Economic Support for Developing Countries

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Economic support for developing countries, or, in common parlance, foreign aid, is a post-World War II phenomenon. Self-interested payments to foreign governments have a long history. Such payments had no connection to the recipient country's progress—or even whether the ruler promoted or retarded the country's development. Humanitarian efforts also have a long history, with international relief being organized for floods and famines. Such programs were targeted, and short term. But the idea that taxes paid by individuals in one country should be used to benefit citizens of other countries in the absence of humanitarian or quid-pro-quo rationales was an American invention.

The purpose of this chapter is to examine the basic ideas that have guided U.S. bilateral development assistance over the decades, and the role that economists have played in their formulation and evolution. U.S. foreign aid has been motivated by an overriding objective of promoting U.S. national security, though with numerous politically motivated tagalongs, such as promotion of U.S. exports or disposal of surplus agricultural commodities. For the most part, it has been motivated by a vision that progress in poor countries was of benefit to U.S. national security. The purpose here is to identify the various approaches taken by the U.S. government to pursue "development" in the context of the U.S. national interest. In doing so, the chapter will address four issues for each major phase of the evolution of U.S. development assistance policy: the conceptual underpinning for the approach; the means used for documentation and performance measurement; the impacts produced; and the reasons the approach was abandoned for another.

Needless to say, it is impossible to identify *the* rationale behind any complex endeavor involving thousands of people. Different participants will view most of the issues discussed here somewhat differently, and any single judgment about underlying rationales will be somewhat idiosyncratic. In sum, this is only one observer's view of the story that can be told about where U.S. foreign aid came from, how it got to where it is today, and what USAID economists had to do with it.

U.S. foreign aid for development dates from President Harry Truman's inaugural address in 1949, when he called for "a bold new program for making the benefits of our scientific advances and industrial progress available for the improvement and growth of underdeveloped countries." This initiative came to be called the Point IV program because it was the fourth of the four major elements of the foreign policy he announced in his speech.[1]

This Truman initiative was a new departure for the United States and for the world. The idea that governments should tax their people to finance long-term improvement in other independent countries dates to this beginning. The U.S. government had provided relief assistance on a variety of previous occasions, as with the aid to Russia managed by Herbert Hoover in the early 1920s, but such efforts were always specific in scope and limited in duration.

Two years earlier, in 1947, the United States had instituted the Marshall Plan for the reconstruction of Europe and Japan. The Marshall Plan, though dwarfing in magnitude any previous effort, was no exception to the historical precedent. Its purpose—the reconstruction of war-torn economies—was clear, the duration of the program was understood to be short, and the relevance of the task to American well-being was also evident. The assisted countries needed help because the war had destroyed their roads, bridges, factories, and houses, bankrupted people financially, and created masses of refugees and unemployed people. The solution was to finance reconstruction, getting factories back into production, and putting money in peoples' pockets so that they again had purchasing power. Once most people had been put back to work in reconstructed factories, the economies would take care of themselves, and U.S. assistance would end. And this is how the Marshall Plan worked in practice.

The Truman proposal was fundamentally different. The answers to both the why (why are these countries poor?) and the how (how can the United States make them prosperous?) questions had no widely agreed upon answers. The remainder of this chapter describes the changes over time in the answers given by U.S. foreign aid theorists to these two questions, and the extent that they were embodied in the approach taken by U.S. foreign development assistance programs.

THE POINT IV PROGRAM: TECHNICAL ASSISTANCE, 1950–1961

Conceptual Basis

The answers given by the Point IV program were clear. Countries were poor largely because their people lacked the technical knowledge to be productive and healthy. The United States could change this by a massive program of technical assistance and training of people from those countries.

It took the Congress nearly two years to approve Truman's Point IV initiative. The legislation emphasized working in friendly countries with a formal agreement between the U.S. assistance program and the host government. Costs were to be shared jointly, and all activities were to be carried out in partnership. U.S. resources were to be used for (1) salaries and expenses of U.S. technicians; (2) costs of training host-country technicians; and (3) materials used in demonstration projects. Large financial transfers were to be avoided, as these created dependency and interfered with the operation of private financial markets.
The Point IV assistance initially focused most heavily on agriculture, as this was seen as the area where American technology was the envy of the rest of the world, as well as the livelihood of the majority of people in poor countries. American "know-how" would transform the poor countries along the U.S. model. Health was the second priority, emphasizing public health measures such as immunization campaigns and the construction of water and sewerage systems.

The United States also financed studies and foreign advisers in a number of other sectors, including public administration, education, transportation, industry, housing, and labor. U.S. aid financed studies of tax administration and local government, helped create government statistics offices, and gave advice on establishing civil service rules for government workers. Large amounts were also spent to send nationals of recipient countries to U.S. universities, particularly in technical areas.

During the early decades of U.S. economic assistance, three regions were the main focus of attention and concern. Latin America, as part of the American sphere of influence since the Monroe Doctrine, was the most traditional interest. India (or the Indian subcontinent) represented a second major concern, both synonymous with poverty and also the battlefield for democratic versus totalitarian models. In the worldwide ideological struggle between the "free world" and the communists, India versus China was seen as the embodiment in the developing world. Other countries were expected to be watching the experience of these two giants in order to model their development approach on whichever was the more successful. The third area was the legacy of U.S. security interests, and included South Korea, Taiwan, Turkey, and the Philippines. Except for a few other cases of historical linkages to the United States, other poor countries were expected to receive aid primarily from former colonial powers.

Documentation and Performance Measurement

In principle, each activity under Point IV was to provide technical cooperation based on (1) a formal request from the participating government; (2) cost-sharing between the two governments; and (3) clearly defined, time-limited objectives. The individual activity, rather than any country-level programming document, was the basis for activities to be carried out. Projects typically included quantified end-of-activity goals (e.g., numbers of seeds tested, numbers of people trained, numbers of water systems installed), but did not include higher-level goals. For many countries, even the establishment of baseline indicators was prevented by the lack of basic statistics.

Under Point IV, resident country missions were established, staffed by individuals with long-term assignments. Initial proposals were developed in the recipient country and approved in Washington. Operations and day-to-day management were decentralized to the in-country mission. This pattern of substantial autonomy for the in-country staff was maintained until the 1990s, when Washington (the State Department, Congress, the White House, and USAID) increased centralization and State Department allocations became more important in country funding decisions and allocations (discussed later).
This use of field missions as the primary locus of action was important in creating a USAID "organizational culture" that continued into the 1990s, when Washington—first USAID headquarters, and later the State Department asserted much greater control in the allocation and country and sectoral distribution of funding. One feature of this culture is the self-image of professionals in the organization as on the front lines of real development work, seeing their superiors in the USAID hierarchy largely as a problem to be managed. Autonomy has been highly prized by the field mission and by the individual professionals. This has meant that policy pronouncements from Washington, or Washington-based theories about the development process, have sometimes differed significantly from the approaches being implemented by the field

missions. Program documents prepared by field missions were always packaged to sound as close to the latest Washington ideas, even where the actual approach to be implemented differed significantly, reflecting the ideas of the field staff.

Impact

Perhaps the first evaluative statement by a policymaker about foreign aid was that of U.S. Secretary of State Dulles, who was quoted as saying in the late 1950s that more foreign aid should be given to countries where it achieves results, like Saudi Arabia, rather than countries, like South Korea, where it is wasted. This illustrates two of the problems with evaluations: dependence on the evaluator's frame of reference and lack of a long-term perspective for judgment of effectiveness.

There is no systematic assessment of the impact of Point IV programs. Nor, because the value of technical assistance is usually dependent upon the specific conditions in each case, would any evaluation have been very useful.

The impressionistic conclusion drawn by one expert is that Point IV assistance seems to have been relatively successful in Latin America but was less so in other parts of the world where country conditions were more primitive. This may be partly due to the fact that modest U.S. economic aid to Latin America had actually started during World War II, so the earlier experience may have made Point IV programs more effective. U.S. agricultural experts, drawn mainly from the U.S. agricultural extension service, were able in many cases to transfer relatively simple techniques that had high payoffs to groups of local farmers. The evident success by early adopters caused their use to spread rapidly to other farmers. Such opportunities for rapid results were available because they were the first introduction of scientific approaches.

In Asian and African countries, it appears to have been more difficult to find things that American agronomists knew that farmers also found useful. Even training local agronomists proved difficult in some countries where only city dwellers were literate. American agriculturists had to develop knowledge relevant to the region before they could be effective. Consequently, this period was one of considerable learning for the development "experts," as they learned that technologies could not be transferred wholesale, and that individual behavior is embedded in institutional and cultural environments.

Factors Leading to Revision

By the mid-1950s, the idea that technical assistance alone would end extreme poverty was being questioned. Obviously, poor countries lacked up-to-date knowledge, but it was equally obvious that they also lacked the stock of capital—roads, factories, power plants—that would make better knowledge useful. Point IV was not so much abandoned as enhanced and enlarged. Technical assistance became a relatively smaller part of a much larger whole. There was concern about the threat to U.S. security if—as many feared—much of the developing world turned to communism as the more rapid road to industrialization and development. These fears lead to steadily larger development aid appropriations in the late 1950s, and the beginning of financial assistance in 1958. The rioting in Latin America in 1958 during the visit of Vice President Nixon and the rise of Fidel Castro in Cuba further stoked these fears.

During the 1950s, the academic community also began to discover underdevelopment, and a wide variety of hypotheses began to emerge. Albert Hirschman, W. Arthur Lewis, Max Millikan, Paul Rosenstein-Rodan, W. W. Rostow, and Hans Singer were among the developmental theorists who sought to explain why poor countries were poor and what might be done about it.

As an example, in 1986 the World Bank convened a conference including the major early development theorists to learn how the experience of the subsequent three decades had altered their ideas. Perhaps the most notable feature of the mature views of many of the participants was how little they had been altered by the vast increase in empirical knowledge about the functioning of the development process in actual practice. That most of the early theorists—whose models were inconsistent with those of other pioneers—could see their hypotheses justified by subsequent experience demonstrates two insights: that deeply formed ideas are not likely to be much altered by subsequent experience and that development is so multidimensional and "evaluate-able" from many different perspectives that considerable evidence can be amassed to support a wide variety of different interpretations.

The theorists whose ideas resonated most were economists. The economists provided concrete ideas about what might be done to change the face of the underdeveloped world that left in the shade the less-formed, or less rigorous, approaches of anthropologists or political scientists. These economists, however, did not limit their thinking to economics. The ideas surrounding modernization and development typically involved assumptions that people in developing countries were bound by traditional values that left only limited scope for rational calculation, and that the expansion of the "modern" sector would lead to the emergence of "modern" people who would accept change easily and rationally.

HIGH DEVELOPMENT: THE ECONOMIST AS KING, 1961–1972

A new era of economic development arrived toward the end of the 1950s, after the Marshall Plan had rejuvenated the economies of Western Europe more than was originally expected. Free trade was recognized as a key factor that would facilitate economic integration and promote further economic growth. In this post-World War II era, decolonization was combined with a "war on poverty" waged at a global level. Along these lines, the 1960s was declared by the United Nations to be the "decade of development."
In his presidential campaign, John Kennedy offered the idea of foreign aid to reduce world poverty as a mechanism to counter the growing threat of communist expansion. He thus created, in 1961, the U.S. Agency for International Development (USAID). In addition, to address the particular circumstances in Latin America at that time, the Alliance for Progress in the Western Hemisphere was proposed.

One of Kennedy's leading economic advisors, W. W. Rostow, had written an influential book entitled, *Stages of Economic Growth: A Non-Communist Manifesto* (1960). In it he argued that poverty was perpetuated by a combination of traditional attitudes and traditional interest groups. It was not that the wealthy in poor countries were hostile to modernization, but that they did not see it as in their interest. Only government could create new economic realities that would cause wealth holders to support modernization rather than oppose it. It was the job of government, therefore, to take the lead in modernization by promoting industrialization—either directly through government ownership or indirectly through low-interest loans to enterprising people. Government expansion of education to the masses would provide the educated labor force needed by a modern industrial economy. The effort by government could not be modest, for the nexus that prevented change was strong. A "big push" was called for. Taxation, directly or indirectly, of agriculture would provide a source of funds for this big push.

The role foreseen for government as planner and agenda setter of the development process is described in USAID's 1961 Congressional presentation:

> The statement by national leaders of the country's goals, four or five or eight years hence, in each of the fields—the government programs that will be necessary, the expansion of private activity that is anticipated, and the results that will be obtained—is a necessary framework for year-to-year budgeting of specific government programs, but it may also serve a broader purpose. The nation's leaders should combine these sector goals into a statement of the nation's purposes and philosophy aimed at capturing the public's imagination. In a new and not very united country, the announcement and prosecution of a development program may help to create the feeling that the country is going somewhere. It may draw the people of the towns and villages toward national unity and into the national effort.

This idea of planning as an essential part of the development process was linked to the key role of government. It owed something to the recollection of the depression of the 1930s, which was seen as evidence that laissez faire was vulnerable to slumps and overproduction. Planning was specifically incorporated into the Alliance for Progress, which required participating Latin American governments to develop national plans. Most went further and established national planning offices or ministries.
For most developing countries where USAID worked, the early 1960s were a period of increasing resource abundance, as aid appropriations rose. There were two major exceptions. Following the exile of Chiang Kai-shek to Taiwan and the Korean War, the United States had inherited a commitment to the security and economic well-being of Taiwan and South Korea. Large economic assistance programs in Taiwan and South Korea were initially provided to assure political stability. As the United States began to tire of its continuing role in closing large balance of payments gaps, it began to press both governments to promote exports to gradually replace U.S. aid. Both countries took the advice (or the implied threat) very seriously and embarked on aggressive export promotion campaigns.

These broader approaches replaced the hands-on approaches used earlier, and USAID respectively changed as well. The agency moved away from relying primarily technical experts who worked directly on specific projects to economists who focused on improving the institutions and mechanisms that existed in developing economies. As it was described at the time, the "programmers" replaced the "well-drillers."

Documentation and Performance Measurement

With the ascendancy of the programmers, the “country strategy” became a central feature of the programming process. Though its name varied over time, the country strategy paper typically included a description of the country’s experience during the last decade or so, included a summary of previous USAID activities with some (limited) evaluative content, and laid out a proposed approach to the country assistance program for the upcoming period, typically three to five years.

The “take-off” metaphor created an optimism that pervaded USAID programming, and carried the Rostow model far beyond the theorist’s intentions. Even in as remote a country as Nepal, where literacy was below 10 percent, the USAID mission director looked for projects to prime the pump of growth, writing of the need: to achieve, and quickly as possible, the take-off point: which according to economists was the point of no return, the point after which growth would continue unimpeded on its own initiative. To achieve this point, inertia must be overcome, projects must be initiated, growth and expansion become the order of the day.

In Latin America, the Alliance for Progress required participating governments to institute a variety of reforms such as improving health and education services, increasing taxes. The expectation was that peer pressure would be more effective in promoting reform than unilateral preaching by the United States. Each government receiving aid made an annual presentation to the Inter-American Committee for the Alliance of Progress describing its accomplishments.

Impact

Seen in its own terms, U.S. assistance during the 1960s should be considered rather successful. Economic growth rates throughout the developing world were unprecedented. For Latin America, GDP growth during the decade was about equal to the Alliance for Progress goal of 2.5 percent per year per capita. Progress toward social goals was also impressive, with primary school enrollments rising dramatically, and life expectancy rising by nearly five years over the decade.
In Asia, India’s growth was a disappointment to planners. Nevertheless, it still was a dramatic improvement over the stagnation of the economy in per capita terms during the first half of the century. South Korea and Taiwan were beginning to show dramatic results by the end of the decade from their export-focused growth strategies. Though USAID economists had a key role, along with consultants like Béla Balassa, the conventional wisdom in USAID was that these two countries were unique.
In other measures of well-being, the progress during the 1960s was even more encouraging. With U.S. help, education and public health ministries were dramatically expanded, electricity, water, and telephone coverage expanded rapidly, often by newly created government enterprises that were bringing modernization to the masses.

One of the early efforts of the evaluation office created by USAID in 1970 analyzed USAID agricultural extension efforts in Latin America. The study concluded, based on extensive and persuasive evidence, that agricultural extension had been a failure in Latin America. USAID had tried to apply the U.S. extension model to the region. The study persuasively demonstrated that the Latin American version lacked the two-way linkages between research and extension that had existed in the United States. In Latin America, extensionists were ineffective because they had little to offer farmers. Researchers, lacking a means to learn which research problems were useful to farmers, worked on problems of little interest to them.

By 1970, USAID was becoming more concerned about drawing on the lessons of its previous work in a more organized way, and it established an evaluation office and associated development library. The evaluation office saw its role as collaborating with the agency’s professionals to draw broad programmatic lessons from efforts in different countries. The evaluation office, however, was only one of several approaches being used to draw lessons from experience. The agency funded a considerable amount of research by academic economists and social scientists. For several years, it also undertook annual conferences (called Spring Reviews) bringing together agency personnel and academics on some development topic. Both practitioners and academics would write papers and the conference would attempt to draw conclusions for USAID policy. The 1973 Spring Review on agricultural credit is remembered by many as overturning the conventional wisdom that small farmers needed subsidized or preferential access to credit, and demonstrating that high interest rates were a better means to assure access.

FACTORS LEADING TO ABANDONMENT OF THE CAPITAL-DRIVEN MODEL OF GROWTH

Though the apparent achievements of U.S. aid programs during the 1960s in encouraging rapid economic growth and social improvement were considerable, many felt disappointed that the achievements were not greater.

The earliest call for rethinking of government-led development apparently came from Ronald Coase in his 1973 presidential address to the American Economic Association, where he noted that "there was lots of literature on market failure, but where was the literature on government failure?" That was to come later. Anne Krueger later deepened Coase's ideas on government failure, inventing a term, opaque to most noneconomists, about "rent-seeking" to describe cozy relations between governments and groups interested in using government regulation for their financial benefit.

There were perhaps three developments that ultimately undermined confidence in the "high development" strategy, and led to its replacement by an alternative formulation.

The first development was disappointment with the development results being produced. This was particularly true in Latin America. As mentioned earlier, the progress against the quantitative goals under the Alliance for Progress was reasonably close to the original targets established for the decade. Nevertheless, the vision that the development community promoted of rapid and dramatic results was impossible to realize in practice. Moreover, there were disturbing trends. Urban upper and middle classes were clearly benefiting from improvements in infrastructure and modern-sector employment, but the growth appeared to bring little improvement for the poor. The programmer's models were failing to produce results that would "trickle down" to the poor.

The 1970 census in Brazil was a major piece of evidence. The census showed a substantial increase in income inequality between 1960 and 1970. The share of the bottom deciles declined significantly. This was sometimes used to argue that the poor had actually become worse off, though the data showed a small absolute rise in incomes. The issue of employment also provided a source of concern, and some argued that unemployment rates were rising inexorably in developing countries, as people flocked to cities that were not generating enough jobs. The International Labour Organization commissioned several studies that appeared to confirm rising unemployment and the prospect of further rises in the future. Finally, the domestic American political issues surrounding the Vietnam War exacerbated suspicions about foreign aid, with some charging that foreign aid taxed poor people in America to help rich people in developing countries.

In some respects, the visual evidence of extreme poverty seems almost certain to assure periodic declarations that foreign aid is failing and that new approaches are needed. The journalist (or Congressman, or academic) visits a developing country and encounters the grim reality of squalor and grinding poverty. The pervasiveness of obvious poverty on the urban fringes must surely mean that conditions for the poor have not improved. The visitor then contrasts this with the high-rise apartments and Mercedes-Benz's of the wealthy. The obvious conclusion is that only the rich have been benefiting from whatever development has taken place, or perhaps even that the poor are poor because the rich have become richer. This visual evidence is available in all poor countries—those where other evidence shows that the poor have gained disproportionately in income, and where the poor have been excluded from the development process.
The second factor undermining the development model was the India–Pakistan war of 1965. This had no direct relationship to the effectiveness of foreign aid, but it fatally undermined the naive belief of development programmers that economic development was the central, or even exclusive, focus of governments in poor countries. It also seriously eroded the moral high ground that the development decade had given to Third-World leaders like Nehru.

The third development, also initially centered on India and Pakistan, was the growing evidence by mid-decade that planning models did not translate so automatically into rapid economic growth. Outcomes fell far short of the expectations in five-year plans; two consecutive bad harvests in 1965 and 1966 further shook confidence.

These last two developments eroded the previous belief that "public sector" was synonymous with "public good." National planning as the main mechanism for ensuring long-term development was also a major disappointment. National Planning Offices typically were discovered to be political entities committed to implement the specific program of the administration in power, and to perpetuate that administration. Even where the government sought a national consensus about the plan, the desire of members of the government in power to use the instruments of office in the usual way—to reward allies and punish enemies, to assure that positive national events or outcomes are linked as closely as possible to the government in power, and that negative outcomes are the result of actions by its opponents. Government planning also failed in a more workaday way. Construction of new roads was favored over the uninteresting task of road maintenance. Ministries were discovered to be nests of bureaucracy—focused mainly on internal government politics and poorly connected to the needs of the country.

POVERTY AND BASIC NEEDS, 1973–1981

Conceptual Basis

The disillusion with macroeconomic concepts by the end of the 1960s was reinforced by a general increase in suspicion of government and its actions brought on by the Vietnam war. The conflict of visions culminated in a Senate vote in 1972 to end foreign aid appropriations. This signaled the need for a conceptual rethinking of the U.S. approach, leading to a major revision in the foreign aid legislation. The 1973 "New Directions" legislation emphasized the focus of U.S. assistance on poverty reduction. It went beyond this goal to specifically direct USAID to redesign its programs to focus directly on reducing poverty and activities directly benefiting poor people—the "poor majority" in developing countries. Where possible, programs should go beyond this standard and reach "the poorest of the poor."

The economics profession generally sought to moderate this concept by continuing to emphasize the importance of economic growth for poverty reduction. The book *Redistribution with Growth: Policies to Improve Income Distribution in Developing Countries in the Context of Economic Growth*, by Hollis Chenery et al. (1974), embodied this view. It argued that important redistributive impacts on poverty would come from expansion of educational opportunities, support for open markets and government efforts to promote employment of rural and low-skill workers.

Conceptually, USAID economists sought to interpret the new approach, anointed as basic human needs, or BHN, in the Chenery context, but others in the organization, prodded by strong interest by Congressional staff, often pressed for activities that directly and tangibly addressed the "poorest of the poor."

Documentation and Performance Measurement

The new approach led to a revision of USAID documentation. Despite emphasis in overarching policy and strategy documents on the importance of broad-based growth, macroeconomic analysis was reduced in country strategy papers to make room for analyses of poverty, of the characteristics of the poor in the country, and of "social soundness." Project proposals had to specify the linkages between project activities and poor people, including quantitative estimates of the impact of the project on the poor. A section analyzing the social soundness of the project was added, and anthropologists and sociologists were recruited to undertake and to review such analyses.

During this period, USAID also introduced a matrix, called the logical framework (or logframe) to aid in the design and monitoring of USAID project activities. The logframe required the project designer to conceptually describe the activity in terms of three levels of impact (goal, purpose, and output level), each with quantifiable indicators of performance, and to relate these expected results to the inputs being provided by the project and by the counterpart institution.

The logical framework gradually came to be seen as a useful tool, and became a standard feature of all projects for the next two decades. Its most important use was generally seen as forcing project designers to think more clearly about their proposed activity. It also provided evaluators in principle with a useful tool for assessing project success. Nevertheless, the value of the approach was often vitiated by the fact that neither baseline nor end-of-project indicators were usually available. An even more serious problem was that the "end of project" was really only the beginning of any permanent result. Only after the funding had ceased could any sustainable change in conditions on the ground begin to be measured.
Impact

Many USAID professionals regard the BHN period as a dismal failure. While poverty reduction was viewed as important, the idea that doing something directly for the poorest without regard for the environment in which they lived was seen as futile. Helping a poor farmer to increase output where there was no market, or where a marketing board was confiscatory, was a dubious proposition.

Two different sets of problems emerged. First, there was considerable pressure from some in policy positions in USAID and in the U.S. Congress for a narrow interpretation of the mandate. This led to pressure to develop programs that directly reached "the poorest of the poor." Most policy analysts and project developers suspected that indirect approaches—where the poor are reached through policy or institutional efforts—were a much more promising avenue. Second, the complex designs of many projects, most notably of "integrated rural development" efforts, encountered serious implementation problems. Coordination among government agencies proved difficult, if not impossible. The idea that different government agencies would cooperate with each other at the local or regional level in developing countries is a development theorist's fantasy.

The increased use of anthropologists and sociologists provided a mixed legacy. On the positive side, the introduction of an approach that centered more directly on people was important. However, the weakness was that it displaced, rather than supplemented, a focus on growth. The idea that poor people were actors capable of independent action, with aspirations and values that needed to be taken into account helped improve the focus and effectiveness of development efforts. The publication of T. W. Schultz's book *Transforming Traditional Agriculture* in 1964 was probably a major step in this direction. Schultz argued that farmers in poor countries were not so bound by tradition as the development programmer thought, but rational calculators of their own interest. If farmers did not adopt new technology, the proposed new technology was probably not suitable. (The unsuitability may have been due more to market factors, such as price controls for the product or lack of access to inputs because of monopoly, rather than any purely technical consideration.)

Nevertheless, the social scientists did not become institutionalized in USAID. These specialists were generally seen as providing perspectives that were so vague or nonaction oriented as to be unhelpful in the project design and implementation process. Staff positions for such social scientists gradually disappeared and incumbents either left the agency or moved into line positions in program or project offices.

Factors Leading to Abandonment

By 1980, the economic environment facing developing countries had deteriorated badly. Oil prices had risen sharply in 1978, and world interest rates rose sharply in 1979 following the tightening of U.S. monetary policy. LIBOR, the London Inter-Bank Borrowing Rate, to which much poor-country debt was indexed, quickly rose from 6 percent to 16 percent. The latter impacted many developing countries directly, as they had borrowed extensively at variable rates to finance the costs of the two oil shocks. Indirectly, the slowdown in world economic activity was to mean the end of the long commodity price boom of the last two decades.

The downturn in the world economy exposed many cracks in the political economy of many developing countries. Particularly in Africa, where countries had been pursuing, with USAID and other donor support, BHN approaches that ignored large economic distortions, the problems forced a basic rethinking of the sustainability of such approaches. Tanzania in particular had been seen as using innovative and promising means to reach its poor majority to satisfy their basic needs. By the early 1980s, the Tanzanian approach came to be seen as a disaster, incapable of providing sustainable improvement in conditions.

OPEN MARKETS AND THE PRIVATE SECTOR

Conceptual Basis

The new approach announced by the Reagan administration in 1981 did not aim for the intellectual coherence of the previous models, but it drew heavily on the accumulated knowledge of the development process. The "four pillars" of this approach were policy dialogue, institution building, technology transfer, and the private sector. Institution building and technology transfer had long been emphases of previous approaches, so they represented no significant shift. The "policy dialogue" pillar signaled a much greater emphasis on changing the policy framework in the recipient country, raising the focus from poor people to the country environment. The emphasis on the private sector was the major new feature, as earlier approaches assumed that the profit-making private sector should largely take care of itself. The implicit goal was that economic growth was the key, and that the emphasis on the four pillars would produce the needed broad-based economic growth.

In effect, the new approach was 1960s developmentalism turned on its head. Macroeconomics mattered, though with greater emphasis on avoiding fiscal imbalances, and establishing market-based trade and international payment systems. But government turned from being seen as the solution to being the problem, and the private sector turned from problem to solution. If economic progress was slow, it must be that government was holding back entrepreneurship, an extension of the earlier work of T. W. Schultz.
In a broad sense, the free markets' approach assumed that the world was Schumpterian, where economic progress was to be discovered rather than designed. Entrepreneurs discovered better ways of doing things,

engaging in “creative destruction” of older ways of doing business. The entrepreneur need not worry about the fact that his success in innovating may mean that other firms will be bankrupted and their workers displaced (in the jargon of economists, he can externalize his diseconomies). In countries where government has levers of economic control, it is likely to prevent or retard such innovation. This could be either because of the power of the existing vested interests or because democratic participatory government will inevitably give greater weight to the views of people likely to be displaced by change than those usually unknown people who will benefit. Acemoglu and Robinson (2012) reiterate the key role of Schumpeterian entrepreneurship in their magisterial *Why Nations Fail: The Origins of Power, Prosperity and Poverty.* They argue that most failing nations are “extractive,” preventing innovation that does not directly benefit the political oligarchy.

The new approach continued and deepened the people-centered ideas from the BHN period. Governments were seen less monolithically than in the 1960s, as made up of people with their own interests that might diverge from the “public good.” In part, that was a legacy of the BHN period. In areas like education and family planning, as well as in economics, the development experts were more likely to look at the incentive structure facing people in order to better understand their likely actions, instead of assuming that they all wanted to “do good.”

This was the golden age of USAID economists as development practitioners, rather than theorists from the principles they learned in graduate school. USAID hired several dozen new economists, most with substantial previous development experience in other organizations, including multilateral banks, the IMF and the U.S. Treasury. The attraction was partly the potential to “get one’s hands dirty” in the issues, like sectoral policies, obstacles to entrepreneurship, and the difficulty of small firms to gain traction in countries where policies smothered the private sector.

In Africa, USAID instituted a wide-ranging series of studies that identified the almost-insurmountable obstacles governments—through marketing boards, government suppliers of seeds and fertilizers, which prevented farmers from access to inputs and markets, and generated substantial rents for national governments. The resurgence of many African countries in the 1990s and later is a testament to the value of these reforms in the agricultural sector and in macroeconomic policy.
In Latin America, USAID promoted the establishment of privately owned export processing zones as a vehicle for avoiding the myriad obstacles to exporting from these countries. Central America eventually developed into a major source of apparel exports to the United States. The simplification of regulations for exporting agricultural products also led to the region becoming a major source of high-value fruits and vegetables, especially during the cold season in the United States.

The 1984 USAID Economists’ Conference epitomizes these skills by USAID economists in identifying country and sectoral-level issues that reflected their understanding of the need for “getting hands dirty” in constraints to growth in individual countries.

<u>Documentation and Performance Measurement</u>

The emphasis on country policy environment led to increased demand for analysis of that environment, so country strategy documents returned to analysis of macroeconomic policy. The analysis was broadened, however, to provide more attention to the obstacles faced by the private sector due to government regulation, such as import licensing, price controls, as well as to other forms of control of business. Initially, the emphasis on a favorable policy environment as a precondition to effectiveness of foreign assistance led to country-by-country reviews in Washington. It proved difficult to draw conclusions about which countries were better performers. Missions in most poorly performing countries could point to some recent policy action that would soon improve conditions or be a harbinger of further actions. There was also experimentation with quantitative approaches to country allocation. In Africa, this led to the establishment of the Development Fund for Africa, which allocated resources based on country performance. These efforts led to closure of USAID missions in some countries, particularly in Africa, and to larger allocations for countries deemed to be better performers. Outside of Africa, the possibilities for such reallocations were much more limited, as aid allocations elsewhere were divided into five “functional accounts.” Resources freed up by eliminating agricultural projects in one country could only be used for agricultural projects in another, substantially reducing the fungibility of resources.

<u>Impact</u>

The new approach did yield important results. USAID was pushing governments in the direction that was becoming evident as the most promising direction, and other institutions, notably the World Bank, subsequently emphasized policy and the private sector. Encouragement of economic liberalization permitted the development of new export products in many countries, reducing pressure on the balance of payments, and creating new jobs in rapidly expanding sectors. USAID's promotion of private-sector business groups to lobby for reductions in government regulation also seemed generally effective, as did other efforts to promote nongovernmental centers of opinion and interest.

Nevertheless, the results did not meet expectations in many countries, though economic growth and poverty reduction in other countries, particularly in East Asia, were unprecedented. At the outset of the initiation of this approach, a cross-section of proponents would have predicted that, following a period of adjustment of several years, developing countries that followed improved macroeconomic policies would begin to grow robustly. In fact, there was major progress by most developing countries during the 1980s in improving policies. Multiple exchange rate systems were eliminated in many countries and replaced by market-based unitary rates. Licensing and other administrative barriers to international trade were dismantled in many countries, and import tariffs were reduced substantially. Price controls were dismantled, monopolistic marketing boards eliminated, and parastatal enterprises sold off. Yet many of the countries that undertook these reforms found that the reforms did not produce robust economic growth.

In Africa, robust growth in countries receiving substantial amounts of USAID assistance only began to appear in the mid-1990s, although Uganda, Mozambique, and later Ghana began to grow rapidly in the 1980s. Since then, many African countries have enjoyed 15 years or more of consistent, rapid, economic growth (Radelet, 2010).

Overall, assessing impact of USAID assistance in general terms had become much harder by the 1980s. For decades USAID flows had been becoming a diminishing share of total donor flows, with the United States falling from the dominant donor in 1960 to a secondary donor by the 1990s. Moreover, donors in general were becoming marginal to the financial condition of developing countries. Export earnings had grown and diversified dramatically, and private capital had become far more mobile internationally. Consequently, USAID had become a relatively marginal actor. Its influence was still important in a group of smaller and poorer countries where more resources are concentrated, but even there conditions had changed dramatically over the last several decades. Ministers or their advisors are likely to have been educated abroad, and modern communications technology gives them access to the larger world of ideas and trends, for which the foreign aid advisor was previously the carrier.

<u>Factors Leading to Abandonment</u>

The failure of planners' or economists' expectations to be fulfilled is not news. What was new in the early 1990s was that the failure of the dominant model to produce desired results did not lead to its rejection and replacement by an alternative. Indeed, studies around 1990, such as the World Bank World Development Report, were broadly accepted by the "Washington Consensus" and by many developing country governments. No alternative seemed plausible. The collapse of communism, and the abandonment of a variety of socialist experiments left no plausible alternative to open trading regimes and market-based domestic policies. This is not to say that there is widespread enthusiasm for the market paradigm. Indeed, criticism of the harshness of market forces, the fear that "globalization" will subject workers everywhere to increased instability and uncertainty because of the massive power of uncontrollable market forces.

REENGINEERED MANAGEMENT AND MICROALLOCATION, 1993–2001

<u>Conceptual Basis</u>

This USAID approach to development, did not involve a major shift in the development paradigm. Instead it emphasized centralized control in an era of declining budgets. Senior USAID officials emphasized that USAID was a "Cold War" agency, whose funding would obviously be curtailed once the Cold War against communism was over.

The two big ideas of the previous decade—that the country policy environment was critical to development and to aid effectiveness, and that most productive activity should be in the private sector with a limited government involvement—continued to have status as unquestioned truisms. In practice, however, both became marginal to actual practice. USAID sharply curtailed its focus on economic issues, arguing that the multilateral banks were better positioned to do such work (Fox, 2006). By 2000, most of USAID's human resource expertise in economics and private-sector development had disappeared, with about a dozen economists having been fired for lack of suitable positions, and private-sector officers migrating to areas like environment.

Documentation and Performance Measurement

USAID's interest in or capacity to theorize about development likewise declined dramatically. Beginning in 1993, policymakers shifted their principal focus from the goal to the means. Development effectiveness would be improved through better management of resources instead of clearer understanding of the complex issues involved. There were two main thrusts. First, USAID central management sought better monitoring of progress in ongoing activities from Washington. This was expected to assure that poorly performing ones could be curtailed and good performers rewarded and duplicated. Second, involvement of people from the host country in the design and oversight of project execution was expected to increase effectiveness. Nongovernmental organizations in particular were sought as implementers, overseers, and constructive critics of USAID activities. This represents a further development of the people-centered approach to development.

During this period, the agency substantially revised its programmatic approach. Under the new system, the focus would be on a small number of "strategic objectives" in each country, under which all USAID activities would be grouped. The strategic objectives replaced projects as the unit of activity. In principle, the new approach gives USAID field missions considerably more flexibility in adapting the activities under a strategic objective. In practice, centralization was the theme of the day. A new information system was designed with the aim of giving Washington policymakers real-time information on progress in the numerous country programs. This would reduce costs by allowing more staff to be located in Washington, with far lower overhead costs compared to overseas staff.

A computerized information system tying together both financial and results was designed to provide this control. Unfortunately, the system design did not meet the requirements, and, after immense effort and massive staff frustration, was finally abandoned. Various short-term fixes followed, but none were able to allow Washington-based leadership to fine tune USAID's overseas activities. Indeed, such a concept was surely a chimera: the idea that quantitative information could improve on the quantitative and qualitative information on the ground in a remote country was surely a case of hubris.

This approach led to a substantial reduction in USAID overseas staff, with economists in particular disappearing from country missions. The organization undertook a reduction in force, or RIF (bureaucratese for the ability to fire numerous employees). Economists were particularly targeted, and a dozen or so were fired as unessential to the new approach. Lack of new hires to replenish the rapidly declining numbers of retiring development experts gradually reduced the numbers of people with substantial experience on development issues.

Impact

The new approach, using strategic indicators and measurements that were often adjusted each year led to a decline of attention to real performance measurement, and to the eventual dismantling of USAID's central evaluation function. Further to the lack of attention to measurement, there was also a shift in allocation of available resources away from economic activities, to "softer" areas of governance, democracy, conflict prevention, and environment, where both goals as well as the most appropriate means to achieve them are inherently difficult to identify. With economic growth, the goal was clear, even if the means were not. For governance or democracy, neither the goal nor the best means could be identified with any specificity.
Factors Leading to Abandonment

The general decline in USAID's capacity to "do development" was widely recognized by the Congress and the executive branch leadership. The view that USAID lacked competence on big issues became the conventional wisdom, even though USAID was recognized as capable in some specialized areas that had strong Congressional support, including family planning, basic education and microfinance. The final impetus was the attacks of September 11, 2001, which led the government to see progress in poor countries as again central to U.S. national security.

DEVELOPMENT AS A KEY FOREIGN POLICY OBJECTIVE, POORLY DONE, 2001–PRESENT

Conceptual Basis

The new government that took office in 2001 initially continued the emphases of the previous administration, treating developing countries as a minor concern, and one where interest was waning. Following 9/11, "development" reemerged as a key element of U.S. foreign policy, along with defense and diplomacy at high levels of government. Providing countries with economic-growth producing institutions for the mass of the population became a larger focus. As a result, foreign aid grew dramatically during this period, following the declines in the 1990s. Total foreign aid rose from $10 billion in 2000 to $22 billion by 2008. Nevertheless, the weakening of USAID's capacity during the previous decade led Congressional and executive branch leaders to conclude that USAID was poorly positioned to lead, so most of the increases in funding went elsewhere.

Two important new initiatives were introduced. The first was the Millennium Challenge Corporation (MCC), intended to reward good-performing developing countries. Its steady-state level of funding was to be $5 billion per year. The second, with a large humanitarian dimension to show U.S. leadership in a critical global problem was an effort to address HIV/AIDS in Africa, with the acronym PEPFAR, which led to a vast increase in resources addressing this issue—$15 billion over five years.

The central concept behind the MCC was that good-performing countries needed to be rewarded, and that other countries needed incentives to become better performers. The MCC would provide large amounts of assistance to countries that met three criteria: economic freedom, ruling justly, and investing in people. Moreover, none of the indicators to judge performance would be internal to the MCC. All 16 (later 17) performance indicators would come from independent sources. Finally, the performance of all eligible countries according to the indicators would be published annually. The MCC was intended to grow to match PEPFAR at a level of $5 billion per year, but annual funding never came close to half of that level. At the level of Congressional and public support, visible progress on humanitarian or health issues will usually trump the vague benefits of faster economic growth and better institutions.
These two initiatives left USAID as a residual category for foreign aid funding, with Congressionally favored programs (basic education, family planning, microfinance) largely squeezing out resources for broad-based economic growth.

Documentation and Performance Measurement

Initially, documentation and performance measurement continued the lack of rigor and analytical rigor of earlier decades, with the main emphasis on input–output measures at the project level. But there was a subsequent parting of the ways between the two new creations of this era. The MCC chose to use a very transparent approach to its activities and to measurement of its performance, including probably the most rigorous approach to evaluation of any donor organization.

The PEPFAR, on the other hand, chose to develop a rigid input–output framework for addressing the HIV/AIDS pandemic. It involved delivery of a fairly uniform package of goods and services, and has common indicators of performance across countries. Higher-level goals (Are we winning the war against HIV/AIDS?) were assumed to be achieved if deliveries of the right medicines to the affected population by trained medical personnel met targets. Such targets were usually met, sometimes at the cost of diverting health staff and resources from other serious health problems. For example, "yes, HIV/AIDS got addressed, but public health in the country deteriorated because workers went where the resources were."

The evident success of the PEPFAR model led the head of the program to be named to a new position in the State Department to oversee the "development" part of the diplomacy, defense, and development trinity. As a Deputy Secretary of State, the incumbent would oversee all U.S. foreign economic assistance as head of the F, for foreign aid, bureau of the State Department. The F Bureau of State, drawing upon staff from both State and USAID, became the arbiter of allocations of foreign aid among countries and purposes. Slicing and dicing the foreign aid budget among the various boxes in the matrix.

This resulted in an even larger separation between the ideas of development economists in USAID and the actual allocation of aid funding. With the departure of the Deputy Secretary of State for F for personal reasons, the F structure persisted, though without leadership to give it direction. State Department officers with little depth in development largely controlled allocation of resources, often favoring the newest new initiative, which would be soon set aside for another. Three former heads of USAID lamented in 2008 that the structure of foreign aid was "chaotic and incoherent" thanks to a lack of clear vision by either the executive or legislative branches (Atwood, McPherson, and Natsios, 2008).

Impact

As yet, the case for the superior effectiveness of the MCC approach is not decided, but its openness about its projects makes such an assessment easier than any other donor organization. Moreover, the MCC's use of objective indicators seems to have led to both greater attention to country-level comparisons with other countries, and to an "MCC effect," where governments made explicit efforts to improve their performance on these indicators in order to qualify for an MCC agreement (Johnson and Zajonic, 2006). The development community still awaits a careful analysis of the MCC's first round of agreements, which only recently have come to completion.

PEPFAR has delivered massive amounts of HIV/AIDS services in Africa, and probably saved millions from early death. Still, the pandemic has continued, and the number of untreated persons still exceeds the number provided with appropriate drugs.

While the MCC and PEPFAR addressed clear ideas about how to "do development," elsewhere, the impact was often questionable, or worse. Huge amounts flowed during this period to Iraq and Afghanistan in support of U.S. military efforts in these countries. One outside assessment (Easterly and Pfutze, 2008) concluded that U.S. government ranked quite high among donors in transparency, but ranked 38th of 39 countries on the share of aid going to "deserving" countries. By their standard, 76 percent of U.S. government aid went to countries they classified as "corrupt"—clearly including the two largest recipients, Iraq and Afghanistan.

For USAID as an institution, however, the outcome over this period was clearly negative. The quality of staff, particularly including economists, continued to decline as a result of retirements without new additions. The increased focus on means rather than outcomes led to what the head of USAID in the early part of the decade (Natsios, 2010) called "the rise of the counter-bureaucracy." Specifically, he argued that: One of the little understood, but most powerful and disruptive tensions in established aid agencies lies in the clash between the compliance side of aid programs—the counter-bureaucracy—and the technical, programmatic side. The essential balance between these two in development programs has now been skewed to such a degree in the U.S. aid system (and in the World Bank as well) that the imbalance threatens program integrity. The counter-bureaucracy ignores a central principle of development theory—that those development programs that are most precisely and easily measured are the least transformational, and those programs that are most transformational are the least measurable. Relieving the tension between the counter-bureaucracy and development practice would require implementing new measurement systems, conducting more research on overregulation and its effects, reducing the layers of oversight and regulation, and aligning programmatic goals with organizational incentives. (Natsios, 2010, 1)

2012 AND BEYOND: BACK TO THE FUTURE?

Some modest reasons for hope for the reemergence of an environment for an analytical approach to U.S. foreign aid began to emerge by 2012. A USAID administrator was finally appointed after more than 18 months of the Obama presidency, with the appointment of most other senior officials coming only months later. The National Security Council concluded a major review of U.S. aid policy in early 2011, proposing greater autonomy for USAID. While the bureaucratic politics of this return of greater authority to USAID are still to play out, USAID has begun hiring new economists and begun again to develop country strategy documents and project papers. For this exercise in memory recovery, a number of retired professionals from an earlier era were brought back as consultants.

CONCLUDING REMARKS

Sixty years into the Truman vision, three conditions seem to characterize the current environment:

1. Undoubtedly, the life conditions of ordinary people are dramatically better than they were in 1950. Many fewer of their babies die, they and their children consume far more calories, they are dramatically more likely to have access to the wider world through television and telephone, their children are far more likely to be literate, and they mostly are able to flick a switch to produce light after the sun goes down. In that sense, efforts to promote "development," pioneered by the U.S. government, have been an enormous success.
2. Nevertheless, all this progress has not produced a world at peace in 2012. In the past decade, probably thousands have voluntarily committed suicide in order to kill others. Many others have gone to war against neighbors in pursuit of political or economic dominance. Clearly, the economics profession, in praising GDP growth or clean water, is talking a different language from many citizens of the world. People do not live by bread alone.
3. In sum, economic development is not a cure for all the problems of the human condition. Economic progress can make people more comfortable, but it is no panacea for the human condition.

Note 1 As Butterfield (2004, p. 4) documents, the proposal only resulted from a junior State Department official's end-running a rejection by his superiors and taking his proposal directly to the White House staff. The White House staff viewed it as precisely the new initiative that they needed to break new ground with the inaugural speech.

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