

## **HOW DOES THE PROPOSED LEVEL OF FOREIGN ECONOMIC AID UNDER THE BUSH BUDGET COMPARE WITH HISTORICAL LEVELS?**

### **And What Would Be The Effects of Bush's New "Millennium Challenge Account"?**

by Isaac Shapiro and Nancy Birdsall<sup>1</sup>

This short analysis examines the trends in U.S. non-military aid to other countries and how the Administration's proposed budget for fiscal year 2003 would affect those trends. It also includes a preliminary assessment of the President's new Millennium Challenge Account, which was first announced on March 14 and was revised on March 19.

The analysis does not address the vital questions concerning the composition and quality of this aid but instead attempts to address another important issue — how the overall level of proposed aid compares with past levels. The analysis examines three standards for measuring aid over time: aid as a percentage of total government outlays, aid as a percentage of the economy, and aid in inflation-adjusted terms.

The Administration's proposed 2003 level for foreign development, humanitarian, and economic aid (referred to in this analysis as "foreign economic aid") generally would continue the parsimonious record of recent years. U.S. foreign economic aid spending has trended downward for some time, with a sharp falloff occurring most recently in 1996. (All years in this analysis are fiscal years. This analysis is not focused on military aid.) After adjusting for inflation, the President's budget does propose a slight increase in foreign economic aid spending for 2003, but this spending has been so low in recent years, and has fallen so much in recent decades, that the proposed level would still be very low by U.S. historical standards. Indeed, by one key metric — how much of the budget is spent on foreign economic aid — the Administration proposes a level of foreign economic aid that would tie with 2002 for the lowest level since the end of World War II. The President's proposal for the establishment of a Millennium Challenge Account does not call for any increases in foreign economic aid until 2004, at which point a significant rise in aid is proposed, to be phased in over three years. Even in 2006, however, when the President's proposal would be fully phased-in, it calls for a level of aid that as a percentage of government expenditures and the economy would be well below historic levels.

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**Table 1**  
**Discretionary Spending on Foreign Economic Aid**

	1980s Average	In 2003 under Administration's Budget	Comment on 2003 Figures
As a share of the budget	0.92%	0.55%	Tied for post-World War II low
As a share of the economy	0.20%	0.11%	Second lowest in post-World War II era
Inflation-adjusted level (in 2003 dollars)	\$13.6 billion	\$11.6 billion	Significantly below historical average
Source: Center on Budget and Policy Priorities analysis of data from the Office of Management and Budget, the Congressional Budget Office, and U.S. AID.			

- *Aid in real dollars.* The Administration proposes to spend \$11.6 billion on foreign economic aid in fiscal year 2003. This would reflect a modest increase from the \$11.5 billion level expected to be spent in 2002.<sup>2</sup> (Both figures are expressed in 2003 dollars). Adjusted for inflation, however, the 2003 level would be 15 percent below the average level of foreign economic aid spending during the 1980s. (See Table 1.)
  
- *Aid as a share of the budget.* The Administration's proposed spending level of \$11.6 billion in 2003 would result in the United States devoting as small a share of federal expenditures to foreign economic aid as in any other year since the end of World War II. (The share would tie with the 2002 share for the lowest level.) Thus, relative to other uses of federal spending, *foreign economic aid would receive a priority as low as or lower than it has received at any other time in more than half a century.* The Administration's budget proposes dedicating 0.55 percent (a little over one-half of one percent) of all federal expenditures to foreign economic aid, or only about 55 cents of every \$100 the federal government spends.
  
- *Aid as a share of the economy.* Under this measure — which assesses how much of its total national resources the country spends on foreign economic aid — the United

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<sup>2</sup>The Administration also proposes increases over the “baseline.” According to the Congressional Budget Office estimates of the Administration's proposal, the Administration proposes a spending, or “outlay,” level for 2003 that would be marginally higher (one-tenth of one percent) than the 2003 baseline. The Administration proposes a “budget authority” level for 2003 that would be four percent higher than the 2003 baseline. Budget authority is the amount of money appropriated to be spent on a particular area; not all of the funds appropriated in a fiscal year need to be spent in that year.

States would devote only 0.11 percent of its resources to foreign economic aid (just over one-tenth of one percent), or about 11 cents of every \$100 in the economy. This would represent the second lowest share of national resources devoted to foreign economic aid in the post-World War II era; only the figure for 1999 was lower. As a share of the economy, the United States spent nearly twice as much on foreign economic aid during the 1980s as it would under the budget proposal for 2003. The decline is significantly larger when measured over a longer period.

## **The Potential Effects of the Millennium Challenge Account**

On March 14 the President sketched out his proposal for a Millennium Challenge Account. The account's stated goal is to "fund initiatives to help developing nations improve their economies and standards of living" and the President originally proposed committing a total of \$5 billion over three years to that account. On March 19 the Administration restated its proposal, indicating that it meant to commit a total increase in foreign economic aid of \$10 billion over three years, with a \$5 billion increase occurring in 2006 alone.<sup>3</sup>

If approved by Congress, once this proposal would be fully phased-in it would represent an important advancement in foreign economic aid funding and would increase aid spending to its highest share of the budget since 1995. As a share of the budget and the economy, however, foreign economic aid would still be below its shares in nearly every year from the end of World War II through the mid-1990s.

- *Aid in real dollars.* Foreign economic aid spending would total \$16 billion in 2006, after adjusting for inflation. This would represent a substantial inflation-adjusted increase of 38 percent over the 2003 level. In inflation-adjusted terms, foreign economic aid spending would rise above its average level of the 1980s.
- *Aid as a share of the budget.* Foreign economic aid spending would equal 0.73 percent of the federal budget in 2006, which would be a higher share of the budget than in 1992, 1994, and every year from 1996 onwards, but would be a lower share of the budget than in any other year since the end of World War II. So in 2006 aid would be a lower share of the budget than it was in the entire period from 1946-1991 (and lower than in 1993 and 1995 as well) and would remain significantly below its average level of 0.92 percent during the 1980s.

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<sup>3</sup>Joseph Kahn, "White House Adds Billions To an Increase In Foreign Aid," *The New York Times*, March 20, 2002, page A9.

- *Aid as a share of the economy.* Foreign economic aid spending would constitute 0.13 percent of the economy, an increase from recent years, but still below every year from the end of World War II through 1995. Aid as a share of the economy would still be far below its average share of 0.20 percent during the 1980s.

Table 2 includes annual figures from 1962 through 2006 on actual and proposed foreign economic aid spending, based on Office and Management and Budget and Congressional Budget Office data. For the years 2004, 2005, and 2006, it is assumed that the President's new Millennium Challenge Account would add \$1.67 billion, \$3.34 billion, and \$5 billion respectively to what the Administration has already proposed for those years. (The precise budget path has not yet been released by the Administration; it is unclear, for instance, if the \$5 billion increase for 2006 is relative to what the Administration proposes to spend for 2003 or what it previously proposed to spend for 2006. By assuming the latter, this analysis errs on the side of assuming a somewhat larger increase than the Administration might actually propose.) For the years from 1946 to 1961, this paper relies on data from U.S. AID.<sup>4</sup> Appendix 1 includes a discussion of comparing data for years from 1992 to the present to data for earlier years (there was a shift in how loans are treated under the budget in 1992).

## Measuring The Level of Foreign Economic Aid

Foreign economic aid can be defined and measured in a number of ways. The definition used here — which is the same definition the Center on Budget and Policy Priorities used in papers released in 2000 and 2001 on this subject — includes the budget category called "International Development and Humanitarian Assistance" (subfunction 151) as well as the "Economic Support Fund" (which is part of subfunction 152). The focus here is on discretionary spending in these areas.<sup>5</sup>

- International Development and Humanitarian Assistance includes funding for areas such as bilateral development aid, assistance to countries in transition (mainly those that once were part of the former Soviet Union), certain contributions to multilateral institutions

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<sup>4</sup>Based on the U.S. AID data, U.S. "Economic Assistance" (the category AID uses that is somewhat analogous to the definition of foreign economic aid this paper uses) averaged 1.75 percent of GDP from 1946 to 1948. From 1949 to 1952, it averaged 1.53 percent of GDP, while from 1953 to 1961, it averaged 0.60 percent of GDP.

The same pattern applies when foreign economic aid is measured as a percentage of all federal outlays. According to the U.S. AID data, Economic Assistance averaged 10.45 percent of all federal outlays from 1946 to 1948. From 1949 to 1952, it averaged 9.58 percent of outlays and from 1953 to 1961, it averaged 3.31 percent of outlays.

<sup>5</sup>More specifically, the definition of foreign economic aid used here includes *discretionary* or annually appropriated spending. *Mandatory* spending in these areas consists primarily of inflows of funds into credit liquidating accounts. This cash flow is a result of loans made before 1992, when the Credit Reform Act went into effect; it does not affect the current level of credit assistance and thus is ignored in this analysis.

that can be used for development aid, the Child Survival and Disease Program, humanitarian aid, emergency relief, migration and refugee assistance, and efforts to combat the drug trade. Some of the areas that fall into this government budget category are not purely "development aid" in that their main goal is not to help strengthen the economies of the world's poor countries.

- The Economic Support Fund consists of economic assistance the United States provides to other countries (such as Israel and Egypt) based on considerations of special economic, political, or security needs and U.S. interests. Not all these funds are targeted on development. Still, since some of the ESF funds that countries receive can assist economic development, this paper errs on the side of a too-inclusive definition and counts ESF funds in its analysis.

By including *all* the spending in the International Development and Humanitarian Assistance category as well as the Economic Support Fund, the figures used here overstate the amount of U.S. aid designed to combat poverty and its effects in the world's poor countries. For instance, for 2003 the Administration proposes to spend \$2.2 billion in Economic Support Funds and \$9.4 billion in the category of International Development and Humanitarian Assistance, yielding the total figure of \$11.6 billion used in this paper. If the Economic Support Funds were not counted as foreign economic aid, the amount of such spending would be \$9.4 billion instead of the \$11.6 billion considered in this paper.

It bears noting that the Administration proposes to increase spending in the International Development and Humanitarian Assistance area in 2003 but to decrease spending in the Economic Support Fund area. Even with the increase in International Development, Humanitarian, and Economic Assistance, however, the share of the budget and the share of the economy going to that category of assistance would be close to the lowest levels on record.

## Conclusion

It has been fairly widely reported in recent years that the United States contributes a smaller share of its economy to development aid than does any other high-income nation. As a share of their economies, the latest international comparisons from the Organization for Economic Cooperation and Development show that the typical high-income nation contributes three times as much as the United States does.<sup>6</sup> What has received less attention has been the decline in foreign economic aid spending in the United States compared with the levels of support provided in most of the post-World War II period. The level of spending proposed by the Bush Administration for 2003 would continue this policy of giving significantly less priority to foreign economic aid. If adopted, the Administration's new proposal for 2004 and beyond would reverse this trend, but would still leave aid spending as a share of all government spending and as a share of the economy well below its historical averages.

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<sup>6</sup>OECD, "Development Assistance Committee Announces ODA Figures for 2000," April 23, 2001.

**Table 2**  
**Foreign Economic Aid Trends, 1962-2007**

<b>Fiscal Year</b>	<b>Aid in 2003 Dollars (outlays in billions)</b>	<b>Aid as a percent of GDP</b>	<b>Aid as a percent of Budget Outlays</b>
1962	\$17.3	0.576%	3.06%
1963	\$16.5	0.526%	2.83%
1964	\$15.9	0.480%	2.60%
1965	\$15.7	0.448%	2.61%
1966	\$17.2	0.457%	2.56%
1967	\$16.5	0.418%	2.16%
1968	\$13.5	0.329%	1.61%
1969	\$11.8	0.274%	1.42%
1970	\$10.7	0.244%	1.27%
1971	\$9.8	0.220%	1.13%
1972	\$11.5	0.245%	1.26%
1973	\$10.3	0.205%	1.09%
1974	\$9.0	0.176%	0.94%
1975	\$10.9	0.218%	1.03%
1976	\$10.0	0.191%	0.89%
1977	\$11.5	0.208%	1.00%
1978	\$12.8	0.220%	1.06%
1979	\$12.2	0.201%	1.00%
1980	\$12.8	0.215%	0.99%
1981	\$13.0	0.214%	0.97%
1982	\$12.1	0.202%	0.88%
1983	\$12.7	0.208%	0.88%
1984	\$13.4	0.204%	0.92%
1985	\$17.7	0.260%	1.14%
1986	\$16.3	0.229%	1.02%
1987	\$12.9	0.176%	0.82%
1988	\$12.7	0.168%	0.79%
1989	\$12.8	0.163%	0.77%
1990	\$13.1	0.165%	0.76%
1991	\$13.2	0.168%	0.75%
1992	\$12.8	0.159%	0.71%
1993	\$13.3	0.161%	0.75%
1994	\$13.0	0.152%	0.72%
1995	\$13.5	0.153%	0.74%
1996	\$11.6	0.128%	0.63%
1997	\$11.2	0.119%	0.61%
1998	\$10.9	0.111%	0.59%
1999	\$10.7	0.105%	0.56%
2000	\$11.2	0.107%	0.58%
2001	\$11.5	0.109%	0.59%
2002*	\$11.5	0.108%	0.55%
2003*	\$11.6	0.106%	0.55%
2004*	\$13.2	0.117%	0.62%
2005*	\$14.5	0.125%	0.67%
2006*	\$16.0	0.135%	0.73%

\*Data for 2002 through 2006 are Congressional Budget Office estimates of the Administration's budget proposal plus assumed effects of the Millennium Challenge Account. Figures are adjusted for inflation based on the CPI-URS from 1962-2000 and CBO's inflation projections for 2001 onwards.

Source: Author's analysis of Office of Management and Budget and CBO data.

## **Appendix 1**

### **Comparing pre-1992 Data to Data from 1992 On**

Although the Office of Management and Budget provides annual data on discretionary spending for fiscal year 1962 onward, the time series is not entirely consistent. The inconsistency reflects the difference in the budgetary treatment of loans prior to 1992 and from 1992 on.

Prior to 1992, loans were recorded in the budget on a *cash* basis; that is, the amount associated with making a loan equaled the cash disbursed. Similarly, principal repayments and interest paid on the loan were recorded on a cash basis as "negative spending," in other words, as a reduction in spending. As a result of the Federal Credit Reform Act of 1990, since 1992 loans have been treated on a *subsidy* basis; that is, the amount of spending associated with a loan equals the estimated amount of the subsidy provided by a loan. Principal repayments and interest paid on the loan are recorded in "non-budgetary" accounts and thus do not affect the spending recorded in the budget. OMB has said that it has found it "impossible to convert the pre-1992 loans to a credit reform basis," and thereby to construct a consistent time series.

As an example of the effects of these differences in treatment, take the hypothetical case of a loan of \$1 million that involved a subsidy of \$200,000.

- Prior to 1992 this loan would have been considered to result in outlays of \$1 million in the year it was issued; since 1992 only the subsidy amount — \$200,000 — is recorded in the budget in the year it is issued. So in the year issued the "same" loan was assumed to cost *more* in the pre-1992 period.
- In the years after the loan is issued, the effect works in the opposite direction. Prior to 1992, any principal or interest payments on the loan would have the effect of reducing spending as recorded in the budget. Since 1992, these payments are handled differently and do not affect discretionary spending on foreign economic aid. So in the years after the loan is issued, the same loan is assumed to cost *less* (since the payments would be recorded as negative funding) in the pre-1992 period.
- The net effect on the measurement of foreign economic aid is difficult to determine. It depends on the nature of the loans issued, the timing of the repayments, and changes in the size of the loans over time. That is, we know the time series is not entirely consistent, but it is difficult to ascertain whether in comparing particular years this inconsistency leads to an overstatement or an understatement of the fall in foreign economic aid over time.

Nevertheless, it is possible to state with confidence that foreign economic aid has declined since the 1960s, and in 2003 will be at or near the lowest levels on record as a share of the economy and

government outlays. First, although the proportion of foreign economic aid that consists of loans is now lower than it was, the data that are available suggest that loans were not the majority of foreign economic aid prior to 1992. U.S. AID data for the period from 1962 to 1993 indicate that 21 percent of their definition of foreign economic assistance consisted of loans, the other 79 percent consisted of grants. (AID did not break these data out on an annual basis.)

Second, the differences between now and the 1960s and 1970s are dramatic (because of the drop in loans during the 1980s, there is little reason to be concerned that comparing current spending to spending in the 1980s leads to an overstatement in the fall of foreign economic aid), suggesting that an inconsistency of difficult-to-determine direction is unlikely to affect the basic trend. From 1962 to 1969 according to the definition of foreign economic aid used in this paper, it equaled between 0.27 percent and 0.58 percent of the economy; in the 1970s, foreign economic aid constituted between 0.18 percent and 0.25 percent of the economy; under the Bush budget it would equal 0.11 percent of the economy. The differences between now and then are so substantial that they are extremely likely to remain even if one were able to account for the loans on a consistent basis.