to the interests of the poor in the Third World (Hayter: 1971). To the extent that it is effected in the underlyi·g purpose, aid from the major Western powers therefore probably does more harm than good to the mass of the population of the Third World.

The first major foreign economic assistance programme was the Marshall Plan (Sclar: 1980), official the European Economic Cooperation over a period of four years. The Marshall Plan was hardly underway when the developed countries turned their attention to problems of economic growth and stability in the developing world. The breakup of colonial regimes, the polarization of World War II alliances, and the threat of both political and economic instability, particularly in East and South Asia, focused Western attention to the developing countries of Latin America, Asia and Africa.

Substantial resources transfers to the developing countries at a large level - as a major strategy of the Marshall Plan to develop these regions - were not achieved until the early 1960s (Little and Clifford, 1965:p.25). As late as 1960 the United States was the source of well over half of all development assistance, with most of the rest supplied by four European countries to their current or former colonies (OECD, 1985:pp.92-99).

By the early 1960s the International Bank for Reconstruction and Development (IBRD, The World Bank) and its associated institutions, the International Finance Corporation (IFC) and the International Development Association (IDA), were emerging as an important source of development lending. The articles of agreement for both the International Monetary Fund (IMF) and the World Bank had been drawn up at the Bretton Woods conference on postwar economic policy in July 1944 (Sclar: 1980). The founders visualized the IMF as supporting the liberalization of trade and payment regimes. The bank's primary role, at least initially, was to support reconstruction rather than development. However, when other institutions devoted to reconstruction came into being, particularly the Marshall Plan and the United Nations Relief and Rehabilitation Administration (UNRRA), and bank membership was expanded to include the new postcolonial states, the bank was pushed into taking a more active role in development.

A variety of motives led to the expansion of bilateral assistance programmes in the late 1950s and early 1960s. In the United States, the late 1950s became a period of rising concern about security because of the percieved threat of Chinese expansions in Asia and concerned with the potential impact of the Cuban revolution on political developments in other Latin American countries (Griffin: 1991).

During the early and mid-1960s development assistance became much more highly institutionalized. In 1960 a Development Assistance Group, later renamed the Development Assistance Committee (DAC), was formed within the Organization for European Economic Corporation (OEEC), which was later reconstituted as the Organization for Economic Cooperation and Development (OECD). The World Bank strengthened its capacity for development assistance by organizing two affiliated institutions: the IFC, established in 1956 to strengthen the Bank's capacity to make capital available to the private sectors in developing countries, and the IDA, established in 1960 to provide the bank with a 'soft loan' fund. The latter was supported by donor member 'contributions', rather than 'capital subscriptions', to countries whose economies were not strong enough to justify loans at market or near-market interest rates (Cassen: 1986). By the mid-1960s the World Bank was joined by three regional development banks - the Inter-American Development Bank (IBD) in 1959; The African Development Bank (ADB) in 1966. The World Bank also sponsor consortia of 'donors' for some major aid recipients to improve coordination between bilateral and multinational assistance programme activities.

By the mid-1970s U.S. aid commitments had declined, and they never regained, in real terms, the levels achieved in the mid-1960s. (World Development Report: 1990). During the 1980s both development thought and development policy were strongly influenced by the effects of a global recession that interrupted a quarter-century of remarkably rapid economic growth in both developed and developing countries. A convenient marker for the emergence of the new set of concerns was Mexico's move to reschedule its debt in August 1982. In 1982 and 1983 almost as many developing countries entered into debt rescheduling negotiations as in the previous twenty-five years. These debt problems emerged at a time of transition for the international economy.

Aid has been transferred in a multiplicity of forms, and for a number of varying purposes. The ultimate objectives of aid-givers have been many and somewhat vague, but an important proclaimed aim has been the improvement of economic and social conditions in the recieving countries (Cassen: 1986). While the needs for assistance in general are obvious, donor countries appear, so far, to have devoted too little effort to designing forms and defining areas in which the impact of international assistance on the development of the recieving country could be truly valuable.

Foreign aid as it is understood today has its origins in the Cold War. It is largely a product of the ideological confrontation between the US and the Soviet Union which dominated international politics for forty-five years between 1945 and 1990. It began not as a programme to assist the long-term development of improverished countries but as a programme to facilitate the short-term economic recovery of Western Europe after the end of the Second World War. The political motivation of what was called the Marshall Plan was to prevent the spread of communism to France and Italy (where the communist party was strong), to stabilize conditions in West Germany (and create an attractive alternative to the socio-economic system imposed in East Germany) and to reduce the appeal of socialist politics in the UK (where the Labour Party enjoyed considerable popularity).

The Marshall Plan was followed by President Truman's Point Four programme (Sclar: 1980) - named after the fourth point in his inaugural address -which was a technical one and economic assistance programme for Greece and Turkey, two poor countries bordering on the communist world and thought to be in danger. The third phase was a response to the disintigration of the old Europian empires and the proliferation of newly independent countries, first in Asia and later in Africa. Freedom from colonial rule led to a contest for the 'hearts and minds' of the people throughout what came to be called the Third World. Foreign aid was one weapon in this contest, not the only weapon and seldom the most powerful one, but none the less a significant tool of Western diplomacy. A comparison of military expenditure with development expenditure gives some idea of the relative significance of foreign aid. Between 1980 and 1990 world military expenditure was roughly US$8030 billion while official development assistance was US$360 billion, or only 4.5 per cent as large (Shaw and Wong: 1990:5).

Particularly difficult problems were posed by the collapse of the Japanese Empire, for it was in the territories occupied by Japan prior to and during the Second World War that the confrontation between the First World and the Second became most heated. After the liberation of China by the communists in 1949, the anticommunist nationalist opposition retreated to Taiwan and mounted a political and economic challange to the mainland. The challenge was supported by large amounts of foreign aid. Korea was divided into two countries, a communist North and a capitalist South, and in the early 1950s the Korean War was fought over the issue of reunification. South Korea won the war, thanks to massive military support from the West, and then after the war recieved large amounts of foreign aid. Similarly in Vietnam, the country was divided into a communist North and a capitalist South, and again a war was fought over the issue of reunification, with North Vietnam ultimately winning in 1975. Throughout the war, however, South Vietnam recieved huge amounts of military and economic assistance. Indeed, the purposes of foreign aid are perhaps most clearly revealed in Taiwan, South Korea and South Vietnam.

The early foreign aid programmes, however, were not confined to the fringes of the communist world. The Cuban Revolution of the late 1950s extended the Cold War to the Western Hemisphere and posed a challenge to the long-standing hegemony of the US in that region. The response was multifaceted and included the diplomatic isolation of Cuba, sponsorship of a military invasion and an economic embargo. Also included in the package was a foreign aid programme for the rest of Latin America - Kennedy's Alliance for Progress - which attempted to use the promise of financial assistance as an incentive to governments of recipient countries to introduce policy reforms.

Later foreign aid programms were not always wholly dominated by US-Soviet rivalry but instead reflected narrower regional concerns, as in French aid to Francophone Africa, British aid to Commonwealth countries and Dutch aid to Indonesia. Moreover, foreign aid was born out of political and ideological rivalry, it has always had an economic dimension, namely, an attempt to create a strong, expanding, global capitalist economy. These qualifications are important, but they must not be allowed to obscure the primacy of politics.

Despite the stimulus of the Cold War, foreign aid may already have been running out of steam before the remarkable political developments of 1989. This is particularly true when seen from the perspective of the rcipient countries, as is apparent in Table 1.

Table 1. Official Development Assistance from OECD Countries to Developing Countries, 1950-1987

(US$ billion in 1980 prices)

1950-5	8.2	1971-5	25.0
1956-60	16.6	1976-80	26.2
1961-5	24.1	1981-5	30.4
1966-70	26.1	1986-87	41.5

Source: Calculated from data in Maddison (1989: 147, Table D-11).

Measured in real terms (Maddison: 1989), i.e. the nominal value deflated by a world export unit value index, the average annual amount of official aid from the OECD countries doubled betwen 1950-5 and 1956-60. In 1980 prices, the yearly flow of aid rose from US$8.2 billion in the first half of the 1950s to US$16.6 billion in the second half. It increased by another 50 per cent in the next half decade (1961-5) and then remained more or less constant until the 1980s, when falling export prices pushed up the real value of aid. The flow of aid reached a peak in 1972, the year before the first oil crisis, and this peak was not regained until 1983.

Even these figures, unexciting as they are, may overstate changes in the real value of aid. A more appropriate deflator might be a unit value series of manufactured export goods, since the content of aid flows consists largely of manufactures; and the technical assistance component of aid would surely be subject to a higher deflation factor, reflecting the increase in salary and other costs of Western advisors, teachers and technical experts. In addition, account should be taken of servicing and debt repayment of loans from multilateral aid agencies. Many borrowers of World Bank non-IDA funds, for instance, are now recieving very little in net terms. Thus, when viewed properly, real flows of foreign aid to developing countries have not increased all that much since the 1960s. The Cold War may have provided the fuel for foreign aid programmes, but the fuel was not very powerful (Griffin:1991).

Now that the Cold War is over, two questions are raised. First, as the ideological divisions begin to blur, as globalization proceeds and the three worlds blend into one, what is the outlook for foreign aid to developing countries? Second, if the end of the Cold War is to be accompanied by a significant reduction in foreign aid to poor countries, will this necessarily damage their development prospects? The focus of this paper is to examine the second question, for if foreign aid does not in fact promote development, our joy over the end of the Cold War need not be tempered by sadness over the possible demise of foreign aid. The intention of this paper is not to outline any optimal general relationship between the donor and the recipient country. As will appear from the discussion in the first chapter, the concept of micro-level aid, on which I wish to focus attention, is narrowly defined as the grant equivalent of the concessional resources transferred. We will not concern ourselves with the effects of commercial transactions between the donor and recipient country. Neither will we treat the important subject of trade policy. Another significant omission will be the intricate considerations and processes on the donor side, which in fact influence the form, size, and country allocation of concessional resources provided to developing countries. The purpose of this paper is to provide some tentative answers, and to discuss, criticize, and formulate methods to be used in assessing, ex ante and ex post, how and to what extent foreign aid contributes to development in developing countries.

1. WHAT IS AID ?

1.1. AN INTRODUCTORY DEFINITION

Developing countries have many types of relationships with industrialized countries. Some of these may promote development while others can be shown to hamper it. From among all these relations we wish to sort out the one that may be defined as aid. It would obviously be wrong to include all the relations that promote development between developed and developing countries in an aid definition. Aid is equivalent to a gift, something given up for nothing by the donor (Cassen: 1986). This means that my proposed definition excludes commercial transactions taking place between developed and developing countries. Likewise, developed country measures, concerned for instance with trade policy (though sometimes implying considerable advantages to developing countries), are excluded, since they do not ordinarily involve any giving up of resources in favour of developing countries. What remains is the value of the grant equivalent in concessional resource flows from rich to poor nations.

1.2. FORMS OF AID

Aid takes the form of grants that need not be repaid or loans. Loans may be hard, i.e., subject to banking criteria regarding probabilities of repayment, etc., or they may be soft, with low (subsidized) interest rates, long grace periods, and long repayment periods. Loans may have to be repaid in hard, foreign currency or in local currency. So the softest loan is much more nearly a grant than it is a loan (Cassen:1986), although we may still choose to call it the latter for a variety of reasons. The economic assistance means a flow of foreign exchange from one set of countries to another. It is usually related to developmental goals. And it is usually associated with governments since the purposes do not usually include activities that are likely to be financed by private sources. Terms vary from outright gifts with "no strings attached" to loans at essentially commercial interest rates for specific purposes (Cassen: 1986).

Loans and grants are the most common, explicit forms of aid, but many other forms exist. A particularly common type of aid relates to trade relationships between the more and less developed countries. Usually these have evolved from colonial relationships. The United Kingdom, for example, initiated an extensive system of "imperial preference" in which all member countries of the Empire accorded one another's goods substantially lower tariff rates that were accorded goods from outside (Cassen:1986). This arrangement made Great Britain's entry into the European Common Market more problematic that it otherwise would have been. The incorporation into the Common Market structure of French colonial tariff preferences for African goods has made it more difficult for Latin American exporters to compete with African commodities in Europe. The United States for years after 1902 maintained reciprocal preferential tariff treatment with Cuba, although this policy has been frequently attacked as an imperialist device to assure dependency rather that an effort to provide assistance (Griffin:1990). It should be recognized that the acceptance of aid, in whatever form, does increase dependency. Recent proposals to grant tariff preferences to industrializing nations because of differences in nominal and effective rates are perhaps more related to redressing old wrongs than they are pleas for assistance. Proposals for increasing the world's monetary liquidity by distributing Special Drawing Rights (SDRs - sometimes reffered to as "paper gold") to the less developed countries are requests for disguised multilateral grants given the need for increased liquidity in the international monetary system.

Military aid, economic or developmentall assistance, and emergency relief are three kinds of programms; although we are concerned only with the second, there is considerable overlapping. Military aid usually consists of equipment, technical assistance, and training opportunities that are made available directly to the armed forces of the recipient country. Particularly when the military is running a country, this aid may be directly related to the development process. There are both military and developmental implications if aid is granted to expand airport facilities or highways. In passing, the military ought not be underestimated as a development agent. It not only provides facilities but also is active in educational areas, providing literacy training and vocational education. On the other hand, the Pan American highway has defense (and "offense") implications, although it is primarily a development project (Griffin:1990). Finally, the granting of funds as an immediate reaction to earthquake damage, for example, is a short-run, charitable response but not unrelated to long-run developmental programmes and political relationships.

Bilateral aid is aid that is given according to an agreement between two countries. Multilateral aid, on the other hand, is usually provided through some permanent consortium of governments, such as the World Bank, the Inter-American Development Bank (Grif in:1990).

1.3. ISSUES RELATED TO FOREIGN AID

Since there are many persons and groups who oppose aid, from the liberal who sees aid as supporting military dictatorships to the isolationist who views events within another country as none of his business, it is no surprise that there are many issues involved and discussed. We list and comment briefly on some of the general criticisms of foreign aid.

Aid is expensive. There are too many U.S. domestic problems requiring taxpayer support to justify taking on doubtful projects abroad (Cassen:1986). There are few definitive things that can be said for or against this criticism. The comparison of costs and benefits of expenditures on diverse projects in the United States and abroad is so elusive that faith and prejudice usually become the final determinants (Cassen:1986).

Aid is intervention. And so it is. And so is withholding aid, and so is the granting or not granting of diplomatic recognition (Frank:1971). And aid involves intervention on another level when aid funds are monitored by the granting agency to ensure that they are spent honestly, efficiently, and for the purposes intended. The associated auditing, reporting, and prying cause considerable friction and resentment from time to time at the operating level. It is understandable that host officials do not like foreign inspection of their activities, but on the other hand, it is unreasonable to expect the Congress and U.S. taxpayers to part with their funds without such review (Frank:1971).

Aid supports governments that do not merit support, i.e., military, "nondemocratic", "elitist", etc (Griffin:1990). Aid agreements are between governments, and aid does contribute to the support of the governments in power, at least in the short run. Does it follow that aid should be tendered only democratic countries? If so, which ones in Latin America qualify? On what criteria? "Democratic", incidentally, is not necessarily the equivalent of "civilian". More important, if external assistance is to be defined poeple living under oppressive regimes,how are they expected to rise above the oppression? These questions are much too complex and too far atield to explore in depth here, but the simple policy of denying assistance to countries with "unopposed" governments is not necessarily a wise solution. Nor does it seem feasible that any very substantial amount of assistance can be provided without its being channeled through existing governments (Griffin:1990). Trying to do so would be properly seen as an effort to subvert the existing governments, and the programs would be stopped. There is no easy solution to this dilemms; but types of aid may be varied, conditions for aid may be imposed, and projects may be varied depending on the attitude toward the government in the power (Seers:1972,pp.6-15). There is, of course, great inconsistency between the view that assistance should be tailored - or even withdrawn - according to some measure of acceptability of the existing government and the view that the United States should not practice "intervention".

Aid is a tool of imperialism that strikes at the sovereignty of poor nations (Alavi:1964). And so it is, as very explicitly stated in the Hickenlooper Amendment to the Foreign Assistance Act of 1962, which requires the President to suspend all economic assistance to any country that expropriates the property of a U.S. company to discriminatory taxation. This amendment was urged by the now more-famous Harold Geneen, president of ITT (Levinson:1970,p.144). To give priority to the interests of U.S. firms over the humanitarian and/or geopolitical objectives of the aid programs was, at the very least, not very bright. This piece of legislation hardly served the best interests of the United States in its relations abroad.

Aid imposes ethnocentric solutions (Bronschier: 1978). With a scarcity of aid resources, officials must make decisions about what they will support; inevitably they must listen to advisors. Advisors are necessarily products of their own experience and environments and, no doubt, some bad advice has been tendered by some culturally unaware and even incompetent people. As a general criticism of aid, though, this may be rationalization or smokescreen for Latin Americans or others who (1) do not know what to do, (2) do not want to do anything, or (3) do not want any good to come from the existing system (Riddell 1987: 154).

U.S. persistence in continuing bilateral aid programs with Latin American countries has reduced the possibilities for integration; the same aid given to the region as a whole or to subgroups would have required coordination, cooperation, and a greater spirit of integration, instead of competition (Riddel: 1987).

The principal effect of foreign aid is the provision of extra foreign resources in addition to those already available, usually for purposes not ordinarily associated with the private sector (Griffin:1990). Normally these funds cover only the foreign exchange component and require some of a great deal of matching domestic funds for the domestic component. Most foreign aid is provided for specific projects, but funds have been made available for general purposes such as balance of payments support or financing of a governmental budgetary deficit Griffin:1990).

Thus, the beneficial effect for the recipient is that more real resources are immediately made available. In addition, the recipient country has to supply resources of its own - the domestic component. This raises all the questions that should be considered with respect to local expenditures for any purpose. As Riddell asks (1987):

(i) Is this a first-priority expenditure? Certainly governments tailor their programms in directions for which aid can be expected and thus may be discourage expenditures for local priorities. University researchers who work on projects that they think will be of interest to, for example, Ford Foundation, perhaps divert and distort priorities. This sort of distortion may not occur at all, and it does, it may not be all bad. For example, aid can be used as a lever to encourage recipient governments to adopt certain policies that will enhance the general welfare: appropriate offers of assistance might encourage a military dictatorship to expand educational expenditures. This implies a certain amount of arrogance on the part of the aid giver, but it is not at all certain that the announced needs (e.g. "Phantom" jets) of governments in power are more representative of the needs of the people than those which can be estimated by careful foreign observers. This dilemma explains how the two-pronged "liberal" argument sometimes goes: decrying aid because it imposes unwanted policies abroad and at the same decrying the policies and priorities of recipient governments.

(ii) Where do the resources for the domestic portion of the investment come from? Viewed from the monetary side these resources arise either by substitution or by expansion. In the case of the former, new funds may be sequestered from the taxpayers, diverting expenditures from previous patterns to the new government projects. Government spending for the particular project is substituted for private hoarding, conspicuous consumption, real investment, or, unfortunately, spending on rice and beans, depending on the values and effects of the tax system. Alternatively, expansion of government expenditures in the new direction may occur at the expense of reduced governmental expenditures in old directions, on programs with either less or greater priority than the new. These results are hard enough to foresee, but they are even more difficult to predict if monetary expansion is used to cover the domestic component. An increased money supply could add to inflationary and balance of payments problems, resulting in forced savings by consumers, other investors, and other government programs, depending on which prices are most affected and how incomes are adjusted, if al all.

Generalization concerning the effects in real terms is also difficult. Under the best of circumstances, the domestic component will utilize unemployed or unemployed resources. Under the worst of circumstances, it will utilize resources already in short supply and fixed in number, such as , hydraulic engineers for an irrigation project. This would imply a curtailment of some other activity to undertake the new one. Most ventures lie somewhere in between these extremes, making effects difficult to forsee.
Even if the domestic component consists entirely of unemployed resources (labour), the method of financing is important. There would be nothing immediately inflationary about the central bank's creating pesos to employ these people; but once the pesos were paid in wages, they would become an increment to the money supply and an increment to the aggregate demand in the economy - in the hands of people with a very high marginal propensity to consume (Griffin:1990).

2. THE ECONOMIC JUSTIFICATION FOR FOREIGN AID

The fact that the motive for foreign aid is political rather than economic does not necessarily imply that the consequences of aid are not beneficial to economic development. Good things may follow from suspect motives - just as Adam Smith argued that self-interested behaviour can result in collective well-being - but in the case of foreign aid one should not lightly suspend disbelief. The proposition that suspect political motives may lead to desirable economic change may, turn out to be not only paradoxical but false (griffin:1990).

Since the 1960s foreign aid has consisted essentially of a flow of resources from the First World to the Third, with the Second World essentially cut out of the loop. True, the major Western donors frequently criticized the communist countries for not contributing more to the aid effort, but in reality First World countries did not welcome competition from Second World countries' aid programmes (Griffin:1990). The First World was content to see the USSR and the communist countries of Eastern Europe concentrate most of their aid on a limited number of recipients such as Cuba, Vietnam, Mongolia, Afghanistan, and Ethiopia.

Some of the Arab countries became major aid donors in a few Islamic countries after the oil price increases of 1973, but Arab aid declined steadily after 1980 when the real price of oil fell (Griffin:1990). Intra-Third World aid from the Arab countries, China and India is unlikely to be quantitatively significant in the years ahead. In 1987-8, for example, foreign aid from the Arab countries was only 6.3 per cent as large as aid from the OECD countries. Aid from the USSR and Eastern Eurpoe in those years was 10.9 per cent as large as OECD aid (Griffin:1990).

Thus, the econiomic justification for foreign aid was and continues to be essentially the justification given by the West. It is perhaps no coincidence that Western nalysts of foreign aid came early to the conclusion that what the Third World needs in order to promote its development is what the First World has in abundance. Underdevelopment was characterized by shortages of capital, technology and skills; economic development occurs as a result of increased supplies of capital, technology and skills; and the donor countries are well placed to provide capital (in the form of loans and grants), technology (often in the form of specific projects) and skills (in the form of technical asistance). J.K. Galbraith saw this clearly over fifteen years ago. Referring to his period as US Ambassador to India he writes:

> There were, broadly speaking, only two things we could provide to lessen the deprivation (of India) - we could supply capital and, in principle, useful technical knowledge. The causes of poverty were then derived from these possibilities - poverty was seen to be the result of a shortage of capital, an absence of technical skills. (Galbraith, 1975:v-vi)

The view that what 'we' have is what 'they' need can be transformed by a slight of hand into two propositions which clearly are false. First, it has been implied that because of its poverty the only way the Third World can develop, i.e. aquire the needed capital, technology and skills, is by relying on foreign aid from the First World. According to this view, foreign aid acts as the missing 'catalyst' in development, as a 'strategic input' or as the agent which romoves 'bottlenecks' and 'binding constraints'. The 'multiplier effects' of foreign aid ensure that its impact on development is grossly disproportionate to its volume

(Griffin:1990). Although the vocabulary of aid - catalyst and multiplier effects - suggests that small contributions sustained for short periods can have large positive consequences, aid has in fact been sustained for long periods and the disproportionality of aid is not its impact but its magnitude. Even technical assistance, a low-cost component of aid package, can be extraordinarily large in comparison to the resources available within the recipient countries (Griffin:1990). The United Nations Development Programmes (UNDP), a major provider of technical assistance, now recognizes that 'in many developing countries the amount of technical assistance flowing each year into the salaries and travel of foreign experts exceeds by far the national civil service budget' (UNDP, 1990:5).

Yet it has long been clear that even in the lowest income countries domestic resources are adequate to finance a high rate of accumulation of capital. The potential economic surplus is substantial and actual savings rates can be high. Shortage of capital is not a major obstacle to development and never has been (Griffin:1990). In 1988, for example, savings accounted for 13 per cent of GDP in the US (one of the richest countries in the world), whereas they comprised 38 per cent of GDP in China, 24 per cent in India and 18 per cent in the other low-income economies (Griffin:1990). Savings capacity clearly is not the major problem. The aquisition of technology and skills is in principle even less of a problem for developing countries, as the historical experience of Japan and the other prosperous countries indicates. Aid doctrine has been based on an utterly erroneous diagnosis (Griffin:1991).

If capital and technology really were the binding conatraints on economic development one would expect transitional corporations to imnvest heavily in developing countries to take advantage of high expected returns to these allegedly scarce factors of production. In fact, however, during the period of 1983-8 only 20.1 per cent of total foreign direct investment occurred in developing countries while 79.9 per cent occurred in rich countries (United Nations Commission on Transitional Corporations, 1990:9). Taking all flows into account, it can be argued that the natural tendency in a fully integrated global economy would be for savings to move from poor countries to rich, because rates of return on investment actually tend to be higher in developed economies than in underdeveloped ones (Griffin, 1974). This runs counter to the conventional view that postulates that because of enormous differences in capital-labour ratios, the marginal product of capital in poor countries should be a multiple of that in rich countries and hence there should be a massive flow of foreign capital into poor countries.

The constraining scarcity in developing countries, however, is not physical capital or advanced Western technology, it is the lack of human development as reflected in inadequate general education, insufficient training and a lack of skills in the labour force, poor nutrition and incomplete coverage of the population by primary health services, etc. As a result, returns on human development expenditure in developing countries, e.g. on primary and secondary education, are often higher than the returns on physical investment

(Griffin and Knight, 1990; Psacharopoulos, 1988). It is quite misleading to compare capital-labour ratios in developed and underdeveloped economies by dividing the value of the stock of plant and equipment by the number of workers. It is labour power that is relevant, not just the number of bodies (Griffin:1990). If the denominator of the ratio were corrected by substituting labour power for lobourers, capital-labour ratios in rich countries would perhaps not be much higher than in poor countries and differences in the marginal product of capital would decline sharply, if not disappear (Lucas, 1990). Moreover, expenditures on human development generates positive externalities that accure to the population as a whole; this, too, increases labour power relative to physical capital in the developed economies and, in the absence of compensating international migration, raises the marginal product of capital in rich countries. Thus what the developing countries need above all is a reallocation of domestic resources in favour of human development and not a transfer of capital, technology and advanced skills from the rich countries.

A second false implication of the view that what 'we' have is what 'they' need is that the only things necessary for development are capital, technology and skills (Griffin:1990). Aid doctrine has been socially and politically conservative. Because of its origins in the Cold War, it has been against radicalism in all forms and has been instead a supporter of the 'status quo'. The relationship between social structure, the concentration of power, the distribution of income and the allocation of domestic resources for development purposes has played almost no part in official doctrines concerning the role of foreign aid. Power enters into the analysis only in the form of purchasing power. Similarly, aid doctrine has tended to ignore if not be openly hostile to institutional change. In agriculture, for exapmle, foreign aid has been used to promote technical change (such as the green revolution), but most donors, and certainly the large ones, have been unwilling actively to encourage land reforms in countries where the need is obvious (as in the Philippines) or even to assist the implementation of reforms in vountries where they were introduced (Ethiopia, Nicaragua, Mozambique).

True, in some countries aid donors have recognized the need for radical change. Haiti is an example. But for ideological reasons donors have been prepared to continue business as usual even when it became evident that the necessary institutional and political reforms would not be introduced. There has been a marked asymmetry in donor policies: aid has often been discontinued by Western agencies in countries which have introduced radical reforms (Cuba, Chile under Allende, Nicaragua under Sandinistas, Angola) and such countries have been branded leftist, socialist or communist, while aid has been sustained in countries where reforms are widely acknowledged to be necessary (Zaire, El Salvador, the Philippinrs, Haiti). Even in Haiti, an extreme case, it is said by enlightened defenders of foreign aid that 'the case for aid withdrawal is far from proven' (Riddell, 1987:262). Surely there is an unanswerable case to reallocate the aid recieved by Haity in favour, say, of

India, which has a lower average income, is democratic, has achieved some development and recieves less aid per head of the population. There seems to be ni limit as to how far the aid lobby will go in supporting the 'status quo'.

At the end of the day the economic justification for foreign aid has rested on the view that development is essentially a financial and technical matter. In its most extreme form, foreign aid is reduced to filling the 'gap' between the (meagre) savings of a poor country and the (substantial) investment needed to achieve an acceptable or desired rate of growth (the most sophisticated version of the gap analysis is contained in Chenery and Strout, 1966). This 'reductio ad absurdum' is not of course openly articulated, but it underlies much of the economic justification of foreign aid and illustrates just how difficult it has been to reconcile the political motives for aid with an economic rationale.

3. FOREIGN AID THEORIES

The process of aid-giving consists of a series of transactions between donors and recipients, in the course of which resources are transferred, in the initial stages at least, from the former to the latter. Theories about aid can be roughly divided into theories about the resources transfer and theories about the transaction in which it is embedded. Analysis of the resource transfer as such leads on to the identification of other resources, such as savings or foreign exchange earnings, with which aid may be supposed to interact, and to the formulation of theories concerning the relationship between them. Transfer theories can thus in general be characterised as economic theories. Analysis of aid as a transaction leads on to the identification of the partners in this transaction, i.e. the users of aid, and to the formulation of theories concerning the interests of these users and how such interests will be persued. Transaction theories can thus in general be characterised as political theories.

Economic theories , in turn, are of two main kinds. One kind of theory focuses on aid as a supplement to the recipient's own resources and purports to trace a positive relationship between aid and the total volume of resources available for the sorts of development purpose in which aid theorists are interested. Most such theories, in fact, are rather more ambitious than that. They purport to trace a positive relationship between the supplement and the proportion of the recipient's own resources devoted to development expenditure, such that the total increase in development expenditure is greater than the volume of resources transferred as "aid". The opportunities created by the availability of aid, according to this value, make it worth the recipient's while to increase his own development efforts. Domestic, or supplemental, economic theories can thus in general be characterised as attributing positive effects to aid.

There is another kind of economic theory, however, which focuses on aid as a substitute for the recipient's own resources, which are switched from developmental to non-developmental expenditure, and perhaps escape from the recipient's economy, so that the resource transfer called "aid" is offset, perhaps by a reduction in savings, or perhaps by a reverse transfer, through the profits of foreign private investors or the transfer of domestic savings to foreign bank accounts. The availability of aid as a "soft option", according to such theories, includes a relaxation of effort. In other words, they purport to trace a negative realationship between aid and the proportion of domestic resources devoted to developmental expenditure, such as the total volume of resources available for developmental purposes may well be reduced by aid. Such theories are often extended to trace an unfavourable relationship between aid and the forms of developmental expenditure, e.g. through imports of "inappropriate" foreign technology, leading to the claim that aid reduces the efficiency of developmental expenditure, as well as its volume. External, or displacement, economic theories can thus in general be characterised as attributing negative effects to aid.

Political theories, similarly, are of two main kinds. One kind of theory focuses on the donor as aid-user, and is therefore concerned with aid as an instrument of foreign policy, i.e. with the interests of the donor country vis-a-vis recipient countries. Donor-oriented theories thus form a part of the study of international relations. But there is another kind of political theory which focuses on the recipient as aid-user and is therefore concerned with aid as an instrument of domestic policy, i.e. with the interests of the recipient government vis-a-vis competing groups within the national polity. Recipient-oriented theories thus form a part of the study of comparative politics.

This brief classification of aid theories is presented below in diagram:

four types of foreign aid theories

	Economic(transfer)	Political(transaction)
Domestic	positive, i.e. supplemental theories	recipient-oriented, i.e comparative politics theories
External	negative, i.e. displacement theories	donor-oriented, i.e. international relations theories

3.1. SUPPLEMENTAL THEORIES

The starting point of supplemental theories is the identification of some key factor of the development process. In the 1950s and early 1960s, on the basis of theoretical work already done in the context of the developed countries' economies (the emphasis on savings in aid theory can be traced back to the work of R. F. Harrod and E. D. Domar, published in the 1930s and 1940s), this key factor was generally taken to be savings. Subsequently, attention shifted to other factors of the development process, notably to the need for foreign exchange, to allow imports of capital equipment and other goods which a country could not yet manufacture itself, and to the need for new skills, to enable a country to progress from its traditional forms of production. The shape of supplemental theories, however, remained strongly influenced by the early focus on savings, in the sense that a country's aid requirements continued to be presented in terms of its inadequate command of some particular resource or resources, essential for development, which could be supplemented by aid.

For simplicity of presentation, let us take savings as the ressource in question; but it should be remembered that the outline of the theory would look the same, whatever factor one identifies as the "real key" to development.

Because poor countries are poor, the argument runs, they have to spend a very high proportion of their incomes on consumption, simply in order to survive at their present low level of living. The problem may be excerbated by rapid population growth: first, a growing population requires growing total consumption to maintain constant per capita consumption; secondly, because a growing population will have a relatively high proportion of children, whose consumption is high relative to output. So long as poor countries remain poor it is very difficult for them to set aside resources in the form of savings, i.e. to accumulate capital. Investment, therefore, remains low, with the result that there is little or no growth in the economy, i.e. the country remains poor, stuck in a low-savings, low-investment trap.

Aid, the argument continues, can supplement savings, thus enabling the country to maintain the level of investment needed for economic growth. As the economy grows, the incomes grow, the country can afford to set aside an increasing proportion of its income in the form of savings, i.e. domestic savings rise faster than total income. Evantually, it reaches the point at which savings are sufficient to finance the volume of investment needed to maintain the desired rate of growth, without further aid. Thus suppemental theories are directed towards the attainment of "self-sustaining growth", i.e. to the attainment of a level of income at which a country can mobilise the resources needed to maintain a desired rate of growth without further supplementation of these resources in the form of aid.

The adoption of a supplemental approach, in short, increase the likelihood that the donor will come into conflict with, and try to bring pressure to bear upon, domestic political forces in the recipient country. Since this likelihood is precisely what the displacement theorist asserts as the basis of his attack on the view of aid as supplementing the recipient's resources, advocacy of a supplemental approach increases the likelihood that aid will fall into disrepute.

3.2. DISPLACEMENT THEORIES

At the level of organizational change, the conflict between supplemental theories and displacement theories is very simple. the supplemental theories contend that the organisational changes which aid stimulates are favourable to development. The displacement theorists argue that they frustrate development, by imposing alien values and alien patterns of organisation and thus inhibiting the emergence of a dynamic process of change within the developing countries themselves.

But the conflict between supplemental and displacement theories goes further back than that. Essentially displacement theories challenge the central assupmtion of spplemental theories, which is the supplementation of the recipient's developmental resources enhances his capacity to mobilise such resources for himself. Aid eases the pressure on the recipient, the displacement argument runs, to that he feels less need to make an effort of his own. If savings are identified as the key resource, for instance, aid relieves the recipient of the necessity of taking unpopular decisions to raise taxes. In other words, aid displaces public savings. Furthermore, aid may affect the distribution of savings, intensifying the negative effect. Some writers, broadly of a "right-wing" persuation, have argued that aid, because it goes to governments, is spent on prestigious public sector projects, with low rates of return (P.T.Bauer:1975). Other writers, broadly of a "left-wing" persuation, have argued that aid, bacause it goes to elite, concentrates the benefits of development in the hands of the rich, who devote their profits to conspicuous consumption or to foreign bank accounts, whereas savings mobilised through domestic taxation of these same rich people, which would have been necessary if aid had not been available, would have transferred resources to more productive uses (K.B.Griffin:1971).

3.3. DONOR-ORIENTED THEORIES

Virtually every study of the economics of foreign aid has an introductory chapter with some such headings as "The objectives of foreign aid" (Little and Clifford:1965). Such chapters usually contain two main elements. First, they show, with a straightforward appeal to the evidence, that donors pursue other objectives in their aid programmes besides the promotion of economic development. Secondly, and more polemically, they argue that the promotion of the welfare of poor countries is ultimately in the rich countries' interest.

The second of these arguments appears to be used for persuasive purposes, as a means of convincing donor governments of the rationality of a supplemental approach to aid-giving. One of the earliest supplemental studies of foreign aid, for instance, was explicitly cast in a foreign policy framework (Millikan and Rostow:1965).

The rich countries' long-term interst in the welfare of poor countries might be both political and economic.

In political terms, the rich countries might be interested in stability. On the basis of an assupmtion that hunger breeds discontent, and that discontent breeds instability, they might see the promotion of economic development as the means of preserving the political status quo. One sometimes hears the case argued along these lines - or, even more crudely, in the West at least, in terms of growth as the best weapon against communism - but it is unconvincing. It could be more plausibly argued that a rise in income, or at least a sporadic rise, is likely to be accompanied by increasing instability, and increasing awareness of and hostility towards those countries which continue to hold the substance of international economic power.

In economic terms, the rich countries might be interested in a world economy organised on principles of comparative advantage and the international division of labour, helping the rich to specialise in what they do best. In principle, the economic case is stronger than the political case. As an explanation of aid, however, it has to contend with the fact that the rich countries do not appear to see their own interests in these terms. In the 1960s, the process to which aid contributed tended to be one of import substitution rather than export promot'on, especially in Latin America. Subsequently, partly influenced by work done under the auspices of the OECD development center (Little and Scott:1970), some aid agencies put more emphasis on promoting the developing countries' export industries, but in general they appeared unwilling to adopt the rational corollary, i.e. opening their own markets to imports of the products in question. It is also not clear that the rich and poor countries have a common interest in the international division of labour. The present distribution of comparative advantage, seen as heavily titlesd in the developed countries' interests would like to change.

The nature of the developed counties' interest in the general welfare of developing countries is in fact seldom specified, even in the very broad terms suggested above, and indeed it is rather difficult to see how such an interest would be sustained, except on a very high plane of moral argument, which is not what foreign policy is usually about. As Mikesell partially admits, for instance, some distinguished specialists in the international relations have derided the notion that the development of poor countries in any general sense serves the interests of the United States (Mikesell:1965,p.10).

International relations theories, therefore, are likely to fall back on the more conventional and much more convincing identification of specific foreign policy objectives which the donors pursue, such as the maintenance of military alliances or trading and investment relationships. In order to explain aid in these terms, however, one would have to demonstrate, not only that the return to the donor in the form of advantages won exceeded the cost to the donor in the form of aid, but also that he could not secure these same objectives by some other cheaper means; or else one would have to assume that donors are irrational. Aid does cost donors something. What do they buy with it? A vote in the United Nations is a commodity of decreasing value. The necessary and sufficient conditions for maintaining a military alliance, as the recent history of relations between the United States and Asian countries has shown, is not foreign aid, but a genuine common strategic interest. If aid is in effect protection money for the donor's overseas investors, or a subsidy for his exporters, one must ask whether aid is really necessary for, or even a positive contribution to, the attainment of his objectives in these fields. It may well be the case that donors see aid as a price paid in return for advantages that they seek, but the price paid would appear to be unnecessarily high in relation to the advantages gained and in relation to the alternative instruments at the rich countries' disposal. The "foreign policy interest" approach to aid goes some way towards explaining what donors do with their aid. It does not explain why they use aid, with all its rather embarrassing moral superstructure, rather than other, more conventional and cheaper means.

The international theorist has an alternative explanation of the growth of aid programmes in terms of historical processes of change in relations between developed countries, and hence in the nature of the instruments available for the pursuit of foreign policy interests. The developed countries found themselves saddled with aid programmes, so to speak, which they had to use as best they could for purposes for which these programmes were in fact ill adapted. Such an explanation is satisfactory in several respects, and indeed it figures largely in the historical account. But it suffers from two limitations as an argument in favour of the view that donors use aid exclusively for the pursuit of specific foreign policy interests.

First, there is the embarrassment of the rhetoric of aid, which is the rhetoric of development, and of the sacrifice of immediate national advantage. The repeated use of this rhetoric at the global level is bound to have some impact on specific decisions taken in its name in relation to individual countries. It is as foolish to assume that they mean everything that they say. The problem for the student of aid is how to distinguish the fiction from the truth, or even from the self-realising fiction which evantually becomes truth.

Secondly, immediate national advantage does not sufficiently explain the geographical distribution of aid. Although there is a predictable bias of donors in favour of countries with which they have close relations, the circumstances which give rise to increases or decreases over time in the amounts of aid that such countries recieve are varied and complex. Thus, the international relations theorist is thrown back on an assumption of irrationality, the assumption that there are no coherent determinants of foreign aid to be identified in the relationship between rich and poor countries, and that one must look always for a particular accident of history by which a donor or donors were involved, without time for judgement or forethought. Several detailed case studies of donors' decision-taking suggest that there is more than a little truth in this picture (Westwood:1966). If there is, then we must turn to the nature of the historical accidents, i.e. to those changes of circumstances in poor countries which attract the interest of rich countries, expressed in the form of aid. In other words, we move from international relations to comparative politics.

3.4. RECIPIENT-ORIENTED THEORIES

In contrast to the "international relations" approach to aid the literature on aid in the context of domestic politics, at a theoretical level, is still very small. Neither Apter nor Almond and Coleman - two of the most influencial works of the 1960s, in the field of general theory on the politics of developing countries - mention the subject in their indexes. Myrdal, in spite of his emphasis on the role of institutions and political systems in development, devotes most of his very brief discussion of the politics of foreign aid to the objectives of bilateral donors (Myrdal:1968, pp.634-40).

In view of the emphasis that some economists have placed on the nature of aid as a key resource in the hands of policy-makers, and the increasing emphasis on the environment of aid agencies in the general policy-making processes of the recipients, the lack of discussion in this field is slightly surprising, but one may hazard an explanation in terms of the nature of the subject. The study of "national" political system is focused on relationships between the constituent parts of the "domestic" polity. The external environment, i.e. the national system's relationship with other national systems, is assumed to be constant, categorised as a separate field of study called "international relations". But aid, once it has entered the national system, is simply a resource at the disposal of governments, like any other resource. The determinants of the nature of this resource, which lie in the relationship between rich and poor countries, i.e. in international relations, lie outside the field of study, so that aid cannot be isolated as a separate factor with separable effects. It is absorbed into the broader concept of "developmental resources". In order to take account of aid as a distinguishable factor in domestic politics, one has to break out the constraining assumption that the external environment is constant, without replacing it with the even more constraining assumption that domestic political relationships are constant. In other words, one has to construct a theory concerning the relationship between domestic and external factors. Some theoretical moves in this direction have been made, but they are still far removed from the stage at which they can be related to empirical identification of the key relationships, such as the relationship manifested in aid, which significantly affect the behaviour of developing countries' domestic political systems (Rosenau:1969).

The disadvantage of that approach, as a way of assessing the significance of aid within the national political system of a country that recieves it, is that it makes it very difficult to trace the uses of aid as a single, identifiable and separable category of resources. To the diversity of aid one has added the diversity of the users of aid. To the extent that these users are pursuing different and perhaps conflicting interests, the way in which any one users makes use of any one sort of aid will have features in common with the use that he makes of other resources at his disposal, as well as features in common with the way in which other users make use of the same sort of aid. His use of aid will not necessarily be the same as his use of other resources, because aid has characteristics of its own which partly determine its uses, but equally the difference between the use of aid and the use of other resources will not be the same for all users.

To assess the significance of aid as a separable factor in the working of a political system, one needs also to look at the political system as a whole, but it is not at all clear that an approach of this kind will reveal the most significant relationships. Reference has been made, for instance, to the disposition of donors to see aid as a means of supporting particular regimes, and to the possibility that this disposition will be self-defeating. In countries in which hostility to "neo-colonialism" is a significant element in the language of politics, the extent to which the regime can extract political credit from publicising aid agreements is circumscribed by vulnerability to the charge that it is exposing the country to foreign domonation. Cases in which publicising aid has clearly brought identifiable political advantages to the regime as a whole - notably the Aswan High Dam in Egypt and the Tan-Zam railway linking Tanzania and Zambia - have nearly all been cases in which the donor in question could be contrasted favourably with other donors, which had taken a more hostile attitude. In the more general case, the government of a recipient country will hardly want to diminish its own stature by giving undue emphasis to the role of aid as a separate and identifiable resource, and donor agencies are making a dubious assupmtion if they take too bland a view of the supportive role which they suppose themselves to be fulfilling.

If, on the other hand, one looks at aid as a collection of varied resources used differently by different users, one is driven back into descrition of a wide range of situations, about which it is dangerous to generalise. An understanding of the particular internal relationships of a country recieving aid is crucial to any assessment of how it will be used and with what effect. And yet it is still necessary to try to generalise about the resources called "aid", because without such generalisation there is no way of saying what sorts of aid will have what effect in the context of any particular set of relationships.

The difficulty in the way of tracing the use of aid, as a separate and identifiable resource, which was identified as the principal obstacle to the formulation of a recipient-oriented general political theory of aid, reflects a more general weakness in all the theories characterised here. The difficulty arises as soon as one looks at the role of aid exclusively within the field in which aid is intended to operate, as if this field were a closed system, i.e. the domestic political system of the recipient country. It would be necessary to separate aid from the broader concept of "developmental resources". Displacement theories see aid as a form, and highly disadvantageous form of savings, which displaces other savings. Supplemental theories take this process of assimilation even further; for they are essentially theories about the role savings or foreign exchange or skills or institutions in development, not about aid as such, and it is from a view about the role of savings etc. that they prescribe, rather than describe, the role of aid.

International relation theories, similarly, are theories about what rich countries do with the instruments at their disposal, not about the ways in which aid as such comes to be seen and used as one of the instruments. These theories as a whole do not rest on any description of aid at all, for a description must be a statement of characteristics which classifies that which is described in terms of a delimited and exclusive category.

4. FOREIGN AID AND THE RATE OF GROWTH

The conventional and seemingly obvious view that foreign aid accelerates growth has long been challenged. Critics have argued that in certain circumstances aid could actually reduce the rate of growth and that in general there is little reason to suppose that aid would have much effect either positively or negatively (Cassen :1986). Using data from the 1960s, it was shown that the association between capital inflows and the growth of GNP was roughly zero for fifteen African and Asian countries and inverse for twelve Latin American countries (Griffin and Enos, 1970). A theory that could account for the result was also presented (Griffin, 1970; Dacy, 1975). The basis for a debate had therefore been launched.

Aid can permit countries to postpone improving macroeconomic management and mobilizing domestic resources. External agencies continued to provide aid to Tanzania while the country experimented with disastrous rural policies and institutions. The ready availability of foreign assistance to Pakistan - largely for political reasons - enabled it to postpone fiscal reform. Sometimes aid can strengthen lobbies that have a strong vested interest in a distorted policy framework and so make policy reform more difficult (World Development Report, 1991:p.48).

Aid at times can replace domestic savings and flows of trade, direct foreign investment, and commercial capital as the main sources for investment and technology development. Several countries, have allowed food aid to depress agricultural prices. They have also postponed critical investments in rural infrastructure and ignored the need to build agricultural institutions (World Development Report, 1991:p.48).

Aid is sometimes turned on and off in response to the political and strategic agenda of bilateral funding agencies, making resource flows unpredictable. This resource instability can result in interruptions in development programs, as in Egypt, India and Pakistan.

Uncoordinated and competing bilateral agencies can transfer incompatible technologies and deliver conflicting projects and advice. These problems of bilateral aid arise partly from the widespread practice of tying aid to the purchase of equipments, shipping, and technical advice from agency sources, with substantially reduces net resource transfers. In Pakistan, for example, the cost of using agency shipping lines to transport aid-funded procurements (often a substantial proportion of total project costs) was 50-115 percent higher than the cheapest alternative.

Swings in policy advice from funding agencies can add to the cost of aid for developing countries. Many recipients, advised to dismantle industrial protection and marketing boards, complain that agencies had encouraged these strategies in the 1960s and 1970s, when import substitution and regulation were in vogue. Agencies can often adjust rapidly to the changing thinking on development, but recipients of aid need more time to adjust because of their weak administrative structures.

Bornschier, Dunn and Rubinson has done an extensive study on the effects of foreign assistance and pointed out five basic contributions:

i) The effect of direct foreign investment and foreign aid has been to increase economic inequality within countries. This effect holds for income inequality, land inequality and sectoral income inequality.

ii) Flows of direct aid have had a short term effect of increasing the relative rate of economic growth of countries.

iii) Stocks of direct foreign investment and aid have had the cumulative effect of decreasing the relative rate of economic growth of countries. This effect is small in the short run (1-5 years) and gets larger in the long run (5-20 years).

iv) This relationship, however, has been conditional on the level of development of countries. Although both rich and poor countries have negative effect, the latter suffer from greater impact.

v) These relationships hold independent of geographical area. (Bornschier, Dunn, and Rubinson: 1978).

4.1. Latin America in Perspective:

Latin America is a highly diverse continent, with incomes per capita ranging from levels near to industrial countries (Venezuela) to the level of the least developed countries. There a number of low and low-middle income countries, especially in Central America and the Caribbean, some of which have aid dependence ratios similar to those in Sub-Saharan Africa. Even the advanced economies of the region (Brazil, Mexico, Argentina, Venezuela, Chile, Uruguay, Colombia and Peru) have marked dual economy characteristics, with extensive areas of poverty and underdevelopment (Statistical Yearbook of Latin America and Caribbean 1991).

Following two decades of impressive and generally widespread economic progress when per capita incomes grew on average at about 3 per cent per year, the 1980s have seen serious setbacks in most if not all of the countries of the region due to a combination of policy deficiencies, imprudent borrowing and lending activities and external economic conditions (OECD, 1990). Per capita incomes in 1987 were lower in real terms than in 1980 in all but five out of 25 countries in the region and in six countries they were lower than in 1970.

While the situations, problems and economic structures of individual countries vary widely, a common underlying factor in many cases was that the extreme reliance on external debt finance to fund expansion in the 1970s was not matched by a fundamental increase in debt-servicing capacity because of the inward-looking development strategies and generally inefficient resource allocation characterizing the region. Export volumes for the region as a whole expanded by less than 2 per cent per year in the 1970s compared with 11 per cent per year for Asian developing economies.

The world recession plus the major increase in real interest rates and falling terms of trade for primary exports in the early 1980s were thus sufficient to undermine the financial, economic and policy foundations of many Latin American Economies (Statistical Yearbook of Latin America 1991).

The very large corrections required involved internal and external adjustments of a magnitude that inevitably affected growth performance and living standards. They also helped to create political and economic uncertainties that have affected investment confidence. The region moved from the position of absorbing significant external resources in the 1970s to exporting domestic resources in the 1980s both as debt service and as capital flight. The effort to increase exports while containing imports, and to raise government revenues while cutting back expenditures and subsidies has been accompanied by a major fall in domestic investment and, in many countries, a significant rise in inflation. The large trade surplus of Latin American region indicates the large external adjustment that has been accomplished, but inflation and the investment decline indicate that the internal adjustment task has not been resolved. Indeed, it could be said that there has been over-adjustment externally and under-adjustment internally. With the recent trend towards democratic government in the region, establishing a political basis for effective and sustainable stabilization and adjustment programmes is a delicate yet essential task for Latin America's leaders. The adoption of more effective and equitable policies, which is hampered in many cases by severe political, social and institutional constraints, is the key task ahead for Latin America in the 1990s.

Given the severity of Latin America's economic and social problems, and the enormity of the tasks that confront the countries, solutions will imply deep structural change. Although these efforts will differ country to country, they will have to incorporate two basic policy themes: stimulating creative market forces through an incentive system that fosters production and efficiency: and comprehensive reform of the public sector to eliminate structural deficits, which erode savings and are at the root of the inflation and debt problem, and to improve public sector efficiency.

Progress to date in individual countries varies widely; indeed these variance in policy reform and adjustment progress produces a new kind of differentiation among the countries of the region. The most comprehensive policy reforms have perhaps taken place in Chile and Mexico; whereas the former is now on a dynamic growth path, growth in Mexico has stagnated, partly because Mexico had also to absorb the fall in oil prices. But in these countries and in some others, including Uruguay, Bolivia and Jamaica, the policy environment is now radically different from the 1970s and provides a promising basis for renewed development progress in future. In Brazil and Argentina, there have also been important efforts to reorient economic policies, but they have been less systematic and furthermore the basic domestic stabilization problem remains unresolved despite successive attempts. In Peru, little effort has yet been made to meet the fundamental policy and institutional requirments and there are serious debt issues which are not being approached on the co-operative basis which almost all other countries of the region have adopted; there is a major deterioration not only in the economic situation in Peru but also on the level of civil order.

On the export front, there are already signs of a new dynamism. The export pattern is becoming much less concentrated on major primary export products than in the past, although a few countries remain very dependent to one or two export corps. The growth of non-traditional exports in a focus of policy in many countries (and, in the Caribbean region, of the Caribbean Trade Initiative launched by the United States). There is more attention being given to developing trade within the region, including various kinds of regional integration shcemes. But the export competitiveness of Latin American countries will depend fundamentally on the total policy environment and on the recovery of investment, which in turn is linked closely to making progress on resolving debt problems so that the countries of the region have more external and internal resources at their disposal to generate efficient economic and social development.

There is as yet no clear strategy in which donors have their role for wider development co-operation to help Latin American countries master their current social and economic problems and develop their economic potential. The existence of large areas of poverty and serious policy deficiencies in countries in the middle-income range and with sophisticated infrastructures presents a difficult dilemma for aid donors.

The DAC met in November 1990 with Portugal, Spain, the Inter-American Development Bank, the World Bank and the International Monetary Fund to discuss aid policies in Latin America. The meeting concluded that Latin America is at a turning point in its political, social and economic development. The review noted that Latin American governments were adopting macroeconomic reforms which also give greater role to the private sector and support a shift toward market economies. Recognising this progress, however, the DAC also noted serious challanges with respect to economic growth and related issues of equity:

- absolute poverty is widespread and basic social services, including health and education have deteriorated over the last decade;

- while development in the last decade have exacerbated this problem, it should be recognised that poverty and inequitable income distribution are long-standing structural problems in Latin America;

- continued macroeconomic reforms is essential, but anti-poverty policies must also be put into the framework for restoring economic growth;

- increased economic participation must result from the new development strategies if political progress is to be sustained (OECD: 1990).

The crucial issue is whether the present systems of economic and social organization in Latin America, based on private enterprise, a respect for property however unequally distributed, and economic and political dependence on the United States, are capable of providing real improvements in the conditions of life of the mass of the people. The policies of the international agencies imply that they are , or that such improvement is unnecessary, or secondary to other considerations, or simply that the United States, supported by the major financial agencies, is determined to preserve the existing situation for as long as possible (Hayter 1971:p.154).

Whatever the reasons, the international agencies are in fact pursuing policies which distract attention from, and frequently conflict with, action to improve the conditions of life of the majority of Latin Americans. They have concentrated on financial and monetary issues, and in particular on effects to achieve or maintain financial and monetary stability. But their stabilization programmes have rarely been successful, even in thier own terms; that is, prices have continued to rise, and the private sector has not made the response expected for it. With few exceptions, stabilization programmes supported by the international agencies have resulted in low or zero rates of growth, and low or negative rates of per capita during the period when stabiliozation was attempted (Hayter 1971:pp. 155-6). Hayter also showed that stabilization programmes tend to reduce employment in both the public and private sectors. In the private sector some existing industries are forced to lay off workers, and there is generally a failure to encourage new industries. In the public sector, the international agencies, especially the World Bank, sometimes press for a reduction in employment, without considering the possibility of alternative employment (Hayter 1971:p.160).

The international agencies' policies thus perpetuate, and sometimes increases, the existing severe inequalities in the distribution of income and power in Latin American countries. They do so not only by discouraging and postponing investment, exerting at times a depressive influence on production, and demanding limitations in government expenditure, especially of a social nature, but also in more direct ways.

4.2. Peru and Guatemala: Some Facts

Due to the factor of limited time and space we are going to study some statistics representing Peruvian and Guatemalan economy. The reasons behind selecting these countries are that they both share a history of indigenous people, they always had an inconsistent and conflicting relationship with donor agencies, and they both have a long history of military dictatorship.

Guatemalan economy is dominated by agriculture, which typically contributes 25% of the gross domestic product (GDP) and more than 60% of export earnings. Guatemala is, however, the most advanced of the Central American economies, with a relatively highly-developed manufacturing sector, which contributes 16% of GDP and exports processed products to the country's neighbours (Statistical Yearbook for Latin America and the Caribbean, 1990:314). Increases in foreign aid since the inauguration of a civil government have been dramatic. For example, the USAID budget for Guatemala has climbed from just $24 million in 1984 to nearly $140 million in 1989. Overall, AID looks to the 1989-92 period as "a stage for significant progress" (Krueger, 1989:4). Hoping to help bolster the Guatemalan economy to a 4 percent annual growth, AID also notes, however, that:

> On the other hand, under present structural conditions, a large proportion of the population, perhaps the majority, would participate only marginally or not at all in the proceeds of real growth (USAID/Guatemala c. 1988).

With an area of 1,285,216 sq km and a population estimated to 21,790,000 at mid-1989, Peru is the fourth largest country in Latin America and the fifth most populous, but in 1987 it ranked only 8th in mainland Latin America in terms of gross national product (GNP) per head, with US$1,070 according to estimates by the World Bank. Peru was one of the first Latin American countries in which the IMF was involved, and from 1954 it had a fairly continuous and close relationship with the Fund. Its econimic situation in the early 1960s, after a stabilization programme in 1959, was sometimes held to prove the validity of IMF policies. In this period Peru had rapid growth, financial stability, no balance of payments problems, almost no exchange or import controls and a very low level of government expenditure and revenues (Hayter 1971:p.143). The World Bank and the AID were little involved. But Peru's combination of growth and financial stability was somewhat illusory. The growth started from a low base and was mainly the result of foreign private investment; it was therefore confined to Lima and one or two other coastal areas. Large areas of the country, particularly the highly populated sierra or mountain areas, were barely touched. Their social and material situation, partly as a result of an extremely inequitable system of land tenure, was desperate. There was heavy migration to slums in coastal cities. Even from the point of view of further economic growth, Peru probably needed to expand its internal market. As for the balance of payments, imports were low partly because the consuming population was small. And finally from the mid 1960s the boom in fishmeal exports was coming to an end, and Peru was having difficulties with its exports of suger and cotton (Hayter 1971:p.143). The reason behind was the stabilization programme taken in 1959 by the international aid agencies (Thorp 1967). From then on Peru is facing an ongoing economic challenge which is growing bigger every year.

Development is a very vast and controvertial concept. Without getting into the debate I have chosen some economic and social indicators which are available to examine the recent development in Guatemalan and Peruvian economy.

i) Economic Growth:

Table 2.1. BASIC ECONOMIC INDICATORS OF PERU

	1986	1987	1988
GDP('000 million intis at 1985 prices)	204.8	220.7	201.9
GDP per head	10,135.1	10,648.0	9,967.4
Annual growth of real GDP(%)	10.1	7.8	-8.5
Annual grpwth of real GDP per head (%)	7.3	5.1	-6.4
Government budget (million intis at current prices): Revenue	45,331	66,424	406,010
Expenditure	58,723	108,713	534,043
Consumer price index (annual average for Lima; base: 1985 = 100)a	178	331	2,536
Rate of inflation (annual average, %)b	78	86	666
Foreign exchange reserve (US$ million at 31 Dec)c	1,407.2	645.8	511.0
Imports (US$ million)	2,908.8	3,562.3	3,080.4
Exports (US$ million)	2,530.6	2,660.8	2,694.9
Balance of payments (current account, US $ million)	-1077	-1,481	-1,138

a 88,733 in 1989
b 3,399% in 1989
c US$ 808.4m. at 31 December 1989

Source: Central American and Caribbean Yearbook, 1991

for comperative purpose, see Table 4.4-4.7.

Table 2.2. BASIC ECONOMIC INDICATORS OF GUATEMALA

	1987	1988	1989
GDP (million quetzales at 1985 prices)	11,592	12,026	12,507
GDP per head	1,374.4	1,385.3	1.399.7
Annual growth of real GDP (%)	3.5	3.7	4.0
Annual growth of real GDP per head (%)	0.6	0.8	1.0
Government budget (milion quetzales at current prices): Revenue	2,330.0	2,989.4	3,170.3
Expenditure	2,340.9	2,878.3	3,480.3
Consumer price index (annual average; base: March-April 1983 = 100)	198.6	220.1	245.1
Rate of inflation (annual average, %)	12.3	10.8	11.4
Foreign exchange reserves (US$ million at 31 Dec)	286.1	201.0	305.3
Imports c.i.f. (US$ milion)	1,474	1,557	n.a.
Exports f.o.b. (US$ million)	998	1,073	1,146
Balance of payments (current account, US $ million)	-442.5	-414.0	n.a.

Source: Central American and Caribbean Yearbook, 1991

Table 2.3. ECONOMIC INDICATORS OF PERU AND GUATEMALA
(average annual rates)

	1970-1980	1980-1985	1981	1982	1985	1986	1987	1988	1989
Growth of Agriculture, Forestry, Hunting and Fishing									
Guatemala	3.8	0.9	3.2	-0.7	0.2	-3.0	4.4	4.6	3.6
Peru	-0.6	3.1	9.0	3.0	3.8	6.2	5.1	7.9	-2.9
Growth of Gross Domestic Product, at Constant Market Price									
Guatemala	5.5	-1.4	0.3	-3.8	-0.2	0.5	3.7	4.0	4.0
Peru	3.9	-0.3	4.3	0.3	2.3	8.7	8.0	-8.0	-10.9
Growth of Real Gross National Disponsable Income									
Guatemala	5.8	-2.9	-3.1	-5.9	-0.5	4.8	0.5	5.5	3.4
Peru	3.4	-1.5	[illegible]	-2.2	0.8	11.9	11.3	-7.4	-11.8
Growth of Per Capita Private Consumption									
Guatemala	3.0	-4.5	-4.1	-6.8	-3.7	-1.3	-0.4	0.3	-1.4
Peru	-0.7	-1.0	4.8	-5.0	-1.6	16.0	7.2	-9.3	-16.9
Growth of Food Production									
Guatemala	3.1	3.8	7.1	5.7	6.3	4.2	-0.8	5.7	4.7
Peru	-0.5	3.4	14.0	3.8	-5.2	0.0	7.3	7.6	-3.1

Source: Central American and Caribbean Yearbook, 1991

Table 2.4. MAGNITUDE OF POVERTY
(percentage of households having incomes of less than twice the cost of the basic foods shopping basket)

Households in condition of poverty						
Country	reference year	National	Urban	reference year	National	Urban
Guatemala	...	...	...	1986	68	54
Peru	1972	50	28	1986	52	45

Source: Central American and Caribbean Yearbook, 1991

Table 2.5. GUATEMALA AND PERU: URBAN UNEMPLOYMENT
(average annual rates)

Country	1982	1983	1984	1985	1986	1987	1988	1989	1990
Guatemala	6.0	9.9	9.1	12.0	14.2	12.1	9.6	7.2	14.0
Peru	6.6	9.0	8.9	10.1	5.4	4.8	7.9	7.9	...

Source: Central American and Caribbean Yearbook, 1991

Table 2.6. GUATEMALA AND PERU: INDUSTRIALIZATION
(elasticity of manufacturing with respect to the GDP)

Country	1970-1975	1975-1980	1980-1985	1985-1990
Guatemala	0.8	1.3	1.0	0.6
Peru	1.0	0.5	7.5	1.0

Source: Central American and Caribbean Yearbook, 1991

Table 2.7. GUATEMALA AND PERU: GROSS NATIONAL SAVINGS
(millions of dollars at 1980 prices)

Country	1970	1975	1980	1981	1982	1984
Guatemala	661.2	866.1	1117.4	948.1	745.2	525.4
Peru	2869.8	2484.4	5408.6	5015.5	4586.1	3030.8

	1985	1986	1987	1988	1989
Guatemala	553.1	733.5	604.2	731.5	861.7
Peru	2960.7	2589.1	3208.7	3000.7	3328.6

Source: Central American and Caribbean Yearbook, 1991

ii) Social Development and Welfare:

Table 3.1. PERU AND GUATEMALA: INFANT MORTALITY
(average annual rates per thousand live births)

Country	1960-1965	1965-1970	1970-1975	1975-1980	1980-1985	1985-1990
Guatemala	119.0	107.6	95.1	82.4	70.4	58.7
Peru	136.1	126.3	110.3	104.9	98.6	88.2

Source: Central American and Caribbean Yearbook, 1991

Table 3.2. PERU AND GUATELALA: ILLITERACY
(percentage of population aged 15 years and over)

Country	1960	1970	1980	1985	1990
Guatemala	62.2	54.0	44.2	48.1	44.9
Peru	38.9	27.5	18.1	18.0	14.9

Source: Central American and Caribbean Yearbook, 1991

Table 3.3. GUATEMALA AND PERU: LIFE EXPECTANCY AT BIRTH*

Country	1960-1965	1965-1970	1970-1975	1975-1980	1980-1985	1985-1990
Guatemala	47.0	50.1	54.0	56.4	59.0	62.0
Peru	49.1	51.5	55.5	56.9	58.6	61.4

*The average life expectancy in years of a newborn child belonging to a hypothetical cohort which is subject to a given rate of mortality throughout life.

Source: Central American and Caribbean Yearbook, 1991

Table 3.4. GUATEMALA AND PERU: TOTAL POPULATION GROWTH
(average annual rates per 100 inhabitants)

Country	1960-1965	1965-1970	1970-1975	1975 1980	1980-1985	1985-1990
Guatemala	2.8	2.8	2.8	2.8	2.8	2.9
Peru	2.9	2.8	2.8	2.6	2.3	2.1

Source: Central American and Caribbean Yearbook, 1991

Table 3.5. GUATEMALA AND PERU: PHYSICIANS
(number of inhabitants per physicians)

Country	1960	1970	1980	1981	1982	1985	1986	1987	1989
Guatemala	...	3656	1733	...	7068	...	...	...	...
Peru	1962	...	1391	1311	1186	1088	1029	1035	...

Source: Central American and Caribbean Yearbook, 1991

Table 3.6. GUATEMALA AND PERU: CALORIES AND PROTEINS AVAILABLE
(Calories and proteins per day, per capita, three-year averages)

Country	Calories and protein per capita,per day and three-year average					Grammes of protein per day, per capita, three year average				
	1969-1971	1974-1976	1979-1981	1983-1985	1986-1988	1969-1971	1974-1976	1979-1981	1983-1985	1986-1988
Guatemala	2085	2156	2220	2298	2327	57.0	57.1	57.0	60.4	60.2
Peru	2289	2243	2179	2144	2277	61.1	58.2	57.5	56.8	60.1

Source: Central American and Caribbean Yearbook, 1991

Table 4.1. GUATEMALA: ANNOUNCED AUTHORIZED U.S. ECONOMIC ASSISTANCE

Year	USAID	FFP	EXP/IMP	other
	Source			
1946	0	0	0	.8
1947	0	0	0	1.0
1948	0	0	0	1.7
1949	0	0	0	2.9
1950	0	0	0	1.7
1951	0	0	0	.7
1952	.2	0	0	.9
1953	.2		0	.2
1954	.2	0	0	.2
1955	5.6	.0	0	1.5
1956	18.2	.5	1.2	14.5
1957	17.5	.3	0	1.3
1958	12.6	.2	0	4.7
1959	8.0	.3	0	3.5
1960	5.9	.3	5.0	.7
1961	21.0	.4	10.5	0
1962	4.2	.7	0	4.4
1963	3.1	1.0	0	9.0
1964	5.6	3.0	4.6	.5
1965	7.0	1.1	0	4.8
1966	-1.1	.9	0	4.0
1967	11.1	1.9	6.5	.7
1968	10.9	3.0	0	3.4
1969	5.8	2.4	70.0	.7
1970	28.7	2.6	0	.6
1971	14.2	2.0	2.9	.5
1972	12.5	3.4	0	.7
1973	9.5	1.7	13.5	1.3
1974	2.5	1.2	.6	1.9
1975	9.4	3.4	.8	1.3
1976	32.7	12.8	.2	3.4
1977	14.3	4.5	6.2	2.0
1978	4.5	4.6	0	1.5
1979	17.4	5.3	0	2.0
1980	7.8	3.3	0	2.7
1981	9.1	7.5	0	2.4
1982	8.2	5.6	0	1.7
1983	22.3	5.4	0	2.0
1984	4.5	13.2	0	2.4
1985	75.7	28.2	0	3.2
1986	89.8	24.0	0	2.9
1987	153.5	31.2	0	3.3
1988	109.5	18.6	0	4.1
total	762.1	197.5	122.0	103.5

Source: Statistical Abstract of Latin America, vol.28 1991

Table 4.2. PERU: ANNOUNCED AUTHORIZED U.S. ECONOMIC ASSISTANCE

	Source			
Year	USAID	FFP	EXP/IMP	Other
1946	0	0	0	.6
1947	0	0	0	5.6
1948	0	0	0	1.3
1949	0	0	0	.9
1950	0	0	.9	.9
1951	0	0	20.8	1.3
1952	1.8	0	.6	0
1953	1.7	0	0	0
1954	2.4	.2	0	0
1955	2.4	6.3	101.2	0
1956	2.8	8.7	0	0
1957	4.6	11.5	.1	0
1958	2.7	6.2	11.6	0
1859	2.8	1.0	54.9	0
1960	7.3	9.9	8.1	0
1961	29.2	3.4	26.5	0
1962	26.6	9.0	17.1	25.5
1963	-3.0	6.6	10.7	4.1
1964	28.6	15.1	28.2	6.4
1965	6.3	6.5	14.2	9.2
1866	18.3	8.2	3.7	13.2
1967	22.0	2.4	5.7	2.2
1968	3.9	7.0	4.7	1.6
1969	3.6	7.8	16.0	1.3
1970	8.2	4.6	0	1.3
1071	6.9	6.9	4.3	1.4
1972	31.7	11.1	0	32.5
1973	3.8	4.2	0	71.0
1974	12.1	3.7	55.3	7.4
1975	8.9	6.4	16.3	15.8
1976	13.6	9.7	38.3	54.8
1977	17.4	5.3	2.2	74.3
1978	22.0	31.9	.7	75.0
1979	34.1	35.3	0	64.1
1980	18.7	33.0	0	41.7
1981	34.5	42.5	13.1	6.1
1982	35.8	16.2	0	2.6
1983	35.5	55.9	26.3	2.1
1934	118.9	42.9	0	3.1
1985	37.9	38.8	0	3.7
1986	25.9	28.8	0	3.7
1987	21.3	33.7	0	10.0
1988	28.0	35.0	0	7.7
total	679.2	555.7	480.0	552.9

Source: Statistical Abstract of Latin America, vol 28 1991

In the tables 4.1. and 4.2. the amounts are in per capita dollars. The first subcategory is labeled "USAID". The USAID was created in 1961 by combining the International Cooperation with various other smaller agencies. The second subcategory, labeled "FFP" (Food for Peace, at times called Food for Freedom), gives data for money and goods promised under Public Law 480. The third subcategory, labeled "EXP/IMP", includes loans given by the Export-Import Bank to help Latin American countries cover their trade deficits, allowing them to continue to purchase goods from the United States. Although some may not regard this as true assistance, it frees funds that can then be used for either military or economic purposes. The last subcategory of economic assistance, labeled "Other", includes money given by the Social Progress Trust Fund and other Organizations. Yearly data on toatal U.S. assistance in dollars of 1970 are divided by the population for each country. The tables does not include assistance allocated by international accounts or agencies over which the United States does not have immediate control, e.g. the Inter-American Development Bank, The International Monetary Fund (IMF) or the World Bank.

U.S authorizations for assistance to Latin America are used for purposes of political propaganda in the recipient countries. (Statistical Abstract of Latin America, vol 28:1081). This project builds upon earlier work by James Wilkie. In 1974 Wilkie wrote:

> What is (U.S.) assistance?.... The following arguments might be used against categories included: Military funds

do not really involve assistance because they only have assisted in repression of the population. Peace Corps assistance has done more to assist U.S. citizens in learning about Latin America than to assist in the development of Latin America. Food for Peace has not only stunted the development of Latin American agriculture but lulled recipient nations into as easy solution for feeding a rapidly expanding population, thus making it possible for governments to avoid implementation of controversial but necessary birth-control programs. Since Export-Import Bank loans are granted for the purchase of U.S. produced goods, Latin Americans pay higher prices than might be obtainable elsewhere, U.S. exporters effectively recieving the assistance in the form of a subsidy. And AID funds, like Social Progress Trust Funds, result in a heavy debt burden for Latin America.

(Wilkie, 1974: pp. 147-148)

Table 4.3. OFFICIAL DEVELOPMENT ASSISTANCE: RECEIPTS

	Net disbursement of ODA from all sources						
	Millions of dollars						
Country	1983	1884	1985	1986	1987	1988	1989
Guatemala	76	65	83	135	241	235	256
Peru	297	310	316	272	292	272	300

Source: World Development Report, 1991

TABLE 4.4. ANNOUNCED TOTAL U.S. MILITARY AND DEVELOPMENT ASSISTANCE

year	Peru		Guatemala	
	development	military	development	military
1946	1.0	0	1.4	0
1947	8.0	0	1.4	0
1948	1.7	0	2.3	0
1949	1.3	0	4.2	0
1950	1.3	0	2.5	0
1951	28.4	0	.9	0
1952	3.1	0	1.4	0
1953	2.2	0	.3	0
1954	3.4	0	.3	0
1955	143.3	0	13.2	0
1956	14.4	0	43.0	0
1957	19.7	0	23.2	0
1958	25.2	0	21.5	0
1959	72.1	5.4	14.5	.1
1960	30.9	4.3	14.5	.2
1961	70.8	17.2	38.2	.5
1962	94.2	16.5	11.2	1.6
1963	22.2	9.8	15.8	3.1
1964	93.4	12.5	16.3	1.7
1965	41.9	9.5	14.9	1.7
1966	48.8	11.0	4.3	1.3
1967	35.6	7.4	22.2	1.5
1968	18.7	10.7	18.8	2.5
1969	30.3	3.1	83.2	1.2
1970	14.1	1.9	31.9	2.0
1971	18.9	.6	19.0	6.4
1972	70.7	.9	15.6	1.7
1973	63.7	.9	21.0	2.8
1974	49.6	10.0	3.9	.9
1975	26.8	12.1	8.4	1.6
1976	63.7	11.5	26.8	1.2
1977	52.3	5.8	14.2	.3
1978	64.0	4.4	5.2	0
1979	57.9	2.4	10.7	0
1980	35.7	1.3	5.3	0
1981	33.6	1.5	6.6	0
1982	18.9	1.7	5.4	0
1983	41.0	1.6	10.2	0
1984	55.7	3.6	6.9	0
1985	27.4	3.0	36.5	.2
1986	19.8	.2	39.6	1.8
1987	21.7	0	62.3	1.8
1988	21.9	.1	40.9	2.9

Source: Statistical Abstract of Latin America, 1991 vol-28.

COMPARATIVE STATISTICS

Economic and social indicators for developed countries

TABLE 4.5. GROWTH OF GDP BY KIND OF ECONOMIC ACTIVITY

Region	Years	GDP	Agriculture	Industrial activity	construction
North America	1980-85	2.8	2.0	3.0	1.0
	1985-89	3.6	0.4	3.3	3.3
Europe	1980-85	2.0	2.2	1.9	0.2
	1985-89	3.0	1.2	3.1	4.6

Source: Statistical Yearbook, 1990.

TABLE 4.6. CANADA: UNEMPLOYMENT AND RELATED STATISTICS

Year	Labour force (1)	Unemployment (2)	Participation rate (3)
1980	3.0	7.5	64.1
1981	2.9	7.5	64.8
1982	0.5	11.0	64.1
1983	1.9	11.9	64.4
1984	1.8	11.3	64.8
1985	1.9	10.5	65.2
1986	1.8	9.6	65.7
1987	3.0	8.9	60.3

(1) Expressed as annual growth rate.
(2) Unemployment as a percentage of the labour force.
(3) Labour force as a percentage of the total population 15 years of age and over.

Source: Canada Year Book, 1988.

TABLE 4.7. POPULATION

Region	Population (millions)			Annual rate ot increase (%)
	1980	1985	1989	1985-90
North America	252	265	274	0.8
Europe	484	492	497	0.2
USSR	266	278	286	0.8

Source: Statistical Yearbook, 1990.

TABLE 4.8. PUBLIC EXPENDITURE ON EDUCATION

ountry	years	Total educational expenditure		
		Amount (000)	% of GNP	$ US per capita
United States (dollar)	1975	118,706	7.4	...
	1980	182,849	6.7	539.3
	1985	269,485	6.7	...
	1987	308,800	6.8	785.3
Canada (dollar)	1975	12790,683	7.6	...
	1980	22100,070	7.3	...
	1985	32429,019	7.0	...
	1988	41599,000	7.1	...

Source: Statistical Yearbook, 1990.

With a birth rate estimated at 34.9 per thousand in 1987 (compared with 46.3 per 1,000 in 1960-65) and a death rate of 9.4 per 1,000 in 1987 (compared with 18.0 per 1,000 in 960), Peru's population was increasing rapidly, at 2.3% per year, in 1980-85 with a little reduction in 1985-90 at 2.1% (Table.3.4.), when the rate for North America is only 0.8% in the period of 1985-90 (Statistical Yearbook: 1991). In Peru, the general trend of growth in gross domestic product (GDP) had been strongly positive until recent years, with GDP maintaining an average increase of 3.9% per year between 1965 and 1980. Since the mid-1970s there have been difficulties, caused by the fall in value of Peru's exports, an increase in imports and the expensive nationalization programme initiated by the left-wing military government. Decline in 1977 and 1978 was followed by a brief recovery, with export-led growth of 3.8% in 1980 and 3.0% in 1981 (Central American and Caribbean Yearbook, 1991:p.504). In 1982,however, the falling prices for Peru's exports (particularly minerals), economic recession and financial difficulties led to a decrease in GDP growth to 0.9% and left GDP per head below the level of 1972. In 1983, when the same factors were aggravated by severe floods and drought (and by efforts to adhere to an IMF-sponsored austerity programme), GDP declined, in real terms, by 12.3%. A modest recovery of 4.8% was achieved in 1984, but GDP per head was still less than it had been in the early 1970s (Central American and Caribbean Yearbook, 1991:p504). In 1988 we see a negative growth in GDP of -8.0% and in 1989 it only grew at -10.9% (Table. 2.3.), when the GDP growth rate in North America was 3.2% in the period of 1980-87 (Statistical Yearbook: 1987).

Following growth of only 2.4% in 1985, Peru recorded exceptionally high growth of 8.7% in 1986, and further growth of 8.0% in 1987 (Table. 2.3.). Growth was demand-led, stimulated by President Garcia's boosting of real wages, his extension of import controls galvanizing the production of national substitutes and the subsidizing of areas of private consumption. This strategy collapsed in 1988 when the consequences of balance of payments defecits, an overvalued exchange rate, fiscal difficulties and rising inflation forced the Government to reduce spending and revert to a more conventional free-market approach to the economy. In 1986 the growth of real gross national diposable income was 11.9% and in 1988 we find a drastic decrease at -7.4% which only strengthened in 1989 at -11.8% (Table. 2.3.). The GDP in 1989 was 13% below that of 1988. In the first half of 1989 real wages were barely halfof what they had been a year earlier. With elections due in April 1990 the Government allowed wages to rise above the level of inflation at the end of 1989 giving the domestic economy a temporary boost, at a cost that President Garcia's successor, Alberto Fujimori, would have to meet. In 1988 agriculture and fishing contributed 13.1% to GDP, although they employed 34.8% of the working population. Growth of agriculture, forestry, hunting and fishing is not very promising either. In 1981 the growth rate was 9.0%, in 1988 it was 7.9% and in 1989 we find a negative growth rate of -2.9% (Table. 2.3.). Mining and petroleum contributed 9.5%

to GDP but employed only 2.4% of the working population; manufacturing and construction were responsible for 30.2% of GDP, and employed 13.9% of the working population. Two-thirds of the expansion in the numbers employed between 1973 and 1981 was in the service sector. There are currently very serious problems of unemployment and underemployment, although both are difficult to measure. Urban unemployment was highest with a rate of 10.1% in 1985; then we see a fall in the rates in 1986 at 5.4% and in 1987 at 4.8%. But then it started to rise in 1988 and 1989 with a rate of 7.9% (Table. 2.5.). Statistics from the Ministry of Labour for mid-1988 reveal that of an economically active population of 7,210,000 (one-third of the total population), about 10% were unemployed and 51.4% were underemployed (defined as those earning under the minimum wage or working fewer than 20 hours a week), when the unemployment rate for U.S. was 6.1% in the period of 1985-90. In 1086 only 2,734,000 people were 'adequately employed' according to official statistics. However, such official statistics ignored those who work in the huge informal economy. In 1980 the International Labour Organization estimated that 60% of the urban employment in Peru was provided by the informal sector and the proportion will have risen since then; estimates of the cotribution by this sector to the national economy ranges as high as 39% (Central American and Caribbean Yearbook, 1991:p.504).

The magnitude of poverty rose in 1986 to 52% in the national level and 45% in the urban level compared to 50% in the national level and 28% in the urban level in 1972 (Table.2.4.).

The growth rate of industrialization also fell from 7.5% in the 1980-85 period to 1.0% in the 1985-90 period (Table. 2.6.). During the 1980s inflation appears to have become endemic to Peru. Consumer prices in Lima more or less doubled in every year between 1983-87; in 1988 inflation averaged 670%, in 1989 it was about 4,000%, and it continued to rise in early 1990s. Export enjoyed the benefit of good export prices and a petroleum surplus in the 1970s, but have since fallen in value, declining from US$3,916m. in 1980 to $2,978m. in 1985 and US$2,694m. in 1988: in 1988 the volume of exports was only two-thirds of that in 1985. External debt is a major problem for Peru. The military regime of 1968-80 accumulated heavy commitments in the public sector, and foreign debt increased further in the early 1980s. in 1988 the country's total debt amounted to $18,579m. of which $12,485m. was long-and medium-term debt in the public sector (Central American and Caribbean Yearbook, 1991:p.508).

Guatemala is the most advanced of the Central American economies, with a relatively highly-developed manufacturing sector, which contributes 16% of GDP and exports processed products to the country's neighbours. The Guatemalan economy stagnated in the 1980s: GDP per head decreased by an annual average of 0.7% in real terms between 1980 and 1987. Unemployment was officially recorded at 13% of the labour force in 1989, but this does not include a further 42% who were underemployed. Much of the population, especially the Indians, are occupied in subsistence farming and do not participate in the formal economy (Central America and

Caribbean Yearbook, 1991:p.314).

Guatemala is the most populous of the Central American states. In the period of 1980-85 the rate of the population growth was 2.8%, and in the period of 1985-90 it rised at 2.9% (Table. 3.4.). Agriculture is the main sector of the economy, contributing about 25.8% of GDP in 1989, and providing employment for more than 50% of the working population. Agricultural products account for about two-thirds of exports, with coffee accounting for an estimated 33% in 1989, although in 1986 it accounted for almost 50%. In 1987 the rate of the growth of agriculture, forestry, hunting and fishing was 4.4%, and in 1989 it went down to 3.6% (Table. 2.3.). In 1986 the USA decreased its quota of sugar imports from Guatemala by almost half, from 82,388 tons to 43,600 tons although it was increased slightly to 48,200 tons in 1987/88 (Central American and Caribbean Yearbook, 1991:p.314).

Guatemala has the largest, and one of the most developed, of all national manufacturing sectors in Central America. It experiences rapid expansion in the 1960s and 1970s, under the stimulus of Central America Common Market (CACM) and foreign investment; this growth has slowed by the late 1970s to around 5% per year. The sector contracted between 1981 and 1983, and recorded growth of only 0.5% in 1984. Stagnation of the sector continued in 1985, but there were signs that some recovery was experienced between 1987 and 1989 when manufacturing contributed over 15% of GDP (Central American and Caribbean Yearbook, 1991:p.315).

Following the handover of power to the civilian Government of

Vinicio Cerezo in January 1986, a programme of austerity measures and financial reform was implemented, and as a result, the economy started to show signs of revival after several years of decline. In 1987 the foreign debt total fell to US$2,400m. from US$2,700m., and inflation fell to an annual average of 12.3%. At the end of 1986 international reserves amounted to $362.1m., and for the first time in four years, they were adequate to cover import needs. Undoubtedly this recovery was significantly assisted by the doubling of international coffee price during 1986, and the devaluation of the quetzel during March 1986. Furthermore, the budget deficit which had been 5.5% of GDP in 1984 was lowered to 3.3%. This recovery was sustained through 1987, and brought increased stability. The budget deficit remained at 3.3% of GDP, in spite of government spending rising by 22%.

However, these positive developments could not be sustained following a fall in the price of coffee and a serious reduction in international reserves. At the end of 1988 inflation was 12%, growth 3.8% and non-traditional exports had increased by 200% in two years, but these successes were overshadowed by the rapidly declining level of international reserves. The crisis over reserves led first to the introduction of a single exchange rate in February 1989, and then to the floatation of the quetzel in November, in response to a marked expansion in domestic credit which, by November, had reduced reserves to $110m. Inflation rose to 14.5% by the end of the year, and continued to rise owing to the inflationary pressure brought about by several devaluations of the quetzel. In April 1989, as inflation increased and the value of the quetzel declined, President Cerezo introduced a series of austerity measures were effective only in provoking discontent, especially in the business community. As the November election approached, although the value of the quetzel had stabilized, inflation continued to rise. Moreover, the fiscal deficit was running at a record high, while per capita income had declined to its level in 1969 (Central American and Caribbean Yearbook, 1991:p.315). Investment fell from 15% of GDP in 1978 to around 10% in 1985, with the largest decline being in private-sector investment, which has been deterred by the uncertain political situation and low demand, and shrank by 67% between 1978 and 1982. The country's total debt was estimated at $2,830m. in December 1988. At the same time debt-servising was estimated at 42% of the total of exports.

Loans and aid from external organizations have been focused on the agricultural and industrial sector and failed to show sing of growth in both sectors when in agriculture it fell from 4.4% in 1987 to 3.6% in 1989 (Table. 2.3.) and in the industrial sector the growth rate fell from 1.3% in 1975-80 to 0.6% in 1985-89 (Table. 2.6.).

In early 1986 President Cerezo outlined plans to improve the standard of living in Guatemala, where an estimated 63% of the population were living in conditions inferior to the officiall-defined level of poverty (according to the Table. 2.4., 68% in the national level and 54% in the urban level).

Exports, in real values, reached their lowest levels for more than 10 years in 1987, at $977m., following a decline of 30% since 1980, as export markets contracted and international commodity prices fell. The growth of real disposable income fell from 5.5% in 1988 to 3.4% in 1989 (Table. 2.3.). The rate of urban unemployment rose to 7.2% in 1889 to 14.0% in 1990 (Table. 2.5.) which is almost double. The rate of food production also fell from 5.7% in 1988 to 4.7% in 1989.

In Guatemala increases in foreign aid since the inauguration of a civilian government have been dramatic. For example, The USAID budget for Guatemala has climbed from just $24 million in 1984 to nearly $140 million in 1989 (Griffin, 1989:p.4). Current projections place the figure at $150 million by 1990. Overall, AID looks to the 1989-92 period as "a stage for significant progress". Hoping to help bloster the Guatemalan economy to a 4% annual growth, AID also notes, however, that:

> On the other hand, under present structural conditions, a large proportion of the population, perhaps the majority, would participate only marginally or not at all in the proceeds of real growth (USAID/Guatemala c. 1988).

In recent months, World Bank officials have been considering the formation of a multimillion-dollar fund for Guatemala, to be used by private voluntary organizations (PVOs) working directly with local population in the hope of addressing the economic crisis at grass-roots levels. Perhaps PVOs represent a better alternative than public-sector institutions, especially in rural areas, but as Annis (1988) and others recognize, the "third sector" is rife with political, religious, and institutional oppositions. Meaningful coordination or complementarity probably will not occur. At the same time, without a supportive economic and political climate, even myriad grass-roots activities cannot create sustainable development.

One of the sad facts of development history in Latin America is that external aid without major social and economic reform is largely a waste of resources. Thus, as USAID and other donors stand ready to release hundreds of millions of dollars in the name of development aid, some officials admits privately to a sense of dilemma and a fear of folly, for no substantive changes have taken place in one of the most stratified and minority-controlled economies and societies in the hemisphere (Griffin, 1989:p.5).

In 1984, the Inspector General's audit highlighted the following observation:

> Many of the conditions adversely affecting project implementation described in this report are common to other Central American and Third World countries generally. This report suggests that simpler, more realistic project designs and more intensive project monitoring are... especially crucial in the light of major new funding initiatives now being proposed for Central America (USAID 1984).

The proposition that aid did not promote growth let alone development was greeted with scepticism and new evidence was presented that seemed to suggest that, after all, aid did help to accelerate the growth was found, this was probably because aid tended to be channelled towards countries where growth rates were low (Papanek, 1972).

In the twenty years since the debate was launched much more evidence has become available (OECD/DAC, 1989) and unfortunately for the conventional view, the data continue to suggest that aid has not significantly contributed to an accelaration of growth and, in some cases, appears to have retarded it. Econometric analysis of eighty-three developing countries in the period 1960-77 showed 'a weak and insignificant but negative correlation between aid and growth' (Mosley, 1980:82). The results were unaffected by introducing a five-year lag on the aid variable and thus the suggestion that the direction of causation is from slow growth to aid rather than the other way round is in general not plausible. A later study of between fifty-two and sixty-three countries covering the period 1960-83 and using more elaborate economic techniques, disaggregating the data into three periods and five groups of countries (by region and by level of income) concluded that 'aid in the aggregate has no demontrable effect on growth' (Mosley et al., 1987:631). The authors go on to add that 'the apparent inability of development aid over more than twenty years to provide a net increment to overall growth in the Third World must give the donor community, as it gives us, cause for grave concern' (Mosley et al., 1987:636).

The statistically more elaborate study, based on multy-equation model, shows that many outcomes are possible, but the general conclusion of the study is unambiguous: 'there is no escaping the implication that reliance on foreign capital (aid, private foreign investment and other sources of external capital) does not offer the solution for high and rapid growth' (Gupta and Islam, 1983:134). This finding is confirmed, albeit reluctantly, by Roger Riddell who, after a thorough analysis of the literature, concludes that 'few, if any studies of aid's long-term impact on a recipient country have ever provided statistical evidence that has been able to show unquestionably that it has had a positive effect at the macro-level' (Riddell, 1987:245).

The statistical evidence, then, for the 1960s, 1970s and early 1980s is not consistent with the hypothesis that aid accelerate growth. The evidence from the 1980s as a whole is even less supportive of the conventional view. In many parts of Africa and Latin America the growth of per capita income was actually negative, yet these were regions which recieved large amounts of foreign capital in the immediately preceding years. In 1988 and 1989 Guatemala recieved total Official Development Assistance of 235m. and 256m. which were the largest amounts since 1983 (Table. 4.3.). Yet we find the growth of real gross national income in 1988 and 1989 as 5.5% and 3.4% which is still below the rate of 5.8% in 1970-80 (Table. 2.3.). Massive foreign borrowing and grant aid in the 1970s led not to development in the 1980s but to a fall in average income. In Asis, on the other hand, growth was sustained, often at a high level, yet in the 1980s many of the rapidly growing countries in Asia recieved either no aid (Singapore) or very little aid, i.e. less than 1 per cent of GNP (China, India) or only a moderate amount of aid, i.e. little more than 1 per cent of GNP (Thailand, Malaysia). The Philippines is the Asian exception that proves the rule; aid was generous (more than 2 per cent of GNP), while growth was negetive and the growth of income per head was sharply negative.

Cases certainly can be found where a fall in the growth rate precedes an increase in foreign aid and thus slow growth causes aid to flow. Cases can also be found where an exogenous event causes both the rate of growth to fall and the volume of aid to increase. But such cases can no longer be used to dismiss the finding of a persistent zero and even inverse relationship between growth and aid. The data now cover three decades and scores of countries. The phenomenon is a real one: there is a problem to be explained (Econometric studies can never provide a wholly satisfactory explanation; there is always a problem of the quality of data).

None the less, one should keep the problem in perspective: foreign aid not all that it seems. First, the flow of foreign aid modest and possibly falling both relative to the GNP of donor countries and absolutely. It has long been a target of the United Nations that official aid should be 0.7 per cent of the GNP of donor countries. Actual aid flows however are less than half the target and appear to 0.33 per cent in 1989 (see Table 2). Moreover, the absolute volume of aid has fallen sharply recently; it was US$1.6 billion less in 1989, the first post-Cold War year, than it was in 1988, which in real terms was a decrease of 2 per cent in just one year (Griffin:1991).

The amount of foreign aid provided by the US has fallen dramatically. In 1975-9 aid accounted for 0.24 per cent of US GNP; in 1989 the aid ratio was only 0.15 per cent, the lowest of any DAC donor country and the lowest by far of the major donors. Furthermore, despite its huge economy (the largest in the world), the US ceased to be the largest aid donor, being replaced in 1989 by Japan which in that year allocated US$1.3 billion more to foreign aid than did the US. Indeed, were it not for Japan and few of the smaller donors such as Finland, Denmark and Itally, the aid ratio in 1989 would have been even lower than it was, by a substantial margin. Six of the eighteen countries in Table 2 gave less aid in 1989 (relative to their GNP) than in 1975-9.

Table 5. Official Development Assistance, 1975-89

	1975-9 (per cent of GNP)	1989 (per cent of GNP)	1989 (US$ billion)
Australia	0.51	0.37	1.0
Austria	0.22	0.23	0.3
Belgium	0.54	0.47	0.7
Canada	0.50	0.44	2.3
Denmark	0.72	1.00	1.0
Finland	0.18	0.63	0.7
France	0.59	0.78	7.5
West Germany	0.39	0.41	5.0
Ireland	0.15	0.17	0.05
Italy	0.11	0.39	3.3
Japan	0.23	0.32	9.0
Netherlands	0.83	0.94	2.1
New Zealand	0.39	0.22	0.09
Norway	0.83	1.02	0.9
Swedwn	0.86	0.98	1.8
Switzerland	0.20	0.30	0.6
UK	0.45	0.31	2.6
US	0.24	0.15	7.7
Total DAC	0.34	0.33	46.5

Source: OECD/DAC (1989) and OECD Press Release, 'Financial

Resources for Developing Countries: 1989 and Recent Trends' (Paris, 14 June 1990).

Secondly, there is a danger that as ideological competition subsides with the end of the Cold War, and commercial considerations become even more prominent, the quality of foreign aid may deteriorate. That is, the grant element of aid may decline and the proportion of aid that is united and freely available for worldlike procurement may also fall. At present the average grant element of official aid is about 90 per cent. Thus as the proportion of total aid provided by Japan rises, the grant element may fall.

The grant element refers only to the financial terms under which aid is provided. Also important for the quality of aid is that the extent to which aid is united. At present, about 36.5 per cent of all bilateral aid is tied to procurement in the donor country, 17.8 per cent is partially united in the sense that procurement must be from the donor country or a developing one, and only 45.7 per cent is completely united (OECD/DAC, 1989:209). In other words, well over half of bilateral aid is effectively tied to purchases in the lowest price market. The danger, again, is that as ideological competition diminishes as a motive for aid, commercial considerations may come to dominate humanitarian motives even more than at present, and consequently the quality of aid may deteriorate further.

Thirdly, the geographical distribution of foreign aid is rather arbitrary. Certainly aid is not allocated across broad regions in accordance with the size of their population. Asia, for example, accounts for 68.7 per cent of the population of developing countries yet recieves only a third of official development assistance from the OECD countries. All other regions except Southern Europe recieve a higher share of aid than their share of the population. Particularly noteworthy are North Africa and the Middle East (where the aid share is more than twice as large as the population share) and sub-Saharan Africa (where the aid share is nearly three times as large).

Of course, if foreign aid were distributed progressively, so that a disproportionate amount was allocated to those regions with the lowest average incomes, one would not expect aid shares to correspond to population shares. It is readily apparent, however, that aid is not distributed progressively across regions. The largest amount of aid per capita (US$244) is given to Oceania, where average income is US$1230. The next largest amount (US$26) is given to sub-Saharan Africa, where average incomes (at US$350) are indeed the lowest. However, the third largest amount of aid per capita (US$25) is given to North Africa and the Middle East, where average incomes (at US$2500) are highest of the six regions(OECD/DAC, 1989:240-1). Moreover, the difference in the amount of aid recieved per capita between the richest and poorest regions is only US$1.25. Evidently it is political criteria, not poverty, that ditermines the allocation of official aid.

Even within geographical regions the allocation of aid is based on criteria other than need. In Asia, for instance, per capita income in the region as a whole is US$430 and the amount of aid recieved on average is US$5.16. Average income in China and India, however, are well below the Asian average, yet the amount of aid they recieve also is well below the Asian average, namely, US$1.80 and US$2.70, respectively. Indonesia, on the other hand, benefits from being by far the largest recipient of Japanese aid and consequently although its income slightly exceeds the Asian average, it recieves 83 per cent more aid per capita than the Asian average.

In Latin America, El Salvador's income is 39 per cent higher than Bolivia's, yet El Salvador recieves 56.6 per cent more aid per head. In sub-Saharan Africa per capita income is about US$350 and per capita aid receipts are about US$26. Nigeria, with an income close to the average, recieves only US$0.74 in aid per head. Ethiopia, with an income one-third of the average, recieves US$19 per capita in aid. Zambia, with an income nearly two-thirds above average, recieves more than the average amount of aid. The most extraordinary situation, however, is in the Middle East. Israel, with a per capita income of US$6810 is no longer even classified by the World Bank as a developing country, yet it recieved US$272 per head of official development assistance in 1987-8, in addition to any military aid it recieved, most of it from the US. That is to say, the amount of aid recieved by Israel was twenty-six times the average of all aid recipients and more than the per capita income of countries such as Bangladesh, Tanzania and Zambia. Israel is the largest recipient of US aid. In 1987-8 this country of only 4.4

million people recieved 12 per cent of all US aid. The next largest recipient was Egypt, with 9.4 per cent.

5. FOREIGN AID AND THE COMPOSITION OF EXPENDITURE

An inflow of foreign aid, whether large or small, represents an addition to the total resources available to a country. These additional resources, in turn, make it possible to increase expenditure, and in principle expenditure on anything. Of course, the aid may be 'tied' in various ways, and hence additional expenditures on some types of items may be constrained, but the 'fungibility' of resources is likely to ensure that the constraints on expenditure are not totally binding. In the conventional early literature it was taken for granted that all aid inflows would be used to increase investment expenditure, and that the productivity of new expenditure would be the same as earlier investment, so that foreign aid would have an unambiguously positive impact on the rate of growth. Indeed, in the simple models designed to illustrate the impact of aid inflows, the growth rate would rise by a/k, where a-the inflow of foreign aid expressed as a percentage of GNP and k the incremental capital-output ratio.

This approach, however, presupposes that an inflow of foreign aid is equivalent to an increase in investment, i.e. an augmentation of the stock of capital, which in turn will increase output in the next period. This clearly is wrong. As Joan Robinson said, 'A country which recives an inflow of finance is not recieving a supply of a factor of production called "capital", it is enjoying the possibility of running a surplus of imports or amassing monetary reserves' (Robinson, 1978:220-1). A great deal of wasted time would have been saved had the Robinsonian view prevailed from the beginning. Aid represents an increase in the availability of resources not, as the conventional view would have it, an increase in capital.

Critics of conventional view argued two things. First, part of the aid flow was likely to finance additional consumption expenditure (and hence reduce the national savings ratio). Second, for a variety of reasons an inflow of aid could well result in a higher incremental capital-output ratio (i.e. a rise in k). The net result of these two effects could be a reduction in the rate of growth of output in the recipient country rather than the increase as commomnly supposed (Griffin an French-Davis, 1964 and Griffin, 1969). The resulting controversy centred on the first point to the relative neglect of the second. One important study, however, did find a significant 'decline in general rate of return on capital in the Third World as between the 1960s and the 1970s' and attributed this to 'the multiplication of the number of donors' and a change in the composition of aid-financed projects from power and infrastructure to more costly and 'difficult' projects such as integrated rural development (mosley et al., 1987:634-5).

In the Harrod-Domer atmosphere of the 1950s and 1960s foreign aid was expected to have a positive effect on saving. The thinking at the time was that aid inflows would cause investment to increase; this would generate subsequent increases in income, which in turn would raise domestic savings. K. Griffin and J. Enos pointed out, however, that the empirical correlation between foreign aid and savings across countries is negative, not positive (Griffin and Enos, 1970:pp.313-27). To explain this they advanced the "revisionist" hypothesis that foreign aid actually discourages domestic savings. Aid recieving countries were seen as engaging in aid-switching: increasing their government consumption expenditures, reducing their efforts to collect taxes, and so on. A large number of papers were written, many using econometric techniques, in which the relationship between aid and savings was explored (Chenery and Eckstein, 1970; Gersovitz, 1971; Weisskopt, 1972; Wasow, 1979; Mosley, 1980; Gersovitz, 1982). Some authors argued that savings were not inversely related to aid and others that it was low savings that caused the aid and not the other way round. Still others suggested that the inverse relationship between capital inflows and domestic savings was simultaneously caused by some exogenous event (Morisset, 1989). But most analysts now agree that aid can be a substitute for local savings and that in fact it often has been. In Guatemala announced authororized U.S. assistance suddenly started to rose in 1985, 1986, and 1987 (Table. 4.1.) and we find a declining amount of gross national saving in the period of 1984 to 1987 (Table. 2.7). In 1988 U.S. assistance decreased and saving started to grow again. It is now widely recognized, for instance, that after the 1973 oil crisis much of the aid and foreign borrowing in Latin America was used to sustain consumption rather than increase investment. Indeed, it is precisely because investment and hence output did not increase that Latin America encountered such severe debt-serving difficulties. In Bangladesh, the savings ratio fell from 8 per cent of GDP before independence to 2 per cent in the 1980s, much of the decline caused by 'chronic dissaving by the public sector' (Khan and Hossain, 1989:177). Similarly in the US, the ready availability of foreign capital is associated not with an acceleration of investment and growth but with a fall in the rate of savings. The US has used capital imports to supplement consumption expenditure (or substitute for domestic savings) and in the process has become the world's most indebted country.

These findings of substitutability do not imply that there is no increase in investment, but only that the increase in investment is less than the inflow of foreign capital. Similarly, the findings do not imply that the increse in consumption (or decline in domestic savings) is inevitable, but only that there is a tendency for this to occur. It all depends on government policy in the recipient country. Where government policy is designed to minimize the leakage of foreign aid into unproductive consumption, military expenditure and prestige investment projects, development-enhancing expenditures will rise and growth will accelerate. It has been shown, for example, that in those countries where the ratio of taxes to GNP was rising, an inflow of foreign aid, contrary to the general pattern, resulted in faster growth (Mosley, 1980). But equally, it has been suggested 'that those developing countries which finance recurrent expenditure out of aid are, in many cases, exercising a conscious and deliberate preference for lower levels of taxation than those which would be feasible in the absence of aid' (Mosley et al., 1987:625).

The effect of foreign aid on the composition of expenditure can be more complex than a simple division between consumption and investment suggests. A more refined analysis should take into account the effects of capital inflows on the following:

- the level and composition of investment and the degree of capital intensity;
- expenditure on human development activities such as, education, training and research, primary health care and nutrition programms; in 1980 the number of inhabitants per physician was 1773 in Guatemala, the number rose in 1982 to 7068 (Table. 3.5.), the current statistics is not available. Calories and protein available in Guatemala and Peru declined gradually over the years. In 1969-71 period the amount for Guatemala was 2085 and for Peru it was 2289 (per day, per capita), and in 1986-88 period it fell to 60.2 in Guatemala and 60.1 in Peru (Table. 3.6.).
- unproductive or non-growth enhancing consumption;
- the amassing of monetary reserves and capital flight;
- the level of military expenditure.

The direct (or income) effect of an increase in foreign aid is to raise the level of investment, but by less than the aid inflow. That is, the marginal propensity to invest is less than 1. The indirect (for price) effect of an increase in foreign aid is to lower the real rate of interest. This tends to depress the level of domestic savings by temporarily widening interest rate differentials between the recipient country and major international financial centers, and encourages domestic savings to be placed abroad. That is, liberalization of exchange controls and the globalization of capital markets make it easier for savers in developing countries to transfer funds abroad in response to market incentives. In addition, lower interst rates alter relative factor prices and create incentives to adopt more mechanized techniques of production (or higher capital-labour ratios), with the resulting employment problems that implies. Higher capital-labour ratios in turn are likely to result in a higher incremental capital-labour ratio. An inflow of foreign aid is also likely to result in an appreciation of the exchange rate. This will create an incentive to adopt more foreign exchange intensive methods of production and to rely on imported capital equipment. Finally, the composition of investment is likely to be affected directly by donors' preferences, and historically donors' preferences have introduced a bias in favour of large, capital-intensive, showpiece projects in the public sector with below average rates of return. The result is that the contribution of foreign aid to raising the level of investment and the rate of growth has been modest if not negligible.

The effects of foreign aid and other inflows of finance capital on interest rates and the rate of exchange are likely to be marginal in most countries. The point is that on the whole capital inflows tilt relative prices in the wrong direction. In some countries, mostly small and poor ones accounting for a minority of the population of developing countries, the inflows are large in comparison to total financial savings and foreign exchange earnings and the effects are likely to be much more than marginal. For example, of the forty-two least developed countries, half in 1987 recieved official aid equivalent to more than 20 per cent of their GNP, another third recieved between 10 and 20 per cent and the rest between 5 and 10 per cent. Inflows of this magnitude will affect the price structure and hence the pattern of expenditure. In a number of the least developed countries large inflows of grant aid, soft loans and commercial borrowings have helped to sustain overvalued exchange rates. These overvalued exchange rates were the cause of so called foreign exchange gap in the first place and provided an economic justification for large foreign aid programmes, but the continuation of overvaluation, facilated by inflows, has hampered the development of exports and hence the ability of the recipient country to repay foreign multilateral and commercial loans.

Many things that cc ventionally are classified as consumption might better be reclassified as human development (or expenditure on human capital formation). The rate of return on primary and secondary education is the least as high as the return on physical capital. The return on applied scientific research is probably even higher. Similarly, expenditure on primary health care and nutrition can make a significant long-run contribution to development. In so far as foreign aid permits an expansion of these types of programmes beyond what would otherwise occur, the fact that aid is

often associated with a decline in savings as conventionally measured is of little significance. Unfortunately,
however, there is not much evidence that aid inflows have systematically resulted in greater overall expenditure on human development, or on those types of human development expenditure with the greatest pay-off, although specific instances can of course be found. Typically, foreign aid has facilitated expenditures on urban hospitals rather than rural clinics, on curative medicine rather than preventive public health measures, on scholarships for university students (often abroad and at the post-baccalaureate level) rather than primary schooling, etc. (there are of course exceptions to these tendencies. France, for example, has sent thousands of secondary school teachers to developing countries in Francophone Africa). Once again, the result is that the contribution of foreign aid to increasing human development and growth has been modest.

In the 1980s, the share of education and health in bilateral aid to developing countries fell from 18 percent to 16.3 percent, and in multilateral aid from 14 percent in 1985 to 12 percent in 1988 (World Development Report 1991:p.68).

Table. 6. INTERNATIONAL AID FOR THE SOCIAL SECTORS, 1980-88*
(percent)

Source and type of aid	1980-81	1983-84	1985-86	1987	1988
Bilateral					
Education	12.7	11.9	10.9	10.6	11.0
Health and population	5.5	5.1	5.3	5.2	5.3
Total	18.2	17.0	16.2	15.8	16.3
Multilateral					
Education	..	..	5.0	4.3	4.3
Health and population	..	..	8.9	7.8	7.8
Total	..	..	13.9	12.1	12.1

* Data not available for 1982

Source: World Development Report 1991

Nearly 10 percent of bilateral aid and 5 percent of multilateral aid were allocated to education, which represented an average annual funding of $4.3 billion. Five to 6 percent of bilateral aid and 8 to 9 percent of multilateral aid was spent on health and population programmes, with an annual average flow of $2.7 billion (Table. 6.).

Evidence suggests that aid has not been allocated to priority areas. More than 95 percent of education assistance was targeted to the secondary and higher levels of education, rather than to the primary level. Moreover, the bulk of aid given to primary education was not allocated to increasing the supply of critical resources for learning, such as teaching materials and teacher training, which have been found to be the most cost-effective. In low-income countries, quantitative expansion has been the focus; buildings, furniture, and equipment accounted for 57.8 percent of all aid. Only 1.5 percent of total aid is given for primary health care, and only 1.3 percent for population assistance (World Development Report 1991:p.68).

In some cases foreign aid was spent in the rural sector and intruded in the natural growth rate with disasterous results. In Chimaltenango, a remote part of Guatemala, vegetable production as a source of cash income has been promoted with increasing success for 15 years. In the recent years, AID and the government of Guatemala are supporting expanded programs of vegetable production in more remote highlands areas, such as southern El Quinche and parts of Huehuetenango. But in Joyabaj (southern El Quinche province), vegetable production for export as an alternative seems doomed, at least until more reliable market mechanisms are established. The small farmers had installed irrigation systems with loans provided by the program. The plan was to grow broccoli and other vegetables for export. So far, however, the program had provided only production supports - irrigation, seeds, pesticides, fertilizer, technical assistance (through rarely seen extension agents), and credit. Marketing has been left to the invisible hand of the private sector. Farmers had had two years of good production results and bad market experience. The first year, payment for crops was delayed by several months. In the second year, crops were not picked up at all because it was cheaper for packing plants based in Chimaltenango to fill their quotas with the overproduction of nearby farmers than to bring in harvests from more distant Joyabaj. So they started to plant tomatos for which there is local demand, and some were expanding corn production by adding another crop per year. Lower profits from these crops, however, were forcing those who had opted for the vegetable experiment to migrate to coastal plantations for day work in order to pay off their irrigation loans, calculated over a ten-year period (Krueger 1989:p.3).In Gualemala and other Third World countries, projects must be designed out of the lives of the people they are intended to affect and insofar as possible should be owned and operated by them.

Looking back over the last twenty years or so , the most striking finding is that foreign aid has permitted a rise in unproductive consumption expenditure (which no doubt has raised welfare in the short term) while contributing relatively little to faster growth either through a greater level and efficiency of investment or through human development expenditure. In some cases foreign aid has stimulated unproductive consumption by enabling governments to reduce taxation. The 'Please effect' has worked in reverse (Please, 1967): the reduction in taxation and consequently in public savings has been offset partly by higher private savings but mostly by higher private consumption. In other cases foreign aid has simulated unproductive consumption by allowing the government to increase its recurrent expenditure, e.g. by hiring more civil servants (sometimes, as in Bolivia and Tanzania, with the donors directly financing the higher salaries of selected civil servants (Griffin, 1992:664).

There is, then, an economically meaningful negative correlation between aid and savings and the correlation is strong and significant. Even more disturbing is the association in a number of countries between capital inflows in the form of aid and commercial loans from international banks and capital outflows in the form of capital flight. Not all capital flight is caused by the aid inflows - some occurs for political and other reasons - but it has become evident during the last two decades that in countries such as the Philippines the outflow of capital would not and could not have occured without the inflow. In the French franc zone of West Africa massive capital flight to London and other international financial centres occured precisely at a time when large amounts of foreign aid (relative to the GNPs of the recipient countries) were made available. A similar pattern can be observed in parts of Latin America. For example, the figures for 1973-87 for the four largest debtor countries in Latin America are instructive (in Pastor, 1990 the data is do not take into account interest earnings on the stock of flight capital and hence understate the value of assets held abroad). During this period the increase in Argentina in external indebtness was US$48.1 billion while capital flight is estimated to have been US$29.5 billion. In Brazil, foreign borrowing increased US$96.6 billion while capital flight was US$15.6 billion. In Mexico, the external debt increased US$95.4 billion while simultaneously there was an outflow of capital of US$61 billion. In Venezuela, capital flight (US$38.8 billion) actually exceeded foreign borrowing (US$29.4 billion).

The main economic causes of capital flight are (i) an overvalued exchange rate, (ii) positive differentials in interest rates on foreign and domestic assets and (iii) an increase in the domestic rate of inflation, which tends to be accompanied by a fall in the real rate of interest (Griffin:1990). As we have seen, inflows of foreign aid of larger than marginal magnitude tend to result in an appreciation of the exchange rate and in a fall in the real rate of interest. It is for these reasons that foreign aid and commercial borrowing are often associated with increased capital flight. The net effect of aid-induced capital flight is of course to reduce the effectiveness of aid in promoting development in the recipient country.

Another disturbing feature of foreign aid is its association with high military expenditure. This would be cause for concern in any group of countries, but it is especially worrying to discover that among the very poorest countries in the world, above average inflows of official development assistance are associated with above average military expenditure. This illustrated in Table 3.

Table 7. Foreign Aid and Military Expenditure

Compared (Percentage of GNP)

	Official development assistance, 1987	Military expenditure, 1986
12 countries with low human dev. and high military exp.	16.2	7.2
All 44 countries with low human development	3.6	3.7

Source: UNDP (1990:162, Annex Table 18, and 164, Annex Table 19).

Consider the 44 countries classified by the UNDP as countries with 'low human development'. In these forty-four countries official development assistance is equivalent to 3.6 per cent of GNP and military expenditure accounts for about 3.7 per cent of GNP. That is aid and military expenditure are virtually identical. Twelve of these countries spent more than average on the military (in fact there is a thirteenth country, Angola, that spends more than average on the military, but it has been excluded from the analysis because of lack of information about foreign aid reciepts) and among these twelve countries military expenditure acounts for 7.2 per cent of GNP, i.e. nearly twice as much as for the group of low human development countries as a whole. Foreign aid in the high military-spending countries, at 16.2 per cent of GNP, is a multiple of the average for the group as a whole. One explanation is that among the very poor countries those that systematically recieve large amounts of aid do so because they spend usually large amounts on the military. But an equally plausible explanation is that the availability of large inflows of aid permits those governments that are inclined to spend large amounts on the military to do so. If this view is correct, a reduction in aid could lead to a reduction in armaments in the developing countries. This, in turn, could lead to a reduction in regional conflicts and to less internal repression. The implication of Iraq and other countries of the Middle East, for example, are obvious.

6. AID AND THE DISTRIBUTIVE ISSUES

Let us set to one side the question of the effects of foreign aid on the allocation of resources and consider instead the effects on the distribution of income and the overall incidence of poverty. While it may be true, as argued above, that one must seek the origins of foreign aid programmes in the Cold War, it is also true that many aid programmes are inspired at least in part by humanitarian considerations. Security, diplomacy, commercial advantage and a genuine desire to alleviate poverty and inequality are all part of the mixed motives that characterize contemporary aid programmes. Statesmen may be preoccupied with issues of diplomacy and national security, but the man and woman in the street are likely to judge foreign aid by its ability to reduce world poverty. This is recognized in the aid legislation of some donor countries. It is stated quite explicitly in the US Foreign Assistance Act of 1974, for example, that the first goal of the aid programme is 'the alleviation of the worst physical manifestations of poverty among the world's poor majority'.

It is instructive to compare the performance of the US bilateral aid programme against this clear legislative standerd. The US Agency for International Development (USAID) is evaluated periodically by outside analysts and their report is published. The latest report, like the earlier ones, consists of an ex ante evaluation of USAID's activities, project by project and country by country. The evaluation consists of an assessment of the conception of the aid programme - what it is that USAID thinks it is doing and how it proposes to go about doing it - and not an ex post evaluation of the actual results. Since actual results are seldom as good as planned achievements, one can be reasonably confident that the report does not understate USAID's accomplishment. Considering all types of US bilateral aid, the report concludes that in fiscal year 1989 only 26 per cent was spent in ways that effectively benefit the poor and 29 per cent in fiscal year 1991 (Prosterman and Hanstad, 1990:14). In some countries the situation was even worse. For instance, in El Salvador (the third largest recipient of US aid) and the Philippines (the fifth largest recipient) only 15 per cent of the aid was spent in ways that help the poor. In other words, on average more than 70 per cent of US aid benefits the minority of the population in recipient countries who are not poor and in some countries the proportion rises to 85 per cent. The clear implication of these findings is that US foreign aid programmes, far from reducing inequality in the distribution of income, greatly accentuate inequalities in developing countries.

It would be nice to think that the US is an exception and that the record of other aid programmes is better, but there is no evidence to suggest that in fact other bilateral donors and the multilateral agencies have been more successful in reaching poor. On the contrary, most of the limited evidence available appears to indicate that most of the benefits of foreign aid are captured by middle and upper-income groups. Even projects specifically aimed at low-income groups often have great difficulty hitting the target. For example, an ex post evaluation was recently conducted of United Nations rural development projects aimed at the poor. Twenty-five projects were examined in three of the least developed countries in Africa, namely, Burkina Faso, Burundi and Tanzania. The projects varied in size from less than US$200,000 to over US$42 million. The most striking general finding was that 'the majority of projects (13 out of 25) did not seem to be really helping to meet an important priority need of the poorest of the poor or of another under-privileged group' (Kabongo and Schumm, 1989:12). In Bolivia, the poorest country in South America, the World Bank undertook a US$46.2 million investment programme in three of the poorest regions of the altiplano (Ingavi, Ulla Ulla and Omasuyos-Los Andes). The three projects were a disaster - the planned investment in deep wells was not implemented, the improvement of alpaca and llama herds did not take place, the wool processing factory was left uncompleted, the forestry component was a failure and the health infrastructure reached only 4 per cent of the target group.

Only 71.2 per cent of planned expenditure was actually implemented and almost none of this had a lasting impact on the poor (World Bank, Operation Evaluations Department, 1988). If this is true of projects explicitly intended to benefit the poor, it is very unlikely that other aid projects have had much direct beneficial effect on the alleviation of poverty.

Even those who believe that aid has been of benefit to the p or accept that 'donors do not pay enough attention to the poverty impact of their projects' (Cassen et al., 1986:51) and acknowledge that 'there have been cases where aid has been raised by the critics of foreign aid goes beyond a small number of individual cases and the amount of attention paid by donors to poverty. The issue is about systematic tendencies, i.e. the operation of official aid programmes as a whole on the well-being of the lowest income groups in developing countries. If it is indeed correct, as has been argued, that on the macro-econimic side foreign aid has in general no measurable effect on the rate of growth of per capita income and on the distributive side that aid increases inequality in the distribution of income, then it follows that aid actually accentuates poverty. This may not occur in most countries most of the time.

7. FOREIGN AID AND THE STATE

A major purpose of foreign aid during the period of Cold War was political, namely, to support countries whose governments were on the side of the West in the ideological confrontation with the

Soviet Union. The effect of any official aid programme, whether bilateral or multilateral, is to strengthen the administration that happens to be in power. Foreign assistance, after all, consists of transfer of resources from one government (or multilateral agency) to another, and an increase in available resources is highly likely to help maintain in power the government of the recipient country, even if that is not the intended purpose of the aid. It is possible to think of the exceptions, e.g. aid to the armed forces or police which ultimately subverts a civilian administration, but in general foreign aid helps those who possess power to retain power.

It is for this reason that the political and social effects of foreign assistance are essentially conservative. Aid tends to perpetuate the status quo even when, through policy dialogue, donor countries and agencies wish to modify the status quo in some non-trivial way. This is as true of Soviet aid to Cuba as it is of US aid to El Salvador. A particular and unfortunately rather common difficulty arises when the status quo is the main obstacle to the alleviation of poverty. In such circumstances foreign aid, by strengthening the status quo , becomes part of the problem of development rather than part of the solution. More generally, for good or ill, foreign aid enables governments to do what they were inclined to do, but perhaps to do it more intensively, thoroughly or quickly than would otherwise have been the case.

The objectives of governments is rarely to help their poorest citizens. Governments want to help the people who put them in power and keep them in power. In democratic regimes, this means their constituents, in other regimes, the fractions, social classes, elites and armed groups that wield political power. Those who recieve aid and administer it more often than not regard development in the broadest sense, at best, as a means to some other end, not as an end in itself, the ultimate objective of public policy. We thus come to the conclusion that niether donors nor recipients of official aid typically see aid as an instrument of development. If some develpoment nevertheless occurs, then it is a by-product of aid, not its purpose. Even such a keen defender of foreign aid as Robert Cassen says only that 'most aid does indeed "work". It succeeds in achieving its developmental objectives (where those are primary)' (Cassen et al., 1986:11).

Because of its strong anti-communist orientation, much Western aid, and particularly US aid, was channelled to countries ruled by dictatorships, often of the extreme right, often military in origin. Examples come readily to mind: South Vietnam and Pakistan in Asia; Liberia and Kenya and Zaire in Africa; Guatemala and Heiti in Latin America. Sometimes aid to right-wi g dictatorships was directly juxtaposed to left-wing dictatorships recieving aid from the Soviet block, e.g. Pakistan vs. Soviet-supported Afghanistan, Somalia vs. Soviet-supported Ethiopia, Honduras vs. Soviet-supported Nicaragua. The juxtaposition of Somalia and Ethiopia is an example of diplomatic musical chairs, since prior to the overthrow of Emperor Haile Sellassie of Ethiopia in 1974, the US was the dominant supporter in Ethiopia and the Soviet Union in Somalia, but after the Emperor's downfall, the US and the Soviet

Union quickly changed sides, the US becoming the major donor in Somalia and the USSR in Ethiopia.

Foreign aid during the Cold War contributed to the militarization of the Third World. It affected democratic process by prolonging military rule in many countries, sometimes for years, and in so doing it obstructed the political aspirations of millions of people.

Another consequence of foreign aid is that it tends to strengthen the state vis-a-vis civil society. Foreign aid increases the resources at the disposal of governments. The resources could of course be passed on by governments to private sector enterprises, other non-state institutions or to individual households, e.g. through loans, tax reductions or direct transfers. More often than not, however, governments use the additional resources to enlarge the state - by increasing recurrent expenditure (civil and military), by increasing public investment in infrastructure and by expanding the number of state enterprises. It would be absurd to claim that foreign aid promotes socialism, but it does promote the state relative to the rest of the economy. As a result, donors now find themselves in the curious position of vociferously advocating the privatization of state enterprises while they themselves have inadvertently facilitated the earlier expansion of state enterprises.

In summery, foreign aid during the Cold War had three prominent political effects. First, it tended to strengthen whatever group happened to be in power and even occasionally to create the groups in power. Second, it tended to prolong military rule and weaken democratic procedures. Third, it tended to enlarge the state and increase its power relative to that of civil society. Foreign aid seldom was the decisive influence in recipient countries, but in so far as it had influence, aid tended to perpetuate the status quo. That was one of its purposes and in that it often succeded.

8. THE PROSPECTIVE VIEW OF FOREIGN AID

The geopolitical context that gave rise to foreign aid programmes after the end of the second World War no longer exist. The political transformations that occured in the former Soviet Union and in Eastern and Central Europe, beginning in 1989, effectively brought to an end the Cold War and the ideological confrontation that inspired and sustained foreign aid programmes for more than forty years. With the end of the Cold War the division of the globe into three worlds has ceased to be credible. There is now just one world. Politically, the process of globalization is occuring at a pace that was unimaginable even five years ago. As a result of this process, the Third World as conventionally understood has ceased to exist, or will soon do so.

Foreign aid programmes are bound to change to reflect the new realities of global international relations. While it is never easy to anticipate the future, especially now during the transition to a new order, a number of predictions follow readily from the preceding analysis. First, it is likely that the transfer of resources from the OECD countries to the rest of the world will decline, gradually at first but then at an accelerating pace as old aid programmes and projects come to an end. The embryonic trend we detected above will become much more pronounced. Political spokesmen in the donor countries have expressly denied that aid to developing countries will be further reduced, but the odds are more than even that aid will decline in the years to come.

Secondly, the direction of flows of resources is likely to change. The composition of foreign aid programmes will shift, relatively less going to the former Third World in order to make room for asistance to the USSR (or its successor states) and its former allies in Central and Eastern Europe. The recent cancellation of a large part of the Polish foreign debt is an early indication of things to come. The formation of European Bank for Reconstruction and Development in London is another. Aid will flow, as always, not necessarily where it is most needed but where the dictates of national self-interest suggest it will be most productive. Increased demand for capital in the former Second World, combined with an overall reduction in foreign aid, is likely to result in higher global real rates of interest.

Third, Germany will begin to look to its east and this will be reflected in the size and composition of its foreign aid programme. In a sense, 'foreign' aid is a partial misnomer in the case of Germany because since reunification the largest resource transfer is to the economically more backward part of its own territory, the former German Democratic Republic. Germany can also be expected to take the lead in Europe in providing aid to the former Soviet Union, Czechoslovakia, Poland, Hungary and possibly a few other European countries. The German aid programme to the developing countries of the former Third World, never very large, will contract, initially as a fraction of GNP and then absolutely in real terms.

Fourth, reflecting its status as a major actor on the world stage and as the second largest economy, Japan will continue to be the larger provider of foreign aid. In absolute terms its leads over the US will increase. Relative to its own GNP, the aid ratio, still very low, may well continue to rise for the next few years. Japan's aid is likely to remain geographically concentrated on East (China) and South-East (Indonesia, the Philippines, Thailand and Malaysia) Asia, with a growing interst in South Asia (Bangladesh, India and Pakistan). If Japan's territorial dispute with the former Soviet Union over the Kuril Island can be resolved to Japan's satisfaction, as now seems likely, Japan could join Germany as a major aid donor to Russia.

Fifth, the US is a large net recipient of foreign capital and is likely to remain so for the foreseeable future. The end of the Cold War will produce pressures in the US operating in opposing directions. On the one hand, the disappearance of ideological confrontation will reduce the political inclination to sustain a global aid programme. On the other hand, the attendant reduction in military expenditure - the so-called peace divident - will in principle increase the economic capacity of the US to sustain a global foreign aid programme. However, given the resistance of the public to increased taxation, the urgency to address pressing social problems at home, the need to invest in economic and social infrastructure and the pressure from the voters to reduce the level of public expenditure, diminished political inclination is likely to count for more than enhanced economic capability. Indeed, the enhanced economic capability - or peace divident - may turn out to be very modest if President Bush's 'new world order' requires the US to be the chief policeman, as in the Gulf War.

It thus seems likely that the total amount of US aid will decline, both as a percentage of GNP (a continuation of existing trends) and absolutely in real terms. Geographically, US aid is likely to shift in favour of Latin America. A key question is what will happen to the huge aid programme in Isreal. If it declines, as seems possible, this will pave the way for the large offsetting aid programme to Egypt to contract. A general settlement in the Middle East following the Gulf War could lead to a substantial decline in US and other OECD countries' aid to the region. A US withdrawal to Latin America will leave Japan a free hand in most in most os Asia and the European Community a free hand in East and Central Europe, the USSR and much of Africa.

Sixth, the Soviet Union and its former allies in Europe can be expected to reduce the amount of foreign aid they provide. In fact the G-7 (Group of Seven: the US, Canada, Japan, Germany, France, the UK and Italy) have almost made a reduction in Soviet aid to Cuba a political precondition for economic assistance to the Soviet

Union from the West. The Second World, never large donors from a global perspective, are nevertheless highly significant for a few recipient countries such as Cuba, Ethiopea and Mongolia. Moreover, although it is difficult to obtain accurate measurements of the size of the Soviet Union's aid effort and its GNP, it is possible that in relative terms 'Soviet foreign aid is about three times as much as West Germany's aid and three and a half times as much as Britain' (The Economist, 1990:52). The transformation of the former socialist bloc countries from net donors to net recipients could be one of the more profound consequences of ending the three-fold division of the globe and creating truly one world.

Paradoxically, seventh, the merging of three worlds into one is likely to be accompanied by the greater regionalization of foreign aid. Donor countreis and groups - Japan, the US and the European Community - are likely to become even more closely identified with particular countries, regions and continents than they are at present and there is a possibility that existing spheres of influence will become consolidate and new ones created. Recipient countries may be less able to play one donor country off against another than in the past.

Eighth, the emerging pattern of foreign aid is likely to entail a move further away from multilateralism in favour of bilateral national programmes. This is another respect in which globalization may prove to be less on close examination than it appears to be at first glance. The accumulation of bilateral programmes implies a relative decline (within a declining total) of United Nations aid programmes, especially the programmes of UNDP, the specialized agencies of the United Nations, the regional development banks and the newer and more imaginative multilateral aid institutions such as IFAD (the International Fund for Agricultural Development). The World Bank probably will begin lending to the Soviet Union and Eastern and Central Europe, or increase its lending where it is already doing so. This will further dilute the emphasis of foreign aid programmes on the developing countries.

Finally, bilateral aid programmes, almost always conducted in the self-interest of the donor countries, are likely to become more explicitely formulated to serve not ideological self-interest but commercial and other interests such as the control of international trade in narcotic substances and the prevention of further deterioration of the global environment. The proposed aid to Brazil to prevent further contraction of the Amazon rainforest is perhaps a harbinger of things to come. The aid relationship between donor and recipient countries is likely in future to be marked by greater candour, less hypocrisy, and to take on in part the character of payment for services rendered.

Let us turn now to the implications. The world is changing rapidly, most people think for the better. Change, however, usually entails both gainer and losers and it is important to consider what foreign aid after the Cold War is likely to imply for the development prospects of poor countries. Much depends of course on the economic strategy the developing countries wish to adopt. No doubt each country will adopt its own set of policies, which may or may not add up to a coherent strategy, but a consensus seems to be emerging within international circles (UN, ECOSOC, 1989; UNDP, 1990; World Bank, 1990) and most importantly from within the former Third World itself (South Commission, 1990) in support of a particular cluster of priorities. This is well summerized in the recently published report of the South Commission where the statement is made that:

> development is a process of self-reliant growth, achieved through the participation of the people acting in their own interests as they see them, and under their own control. Its first objective must be to end poverty, provide productive employment, and satisfy the basic needs of all the people, any surplus being fairly shared. (South Commission, 1990:13)

The emphasis in the quotation is on self-reliance, abolishing poverty, creating employment, satisfying basic needs and creating an equitable society. A number of policy suggestions are made in the report, almost all of them very sensible, but emphasis clearly is placed on human development. Indeed 'the development of human resources has to be a key element of new strategies' (South Commission, 1990:15; 99-108).

One implication of the priorities being recommended by and for developing countries, and hopefully soon to be adopted by their governments, is that they can be implimented without resource to a large inflow of foreign resource. Self-reliance is more feasible than previously because the recommended strategy relies more on a reallocation of existing resources than on an injection of aid from abroad. This point is not highlighted in the report, in fact it is nearly invisible, but the South Commission does say that because no significant improvement in the international economic environment for development is likely to occur, 'the development of the South will therefore need to be fuelled by its own resources to a much greater degree than in the past' (South Commission, 1990:79). Thus, precisely at a time when foreign aid for developing countries is likely to decline, a report by the South is published calling for greater emphasis on the mobilization of domestic resources and stating bluntly that 'the central message of this Report is that, to get ahead, the South must primarily rely on itself' (South Commission: 1990:211).

This comes as a gush of fresh air after years and years of clamour for more aid. The old habits, however, die hard. The South Commission is 'deeply concerned' that the events in the former Second World will lead to 'a probable diversion of both attention and resources from development' and hence the Commission puts in a bid for part of the 'peace divident' to be 'set aside for agreed international purposes - particularly ... meeting the basic needs of the the South' (South Commission, 1990:230).

The 0.7 per cent target was adopted by the United Nations in 1968, i.e. more than twenty years ago. Since then there has been no movement toward the target; if anything, movement has been in the opposite direction. It is not only futile but foolish to continue to insist on a target that is becoming even more distant: it raises false hopes and disracts attention from more pressing matters. A dose of realism about aid targets would be to everyone's advantage. This is equally true of the target, adopted in 1981, of 0.15 per cent of GNP the donors should allocate to the so-called least developed countries. In 1981 there were thirty-one least developed countries; today there are forty-two and Liberia has been declared by the United Nations Committee for Development Planning, the advisory body for such matters, to be eligible to become the forty-third. In 1981 the donor countries allocated 0.09 per cent of their GNP to the least developed countries and the proportion has remained constant ever since. In other words, because of the substantial growth in the number of eligible recipients and the relative constancy of the amount of aid provided, there has been a considerable dilution of aid flcws to the least developed countries. Undeterred by this disappointing record, the South Commission not only reaffirms the 0.15 per cent target but says 'it is imperative' to raise it 'to 0.20 per cent of donors' GNP by the end of 1990s' (South Commisiion, 1990:231). This is not just unrealistic, it is quixotic. The Us in 1989 allocated only 0.15 per cent of its GNP to its entire, global foreign aid programme and nearly half of that went to Israel and Egypt, two countries that are evidently not among the least developed. It can be taken as a fact of international economic relations that the US is not going to expand the relative size of its aid programme by a third (from 0.15 to 0.20 per cent of its GNP), cancell all aid to countries not on the list of forty-two (or forty-three) and allocate all assistance to the least developed countries - simultaneously and within a period of ten years. The US may be extreme in its lack of generosity to the least developed countries, but one can be quite certain that the donors as a whole will achieve niether the South Commission target of 0.20 nor the United Nations target of 0.15 per cent of GNP. On this point at least, we have reached the end of the road.

The 0.15 target was in any case a side-road. Perhaps the main highway also is coming to an end. Perhaps the era of large development aid programmes will fade away as the Cold War becomes little more than an historical memory. This is a distinct possibility. And if it should occur, should the world mourn the passing of aid? It is an ill wind that blows no good. Was development aid the good that was carried along by the ill wind of the Cold War?

Nobody can deny the good will, the humanitarian instincts and the sense of solidarity that always formed part of the foreign aid effort. If political expediency fuelled most programmes, it was tempered by a desire to promote development. Unfortunately, however, the record shows that development seldom was in fact promoted by aid. On average, foreign aid seems not to have accelerated the rate of growth. In general, foreign aid went not so much into investment and human development also into unproductive consumption, military expenditure and capital flight. More often than not, foreign aid failed to reduce the great inequalities that characterize so many developing countries. Worse still, after half a century of foreign aid it cannot be demonstrated that aid has actually reduced poverty. The Development Assistance Committee of the OECD candidly admitted this a few years ago when it wrote that 'the most troubling shortcoming of development aid has been its limited measurable contribution to the reduction... of extreme poverty' (OECD, 1985:18). Even the World Bank, the largest of the multilateral development agencies and far from disinterested advocate of aid, is mildly defensive about its claims. In the latest World Development Report, devoted to poverty, it says:

> Aid has often been an effective instrument for reducing poverty - but not always. Donors sometimes have other objectives. In 1988 about 41 percent of external assistance was directed to middle-and high-income countries, largely for political reasons. Even when aid has been directed to the poor, the results have sometimes been disappointing - especially in countries in which the overall policy framework has not been conducive to the reduction of poverty. (World Bank, 1990:4)

Finally, it cannot be said that for all its economic weaknesses, foreign aid has at least encouraged democratic government. The opposite is closer to the truth: foreign aid has a shamefull record of supporting dictatorships and authoritarian regimes.

Latin America and the Caribbean face numerous challenges over the next decade, not all of which are under the complete control of the governments involved. For example, progress on the foreign debt and trade components will largely depend on the receptivity of industrialized countries, particularly the USA, Japan and Western Europe, to strategies for debt reduction and lower interest rates, as well as increased access for the region's products to their markets. At the same time the region is under growing pressure to liberalize its policy on imports. Meanwhile, major problems with regard to domestic policy appear formidable. These include: substantially increasing employment opportunities for a rapidly expanding population, especially in urban areas; simulating new productive investment and commercial activities; improving agricultural efficiency and tenure rights of those who work on the land; reforming and rationalizing internal public finance mechanisms. Apparently foreign aid has no direct effect on these problems.

Those who have long supported aid because they believed it contributed to development have begun to suffer from 'aid fatigue'(Hancock, 1989:189). Those who supported aid for political reasons, as a weapon in the Cold War, have lost their justification for continuing. The 'aid constituency' is gradually being reduced to businessman who see foreign aid programmes as a way to increase sales. If aid has indeed come to this, there is no reason to mourn its demise. But before foreign aid can be interred with dignity, the affairs of the deceased should be put in order.

Foreign aid, in combination with commercial bank lending, has imposed an enormous burden on many developing countries. Indeed the

World Bank has classified forty-five countries as 'severely indebted' and there are a number of others which also have serious debt problems. In 1988 the total external public debt of low-and middle-income developing countreis was US$911,520 million, of which more than two-thirds was in three regions: sub-Saharan Africa; Europe, the Middle East and North Africa; and Latin America and Caribbean. In these three regions between 1970 and 1988, external public debt interested from 10.5-13.6 per cent of GNP to 40.6-78.2 per cent and debt service rose from 5.3-13.1 per cent of exports to 16.5-28.1 per cent (World Bank, 1990:225). The South Commission is absolutely correct in saying 'the point must be accepted once and for all that the external debt of the developing countries is not repayable in full, and that its full nominal value will not be repaid' (South Commission, 1990:226).

There are many reasons why the debt burden has become insupportable in so many countries, but a fundamental reason is that a large part of foreign aid and commercial external loans were not used for development purposes but instead were squandered in the ways indicated above. Supporters of foreign aid try hard to separate the ill effects of commercial lending from the assumed beneficial effects of official bilateral and multilateral lending, but the attempt to separate the commercial bankers from the aid donors is disingenuous. In 1973 and again in 1979 when oil prices were increased sharply and huge surpluses emerged in the OPEC countries, the commercial banks were urged by the multilateral and bilateral development agencies to recycle the surpluses by lending as much as possible to developing countries. Similarly, the multilateral development banks were encouraged to increase their lending in order to counteract the feared deflationary impact on the world economy of the OPEC surpluses. Lending did in fact increase dramatically and for a while the 'success' of recycling was widely celebrated. Roughly speaking, commercial lending was channelled disproportionately to Latin America while multilateral lending was channelled disproportionately to Africa.

When the debt crisis emerged in 1982, triggered by Mexico's inability to service her external debt, lending to developing countries ceased to be regarded as a success. The commercial lenders in particular were blamed for being incautious, for not scrutinizing projects properly and for relying on the taxing power of governments to ensure that sovereign debts would be repayed. Less was said about the reversal of economic policy in the OECD countries, the cuts in public expenditure and the introduction of tight monetary policies, which caused a world recession, a collapse of primary commodity prices, a slowing down in the volume of international trade and a sharp rise in real rates of interest. Massive lending followed by macro-economic policies in the donor countries which would have made it impossible even in the best circumstances to repay the debt, were combined with equally foolish policies in most recipient countries. Develonment in many countries came to a halt and was thrown into reverse; average incomes fell; poverty increased.

The truth is that the debt burden, not economic development, has become the legacy of forty years of foreign aid. It would be better to write off the debts - completely in the poorest countries and very substantially in the other developing countries - than to give more aid. Cancellation of a large part of the external debt of developing countries would be a once-and-for-all gift from the rich countries to the poor, a form of foreign aid that would help to remedy the errors of the past, and a gift that would cost the donors little in terms of forgone income since they are unlikely to be paid in any event. Debt cancellation would be a last hurrah, a bonfire of the vanities that would bring to an end the era of foreign aid. It could be said that nothign so became the true spirit of development assistance as the manner of its departure.

The thrust of my argument is that enough years have passed to be able to assess the effectiveness of official development assistance and on the whole the assessment turns out to be rather negative (such as in Peru and Guatemala). This does not imply that all official aid should be discontinued.

Short term assistance during emergencies is not being questioned. The case for disaster relief - to overcome suffering caused by earthquakes in the Philippines, floods in Bangladesh, drought in the Sahel, famine in Ethiopia - is evident and compelling. The effectiveness of disaster relief certainly can be increased, but there is no evidence that in general short-term emergency aid has caused harm or even on balance done no good. The evidence suggests the opposite, although moral dilemmas can arise when emergency aid is given to a government in the midst of a civil war. Moral dilemmas aside, the response of ordinary people to disasters elsewhere, be they in rich country or poor, is testimony to the empathy and solidarity which can arise spontaneously when other human beings are suddenly exposed to acute distress.

Next, a convincing case can be made for official assistance to political refugees. The number of refugees scattered throughout the world is large and growing and hence more rather than less assistance for political refugees would be desirable. Many groups of reugees - Sudanese, Ethiopians, Somalis, Combodians, Vietnamese, Palestinians, Salvadoreans - are forced to spend long periods in exile and for this reason aid to refugees can be quite different from short-term emergency aid. There is a need not only to help refugees earn a livelihood while they are in exile but also to ease the economic burden on the host community caused by a large influx of impoverished people. Eventually, when refugees are able to return to their own country, foreign aid may be needed to assist resettlement.

Finally, a case can be made for medium-term assistance to five to ten years to Eastern and Central Europe and the Soviet Union. The former Second World does not have a long-term development problem, but it has a severe midium-term restructuring problem. Large injections of foreign finance over a finite period, if used properly, can be expected to yield high returns. There is no case of prolonged assistance to the Soviet Union or to the countries of Eastern and Central Europe: they are not poor, they have a well educated, highly skilled, experienced and healthy labour force, a reasonably good physical infrastructure and a large (if inefficient and technologically obsolete) manufacturing sector. All they need in order to become relatively prosperous is time and a resonable amount of external resources to give their economies some flexibility and smooth the way through the transition period. The situation in these countries is more analogous to that in Western Europe after the Second World War than it is to the developing countries of today and hence a foriegn aid programme similar to the Marshall Plan in size and duration could be remarkably successful.

Thus the case of short-term aid during emergencies, medium-term aid to the former Second World and assistance to political refugees for as long as necessary is not under dispute. These forms of foreign aid clearly are desirable. It is long-term foreign assistance intended to alleviate poverty by promoting economic development that has failed and that urgently needs to be reconsidered.

Overall assessments of aid effectiveness are inconclusive, but country studies yield four important lessons that could srengthen the effectiveness of aid. First, aid often serves multiple objectives. When it is detenmined primarily by political considerations, special care is needed to ensure that its economic effects are satisfactory. Second, foreign assistance can reinforce good domestic policies as well as bad ones, and in the final analysis, efforts to support good policies are crucial. Third, a country's capacity to absorb aid depends on its human, financial, and administrative capabilities. Strengthening these capabilities must be a priority. Fourth, stability in the volume of funding are transparency of conditions on the aid help its recipients put it to better use.

The origin and objectives of foreign aid cannot be understood outside the global context. Foreign aid is a product of the Cold War, o. the division of the globe into First, Second and Third World's and of the hostility of the two superpowers. Were it not for the Cold War there would have been no foreign aid programmes worthy of the name, for without the Cold War it would have been impossible to generate the domestic political support in the donor countries necessary to sustain foreign assistance for more than four decades. Other motives apart from ideological confrontation also played a role, not so much in initiating aid programmes as in sustaining them once the general principle had been accepted. Diplomatic considerations clearly were important, e.g. in mobilizing support in the General Assembly of the United Nations and, in the case of France and Britain, in retaining influence in colonial territories after they became independent. Commercial advantage soon became a prominent motive: securing markets, promoting exports, creating a favourable climate for private foreign investment. And of course, there were genuine humanitarian motives, e.g. in Scandinavia and one or two other small donor countries.

This paper argues that foreign aid programmes originated as part of the ideological confrontation known as the Cold War and the motives behind aid were always more political than economic. It is further argued that the economic justifications for foreign aid - filling 'gaps' in capital, technology and skills - are suspect and that the economic benefits in terms of long-term development are at best negligible. Turning to the future, foreign aid programmes are bound to change to reflect the new realities of global international relations. The outlook for those who favour aid is not bright, but recent changes in thinking about development suggest that more self-reliant strategies could well be more beneficial to the poor than conventional aid-supported strategies.

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