

# The Heritage Lectures

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## Conservative Perspectives on Economic Development

Grace Goodell    Jeffrey T. Bergner



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# Conservative Principles and Multinational Companies in Economic Development

GRACE GOODELL\*

When a prominent conservative, invited to attend a Heritage Foundation discussion on multinational corporations and economic development in the Third World, learned that it had been sparked by the observations of an anthropologist, he protested: Why should we businessmen and economists have to listen to an anthropologist? Don't anthropologists just go and live in Third World villages? What could they know, then, about economic development? To an anthropologist, of course, what businessmen and economists see is but the tip of the iceberg. One of the ironies of such *hubris* is found in conservatives' (or at least Burke's) trenchant charge, that those who measure the welfare of the polity, mainly in terms of economic efficiency and from the perspective of central elites, violate the holistic fabric of human society—its traditions and history—and will stand by watching the destruction of irreplaceable mechanisms that guarantee local accountability.

How can American conservatives, who advocate decentralization in our own country, place such unswerving confidence in the ability of mammoth multinationals to bring sustained economic development to the Third World? In this regard, Peter Drucker's classic study of General Motors lies squarely in the Burkean tradition. All enterprises in society have a social context to which they are responsible. In a republic it is not enough that anyone simply make money and "leave the driving" to others. If Professor Drucker received the rebuke that he did from the large corporation that hired him for his criticisms, will a provincial community in Sumatra or Chiclayo have any more leverage over multinationals in their midst?

Conservatives share basic principles with many Third World villagers, provincial townspeople, and urban citizens. Conservatives' keen perception of the dangers of centralization—especially of the dangers of being engulfed by distant and inaccessible power—

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\*Grace Goodell is an anthropologist at the Harvard Institute for International Development. She spoke at an Alternatives to Development seminar at The Heritage Foundation, March 30, 1982.

echoes the Third World objections to colonial rule and the developing nations' long, continuing struggle to protect the regional and local integrity they have won. Conservatives have always been sensitive to transnational agencies' threat to national self-direction; so is the Third World. Conservatives mistrust government elites and warn against the difficulty of holding concentrated power accountable to law; so do many in the Third World. They, like conservatives, deplore the poor's debilitating dependence upon the strong and the rich. Moreover, the conservatives' prescription for a nation's prosperity, economic pluralism, is often the Third World's as well. Indeed, the people of the Third World—far more ardently than Americans—seek to expand opportunities for new entrants to participate in the world economy. When citizens there object to multinationals' domination of global production and sales in many fields, they are expressing Adam Smith's concern for an open marketplace. Conservatives would take the broad base of Third World producers and citizens more seriously if they appreciated that the people "on the ground" in the Third World must counter centralization in their own countries as well as international centralization in the world at large.

The question, then, is to what extent and under what conditions will American private enterprise, as we generally find it in developing countries, further these decisive fundamentals of conservatism. The British colonial policy of enforced free trade ruined whole sectors of India's flourishing textile industry; after as much as a century of U.S. investment in certain areas of Latin America, those same areas still remain poor and polarized. Some Southeast Asians attribute the strength of Japanese corporations today to Japan's exclusion of foreign enterprise for many years. American private investment may enrich Third World nations, but by no means always. Nor automatically.

Of our various forms of investment abroad, multinationals—including banks—constitute this discussion's main interest. By multinationals we do not simply mean companies owned by stockholders from more than one country, but rather companies with global operations. Affirming their contributions to the Third World (employment, technology transfer, etc.—multinationals constitute one third of the world's GNP), recognizing the many exceptions to any generalizations in such a diverse field, and apologizing for the oversimplification which brevity requires, we focus here on a few of their liabilities to the development of a Third World country:

“liabilities” in conservatives’ own terms of what conservatives want for our country.

In essence, the quick returns to economic efficiency that are promised by American enterprise abroad often clash with those countries’ and provinces’ more long-term concerns: decentralization, the continuity of the cultural and social fabric, the accountability of power, and diffused responsibility. Disproportions in scale and their likely exaggeration over time (especially when complementary American policies encourage political centralization in many Third World countries) constitute the heart of the problem.

Since foreign investment requires the ability to absorb large initial costs, an American company’s sheer size is a major factor in determining whether it will invest overseas. Many multinationals in the Third World are much larger than their would-be local competition, and larger, too, than local (or even sometimes national) governments. Those countries which need our help the most are the least likely to attract firms suitable in size to their own domestic scale. Poor countries are less able to bear the task of advertising investment opportunities, especially for reaching smaller firms. Furthermore, investment risks are often highest in the poorer countries; hence, it is more difficult for medium-sized firms to bear, and smaller American firms find it very expensive to appraise investment environments abroad. In short, all these factors favor investment by mammoth multinationals rather than medium-sized firms, although the countries most in need of assistance are also most vulnerable to the disruptive effects of these enormous foreign enterprises.

### The Ramifications of Size

Small is not beautiful, nor is big bad. Rather, the problem is one of proportions, and mixed sizes in an arena of interaction. (This was always foremost in Burke’s understanding: the balance which is required for healthy give-and-take, for advancement and retrenching, and for the possibility of opposition being able to combine with challenge and concentrated bigness.) In a free economy, as in a healthy polity, the units of participation must span from small and local to large and national—step-by-step, organically to enable combinational flexibility (both economic and political combinations). This means that there must be a broad range of middle-sized actors, political groupings, institutions, and firms. Into a poor and inexperienced Third World country with a small

population comes an American multinational. Its scale, with its worldwide production and marketing systems (one small part of which extends into any given Third World country), causes enormous disproportions; and these disproportions threaten the flowering of indispensable, indigenous middle-sized units.

By the time a multinational has imparted new expertise to its Third World rivals, counterparts, or employees (so-called technology transfer, which is often completed just as the company is ready to switch to even a newer technology), the multinational's overwhelming success in the market precludes any Third World firm from putting these new skills to use in competition against it. Even with the new "technology," who can raise the billions of dollars necessary to match a multinational in its field? And yet surely, in Adam Smith's terms, the key determinant of whether such a process is successful, from the Third World's point of view, is whether it fosters economic pluralism in which new firms can eventually challenge old ones in their domain. According to Professor Laura Nash of the Harvard Business School, whose work concentrates on multinationals abroad, the evidence that this process does take place, or that it is likely to, is extremely thin.

After a generation of our intensive postwar investment in Asia, Africa, and Latin America, few indigenous firms now compete with ours on their own ground. At best, local entrepreneurs become national suppliers or marketing outlets for multinationals, freeing the latter to expand further on a global scale. In a Third World nation's view, the relational equation in such "growth" between its firms and the American multinational only shifts the previous subordination/superiority to a higher level or broader scale, but the equation itself has not changed. More commonly, Third World associates who have benefitted from "technology transfer," but whose competition as independents would have to face the multinational's command of the market, simply acquiesce to our presence—just as citizens become politically apathetic and dependent when confronted with the monolithic State. Thus, while more jobs have been generated by these multinationals' success, the disproportion between them and any countervailing forces has been widened in the process.

Another ramification of the characteristic size of American investment abroad is that it bloats Third World capital cities at the expense of the provinces, centering all modern resources there and then requiring governments to provide expensive urban amenities quite prematurely (considering the national context). Further-



more, few multinationals at home or abroad manifest the civic responsibility that frequently distinguishes provincial family firms in the Third World—who however do not enjoy the same tax relief as the multinationals or their many other special incentives. Third World citizens and workers trying to tackle local problems on their own often find it impossible to locate anyone in a particular multinational who will accept responsibility for decisions which affect their community—a complaint reminiscent of many businesses' lack of concern here at home (until recently), about the decline of the neighborhoods around them. While stronger alliances between neighborhood businesses and neighborhood groups are increasingly important in the U.S., a sense of place, which conservatives cherish—and which is so vital to political development—is almost unknown among multinational giants. Local groups and governments have little claim on them. When pressed hard they threaten to leave—and will. The world is their oyster.

However, the main way in which American investors undermine political development in the Third World is by binding their fortunes to the host country's oligarchs. Such alliances are rational, but more is at stake than company profits! Through the elites' all-pervasive financial affiliations with American investors they concentrate political control as well as wealth—and this, in societies with very weak countervailing institutions. Doesn't Iran today charge our economists with a once fabulously booming GNP, won under their tutelage at the price of political development? If Tocqueville were to hold American investment accountable for its effects on the vigorous give-and-take of public life in these new nations—give-and-take which he thought to be the foundation of every society's common enterprises—would he view that investment favorably?

The size of our firms abroad, their relative centralization, and their external base enable them, far more than local entrepreneurs, to accommodate the insatiable demands of the ruling elites, while the scale of their risks makes such partnership mutually attractive. After all, the elites implement regulations and allocate government contracts (in countries where the State is often the major spender). Foreign firms frequently serve as public agencies for entire sectors of the national economy, making it difficult to distinguish Ministers from Board members. The small coterie of the very rich prospers from consumption and government spending rather than from local investment. So it is no wonder that the elites promote the establishment of foreigners rather than the par-

ticipation of upstart local businessmen and labor unions—who might someday challenge their oligarchy.

On their part, the interests of many American firms match those of the elites in protecting short-term order at the price of long-term development; in resisting legal and bureaucratic reforms; in excluding competition; in intimidating dissenting voices; in silencing regional and local politicians; even in opposing effective taxation for fundamental government services which might help usher in an expanding middle class. This apparent hand-in-glove collaboration between our free enterprise “assistance” and debilitating political centralization and corruption is not always deliberate, but rather a result of the host country’s political environment. Indigenous entrepreneurs themselves respond to such an environment by investing abroad, many in America; only multinationals were wealthy enough to pay the prices demanded by autocratic rulers. Still, in doing so they exacerbate domestic imbalances by lending their disproportionate weight to the cause of the autocrat, thereby working against our own long-term interest in sustaining development in the Third World.

Often U.S. multinationals conflict with our most widely acclaimed foreign aid programs as well, such as land reform or human rights. In summoning the State Department or prominent international financial agencies to reshape host-country politics to their liking, they imperil conservatives’ cornerstone of international order, the primacy of national sovereignty.

Indeed, one is hard put to find many historical cases in which American enterprise in the Third World has advanced the political principles for which conservatives stand, instead of concentrated power.

Nothing could illustrate this better than the four Third World countries which multinationals hold up as models for development along lines they recommend: Korea, Taiwan, Singapore, and Hong Kong. These four countries stand out among Third World nations for their exceptional ethnic, religious, and tribal homogeneity, which should facilitate pluralism and decentralization; yet they are also noteworthy for their minimal political life—Hong Kong in fact being the last vestige of British colonialism left in the world. Unlike most other Third World countries in the world, they are distinguished politically by the dominant siege-or-survivor mentality resulting from the massive immigration of refugees: a situation which makes multinational investment a more expedient development strategy in these countries (at least for the first generation) than it might be elsewhere—although at the same time re-

tarding even more seriously the evolution of an indigenous social and political fabric. Can conservatives remain credible to the Third World when they advocate these four illustrations of political vacuum as realistic and imitable models for development?

Despite particular exceptions, a general pattern emerges. The risks of investment in the Third World make such prospects attractive only to very large companies. But this very scale, in turn, causes disproportions which are hazardous, if not fatal, to the development of a firm social fabric with its middle-range institutions and political life in many new nations. We know that without political maturity no society can sustain development or even retain its benefits. The larger our private investments abroad, the greater the dislocation of indigenous social and political life, cultural norms, local investment, purchasing, production, and marketing patterns. The larger our private investment, the more likely is economic and political centralization, both in each poor country and in the world at large. While saying that we will only assist countries which take free enterprise more seriously by favoring more multinational investment, we are thus at the same time fostering political centralization.

In any event, we see in our own country as well as in the Third World that the large firms provide far fewer jobs per dollar invested, and fewer technological advances than the smaller and medium-sized ones; multinationals, the fewest of all. Shouldn't we expect the same abroad? The larger firms import more machinery and materials than the smaller and medium-sized ones, contributing less to domestic manufacturing; the larger ones are more energy-intensive and require much higher technical and managerial skills than the small and medium-sized firms. There is evidence in Latin America that the large, multinational firms are less flexible in meeting changing markets and, as we have said, foster concentration instead of competition. It would seem, then, that a conservative economic development policy would place particular emphasis on encouraging indigenous small- and medium-sized firms in the Third World itself, and on helping American firms of similar scale to invest abroad.

## Suggestions for the Future

### *1. Small-Scale Entrepreneurs*

In many Third World countries the informal urban sector employs as much as 40-50 percent of the urban labor force, a percentage which is steadily increasing. The average size for all indus-

trial firms in Sierra Leone is 1.8 workers, producing 43 percent of the industrial sector's value added. In the Philippines, 40 percent of the new urban jobs added annually (200,000) will be created by tiny businesses of one or several people. In the poorest residential areas of Third World cities, self-employed entrepreneurs outnumber those working for others, and the net income of the former frequently exceeds that of unskilled labor.\* The growth of these tiny firms into middle-sized firms is often obstructed by lack of access to institutional credit, lack of information about appropriate production processes, and lack of suitable market outlets, not to speak of the special concessions favoring multinationals which they do not enjoy: subsidies, protection, incentives of various sorts, the ability to influence policies and bribe officials. American assistance could foster conservative economic and political principles by focussing on this level of the Third World's own indigenous capital development, rather than by simply reiterating the need for more of our own multinationals.

Business women constitute the large majority of these small-scale entrepreneurs. They derive from the low-income sector and mainly serve that sector's needs. These entrepreneurs are extraordinarily flexible—canteens moving from one construction site to another, vendors and services following rural market-cycles. They require little initial capital investment (\$3.00 to begin roasting and selling corn-on-the-cob in Cairo; \$8.00 to begin manufacturing woven baskets and mats in Indonesia). Most such small entrepreneurs have thought out their plans clearly for operation and expansion; small loans of \$50–\$100 enable them to cut the time they spend procuring raw materials (weekly rather than daily), to buy these in bulk quantities at cheaper rates, to improve their equipment, and expand to new markets. Even increasing their income by a dollar a day may enable a child to attend school or allow the business to employ a new worker. Programs assisting these small businesses have very low administrative costs, and their credit components often enjoy a 90–98 percent repayment rate.

## 2. *Middle-sized Firms*

Middle-sized firms in the Third World need our assistance as much as the small entrepreneurs do. By the time a firm is middle-sized its growth has usually tested the entrepreneur's abilities and drive, yet these firms are the most seriously harassed of any by government taxation, regulation, and restrictions (since the small

\*United States Agency for International Development, *Pisces Studies I*, 1981.

ones are too miniscule to justify bureaucrats' attention, and the large ones can afford to bribe officialdom). In countless Third World countries we note how few middle-sized firms occupy the space between mini-businesses and large corporations: a highly unfavorable situation for the stability and health of the economy.

Middle-sized firms often have the greatest difficulty gaining access to funds from abroad, especially public funds. The United States could encourage the growth of capital markets; help improve privately owned development finance companies (and perhaps even finance them); and facilitate medium-sized firms' search for foreign investment partners as well as suitable markets abroad. In Japan the Tokyo Stock Exchange and MITI are both studying proposals for listing medium-sized firms on the stock exchange, in order to provide better backing for young companies as well as to stimulate individual investors' interest in the stock market. Their decision might provide a useful model for some developing countries. The Federal Republic of Germany invests directly in small Third World firms to encourage their development, and Japanese trading companies enter into partnerships with indigenous entrepreneurs in developing countries.

We could assist middle-sized firms considerably more in upgrading managerial expertise. Aid programs could help the private sector in project identification and elaboration, establish clearing-houses and promote more entrepreneurial exchanges. Many industrial extension services for medium-scale firms need improving, which should be done according to the type of industry, not the location. This ought to publicize the full range of production-technique alternatives available to indigenous entrepreneurs, documenting such alternatives for general use. We could encourage the growth of "technology middlemen" who bring together would-be users and sellers of technology for medium-sized firms: for instance, like the British Technology Transfer Group, a non-profit concern established by 10 British companies for technology exchange. Many older technologies would find a ready market in developing countries.

### *3. Multinationals*

Finally, we might much more creatively and vigorously assist those multinational corporations which do invest abroad, in learning how they might spend their "social responsibility" budgets (often called "good will costs") more constructively. Most multinationals set aside millions of dollars for token hiring of local people

they do not actually need, for hospitals, schools, and other philanthropic endeavors which essentially make beneficiaries more dependent on them. For example, they may plow farmers' fields rather than helping them do so themselves. This only creates more resentment, the natural reaction to dependence. Furthermore, when the lucrative period of plant construction ceases, when the company ultimately exhausts the local raw materials, or when conditions prompt a move elsewhere, the multinational's withdrawal leaves behind it a region-wide economic disaster. Instead of providing these services paternalistically, foreign banks and the multinationals they fund can be urged to adopt approaches which will build a self-sufficient regional economy based on initiative and enterprise. These approaches would in fact reduce companies' "social responsibility" costs and more certainly assure local good will. This has been dramatically demonstrated by Partners for Productivity, a private voluntary organization, advising the Liberian American Mining Company in anticipation of the company's departure from Liberia in the near future.

What other existing attempts to offset the present centralizing tendencies of our investments can Third World countries build upon? Some license multinationals for a limited period of time, after which they are bought out by nationals. Can that approach be improved? Can we do more to integrate our businessmen into Third World companies as individuals, for prolonged periods, or to foster the exchange of expertise among Third World businessmen themselves? Can we encourage the enterprise of smaller American firms abroad, even of individuals (like the early merchant-adventurers or, indeed, like Jim Thompson's work in Thai silk)? Can we increase the number of American stockholders—and not just large banks—investing on their own in Third World firms of all sizes, and yet not dominating them? Can we develop means by which Third World entrepreneurs might secure access to patented technology they need, without having to enter into partnership with multinationals? What can we learn from the older British firms, which do assume vital civic responsibilities in Hong Kong, Singapore, and Kuala Lumpur? Finally, how can conservatives help Third World citizens more effectively to hold multinationals accountable to their local communities?

Increasing American investment abroad develops our own capacities further. By lowering trade barriers, on the other hand, we might more directly spur the initiatives of Third World entrepreneurs and the productivity of their institutions. It is not at all clear,

for instance, that our new Caribbean Basin Initiative encourages substantive indigeneous development of small- or medium-sized producers rather than simply greater prosperity for corporate America. Multinational corporations are the first to realize what conservatives once disparagingly called "One Worldism." How can small and poor countries comprehend (let alone monitor) such massively complicated organisms upon whom so much of their stability and development depends? Attempting to do so, the Third World resorts to international agencies, such as the one proposed to regulate mining and seabed, or international labor alliances. Thus, in time global centralization itself may elicit global counterbalances. Suspicious as conservatives are of unchecked power, they can only either applaud these efforts or help to find alternative approaches to development.

Despite our wealth and expertise, American multinationals as we see them today in the Third World may be bound by their very strengths. The organizational requirements of scale may determine their investment options abroad, despite themselves. Perhaps there are laws of comparative scale which distinguish between economic free enterprise on the one hand and freedom from social accountability on the other. Perhaps because they have ignored the importance of this second factor, American multinationals as well as economists have proven to be notoriously poor judges of political maturity in the Third World and its importance for sustained economic development.

# Does Development Assistance Have a Future?

JEFFREY T. BERGNER\*

In 1961 President John Kennedy called for a “Decade of Development” in which the world’s poor nations would at last make substantial progress toward prosperity. We have now had *two* decades of development, and are entering our third. In the past decade alone, the United States has provided \$57 billion to the developing countries, \$43 billion in bilateral development assistance and \$14 billion in contributions to the multilateral development banks.

Despite this record, and the record of other industrialized nations, there are currently many voices calling for substantial new transfers of development assistance. These voices are not likely to grow quieter in the coming years, for they do not reflect in any sense a new venture; what they call for is simply more—and perhaps much more—of what we have been doing for two decades.

In the face of calls for increased redistribution of the world’s wealth, the United States government will be obliged to think through its position carefully. It will not suffice for either theory or practice to espouse a development policy which is but a paler copy of that demanded in the name of global redistribution of wealth. Nor is there any reason for this; careful attention to our considerable experience with economic development provides many clues for shaping a program of assistance into a truly useful tool to aid the development of nations.

A careful examination of the premises of what now passes for “development assistance” reveals shortcomings that cannot and will not be overcome by increases in quantity, however large they might be. These premises were first set forth in 1961, and despite the fact that much new ideological baggage has been attached to them over the years, they remain fundamentally the same.

The Foreign Assistance Act of 1961 remains the basic legislation governing development assistance. This legislation reflects the belief that substantial long-term resource transfers are indispensable for economic development. Its chief characteristic—and its

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\*Jeffrey T. Bergner is Administrative Assistant to Senator Richard G. Lugar.

This paper, prepared for The Heritage Foundation’s Alternatives to Development series, has benefitted from a number of discussions several years ago with Alvin Drischler.



chief limitation—is its thoroughly apolitical, economic view of the world. Development assistance has for twenty years been predicated on the view that economic affairs drive political events, and that nations will develop more or less quickly regardless of the character of their political regimes. This, however, is a particularly inappropriate notion to apply to the less developed nations, for it is precisely in the less developed nations that political decisions are crucial. A relatively full range of political and economic alternatives is open to the leadership of many developing nations, and the choices which are made there are apt to be of a deeper, broader nature than those made by industrialized nations with long records of tradition and precedent.

### Premises of Current Development Assistance

To understand the nature of current development assistance, we must distinguish it from other forms of economic assistance. Emergency food assistance, disaster assistance, and refugee assistance represent humanitarian actions, pure and simple. As such, they have enjoyed widespread support from the American people and from their elected representatives in Congress. Development assistance, however, is a far more abstract project, and one which has throughout its existence been informed by a quite specific and complex view of the world.

Development assistance has been predicated on an assumed causal relationship between poverty, instability, and tyranny—Marxist tyranny at that. In arguing the self-interest of the United States to provide development assistance, President Kennedy said in March 1961 that:

widespread poverty and chaos lead to a collapse of existing political and social structures which would inevitably invite the advance of totalitarianism into every weak and unstable area.<sup>1</sup>

The obverse of this, of course, is that prosperity leads to stability, which in turn leads to the formation of democratic institutions. The question of how to achieve economic growth leading to prosperity is answered by development assistance. Underlying the development assistance program, therefore, is a complex syllogism:

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1. *Public Papers of the Presidents of the United States: John F. Kennedy (1961)*, p. 204 (March 22, 1961).

development assistance leads to sustained economic growth; sustained economic growth leads to stability; and stability leads to the formation of democratic institutions.

Despite the everyday familiarity of these views, no one of them is self-evidently true. Indeed, there are excellent counter-examples for each of these propositions. Consider the claim that development assistance leads to sustained economic growth. In the last decade, the country of Tanzania has received by any standard an enormous amount of foreign assistance. Organization for Economic Cooperation and Development (OECD) estimates indicate that Tanzania has received approximately \$2 billion in assistance in these years. At the moment, however, Tanzanians labor under a remarkably depressed standard of living, and the economy of the country is in extremely poor shape. Nothing remotely resembling sustained, internally generated growth is on the horizon for Tanzania.

Perhaps an even better example is provided by Jamaica. In the years 1972 to 1979, OECD accounts indicate that Jamaica received in excess of \$525 million in economic assistance. During these same years, Jamaica experienced one year after another of actual economic decline. It has been estimated by some observers that at the end of the eight years of the Manley government, Jamaica's official economy was only 40 percent of the size it had been when the Manley government came to power.

Consider, too, the proposition that sustained economic growth leads to stability. Historians have long debated the theory of "rising expectations." According to that theory, economic development increases citizens' desire for social change so that revolutionary situations arise out of periods of economic expansion. Whatever one may make of the empirical evidence for this theory, development assistance blithely assumes its opposite: namely, that growth leads unambiguously to stability.

Contemporary Iran provides an interesting case in point. By any available measure, Iran grew rapidly under the long rule of the Shah. The "result" of this growth, however, and of its attendant social changes, was a complete disintegration of the economy and the society within six months of its first serious shock back in 1979. Despite some successes in prosecuting its war with Iraq, Iran remains a highly unstable place.

Finally, consider the claim that stability leads to democratic institutions. Judgments about relative stability are of course very difficult to make with certainty. Nevertheless, there are any number

of relatively stable regimes ranging from Taiwan to South Africa which represent very partial versions of democracy. And it is by no means clear that these nations must necessarily become more democratic with time.

But the clearest examples of stable regimes which are decidedly *not* moving toward democratic institutions are the Marxist regimes. The East European nations, Albania, North Korea, Vietnam, Cuba, and the Soviet Union have enjoyed considerable "stability"; that democracy is just around the corner in these nations is suggested by no responsible observer. Interestingly enough, Poland presents a case in which it can be argued that austerity, not prosperity, led to instability and to the prospect of wider, more democratic participation in its political life—until, of course, stability was forcibly reimposed in December of 1981.

What is characteristic of each of the foregoing propositions is the absence of *political* factors as causal agents in the process of change. Economics drives politics, in this view of the world; economic assistance leads to economic growth, which leads to desirable political outcomes. Conversely, the absence of economic assistance is thought to condemn many nations to economic stagnation and poverty, leading to instability and undesirable political outcomes.

Lying at the heart of this view is a vision of linear, one-time "development," a long-term secular process which may be marginally hindered or hastened by political regimes, but which cannot be altered decisively by them because it represents what is most real about history. At bottom, this process not only defies political events, it is the machine which moves them. The political parameters within which economic growth does or does not take place are taken for granted, and so relegated to minor importance as springs of human action.

### Development Assistance and Economic Growth

Let us leave aside for now the relationship between growth, stability, and democracy, and focus specifically upon the relationship between development assistance and economic growth. Prior to 1961, American economic assistance—which is to say, world economic assistance—was indeed a congeries of assorted programs administered by different agencies. Much of it was political/military in nature, designed to oppose the spread of communism. The originators of the 1961 legislation were indeed correct about the limitations of such an assistance program when they created the Agency for International Development (AID).

From its inception in the 1961 legislation, however, "development assistance" enshrined the importance of economics at the expense of politics. President Kennedy said, for example, that the provision of money for crisis and short-term *political* goals had not moved nations into the stage of sustained growth.<sup>2</sup> Political freedom, President Kennedy said, depended upon economic growth. Accordingly, the new legislation of 1961 established a program of specifically "development" assistance unrelated to short-term political phenomena, and directed at the long-term development of nations. The overriding task was to move nations into a position from which they could achieve *sustained* growth. In his letter to Congress of May 26, 1961, President Kennedy said:

Economic development assistance can no longer be subordinated to, or viewed simply as a convenient tool for meeting, short-run political objectives. This is a situation we can ill afford when long-range, self-sustained economic growth of less developed nations is our goal.<sup>3</sup>

There is an implication here that economic growth occurs "by itself" once it reaches a certain stage.<sup>4</sup> But what is ignored in this formulation, of course, is that political decisions can reverse economic growth at any time, as the cases of Castro's Cuba or Allende's Chile or Manley's Jamaica prove. A context of conditions, many of them political, is required for continuing economic growth; going "backward" is possible at any time. This painful reality, known well enough by everyone during national election campaigns, is wholly absent from the theory of "sustained growth."

The principal instrument of development assistance in the 1961 legislation was to be the "long-term development loan" at little or no interest.<sup>5</sup> Loans of this sort were to be made based upon long-term planning and careful attention to the "precise" needs of recipient nations. In some cases, more capital would be required; in others, greater technical assistance. In all cases the key to success would be long-term planning with unique, integrated country plans.<sup>6</sup>

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2. *Ibid.*, p. 204, Emphasis added.

3. *Ibid.*, p. 409 (May 26, 1961).

4. Much has been written about the "take-off" stage of economic growth advanced by Walter Rostow and others.

5. *Public Papers*, p. 209 (March 22, 1961).

6. *Ibid.*, pp. 206, 208.

In fairness to the new scheme, it should be noted that President Kennedy made numerous references to the fact that development assistance would not help if recipient governments were not willing to participate actively, to assist the process, and even to undertake internal reforms in some cases.<sup>7</sup> Such reforms were to be made in the service of the larger economic development program which dictated their necessity.

In practice, demands for structural reforms have never amounted to much, and aid once provided (usually) has been continued whether or not significant political or economic reforms have occurred. Since 1961, development assistance has had grafted onto it wish upon wish, and hope upon hope, often bearing no arguable relationship to economic development. It is not enough now simply that economic development occur—it can and will and must occur in an egalitarian manner, with the full participation of women, in the context of complete human rights, within an environmentally sound framework, with due attentiveness to reforestation, and so forth. The result of this has been pretty much what one would expect. Where there are many “priorities,” there are really none at all.

The two principal changes in the development assistance program since 1961 have both served further to undermine the thought that political regimes are important for economic development. The so-called New Directions mandate of the early 1970s rightly criticized the fact that much aid was ineffectual and that it did not help those who needed it the most. Thus, legislation directed that assistance should go to “the poorest of the poor.” There is no doubt that assistance to people in desperate need is a worthy thing, or even that it is supported by the humanitarian instincts of the American people. What it has to do with “economic development,” however, is far less clear.

The second major change occurred during the years of the Carter Administration, which moved dramatically away from bilateral development assistance and toward multilateral development assistance. This was a strategy founded not only on principle, but upon budgetary realities as well. By sharing costs with other nations and by paying in a small portion of capital at risk—in effect, by running a large loan guarantee program—direct expenses through appropriations could be minimized at the same time that their ef-

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7. *Ibid.*, p. 208.

fect was greatly leveraged. The result of this movement, however, was to apotheosize the notion that political considerations are not significant for the provision of foreign assistance. The multilateral banks, as they must, pride themselves on being wholly apolitical, professional decision-making bodies. The *raison d'être* of the banks is to loan money, and loan money they do.

In this process the multilateral banks reinforce the large international lending of the private commercial banks. Lending to the central governments of developing nations is often a highly profitable business. Commercial banks are desirous of securing official multilateral lending in nations in which they are commercially involved. The very presence of official lending constitutes a guarantee of government interest in the situation of the recipient country. The presence of official lending indicates that possible defaults will be covered by refinancing—again and again if need be—negotiated under the umbrella of an official presence which can often compel compliance with difficult economic conditions which might be imposed. Many nations now confront a crushing burden of public-sector debt, for which higher and higher levels of capital transfers must be provided simply to meet debt servicing demands. These debts reflect decisions made by recipient governments which frequently would not have been made by private economic entities.

Although the budget for development assistance has not increased substantially in the past several years, funding continues to run to several billion dollars each year. The difficulty is that after two decades and many billions of dollars, there is no observable correlation between the provision of development assistance and economic development. We might approach this issue in another way, namely, by asking what are the common features of nations which *have* progressed in the last several decades to relative affluence. Some nations, such as Saudi Arabia, possess the commodity of oil. But other nations not so blessed by nature, countries whose fate is based more fully on human resources, have done quite well: Hong Kong, Singapore, Malaysia, Ivory Coast, Colombia, Taiwan, and South Korea, to name but a few. What each of these nations possesses is a political system that has permitted a reasonable degree of economic freedom; has encouraged external investment, as opposed to aid; has fostered export development rather than import substitution; has refrained from imposing ill-conceived development plans upon its people; has been attentive to balance of payments problems and, where possible, avoided large public sector debt; and has

avoided the temptation to impose politically popular pricing mechanisms upon its producers.

### Politics and Economics in Development

What the above implies is the importance of *political* judgments for the economic development of nations. This implication will at once be branded by hostile quarters as “ideological,” since for the most part beneficial political decisions appear to be those which restrain the interference of governments in all economic activities of their citizens. To be sure, policies pursued by one nation will not always be appropriate for another nation. For example, one cannot “let the market work” where there are no established market traditions in the first place. But a genuine development policy—as opposed to the rhetoric of development—must respect the fact that nations, like individuals, will suffer the consequences of their choices, and that there is no justification for “assuming away” the political context of economic development.

The fact is that development assistance, as it is currently structured, greatly exaggerates the purely economic component in human affairs. At times, its rationale borders on the crudest form of historical materialism. The thought that economics determines human affairs riddles the fiber of Western, democratic thought, and assumes a central role in the concept of “development.” So, far from being a Marxist notion, this kind of mushy economic determinism is indeed quite to be expected in commercial, democratic societies.

It is in part for this reason that American policy-makers have been so little able to respond—either intellectually or in practice—to revolutionary situations around the world. What is lost in the theory that poverty causes revolutions is the fact that **revolutionaries cause revolutions**. Revolutionaries cause revolutions in order to impose a new view upon people, and there are more things in heaven and earth that move revolutionaries than poverty. Contemporary Iran ought to offer firm enough indication of that. Beyond this, there is simply no established correlation between absolute poverty and revolution. For this reason, stability provides a very dubious guiding principle for American foreign policy.

Parenthetically, if we look at the so-called Marxist regimes and policies, we find a practice which is wholly antithetical to economic determinism. Those loyal to the Soviet state and to its policies have accentuated the Leninist elements of Marxism to a very

considerable degree. To be polite about it, the theory of historical materialism has nothing whatever to do with the practice of Soviet policy around the world, which is "voluntarist" through and through: work, organize, agitate, work, unify, subvert, work, exploit, infiltrate, and work, work, work. One could not today deduce one single action of Soviet foreign policy—as opposed to its jargon—from a reading of Marx, however careful that reading might be.

All of this was realized, though in a limited way, when President Kennedy said in his 1961 State of the Union Address:

It is one of the ironies of our time that the techniques of a harsh and repressive system should be able to instill discipline and ardor in its servants—while the blessings of liberty have too often stood for privilege, materialism, and a life of ease.<sup>8</sup>

There is of course nothing ironic about this at all; it is a long-known and natural phenomenon. As we have been told, eternal vigilance is the price of liberty.

The economicism (to coin an ugly term) of the Western, industrialized nations prescribes a development strategy of economic assistance rather than a broader one of political, moral, and economic assistance. It may well be true that political orders cannot be entirely stable without economic development; but economic development cannot and will not occur without appropriate political decisions and conditions. And nations which criticize the principles and the politics of developed Western economies raise grave and justified doubts about whether they are likely to create suitable political conditions for economic development in their own countries.

We can be blunt: there is no way that economic assistance can offset the harmful effects of ill-conceived economic policies pursued by recipient nations. There is no way whatever that foreign assistance could have rescued an economy such as Jamaica's, for example, so long as the government of that country pursued the policies espoused by Mr. Manley. Nor is there any reason to think that foreign assistance will offset the policies being pursued now, for example, by a government like that of Nicaragua. Despite rhetoric about preserving "pluralism," the government of Nicaragua is undertaking policies which can have no end but to destroy the

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8. *Ibid.*, p. 27 (January 30, 1961).



private sector altogether. In such circumstances there is simply no role for "development assistance."

Assumptions underlying our current development assistance program exaggerate purely economic factors by taking for granted (and therefore ignoring) the political, moral, human basis for development. It is little wonder that the results of a program founded on such a restricted understanding have not been impressive.

### Reforms

What is required today is a comprehensive revision of the premises, the laws, and the structures governing development assistance. Without such revision, the gap between the demands of recipient nations and the concerns of the Congress are likely to grow larger, not smaller, in the coming years.

New legislation of course cannot descend with success to the level of specific cases and examples. These must remain the province of an active, intelligent administering agency. Nevertheless, it is long past time to sketch out the broad legislative guidelines for a new, defensible development assistance program—guidelines which would reflect a deeper, more political understanding than has informed the Foreign Assistance Act of 1961 and its subsequent revisions.

In setting out a new program we must restore to a central position the importance of *political* choices in recipient nations. We must of course give due regard to the uniqueness of each and every nation we are assisting. But we cannot and should not allow foolish and ideological notions to masquerade as serious reflections upon what is actually unique in given nations. Some policies will not work anywhere, no matter how and why they are adopted. One can hear only so much about "African socialism," for example, before one stands in wonder of the remarkable economic failures which this idea has been employed to rationalize. The defense that each nation, or each continent, is unique can easily be taken far beyond what is justifiable; the "*sui generis* defense" of peculiar policies is usually the prelude to an all-too-common failure.

The basic question which we must address is a very difficult one: given the international character of capital in the modern world, why is insufficient capital for development reaching some nations? If private capital is not reaching certain nations in amounts "sufficient" for economic development, why not? And what could or should induce public money to fill this gap? More-

over, if certain nations (India provides a timely example) place their own scarce resources into military hardware rather than economic development, what is the rationale for the provision of external capital?

If the United States is to proceed with government-to-government loans or grants, the cardinal rule should be: strong conditionality from the beginning. The market offers its own form of "conditionality," that is, the lender's risk of losing his funds. If there is a pressing reason to supply public funds where private funds will not go, there simply must be some counterpart, some controlling rationale, which fills the role of risk. There must be something which helps to order priorities among possible programs and projects.

What we mean here by "conditionality" is decidedly *not* the kind of conditionality characteristic of international lending today. Typically, in current practice, we see a cycle in which private and public funds are extended to a recipient government on the basis of very wistful ideas, and on the premise that Western governments will always bail out troubled lenders and borrowers. Then reality intervenes, miscalculations become apparent to all, and further funds are needed. At this point austerity is required, because commercial lenders will not supply new funds without guarantees of economic changes within the recipient nations. So official international lending agencies—principally the IMF—impose austerity as a condition for further lending, and are widely criticized for their lack of concern for the poor. This entire process serves no developmental goal whatsoever; what is most unfair about it is that the poor in recipient nations are its primary victims. The poor received no benefits from ill-conceived public sector projects which generated large debt, but they feel the very real shortages that occur when austerity is imposed.

What can be done, then, to restructure development assistance?

*First, all government-to-government assistance should be marked by strong conditionality which encourages economically sound political decisions by recipient governments.* These decisions are of course difficult to spell out abstractly, and no set of them will be entirely appropriate for any given country. Among important conditions, however, are the following:

- (1) An end to artificial pricing schemes imposed by central governments. Such schemes have come into existence in order to strengthen the power of the central government and to "buy" political stability among the urban poor who might not otherwise be

able to afford basic food products. As such, these policies have contributed to the urbanization of nations in an artificial way, and to a situation in which there is insufficient incentive to grow agricultural products. This entire matter of course must be treated very gingerly, because it relates directly to the security of the governments in question. It must be treated, however, if there is any degree of seriousness about the prospect for economic development. Accordingly, although the realistic pricing policies may be phased in over a number of years, this is a policy which must be undertaken or development assistance will make no sense.

(2) Current account balances and projections are vitally important to attracting external private capital. Accordingly, a well-thought out program to balance exports and imports is an integral part of any development program. Capital simply cannot be loaned on the basis of hopes that "development as such" will somehow lead to exports. Central planning for export product development has been notoriously poor, and *any* wholly government-directed plan or any wholly government projection for producing exportable products must be examined with the deepest reservations.

(3) A manageable and reasonably sized government bureaucracy. The recipient government itself should not be the chief beneficiary of development assistance under any conditions. Assistance might well pass through the bureaucracy, but its purpose ought to be to aid the private citizens of recipient nations.

(4) Adoption of conditions that will attract private external capital. This means that favored government monopolies in many products will have to be disbanded to allow open competition. It means, too, carefully crafted agreements to guarantee that external capital will not be expropriated without just compensation. Finally the government must allow a broad degree of freedom to domestic and foreign business ventures, and be willing to countenance the growth of a middle class (of business people) that is likely to become politically active, demanding, and important.

(5) A reasonable plan for the management of public sector debt. In the case of many nations whose economies are largely officially owned and managed by central governments, this is closely related to the question of current account balances. It is not identical with current account balance, however, and hopefully in many instances would become less so with time.

(6) An incentive-oriented tax system. Such a tax system would avoid confiscatory taxes designed to support large central govern-

ment bureaucracies, military adventures, and foolish developmental projects. This is a particularly important factor in the development of a class of people with a strong stake in the development process and in the restriction of the central government's role in the overall economy of the nation.

*Second, strong new efforts should be made to explore the ways in which U.S. assistance could go directly to private sector groups in developing nations.* Several promising initiatives have been undertaken in recent years, but much remains to be done. Among proposals that deserve careful consideration:

(1) Replacement of much government-to-government lending with direct lending to private entities. This would be done either directly (where possible) or with the cooperation of the governments of recipient nations. Such a program would provide needed capital to those sectors of the economy that actually could and would use it efficiently. There of course must be continuing awareness of the sensitivity of host governments to this process and a clear commitment on the part of the host government to the main lines of this enterprise. But if there were not such a commitment, there would be justifiable doubts about development there anyway.

(2) A program to bring middle- and upper-level political leaders to the United States and to other nations to study the relationship of politics and economics in the development process. In most spheres of human activity, one turns to people who have demonstrated some expertise if one wishes to know how to carry out a task successfully. If help is needed in building a house, for example, one turns to a carpenter. For some reason, however, in the "development business" the tendency has been to turn for instruction to people who *wish* to develop, but who have not yet done so. This inversion of the natural order of things should be reversed immediately.

This suggestion should not be taken as an attempt to indoctrinate certain narrow ideological notions into the minds of leaders of developing countries. The program could include study in as broad a variety of nations as have had some actual success in economic development. Leaders of developing nations could travel to places such as South Korea or Taiwan and learn how economic development occurred in those nations—hearing from the people who have been responsible for it. If the U.S. were to participate in any multilateral project, what could be a higher priority than this: a consortium of developed nations with differing cultural and his-

torical backgrounds, with jointly funded and managed seminars in which real learning took place about how development does and does not occur? This would offer a useful antidote to the ideological notions about development which are currently circulated at a variety of institutions of higher learning in the West.

*Third, the United States should establish a strong and clear policy about commercial lending abroad.* Commercial banks should be given a free and clear choice: either they will lend relatively freely and suffer the consequences, or they will not. It would be a simple matter to create substantial legal strictures on commercial loans to foreign governments. In the event that banks indicate that they do not seek such strictures—as will surely be the case—then they must be forewarned that they will be allowed to reap the consequences of their decisions however unpleasant they may be. It is not good practice for commercial banks to overextend both themselves and the creditworthiness of foreign governments, and then seek official actions to cover them in the event of economic difficulties.

*Finally, the United States must redouble its efforts to achieve a working consensus among developed-nation lenders about the terms and loans to non-developed nations.* Why should the United States be concerned if other developed nations subsidize loans to developing countries? After all, if they wish to employ their resources in this way, what business is it of ours? Given the fact that all developed nations, including the United States, maintain an extensive—and expensive—program of unemployment insurance, it is very much a matter of continuing concern. For the fact is that subsidized loans which require purchase of products from other industrialized nations result in diminished unemployment in those nations. In the long run, it does the developed nations no good to compete to export unemployment by providing officially guaranteed, subsidized loans for projects which are not economically feasible without such guarantees.

## Reflections

Much of the foregoing may strike the reader as “conservative,” inasmuch as it implies the superiority of market economies over command economies. On a deeper level, it is anything but conservative, for it also implies sweeping changes in how the United States approaches development and our relationships with less developed nations. What it proposes does *not* simply conduce to the stability of existing governments, as does the current program.

What it proposes is change—often change of quite revolutionary proportions.

To succeed, long-term development must occur in an organic way, such that a reasonably broad element of the populace is involved in it and has a stake in the process. A strong, independent middle class is indispensable to successful economic development. A program which encourages governmental restraint and private-sector involvement is likely to be a dynamic one. Neither the forces of military oligarchy nor the forces of left-wing totalitarianism are comfortable with the creation of a healthy middle class. Many governments, ranging from the right to the left, are unlikely to be comfortable with the genuinely dynamic aspects of this kind of program, and with a serious endeavor to bring about economic development; it is far easier to mouth pious phrases which do not threaten the fundamental control which many leaders maintain over their people.

It will not do to lavish large sums of money upon rulers who have no real desire to do the things necessary for economic development, some of which include moderating their own powers. Foreign assistance, when viewed as “walking around money,” as it has been sometimes characterized, is expensive and ineffective. It represents little more than “bribery with a human face.”

A final political note. Under both Democratic and Republican administrations in the last several decades, the United States has tended to make stability the paramount goal of foreign policy. This is understandable in those cases in which democratic regimes have been under attack from totalitarian quarters. But this has been a confusing and difficult role for the United States, which remains the most revolutionary society on the earth today. Our policy has too often presumed that instability and change are better managed by totalitarian opponents than by ourselves. To a degree, this has been a self-fulfilling policy.

Although an egalitarian ideal does permeate our times, change is **not** necessarily fated to favor totalitarian forces of the left. Our task now should be, as it has been throughout our history, the advocacy of freedom—that is, of limited government. Without a broad measure of freedom there will be no development—economic, political, or human. There will be but a succession of mind-numbing tyrannies committed above all to their own perpetuation. In this regard, the need to re-think the premises of our current development assistance program is as necessary as it is overdue.

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# The Heritage Lectures

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Over the last decade, the United States has given more than \$57 billion in development assistance to the world's poorer nations. Calls by many of these nations for massive aid increases have prompted some fundamental questions from policymakers. Among them: What is development assistance supposed to do? How well has it accomplished its objectives? Are there alternatives? Can multinational corporations, for example, help to raise the economic level of countries where they operate?

Harvard anthropologist Grace Goodell and Senate aide Jeffrey T. Bergner offer conservative perspectives on these difficult questions. U.S. aid efforts, they argue, should focus on the small entrepreneur. No matter what the country, they conclude, a strong, independent middle class is indispensable to successful economic development.

  
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