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Foreign Aid, New Economic Order and Basic Human Needs

by Neil Dias Karunaratne, St. Lucia, Brisbane*

The maldevelopments due to aid-tied growth-maximisation strategies of the past decades have led to cynicism, and sometimes downright opposition to aid donation by taxpayers in the industrialised countries. On the other hand, radicals in the developing countries view aid as a Trojan horse to perpetuate neo-colonialism and dependency. Dr. Karunaratne reviews the shortcomings of conventional aid and presents a package of proposals for a reformed aid strategy.

The present economic order or the constellation of trade, aid, monetary, technology, capital, labour and other resource flows between the rich industrialised nations or the advanced countries (ACs) and the poor nations or the less developed countries (LDCs) were designed by the ACs over three decades ago to preserve their economic hegemony. Several institutions such as the IMF, World Bank, and GATT were established to regulate economic transactions between ACs and LDCs in order to achieve efficient allocation of resources based on the neo-classical tenets of free trade and perfect competition. The mystique of allocative efficiency was emphasised in economic transactions both internationally and nationally and the need for distributive justice and equity was ignored particularly in discussing ACs-LDCs economic relationships. The ACs-LDCs nexus was one of AC domination and LDC dependence or a centre-periphery relation. Trade, aid and other economic transactions occurred in a manner that reinforced and perpetuated the "dependencia" cult of the established economic order. The post-war decolonisation movement and the

emergence of politically liberated nations with the growing perception that political independence to be meaningful has to be followed by economic liberation led to a growing articulation by LDCs of the demands for a new economic order devoid of "dependencia".

Demands of the LDCs

The demands of the LDCs found expression in the UN General Assembly Resolutions in 1974¹. The UN Resolutions called for a programme of action to terminate the economic hegemony of the ACs over LDCs by establishing a New International Economic Order (NIEO). Amongst the key proposals for a NIEO were the following:

- Fair international trade between ACs-LDCs based on stable prices for primary exports;
- Liberalisation of protective barriers imposed by ACs against manufactured imports from LDCs;
- Increase in the quantity and quality of foreign aid;
- The regulation of the activities of multinational corporations and the transfer of technology at fair prices from ACs to LDCs.

The proposals for NIEO evoked a stance of confrontation between ACs and LDCs which has now given way to a meaningful dialogue on the need for a NIEO. However the NIEO proposals continue to be chastised by an avalanche of writings that are widely publicised in leading journals.² The NIEO proposals have been dismissed as pipe-dreams of untrained economists or blackmail by

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¹ UN, Resolution Adopted by the General Assembly: Charter of Economic Rights and Duties of States. Mimeograph A/RES/3281/XXIX, New York, January 1975. UN, Publications of the Ad Hoc Committee of the Seventh Special Session, A/AC.176/23 and Add. 1-7, New York, September 1975.

² H. G. Grubel, The Case Against the New International Economic Order, in: *Weltwirtschaftliches Archiv*, Vol. 13, 1977. J. B. Donges, The Third World Demand for a New International Economic Order: Government Surveillance Versus Market Decision in Trade and Investment, in: *Kyklos*, Vol. 30, 1977, Fasc. 2, pp. 235-258. M. E. Kreinin, J. M. Finger, A Critical Survey of the New International Economic Order, in: *Journal of World Trade Law*, Vol. 10, 1976, pp. 493-512. M. Bronfenbrenner, An Old Reactionary Free Trader on the New International Economic Order, in: *Nebraska Journal of Economics and Business*, Autumn 1977, Vol. 16, No. 4, pp. 5-18.

LDCs to force the ACs to surrender their legitimate achievements.

A Silhouette of Global Poverty

However eminent the critics of the NIEO may be one cannot acquiesce with theories that attempt to perpetuate a blatantly unjust world order that has relegated two thirds of mankind to economic subjugation, wretched poverty and continual misery! A cursory glance at a silhouette of global poverty³ is sufficient to challenge the predilections of the ordent supporters of the *status quo*.

We live in contrasting a world of affluence and poverty. Whilst in ACs the per capita consumption exceeds 25 times the consumption in LDCs and millions suffer from cardiovascular diseases and obesity due to over-eating, in the LDCs 700 mn are malnourished and millions die of starvation. The vast amount of grain fed to cattle in USA alone is estimated to be sufficient to feed 1.2 bn starving humans in LDCs. Millions in LDCs are condemned to a life of debilitating disease due to lack of proper diet and basic sanitation. It is reported that 1.2 bn people do not have access to safe drinking water or sanitation facilities.

250 mn live in appalling conditions of squalor in urban slums in LDCs and 550 mn are illiterate. In stark contrast to the poverty and deprivation in LDCs is the opulence and wasteful consumerism in the ACs. A week-end pleasure cruise of an AC citizen is estimated to burn up the same amount of fossil fuel that an LDC peasant would have used during his whole life time! Further, the amount of steel dumped in the car yards of USA for any one year is estimated to exceed the demand for steel for agricultural purposes in a populous nation such as India. Surely, a world economic order that harbours and nurtures colossal poverty for the majority of mankind is morally indefensible and no economic theoretic incantation, however pretentious, need be tolerated, if it argues that the present world order is efficient and satisfactory. Today's pleas for a NIEO may appear heretical on the basis of neoclassical orthodoxy but they may well be the harbinger of tomorrow's *a la mode* theories!

Some of the stout defenders of the present economic order see foreign aid as an instrument for tinkering with the system based on marginalism or Benthamite calculus to overcome what they perceive as aberrations of the present order. The spectrum of LDC motives for contemporary aid donations range from purely humanitarian and altruistic considerations to the *real politik* of perpetuating the economic, commercial and political hegemony of donor ACs over the recipient LDCs. However, the osten-

sible purpose of much of contemporary aid is the promotion of economic growth and development in recipient LDC economies.

The role of foreign aid in growth and development has been much propagandised. The rationale for foreign aid has been justified on the basis of the operation of a foreign exchange constraint when the development problems of LDCs are analysed using variants of the Chenery-Strout two gap models.⁴ It is hypothesised that the prevalence of a foreign exchange bottleneck impedes investment programmes of LDCs based on capital imports. Foreign aid bridges the exchange gap and enables the attainment of specified growth targets. The above logic of the two-gap modelling also influenced the Pearson Commission⁵ to recommend that AC donors should attempt to give 1% of their GNP of which 0.7% should be Official Development Assistance (ODA) to enable the LDCs to grow at a rate of 6% so that they may be able to participate in the international economy as self-reliant partners by the end of the century.

Negative Feed-Backs of Foreign Aid

Empirical studies by Griffin and Enos⁶ reveal that growth and foreign aid are not positively correlated. Papanek,⁷ however, discovers a slight positive correlation between foreign aid and growth and argues that the inverse relationship between savings and aid demonstrated by most empirical studies may be misleading and may be due to faulty data or mis-specification of the econometric models used in the analysis. Dacy has demonstrated using a simple dynamic model "that aid also can help to produce a lower long-term growth rate than would occur in a no-aid situation".⁸ Bauer⁹ argues that foreign aid is neither a necessary nor a sufficient condition for economic development. Aid, he asserts, promotes a cargo-cult mentality in the recipient countries and this stifles initiative and private enterprise in LDCs. Foreign aid has left donors and recipients disenchanted with its performance. Wall observes: "When the rhetoric of aid is confronted with the facts of aid, when promises do not materialise and the supposed generosity appears more like parsimony, then, hardly surprisingly, the expected friendship frequently does not manifest itself or appears

⁴ H. B. Chenery, A. Strout, Foreign Assistance and Economic Development, in: American Economic Review, September 1966.

⁵ L. B. Pearson, Partners in Development. Report of the Commission on International Development, New York 1969.

⁶ K. B. Griffin, J. L. Enos, Foreign Assistance: Objectives and Consequences, in: Economic Development and Cultural Change, Vol. 18, April 1970, p. 317 et seq.

⁷ G. F. Papanek, The Effect of Aid and Other Resource Transfers on Savings and Growth in Less Developed Countries, in: Economic Journal, Vol. 82, No. 327, September 1972, pp. 934-51, and: Aid, Foreign Private Investment, Savings and Growth in Less Developed Countries, in: Journal of Political Economy, Vol. 81, No. 1, January/February 1973.

⁸ D. C. Dacy, Foreign Aid, Government Consumption, Saving and Growth in Less Developed Countries, in: The Economic Journal, Vol. 85, September 1975, pp. 548-561.

⁹ P. T. Bauer, Dissent on Development, London 1971.

³ J. Tinbergen et al., Reshaping the International Order, London 1977.

mented."¹⁰ The overwhelming consensus in the aid literature has been that aid has been counter-productive when measured in terms of its growth and development effects in recipient LDCs. Nevertheless, there is no advocacy to expunge aid from the present economic system or the proposed NIEO.

Foreign Aid Structure and Magnitude and Hyperbole of Donor Costs

Foreign aid refers to outright grants or gifts and loans on concessionary terms having a grant element of at least 25%. In 1976¹¹ the total net resource flows from ACs to LDCs amounted to approximately US \$ 59 bn and nearly 34% or US \$ 19.8 bn fell upon foreign aid or Official Development Assistance. Nearly 80% of this aid came from the 17 ACs. OPEC contributed 16% and the balance of 4% came from the centrally planned economies. The aid efforts of all donors are relatively declining despite the rise in their GNP. Although the nominal contribution to aid by the ACs or the largest group of aid donors has been rising, when corrected for inflation the real aid flows have been static during the 1970s. This mainly is due to the dwindling contributions from large donor countries like USA, Japan, and Germany who account respectively for 30%, 9% and 6% of the total AC aid disbursement. The ODA/GNP ratio of the DAC group has declined from 0.42 in 1964-66 (average) to 0.34 in 1975 and it is projected that if the present trends continue the ratio will dwindle to 0.28 by 1985. The aid contributions from OPEC which rose dramatically since 1973 have also declined and the centrally planned economies have made smaller contributions during the past two years. These declining trends have been recorded against the background of rising GNP in most of the donor countries. Hence, despite the platitudinous pronouncements of increasing aid from ACs to LDCs many large donors have failed to commit themselves to the UN ODA/GNP target of 0.7%. Only small countries like Sweden, Netherlands and Norway have attained the UN target. One of the demands of the protagonists of the NIEO is that all aid donors should strive to achieve the UN target forthwith.

The declining aid flows from ACs to LDCs do not augur well for the eradication of the mass poverty in LDCs. Despite the popular belief to the contrary the published figures of aid flows grossly exaggerate the cost of aid to the donors and the benefits accruing to the recipients. It should be noted that nearly 75% of total aid or ODA disbursed in 1975 was bilateral and 25% was multilateral. Most of the bilateral aid is tied to procurement from donor countries or to projects that are not injurious to the

economic interests of the donors. The aid "tying" practices of donors through monopoly pricing of procured goods and inflated shipping costs reduce the value of aid received by LDCs by as much as 20%.¹² Further, although the ACs report elatedly that they collectively exceeded the target of 84% grant element established in 1972, it should be noted that the grant element is computed on the basis of a hypothetical interest rate of 10%. Besides the terms (i. e. interest rates, grace period, maturity period and repayment schedules) the aiding and other leverage factors seriously undermine the benefits of aid to the recipients in LDCs. This results in substantial reverse flows to donors besides interest payments and amortisation.

There is much hyperbole in published aid statistics. It has been estimated that without even making allowances for all the reverse flows to donors through trade and other leverage activities, "the present official system overstates combined aid totals by more than 50 percent compared with real costs."¹³

Aid as a Debt Trap

Although aid giving originated for the ostensible purpose of promoting economic growth in the LDCs in order to make them eventually self-reliant, in retrospect aid has made recipient LDCs more and more dependent on the AC donors. Aid has been used increasingly by AC donors to prop up the capitalist system. The economic imperialism that rears its ugly head in the guise of aid has been condemned by Hayter.¹⁴

The rationale of foreign aid as embodied in the debt cycle models¹⁵ argues that aid is necessary during an initial phase of development to provide the investment funds required to attain a specified growth target. When the growth target is attained the economy would generate the savings needed to pay the debts. However, if the targeted growth rate fails to materialise, as has happened, the debts would grow at an exponential rate, sinking the debtor deeper and deeper into the quagmire of debt with no prospect of extrication.

In the 1950s the LDCs' debt crisis was non-existent; the indebtedness of LDCs is one of the main problems that needs resolution in the present order. By the end of 1977 the debts of LDCs had cumulated to the figure of US \$ 250 bn, the debts had more than doubled over its level

¹⁰ D. Wall, *The Charity of Nations*, London 1973, p. 58.

¹¹ M. J. Williams, *Review of Development Co-operation*, OECD, Paris, November 1976. Report of the Chairman of the DAC (Development Assistance Committee).

¹² M. L. Haq, *Tied Credits: A Quantitative Analysis*, in: J. Adler, S. Kuznets (eds.), *Capital Movements and Economic Development. Proceedings of a Conference held by the International Economic Association*, New York 1967. J. Bhagwati, *The Tying of Aid*, in: J. Bhagwati, R. S. Eckaus (eds.), *Foreign Aid*, London 1970.

¹³ J. A. Pincus, *The Cost of Foreign Aid*, in: *Review of Economics and Statistics*, Vol. 45, No. 4, 1963.

¹⁴ T. Hayter, *Aid as Imperialism*, London 1971.

¹⁵ D. Avramovic et al., *Economic Growth and External Debt*, Baltimore 1964.

five years ago. The total debt and debt service as a ratio of GNP are estimated to be approximately 20% and 5% respectively for the LDCs. The LDCs have to commit nearly 25% of their export earnings for debt servicing. In 1977, some individual LDCs spent nearly 50% of their export earnings on debt servicing or repayment for past foreign aid.

Proposals for generalised debt relief have been vigorously resisted by creditor ACs on the grounds that it will lead to financial truancy. Some accommodation of the debt of the LDCs has been made recently by ex-post correction for harsh lending terms made in the past and by rescheduling debt repayments. Many suggestions to treat debts as "bygones" have fallen on deaf ears of ACs' creditors. Payer compares the prevailing LDC debt situation to international peonage or debt slavery. Such a system operates to keep the LDCs in a state of perpetual underdevelopment for the benefit of multinationals and other vested interests of the ACs' capitalist system.¹⁶

Maldevelopment and the Need for a Reformed Aid Strategy

Past aid flows directed at maximising GNP in LDCs exacerbated the plights of income inequality and unemployment in LDCs.¹⁷ The anticipated trickle down of benefits of growth to the poverty stricken masses failed to occur because those who benefited from growth did not wish to redistribute their "spoils". In fact, the charge that "the poor in the rich countries were aiding the rich in the poor countries" had more than a grain of truth when one examines the maldevelopments bequeathed by the aid fostered trickle down strategies of GNP growth pursued in the LDCs in the 1960s and 1970s. Aid during this period was channelled to rapid import-substituting industrialisation in most LDCs.¹⁸ Industrialisation often based on modern large-scale technology was promoted at the expense of agriculture. The large-scale technology was counter-employment generating and excessively dependent on the use of further imported inputs while neglecting the use of the indigenous raw materials. Besides under the grip of multinationals, in the search for abnormal profits, sophisticated products totally unrelated to basic needs of the poverty-stricken majority were produced. Rather than alleviate poverty the aid-growth strategies aggravated the vector of problems associated with poverty. Growth by-passed the "bottom 40%" of the most needy in the LDCs.

Aid in order to percolate to the poverty-stricken masses of the LDCs needs to be disbursed only through a reformed aid strategy, lest aid continues to reinforce the maldevelopment in LDCs observed in the past. This would involve reshaping planning policies and institutional mechanisms in LDCs. There should be concrete steps undertaken in LDCs to cater for the satisfaction of the basic needs of the poor. Benefits of planned growth should be redirected to the poor rather than to the rich as in the past.

This would involve the pursuit of anti-elitist policies (e.g. taxation, price control); re-orientation of bureaucracy perceptions and priorities. Further structural changes like land reforms have to be implemented. The ethics of co-operative management rather than cut-throat private competition has to be inculcated at the level of village enterprise. Education needs to be purged of its disdain for the indigenous culture and values and the premium it puts on "coca-cola" culture or imported goods and values. A plethora of measures have to be initiated by governments of LDCs so as to redistribute the fruits of aid induced growth amongst the poverty stricken masses rather than concentrate it in the hands of a rich coterie as happened in the past. The demands of the NIEO to reform the AC-LDC aid and trade nexus would not lead to meaningful development in LDCs unless *pari passu* with the changes in the international order, changes are effected in the LDCs' domestic order. The changes in development strategies, value basis, institutional bottlenecks in the domestic order of the LDCs are critical if the NIEO is to fully have its impact on the LDCs' development without turning malignant as in the past.

Dimensions of a New Basic Human Needs (BHN) Focused Aid Strategy

The maldevelopments due to aid-tied growth-maximisation strategies of the past three decades have led to cynicism, and sometimes downright opposition to aid donation by taxpayers in ACs. Further, radicals in LDCs view aid as a Trojan horse to perpetuate neo-colonialism and the dependency syndrome and they point to the "widening gap" domestically and internationally as evidence of "dependencia" and perverse development. However, an assault on the colossal problem of global poverty cannot be successfully mounted by taking any one of these polarised positions. A *via media* would recognise that an aid strategy geared to redistribution primarily in LDCs would mitigate the pernicious income skewness effects of the past.

A reformulation of aid strategy so as to achieve "Basic Human Needs" rather than grandiose maximisation of the rate of growth of GNP would re-animate the flagging

¹⁶ C. Payer, *The Debt Trap*, London 1974, p. 49.

¹⁷ F. Stewart, P. Streeten, *New Strategies for Development: Poverty, Income Distribution and Growth*, in: *Oxford Economic Papers*, Vol. 28, No. 3, November 1976, pp. 381-406.

¹⁸ I. Little, T. Scitovsky, M. Scott, *Industry and Trade in Some Developing Countries*, London 1970.

support of donors and meet the primordial objectives of development aid. The ILO¹⁹ has already enunciated the dimensions of a Basic Human Needs strategy which could serve as a framework for an effective aid strategy in the NIEO. It needs to be emphasised that there is no unique Basic Human Needs strategy as basic needs are country-specific, resource-specific and aspirations-specific. The broad strands of such a strategy could, however, be sketched for the purpose of aid, as the planning for economic development that ensures the satisfaction of:

- Basic human wants of the masses such as food, clothing and shelter.
- Communal services such as education, transport, health and sanitary services and safe drinking water.
- The creative energies of the masses by encouraging popular participation in planning decisions that map out the economic destiny of the LDCs.
- The need for gainful employment or self-employment opportunities to provide for basic family consumption demands.

A World Treasury and other mechanisms proposed in the next section can harvest the resources needed to double aid flows and would infuse the much needed automaticity for development aid in order to plan in a long-run integrated perspective the assault on global poverty. The perpetuation of global poverty is morally indefensible and is a threat to the long-term peace and stability of the world economic order. Both ACs and LDCs need to co-operate in redirecting aid to redistribute the fruits of global growth and development in a fair manner both internationally and nationally. Aid despite its misdirection in the past holds promise as a viable instrument for an equitable new world order in which both ACs can continue to prosper and LDCs can survive harmoniously. The quantum and structure of aid have to be completely revised if it is to make the required impact in the campaign to eradicate global poverty. If aid does not provide the escape route from poverty the LDCs in desperation may seek more radical alternatives like auto-centric development or even as some have suggested nuclear blackmail.²⁰ However loathsome such a prospect may appear to us, one cannot dismiss this as fantasy. There are enough resources in the present world order, said Ghandi, to meet everybody's need but not everybody's greed. In a new world order the world's resources must be redirected to meet basic needs of humanity before creating more and more wants. The pace of consumerism in ACs needs to be slowed down and re-

sources diverted to meet basic human needs of the suffering billions in LDCs through more meaningful aid.

The Need for More Aid Automaticity

Neither the past performance nor the current trends of aid disbursements augur well for the conventional aid from ACs to LDCs. The NIEO plea for "predictable continuous and increasingly assured" aid flows may appear wishful thinking in the context of the prevailing aid scenario. However, if the aid operation is restructured not only can the NIEO pleas be met and the UN target of 0.7% of GNP as official development aid be surpassed, but also global welfare and long-term development prospects for both ACs and LDCs can be assured.

This could be achieved by the implementation of the following package of proposals:

- The establishment of a link between world liquidity creation and aid, i.e. the SDR (Special Drawing Rights) - aid link. This SDR-aid link has been consistently resisted by ACs on the grounds that it violates efficiency and aggravates global inflation. The inequity of creating liquidity for the ACs who have the largest IMF (International Monetary Fund) quotas and who perhaps least need it are glossed over in the opposition to the link.
- The revenue from profits of sales of IMF gold is directed to a development fund for LDCs, but there is much scope for redirecting a larger share of ACs' profits to this development aid fund.
- The establishment of a World Treasury to internationalise the *raison d'être* of national progressive taxation. Taxes could be levied on the manufacture of armaments, on the generation of pollution, on wasteful consumerism, on the excessive use of non-renewable resources like fossil fuels and minerals and the exploitation of the common heritage of mankind (seabed resources and space). Besides a brain drain tax, taxes on the exploitation of Antarctica have been mooted.

The serious consideration of proposals for establishing a World Treasury for progressive global taxation of wasteful economic activities and the use of common heritage of mankind for the common good of humanity is imperative.

The implementation of a reformed aid strategy would revitalise aid as an engine of development in the LDCs. It would also ensure the stability and prosperity of ACs which would come under increasing threat due to the growing epidemic of LDC poverty and misery. A reformed aid strategy is a vital key to world peace and global economic development through harmonious co-operation of ACs and LDCs.

¹⁹ I. L. O., *Employment, Growth and Basic Needs*, Geneva 1976.

²⁰ R. L. Heilbroner, *Inquiry Into the Human Prospect*, New York 1974, p. 42.