
The Phenomenon of Foreign Aid

What Is Foreign Aid?

Foreign aid is often used to refer to a wide variety of resource transfers. Some think of any transfer of public funds abroad—including military expenditures or trade financing—as foreign aid. Others think of it only as humanitarian relief for victims of disasters. In fact, foreign aid has an official meaning. According to the Development Assistance Committee (DAC) of the Organization for Economic Cooperation and Development (OECD), foreign aid (or Official Development Assistance) is the transfer abroad of public resources on concessional terms (with at least a 25 percent grant element), a significant objective of which is to bring about an improvement in economic, political, or social conditions in developing countries. This definition—expanded to apply to concessional resource transfers, one objective of which is to improve economic, social, and political conditions in any foreign country—is the one we shall use for the purposes of this study.¹ It does not include military expenditures or military aid, trade or investment financing, public funding for cultural exchanges, expenditures on foreign intelligence gathering or covert action, or government-to-government loans at market rates of interest. Funding for anti-drug or anti-terrorism activities abroad, international peacekeeping operations, or efforts to stop the spread of weapons of mass

1. The practical difference in these definitions is that the DAC excludes concessional resource transfers to the better-off countries of Eastern Europe, the former Soviet Union, and Israel. We shall include these transfers, which are significant in size, in our calculations of US aid.

destruction are not included in the DAC definition of foreign aid, although they are often lumped together with that aid in the public mind and, at times, in the statements of government officials. We shall note the size and importance of such flows here but not include them in our overall definition and data on foreign aid.

US foreign aid is provided largely as grants to international organizations, foreign governments, or NGOs. In 2000, of an overall aid level of \$9.4 billion, just over \$1.4 billion, or 14 percent, was planned as contributions to multilateral development banks and international organizations. Detailed data are not available on the proportion of US bilateral aid channeled through NGOs, but USAID officials have estimated that about a third of the nearly \$2 billion Development Assistance funds are implemented by NGOs. US aid is used to fund relief activities, investment projects, technical advice and training, and balance of payments and budgetary support—the latter two are usually termed “program” aid. Aid can also be provided in kind rather than in cash or credits, in the form of food, medicine, or other commodities.

How Much US Aid?

The \$9.4 billion in US foreign aid in 2000 was appropriated to the agencies and programs listed in table 1.1.²

US bilateral economic assistance programs include Development Assistance, intended primarily to promote economic and social progress in recipient countries; Economic Support Fund (ESF) monies, used mainly in support of diplomatic purposes (e.g., peacemaking in the Middle East); food aid (called Public Law 480 (PL 480)) primarily for disaster relief and nutrition intervention in poor countries; programs in Eastern Europe and the former Soviet Union to support economic and political transitions in those countries; funding for the Peace Corps, which sends US volunteers who usually work in communities in poor countries or countries in transition to help improve social and economic conditions there, and for the African Development Foundation and the InterAmerican Foundation, which work on community improvement and empowerment in their respective regions. USAID has policy leadership in Development Assistance and food aid and manages the implementation of those programs as well as the ESF and aid in Eastern Europe and the former Soviet Union. US contributions to and participation in multilateral development banks are managed by the Department of Treasury. The Department of State manages funding for international organizations and programs for refugees.

2. The data included in table 1.1 cover voluntary contributions made by the United States to international organizations and programs. The United States also makes assessed contributions to such programs, amounting to \$880 million in 2000. Only a proportion of

Table 1.1 US foreign aid, 2000 (millions of US dollars)

Type of aid	
<i>Bilateral</i>	
Development Assistance	2,008
Economic Support Fund	2,792
Food aid	800
Eastern Europe and former Soviet Union	1,369
Debt relief	123
InterAmerican Foundation and African Development Foundation	19
Peace Corps	245
State Department Refugee Program	623
<i>Multilateral</i>	
World Bank	811
Inter-American Development Bank and Investment Corporation	43
Asian Development Bank and Fund	91
African Development Bank and Fund	131
European Bank for Reconstruction and Development	36
International organizations and programs	283
Total	9,374

Note: The data in this chart do not include USAID's operating expenses (\$520 million) and other overhead costs. The funds included in "International organizations and programs" are voluntary contributions only and mainly go to the United Nations Development Program, UNICEF, and other agencies.

Source: The numbers used here are drawn from USAID's "Congressional Presentation 2001," <http://www.info.usaid.gov/press/releases/2000/budget2001.html>, supplemented with details from the US Department of State's "Summary and Highlights FY2001 International Affairs (Function 150) Budget Request," http://www.state.gov/www/budget/numbers_full.html#2001. These documents include actual appropriations for FY 2000. Obligations and disbursements of aid may vary somewhat from appropriated levels.

Not included in these numbers are funds spent abroad to fight drugs, crime, and prevent the spread of nuclear weapons. US government expenditures (managed by the Department of State) for these purposes were set at \$520 million in 2000, and the Clinton administration planned to request a further supplemental from Congress for Plan Colombia (to fight drugs and violence there) of \$818 million. One could also include the funds spent on several private institutes and foundations, including the Asia Foundation, the North South Institute, the East West Institute, and the National Endowment for Democracy, which would add just over \$50 million to this total. They are not normally included in foreign aid data, and so they were not included here.³

these agencies provides what could be considered as foreign aid under the definition used here, and much of the US contribution is used for overhead. See <http://www.state.gov>.

3. Ibid.

Other US Foreign Aid Programs

There is reason to believe that table 1.1 underestimates US government expenditures on foreign aid as defined here—perhaps by a considerable amount. A 1994 study by the Office of Management and Budget (OMB) found that domestic US government agencies requested \$1 billion in appropriations (slightly up from the level in 1993), to fund technical assistance and training for foreign nationals.⁴ There have been no studies updating these numbers, and US domestic government agencies do not usually classify their expenditures according to foreign versus domestic activities. But anecdotal evidence and an examination of the Web sites of most US domestic agencies suggest that these foreign aid programs (though they are never termed such by the agencies) have continued, almost certainly expanded, and increasingly become institutionalized with the establishment of international divisions or bureaus. For example, the Department of the Treasury provides advice to foreign governments on taxes and customs laws and administration (and has a line item in its fiscal 2000 budget for \$1.5 million to fund those services). The Department of Justice provides help on strengthening the judiciaries of foreign countries. The Departments of Transportation, Agriculture, Commerce, Labor, Interior, Energy, and Health and Human Services (HHS) and the Environmental Protection Agency (EPA) also have their own programs of foreign assistance relating to their particular portfolios, involving mainly the provision of technical assistance and training to foreign nationals. Finally, the Departments of State and Defense fund concessional expenditures abroad in the areas of humanitarian relief.

It is worth spending a moment examining what has given rise to the establishment of foreign aid programs by federal government agencies whose focus has traditionally been primarily domestic. Many of these agencies have long had international responsibilities. The Labor Department, for instance, has had the lead in representing the United States at the International Labor Organization. The HHS Department has had a major role in US participation in the World Health Organization (WHO). What appears to be new is the technical assistance and training offered by these agencies to foreign governments. The programs are in part a response to the “globalization” of US domestic policies: Acting globally is increasingly becoming essential for dealing with local problems. One

4. Office of Management and Budget, “International Activities of US Government Agencies,” draft, 1994 (part of NSC/PRD-20). This report was never published. Domestic US government agencies actually implement larger “aid” programs abroad than these figures would suggest, because USAID transfers some of its funds to them to finance technical assistance and other development-related activities in foreign countries. Several foreign governments—e.g., the government of Saudi Arabia—have also “bought” technical assistance from various US government agencies, which further increases the overall size of these agencies’ expenditures abroad.

recognition of the globalization of US domestic policies is reflected in a recent statement by the EPA that “international cooperation is critical to achieving EPA’s mission,” including “. . . reducing global, regional and transboundary risks that directly affect health and environment in the United States.”⁵ Other US government agencies have clearly come to similar conclusions. Another sign of the impact of globalization on the US government is the appointment of the HHS secretary to a seat on the National Security Council (NSC) in her agency’s role as a lead on issues of bio-terrorism.

Another spur to the establishment of foreign aid programs in most US government agencies has been the end of the Cold War. With the collapse of communist regimes in Eastern Europe and the former Soviet Union in 1991, the United States initiated aid programs in most of these countries, with funding managed mainly by USAID. But because USAID had no presence in these countries and there were few private organizations experienced in working there, much of the aid from USAID was channeled through other US government agencies to give new governments advice on tax regimes; judicial reform; commercial, civil, and criminal law; and environmental regulations. These activities in former socialist bloc countries moved domestic US government agencies directly into international aid activities. Not surprisingly, once they had established programs abroad and allocated staff to manage them, the agencies made an effort to continue these programs even after USAID funding channeled through them decreased, by allocating their own funds for such activities.

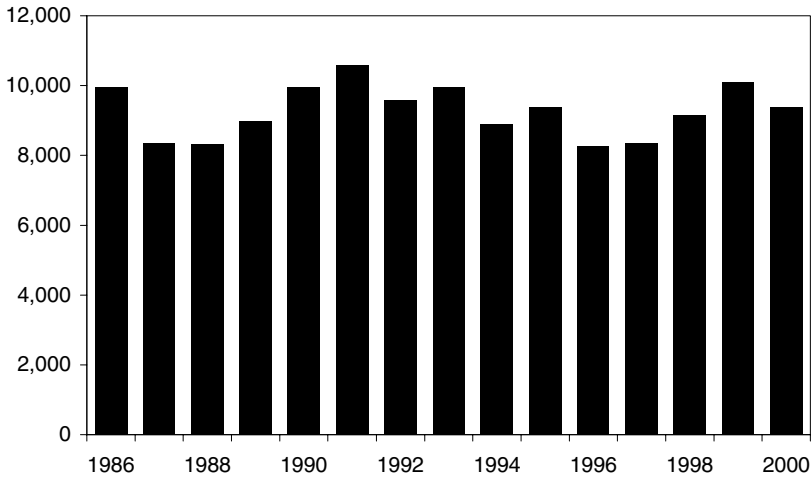
Another important factor stimulating domestic agencies to create aid programs abroad appears to have been the binational commissions set up under the Clinton administration and headed by Vice President Al Gore. Five such commissions have been created—one each with the governments of Egypt, Kazakhstan, Russia, South Africa, and the Ukraine. These commissions, which meet twice yearly, are made up of cabinet secretaries who cochair committees with their counterparts in the partner governments to examine problems in their particular areas of responsibility and come up with programs to address them. These programs, or deliverables, usually require funding, some of which typically comes from the budgets of the agencies themselves and some from USAID or the Department of State.

The dozens of US government agencies active in Egypt, Russia, and South Africa reflect the pressures generated by these commissions. A similar dynamic is at work whenever the president travels abroad with cabinet officers. (Including cabinet officers in these trips now appears to be a common practice, judging from the official delegations traveling with President Clinton to Africa, China, and other countries.) They typically meet with their counterparts in the countries being visited to

5. See <http://www.epa.gov>. Environmental Protection Agency, April 1998.

Figure 1.1 US foreign aid, 1986-2000

millions of US dollars



discuss issues of common interest and frequently to announce new programs.

A final reason—often cited by government officials themselves—for the proliferation of foreign aid programs in domestic US government agencies is that cabinet officers find international travel and work attractive because it is often less stressful or politically contentious than the domestic issues they must spend most of their time addressing, and they like to back up their increasing penchant for travel and work abroad with resources.

The globalization of domestic policies and politics suggests that these programs are likely to continue and grow in the future.

Trends in US Aid

Figure 1.1 shows the trends in US aid (excluding aid from domestic agencies) from 1986 to 2000. From nearly \$10 billion in 1986 (which included a special supplement of ESF for Israel and emergency food aid in the wake of the Ethiopian famine), aid levels dropped until 1989, when they began to rise again, with new aid programs in Nicaragua and Panama in the aftermath of political changes in those countries. Aid reached a peak in 1991, with increases for drought-stricken countries of Africa and former socialist countries in Eastern Europe, and a rise in US contributions to several multilateral development banks. Aid levels dropped in 1994, as a Democratic Congress cut government expenditures in an effort to balance

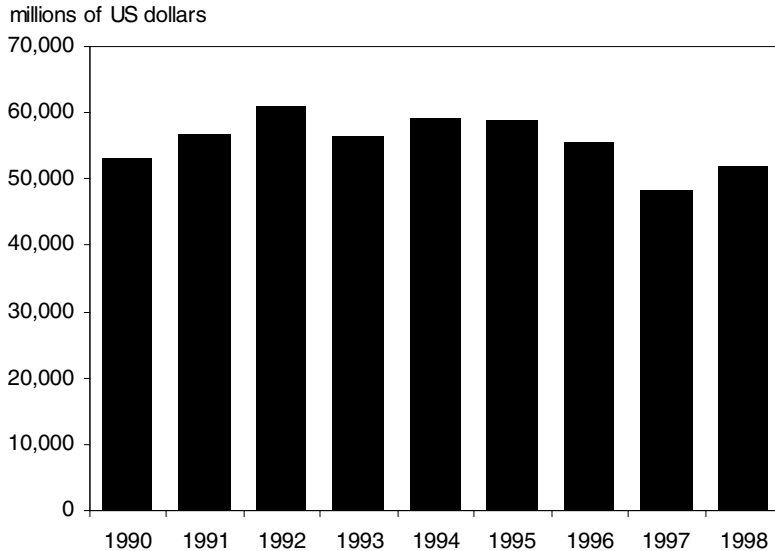
the budget, and dropped again sharply in 1996 and 1997 with the new, Republican-controlled Congress. In 1998, US aid levels rose after Congress agreed to appropriate funds to clear nearly \$400 million US arrears to the World Bank. In 1999, there was a \$2 billion spike in US foreign aid, raising it to \$11.1 billion. This increase was almost entirely for disaster assistance to Central America and for Kosovo refugees. The total aid for fiscal 2000 (as of May 2000) fell back to just under \$9.4 billion. This amount included \$450 million to fulfill US commitments under the Wye River Agreement between Israel and the Palestinians. (Along with the foreign aid budget request to Congress for 2001 was a supplemental request for 2000 of \$1.2 billion for Plan Colombia, further expenditures in Kosovo, and additional funding for debt restructuring.) Clearly, the elimination of the budget deficit has eased pressures to cut foreign aid generally. It is important to note, however, that most of the increases since 1998 have been for humanitarian relief and peacemaking. Apart from funding to clear past arrears in US commitments to the World Bank, aid for long-term development programs has increased by a relatively small amount. And Development Assistance funding remained lower in 2000 than in 1988.

US Aid in a World of Foreign Assistance

The DAC compiles annual data on foreign aid from its member states.⁶ Japan is the largest aid donor, at \$10.6 billion, with the United States in second place, at \$8.8 billion. As a percentage of gross national product, aid from Norway is the largest, amounting to nearly one percent in 1998. Aid from the United States is the smallest, amounting to 0.1 percent in the same year. Trends in aid-giving show that total aid worldwide declined from a peak of \$61 billion in 1992 to \$52 billion in 1998. The largest decrease was a nearly \$4 billion drop in Japanese aid between 1995 and 1998. (Japanese aid had risen sharply before then.) The second largest drop was a \$3 billion real fall in US aid between 1992 and 1998. Canadian, German, French, and Italian aid levels have all declined since 1992. Only the United Kingdom and a number of smaller European countries have increased their aid since that year. It is worth noting that after 5 years of decline, foreign aid worldwide increased slightly in 1998. It is not yet clear whether this was a trend or a hiccup. (See figure 1.2).

6. DAC members include Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, The Netherlands, New Zealand, Norway, Portugal, Spain, Switzerland, the United Kingdom, and the United States. The data in this section are drawn from the DAC, Development Cooperation 1999 Report, OECD, Paris 2000.

Figure 1.2 Net official development assistance, 1990-98



Foreign Aid in Total Financial Flows

One final point needs to be made to set the stage for the analysis in the following chapters. The decline in foreign aid during the past decade has occurred in conjunction with a dramatic increase in private financial flows. From \$53 billion in 1993, private flows to developing countries increased to \$147 billion in 1998. They had risen to \$292 billion in 1996 before the Asian financial crisis and have since fallen. What has not decreased, however, has been the level of foreign direct investment (FDI), which reached \$118 billion in 1998, up from \$70 billion in 1996. Much of this investment has been concentrated in a dozen or so countries, including Brazil and China. (For further details, see chapter 5.) But many other developing countries have benefited from a substantial increase in FDI as well.

FDI is not a substitute for foreign aid. Foreign investors are usually reluctant to invest in basic infrastructure (e.g., rural roads), primary education, basic research on problems related to poor countries (e.g., malaria cures), providing for international public goods, offsetting market failures, providing relief, or helping the needy. But foreign aid can help create the preconditions that encourage foreign investment and enable governments both to finance and manage their own investment without resorting to aid. Thus, for the many developing countries that have made good progress in creating the basic infrastructure and social services necessary to underpin their economic and social progress, and have the policy and institutional environment that private investors demand, the rise in FDI is good news indeed.