

Aid, Trade and Economic Growth: The Value of Foreign Assistance

Like other budget priorities, spending on foreign assistance can be weighed against three questions: What does it buy? Is it worth it? And, can we afford it now? In that discussion, the term “investment” can lose currency as soft estimates of distant results, returns and savings confront hard and immediate budget realities. All expenditures are not investments because they do not meet the test of yielding quantifiable, net economic output for every dollar spent. Facing extraordinary fiscal challenges, policy makers and the public want to be sure, and to be able to demonstrate, that spending on international assistance and development projects meets that test.

What does it buy?

Since enactment of the Foreign Assistance Act of 1961 (P.L. 87-195; 22 U.S.C. 2151 et seq.), aid has been viewed as an essential instrument of U.S. foreign policy. The end of the Cold War and the attacks of September 11, 2001 changed the focus of assistance efforts from cementing friendships with anti-Communist states to more broadly nurturing prosperous, justly governed allies and trading partners. As early as the 2002 National Security Strategy, to the first ever Presidential Policy Directive on Global Development in 2010 and the State Department’s 2010 Quadrennial Diplomacy and Development Review (QDDR), development assistance has been elevated as a co-equal and indispensable third pillar of national security, alongside diplomacy and defense.

In short, foreign aid is used to enhance the United States’ international reputation as compassionate and democratic, to stabilize and strengthen allies in the war against transnational terrorism, and to support domestic economic growth by expanding access to emerging global markets and building economic capacity in developing countries.

Assistance takes many forms: disaster and humanitarian relief, economic support in pursuit of U.S. economic and security objectives, bilateral development aid, multilateral program funding and military aid. The Administration uses those aid expenditures to pursue objectives across five major program areas: peace and security (counterterrorism and counternarcotics), investing in people (health and education), governance (rule of law and anti-corruption), economic growth (trade, infrastructure and agriculture), and humanitarian assistance (disaster response and refugees). Expenditures in these programs or sectors are made in the form of direct cash transfers, purchase of equipment and commodities, construction of economic infrastructure, and provision of training and expertise by for-profit companies and non-profit organizations.

October 11, 2011

According to U.S. Agency for International Development (USAID) data, traditional U.S. assistance in fiscal year 2010 totaled \$39.4 billion, coupled with another \$4.7 billion in military assistance.¹ Afghanistan remains the top recipient of total U.S. economic and military assistance—both obligations and disbursements. Iraq received the most U.S. aid from 2003 to 2007. According to the [USAID website](#)², the top 20 countries receiving U.S. assistance in fiscal years 2010 and 2011 (through March 31, 2011) were:

Chart 1

	Country	FY 2010	FY 2011
1	Afghanistan	\$2,755,671,228	\$57,610,006
2	Pakistan	1,351,634,685	343,698,200
3	Haiti	701,379,625	133,601,639
4	Israel	596,529,460	504,696
5	West Bank/Gaza	387,120,025	168,674,476
6	Kenya	500,427,374	5,580,373
7	Sudan	462,877,610	37,239,593
8	Jordan	363,375,929	100,249,366
9	Ethiopia	350,258,089	27,219,396
10	Georgia	339,465,998	10,405,429
11	South Africa Republic	347,449,184	1,953,872
12	Egypt	320,115,027	8,242,346
13	Nigeria	295,792,542	23,333,516
14	Tanzania	312,689,352	3,134,891
15	Uganda	269,467,038	11,850,768
16	Iraq	220,524,820	60,688,407
17	Indonesia	262,002,937	17,848,628
18	Democratic Republic of Congo	163,325,098	92,438,351
19	Mozambique	234,429,203	4,379,934
20	Liberia	229,133,134	8,070,512

Often, U.S. assistance funds are spent to procure U.S. goods and services. The bulk of USAID assistance projects are implemented through contracts, cooperative agreements and grants to U.S.-based partner companies and organizations. They provide goods, services and

¹ The Congressional Research Service (CRS) defines “traditional” foreign assistance as funds spent through the international affairs budget, or budget subfunctions 150 (international affairs), 151 (security assistance) and 152 (humanitarian assistance). “Non-traditional” foreign aid consists of expenditures by other federal agencies such as the Department of Defense, Energy, and Health and Human Services on international programs. CRS estimates that non-traditional assistance in FY2009 totaled \$12.6 billion.

² Retrieved from <http://www.usaid.gov/policy/budget/money/>

technical advice to build the permanent capacity of foreign governments, host country companies and civil society organization to sustain economic growth. Some legislative “Buy American” provisions require purchase of food aid commodities from U.S. producers and shipment on U.S. carriers.

The direct and indirect domestic economic impact of foreign assistance spending varies by program and is often difficult to quantify, but the economic rationale for international aid has taken on increased significance as global markets have become more interdependent and volatile. [Advocates for international assistance](#) cite the fact that 10 million American jobs are tied to exports and that access by U.S. companies to markets in the developing world is an essential element of future job growth.³ With Western economic growth projected to be flat or meager in the next five to ten years, opportunities for market expansion will be found in the emerging economies of Latin America, Africa, Asia, and China. In July 2011, the [U.S. Chamber of Commerce](#) told Congress, “The international affairs budget play[s] a vital enabling role for U.S. companies to tap foreign markets and create jobs and prosperity at home.”⁴

Economic and technical aid drives the creation of export-related jobs. In emerging markets U.S. companies need government help to lower trade barriers, spur adoption of modern commercial legal codes and practices, and raise health and education standards to nurture growth of a middle-class of consumers. In one widely-cited example, South Korea “graduated” from being an aid recipient country to an aid donor and today is ranked as the 13th largest economy in the world and the 7th largest U.S. trading partner. South Korea received a total of \$4 billion in assistance between 1953 and 1973. That long term investment accelerated economic development there and made sure the United States remained a favored trading partner. U.S. exports to South Korea in 2010 were \$39 billion, double the amount in 1990.

In a January [2011 speech](#), Secretary of State Hillary Clinton stressed the domestic economic benefits of commercial advocacy abroad, touting successes like the sale of Boeing 737s to Russia and signing of a \$20 million mining contract by a U.S. company doing business for the first time in the Philippines. She said creating U. S. jobs at home starts abroad, citing new Open Skies agreements negotiated by the State Department that open new cities to U.S. air carriers and open new markets for U.S. businesses. Regarding two such agreements, she said, “The direct connection between Memphis and Amsterdam has a \$120 million annual impact on Tennessee’s economy and supports more than 2,200 local jobs. American Airlines now flies direct to Madrid, a connection that has a \$100 million annual impact on the Dallas-Fort Worth economy.”

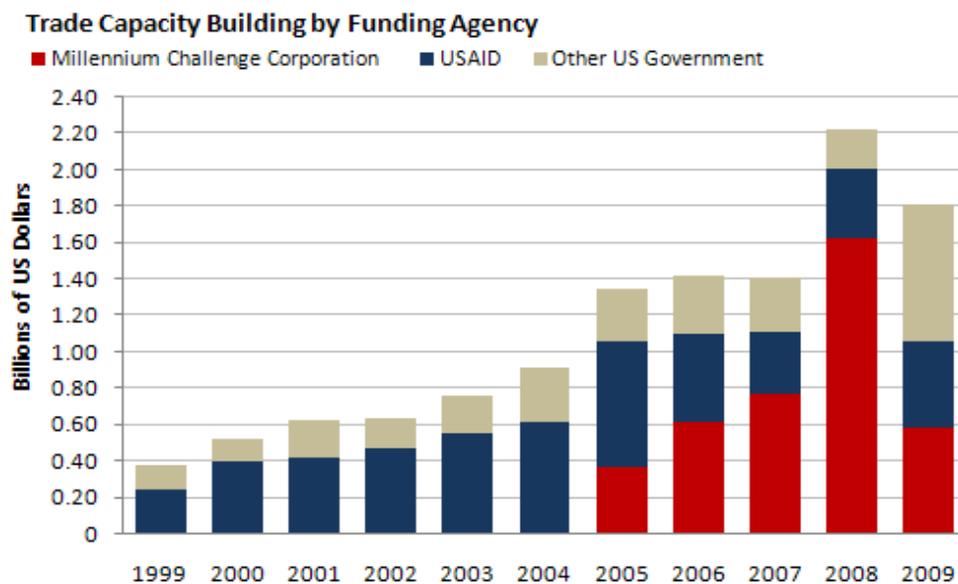
A substantial portion of annual U.S. assistance spending is devoted to building the trade capacity of developing countries. (See Chart 2) The Obama administration’s Partnership for

³ U.S. Global Leadership Coalition (USGLC) Economic Working Group (2011). *America’s Global Leadership: A Strategic Investment for U.S. Jobs*. Retrieved from <http://www.usglc.org/2011/07/12/read-the-new-report/>

⁴ Retrieved from <http://webcache.googleusercontent.com/search?q=cache:je7Qs3n8RMUJ:www.usglc.org/wp-content/uploads/2011/02/US-Chamber-of-Commerce-Letter-FY12-StateForeignOpsAppropriationsBill.pdf+The+International+Affairs+budget+play%5bs%5d+a+vital+enabling+role+for&cd=1&hl=e>

Growth initiative was launched as a follow-up to issuance of the nation’s first Global Development Policy to place a central emphasis on sustainable economic aid outcomes. In Ghana, Tanzania, El Salvador and the Philippines, the program coordinates the activities of multiple federal agencies and identifies barriers to increased business investments. On trade development and commercial diplomacy generally, Secretary Clinton said, “Much of what State, USAID and the Millennium Challenge Corporation and other government agencies do to promote development overseas, addresses the very same problems American companies encounter when they do business abroad. We fight corruption, we strengthen the rule of law, we help countries write new commercial codes and overcome the bureaucratic red tape that stifles business. As we help build infrastructure like ports and roads.”⁵

Chart 2



Source: MSI, November 24, 2010

Is it worth it?

Measuring the tangible results and indirect impacts of assistance has always been a challenge, particularly because so many interventions (e.g., programs to increase literacy or to reduce violence against women) may take years to manifest desired economic or social outcomes. Also, natural disasters like the tsunami in Indonesia can literally wash away decades of aid-stimulated progress. Nevertheless, new approaches to monitoring and evaluating assistance projects have enabled development professionals and policy makers to measure the economic impacts of many U.S. assistance efforts more accurately.

One basic unit of economic impact measurement is the net income gain in a target population. Using that standard, [USAID](#) noted that “benefits can be compared across different programs and weighed against project costs to determine whether a particular

⁵ Retrieved from <http://www.state.gov/secretary/rm/2011/07/168061.htm>

intervention is a good investment of aid funds.”⁶ However, causal attribution of net income effect to aid projects requires detailed data and collection of “counterfactual” or control group information to distinguish between assistance impacts and economic activity that was happening anyway. For discrete economic growth projects, scientifically valid impact data and evaluations can be conducted, but for aid projects in other sectors (e.g., human rights and governance), impacts are generally indirect and dispersed and denying program access to controls groups may be unethical.

Using this improved methodology, USAID recently highlighted several economic growth efforts that demonstrated a compound return on the investment of assistance dollars. In Mozambique, two projects provided technical assistance to the government to reduce trade and investment barriers. According to USAID:

an analysis of program activities ... found five interventions for which benefits to the private sector were observable, measurable and attributable to USAID: reducing the time to register a new business; reducing fees for scanning shipping containers; reducing refund delays for the value added tax; suspending problematic new rules that would have increased costs and slowed payments for international trade transactions; and eliminating tourist visas and associated fees for visitors from other SADC countries.⁷

Using conservative assumptions, the report estimated that these five interventions **generated approximately \$6 in net benefits to Mozambican businesses for every \$1 of total USAID project funding.**⁸ [emphasis added]

In Bosnia and Herzegovina (BiH), the USAID-funded Tax Modernization Projects (TAMP) provided more than \$12 million between 2001 and 2006 to reform tax collection and administration systems. According to USAID:

TAMP modernized the tax law, centralized and unified systems for managing and processing tax information, created more effective control and enforcement teams, and streamlined and automated the core business processes of tax administration, among other contributions. These reforms greatly improved the efficiency of tax collection. TAMP’s achievements include

- Fifteen percent annual growth in tax revenues, which helped BiH provide critical public services;

⁶ USAID (June 2010). *Programming for Growth: Economic Impact*. Retrieved from http://www.countrycompass.com/policy_briefs.php

⁷ USAID (June 2010). *Programming for Growth: Economic Impact*. Retrieved from http://www.countrycompass.com/policy_briefs.php

⁸ Ibid.

- Five new tax laws, including a new personal income tax that provides relief to the poorest segments of the population and a new corporate tax that reduces filing costs and eliminates most tax incentives; and
- A 35 percent reduction in tax collection costs in one major region, and an 18 percent reduction in other parts of the country.⁹

USAID concluded that these efforts “**yielded an estimated \$7 in net benefits to BiH for every \$1 of total USAID support** for TAMP.”¹⁰ [emphasis added]

USAID’s upgraded [evaluation policy](#) looks to improve data collection, expand the use of impact evaluations, and link findings to program design and budget decisions.¹¹ A July 2011 Government Accountability Office ([GAO report](#)) on trade capacity building (TCB) assistance efforts concluded that, “USAID has improved its assessment of TCB activities, including developing performance indicators and taking the positive step of commissioning a multi-country evaluation of the effects of TCB, but it has yet to develop plans to make use of the evaluation’s valuable insights.”¹²

According to USAID, that multi-country evaluation, [From Aid to Trade: Delivering Results, A Cross-Country Evaluation of USAID Trade Capacity Building](#), “provides quantitative evidence that elements of USAID’s TCB projects impact host countries’ economies in positive and measurable ways.”¹³ The study found that overall U.S. government trade assistance resulted in a \$53 increase in total merchandise exports for every \$1 in aid, and that USAID funded trade capacity efforts produced \$42 of that total increase in exports for every \$1 in assistance over the two year study period.¹⁴

In Senate [testimony](#) on March 10, 2011, Deputy Secretary of State Thomas Nides pointed out that “the likely ‘surge’ in contractors in Afghanistan and Iraq after U.S. troop drawdowns is projected to add \$4 billion to State Department costs while saving DOD \$45 billion.” He concluded: “Now, in the business world, they call that leveraging an investment, investing \$4 to save \$45.”¹⁵

⁹ Ibid.

¹⁰ Ibid.

¹¹ Retrieved from <http://forward.usaid.gov/reform-agenda/strengthening-monitoring-eval>

¹² U.S. Government Accountability Office (2011) *The United States Provides Wide-ranging Trade Capacity Building Assistance, but Better Reporting and Evaluation Are Needed*, GAO-11-727.

¹³ Retrieved from http://www.usaid.gov/our_work/economic_growth_and_trade/eg/pdf/TCB_Evaluation_Fact_Sheet_7_12.pdf

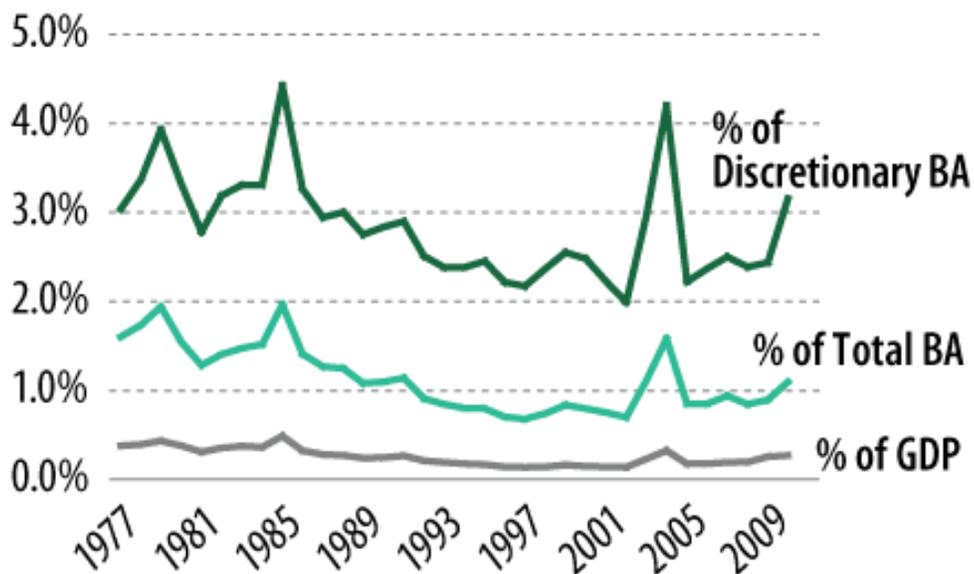
¹⁴ Management Systems International. (2010). *From Aid to Trade: Delivering Results, A Cross-Country Evaluation of USAID Trade Capacity Building* Retrieved from http://pdf.usaid.gov/pdf_docs/PDACR202.pdf

¹⁵ Retrieved from <http://budget.senate.gov/republican/hearingarchive/testimonies/2011/2011-03-10Nides.pdf>

Can we afford it now?

Since the infancy of the American republic, payments to foreign states and actors have been a controversial but essential tool to advance the national interest. John Adams and Thomas Jefferson famously disagreed on the relative merits of paying tribute to Barbary pirates to induce them to spare American merchant shipping. In the modern era, foreign assistance has always been a significant component of American statecraft. While the U.S. remains the world leader in net disbursement of what is called Official Development Assistance (ODA), the portion of the federal budget that supports all foreign operations and assistance has stayed between one and two percent of total budget authority since 1977. (See Chart 3)

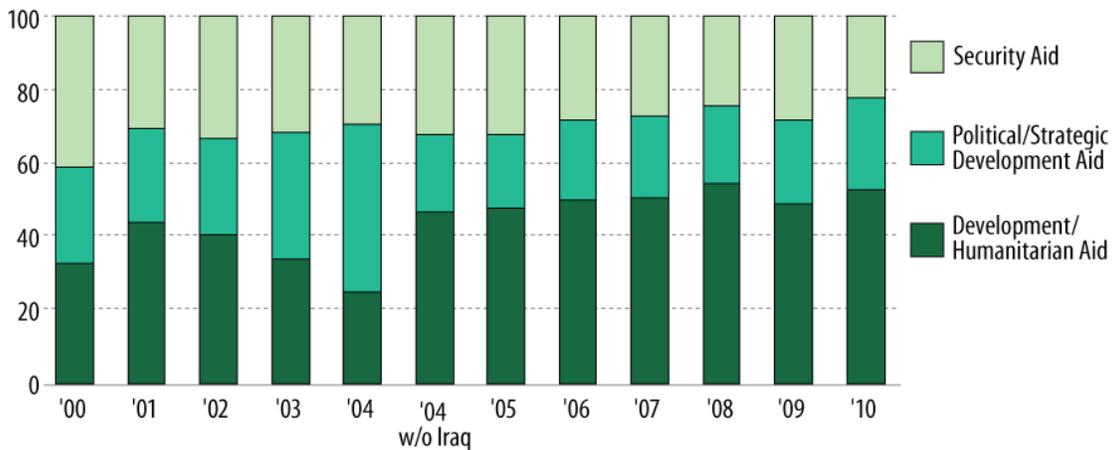
Chart 3



U.S. Foreign Aid: FY1946-FY2010
Source: CRS R40213

Reflecting both geopolitical and fiscal trends and challenges, Democratic and Republican administrations adjusted the mix and focus of foreign aid programs, but agreed on the value of development assistance in advancing U.S. security, diplomatic and economic interests. (See Chart 4)

Chart 4



Shifts in Program Emphasis (FY2000-2010)
(as % of total U.S. foreign assistance appropriations)
Source: CRS R40213

The current focus on the affordable levels of international development aid as an essential enabler of domestic economic growth comes in response to several factors including the global economic downturn, the rise of China as an economic power, and concern that lack of economic opportunity abroad breeds instability and fertile ground for terrorism. The [9/11 Commission's final report](#), issued July 22, 2004, stressed the danger of undervaluing foreign assistance as an element of national security, saying: “But long-term success demands the use of all elements of national power: diplomacy, intelligence, covert action, law enforcement, economic policy, foreign aid, public diplomacy, and homeland defense. If we favor one tool while neglecting others, we leave ourselves vulnerable and weaken our national effort.”¹⁶

Other nations find strategic and economic value in making sustained investments in development assistance. The United Kingdom, despite severe domestic budget constraints, continues to increase aid expenditures. And China has embarked on an aggressive program of grants and loans to developing countries, many to gain access to raw materials needed by Chinese industry. U.S. Treasury Secretary Timothy [Geithner told Congress](#) that reduced U.S. aid would “give China a substantial advantage in promoting its own commercial and security interests across numerous regions and sectors.”¹⁷

Sen. John Kerry (D-Mass.), Chairman of the Senate Foreign Relations Committee, wrote in the [August 3, 2011 Washington Post](#) that, “Energetic global leadership is a strategic imperative for America, not a favor we do for other countries. It amplifies America's voice and

¹⁶ Retrieved from <http://www.911commission.gov/report/911Report.pdf>

¹⁷ Retrieved from http://appropriations.house.gov/_files/TreasurySecretaryGeithnerTestimony.pdf

extends our reach. In a world growing more not less interdependent, slashing foreign aid and development investments is a formula for isolation and shrinking influence. America can't opt out of a networked world.”¹⁸ He and others argue that spending less than two percent of the annual federal budget on the fundamental elements of U.S. global leadership - diplomacy, humanitarian assistance, economic development - is affordable and essential. Similarly, in August, 2001, [Sen. Lindsey Graham](#) (R-S. Car.), ranking Republican on the Senate Appropriations Subcommittee on Foreign Operations, told constituents that aid remains an essential budget item. “Being a broke nation doesn’t mean that you have the luxury of ignoring things going on around you,” he said.¹⁹ Recognizing the criticality of U.S. spending on foreign operations, Congress included State Department and USAID accounts under the cap for fiscal year 2012 “security” spending in the Budget Control Act of 2011.

Conclusion

Spending on diplomacy and foreign assistance meets the test of being a sound investment. It buys tangible results, yields multiple benefits for every dollar spent and, at less than two percent of annual discretionary spending, is an affordable element of U.S. global leadership. When done right, it is an efficient soft power tool that effectively expands American influence, opens markets to American companies and enhances national security without resort to military force. U.S. development companies, working as contract partners with USAID, DoD, State and other federal agencies, play an indispensable role in achieving quantifiable results for every dollar spent. Development contractors chose the for-profit business model because it is powered by built-in incentives to productivity and efficiency. Companies bring those same incentives and acquired expertise to assistance projects in building, and leaving behind, sustainable economic enterprises and communities.

PSC and its member companies are ready and willing to contribute to these objectives and recommendations. For more information, please contact PSC Development Initiative Director Larry Halloran at 703-875-8059 or halloran@pscouncil.org.

¹⁸ Retrieved from http://www.washingtonpost.com/national/on-leadership/amid-budget-crisis-a-defense-of-foreign-aid/2011/08/03/gIQABVFdrI_story.html

¹⁹ Retrieved from <http://thinkprogress.org/security/2011/08/23/301972/lindsey-graham-says-u-s-needs-to-spend-more-on-foreign-aid/>