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THE GRANT COMPONENTS IN OFFICIAL UNITED STATES ECONOMIC AID TO LESS-DEVELOPED COUNTRIES, 1953-1969

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I. INTRODUCTION

With the recent development of grants economics, the real transfers involved in economic aid by advanced countries to less developed ones can be assessed on a quantitative subsidy basis. The purpose of this paper is to measure and analyse the grant component in official United States economic aid to less-developed countries from 1953 to 1969. The United States is chosen, not only because of the availability of relevant statistical data, but because she merits special study as contributor of over half of net global foreign aid.

This paper is organized as follows: Section II lays out the conceptual framework for analysing the grant component in foreign aid; section III describes the official United States foreign assistance programs in conjunction with the empirical analysis; and section IV presents the summary of our findings and conclusions.
II. CONCEPTUAL FRAMEWORK

Economic Aid

Our definition of economic aid in this paper follows the O.E.C.D. (Organization for Economic Cooperation and Development). It consists of "all flows to less-developed countries and multilateral institutions provided by official agencies,"\(^2\) which meet the following tests:

(a) their prime objective is to promote economic welfare and development in less-developed countries; and

(b) their financial terms are intended to be concessional.

Grants

"Grants economics identifies the bilateral exchange versus the unilateral transfer components in the varying admixture of market and non-market economic activity."\(^3\) A grant in this context is an outright gift for which no repayment or favor is directly expected in the sense of an exchangeable quid pro quo.\(^4\) Certain portions of U.S. aid are 100 percent grant (e.g., Peace Corps expenditures, contributions to multinational organizations, surplus food donations, etc.). In addition, there are significant grant elements in development and Eximbank\(^5\) loans, due to their varying concessionary terms. A loan at (or above) the prevailing market rate of interest and without concessions in repayment terms contains zero (or negative) percent grant. As the loan terms "soften" from this point, the proportion of grant increases, approaching 100 percent (though never reaching it as long as repayment of some kind, regardless of how concessional or "soft," is due). Our task in this research is to identify
the grant components (from 0 to 100 percent) in various official U.S. foreign economic aid programs.

The Grant Component of Economic Aid

The grant (subsidy) component of an economic aid program may be measured in absolute value, called "grant equivalent," or in relative terms, called "grant ratio." The latter is the ratio of the grant equivalent to the value of the aid commitment. If the grant equivalent is equal in value to the aid commitment, the grant ratio is 1. The grant ratio therefore varies between the extremes of 0 and 1.

Since the nominal or face value of the aid commitment constitutes the base from which the grant equivalent or the grant ratio is computed, neither measure of the grant component presents a complete accounting of the net cost or sacrifice of the aid program to the donor or its total impact (positive or negative benefit) on the recipient. This is a limitation of the present state of grants economics for which much additional research is needed. On the empirical level, the effects of grants have not been successfully cast within a completely specified cost-benefit framework. Understandably, this is due in large measure to the difficulty in measuring all secondary effects or repercussions of economic aid. We shall therefore rely on the conventional "pure" measures of the grant component in economic aid, that is, on what may be called the "contract terms basis" which will become clear as we proceed.

Concessionary Factors

In attempting to measure the grant equivalent embodied in foreign economic aid loans, concessionary factors are crucial. At the outset, the contract terms of the loan to be considered are the interest
rates, years of maturity, and moratorium (grace) periods. Goran Ohlin's pioneering formula may be used to yield the familiar grant ratio. This formula calculates the discounted present value of the loan principal and interest repayments. These repayments are deducted from the face value of the loan, the difference being the grant equivalent of the loan. The grant equivalent can be considered as the value of the resources sacrificed by the donor country because of its aid loan at comparatively "soft" terms as against the return which could presumably be earned if invested for commercial profit (the opportunity cost) in developing countries.

During the grace years, only interest is repaid. Interest and principal repayments are made during the remainder of the loan period until maturity. The interest during the grace and non-grace years may differ.

Following Ohlin, the present value of the grace years interest repayments is given by:

$$P_1 = \int_{0}^{M} i_M L e^{-qt} \, dt = \frac{i_M}{q} L (1 - e^{-qM})$$  \hspace{1cm} (1)

and that of the non-grace years principal and interest payments is:

$$P_2 = \int_{M}^{T} \left[ \frac{L}{T - M} + i_T L \left( 1 - \frac{t - M}{T - M} \right) \right] e^{-qt} \, dt$$

$$= \frac{i_M}{q} L e^{-qM} + \left( 1 - \frac{i_T}{q} \right) L \frac{(e^{-qM} - e^{-qT})}{q (T - M)}$$  \hspace{1cm} (2)

where

- $L$ face value of loan
- $P$ present value
- $i_M$ interest during grace years
- $i_T$ interest during non-grace years
The grant ratio, \( g \), is given as:

\[
g = \frac{L - (P_1 + P_2)}{L} \tag{3}
\]

Inserting the \( P_1 \) and \( P_2 \) values and simplifying,

\[
g = 1 - \left[ \frac{i_M}{q} (1 - e^{-qM}) + \frac{i_T}{q} e^{-qM} + (1 - \frac{i_T}{q}) \left( e^{-qM} - e^{-qT} \right) \right] \tag{4}
\]

For a "typical" example, a loan which has a 10-year grace period at 2% interest and a total maturity of 40 years at 3% interest (the 3% interest is applied to the last 30 years of the loan), and using a comparative discount rate (\( q \)) of 10%, gives,

\[
g = 1 - \left[ \frac{.02}{.10} (1 - e^{-.10}) + \frac{.03}{.10} e^{-.10} + (1 - \frac{.03}{.10}) \left( e^{-.10} - e^{-.40} \right) \right] = 0.6816 \text{ (or } 68.16\% \text{ grant).} \tag{5}
\]

Trading Factors

Our formulation of the grant ratio in this research goes beyond that of Ohlin's to include the recent expanded considerations of Janos Horvath to which he refers as "trading factors" as distinct from concessionary factors. These trading factors include: (1) tied aid; (2) loans repayable in local (recipient country's) currency; and (3) surplus commodities.
(1) **Tied aid:** The tying of aid to purchases in the donor country tends to reduce the aid value to the recipient. This results if the prices paid for equipment or commodities in the donor country are higher than world market prices, or if such equipment is designed inappropriately for the recipient country's utilization. To the extent that the recipient country is restricted from importing from the cheapest source, the extra cost clearly reduces the grant element of the aid transfer.

The computation of the tied aid adjustment factor, designated as $g_1$, is made according to the formula:

$$g_1 = \frac{P_v - P_{U.S.}}{P_w} \times \text{percent of aid tied}$$

where

$P_w = \text{the price index on the world market}$

$P_{U.S.} = \text{the U.S. price index}$

Tied aid contains a "negative grant." It is acceptable to recipient countries because "tied aid is better than no aid." There may be cases in which the direct costs from aid tying not only reduce but even offset the concessionary benefit of the loan terms. The U.S. initiated aid tying policies in 1959 with the intention to ease balance of payment pressures. The balance of payments gain from tied aid, however, is less than the face value of the aid because, even if aid were offered untied, it is likely that at least a few commodities would be purchased in the donor country. The true gain in trade expansion is the difference between the export under the regime of tied aid and those exports attributable to an equivalent amount of untied aid. Throughout this analysis we assume that forty percent of aid amounts would be spent in the United States even without tying; this appears to be a conservative estimate because, during 1959, before aid-tying restrictions were imposed, the percentage of U.S. aid-
financed commodities purchased domestically was 47.41 percent and similar figures prevailed for earlier years.

(2) Loan repayment in local currency: In the 1950's and early 60's, local currency loans comprised the major portion of U.S. development assistance and, after 1962, were gradually converted to dollar values. Since 1967, virtually all development loans were on dollar repayment terms.16

As local currency loan arrangements prevent the conversion of the repayments to U.S. dollars (or any other currency), their monies eventually return to the recipient country. Specifically, the U.S. retains part of the proceeds for its own uses within the recipient country (e.g., for payment of embassy personnel, scholar exchange activities, etc.), and returns the remainder in the form of loans and outright grants. For this reason, the O.E.C.D. treats local currency loans as grant-like-flows which is technically inaccurate. John Pincus estimated them as 80 percent grant and 20 percent loan.17 To identify precisely the Pincus estimate, local currency loans are analyzed by the following procedure:

Initially they are submitted to the grant ratio formula described above. From the "exchange equivalent" (the grant equivalent complement), the funds designated for U.S.-use are deducted. Of the remaining exchange equivalent, the portion designated for grants is valued as 100% grant, and the loan portion is submitted to the grant ratio formula a second time. The second exchange equivalent is subject to one final manipulation to arrive at the local currency re-loan factor, designated as g2. The repayment funds are blocked except for U.S.-use in the recipient country. "The trick is to value the blocked local currency at its
true worth to the donor country by use of what is called a 'shadow' rate of exchange, as opposed to the nominal rate; in other words, the rate at which the donor would be willing to buy the blocked balances.\textsuperscript{18} The calculation of this "shadow exchange rate" index is presented in the Appendix, Table B. The index is multiplied by the percent of total aid which the blocked local currency loans represent. The product reflects the official (higher) exchange rate versus the market rate and, therefore, indicates an additional grant component. Due to occasional currency depreciation, the $g_2$ trading factor's grant ratio is raised 15.4 percent.\textsuperscript{19} The factor is raised an additional 50 percent to account for waivers on installments and interest in connection with their particular items.\textsuperscript{20}

(3) \textbf{Surplus commodities:}

For the third trading factor, Horvath\textsuperscript{21} provides a generalized formula to reduce the domestic, government supported price of surplus agricultural commodities to export market values. However, as the agricultural aid data were obtained in terms of export market values,\textsuperscript{22} the third trading factor formula needs no elaboration here.\textsuperscript{23}

\textbf{Comprehensive Grant Ratio}

From the preceding discussion, the appropriate final grant ratio formula which adjusts for the trading factors is\textsuperscript{24}

$$g' = g + (-g_1 + g_2)$$

(7)

where

- $g'$ the comprehensive grant ratio
- $g$ the conventional grant ratio (a la Ohlin)
- $g_1$ the tied aid factor
- $g_2$ the local currency factor,
III. EMPIRICAL ANALYSIS

The period chosen for this study is 1953-1969, because during the post-World War II years prior to 1953, U.S. foreign aid was directed principally toward European recovery under the Marshall Plan, and was not extended on a world-wide basis until 1953. Direct military aid is excluded from our scope of consideration. Currently, U.S. foreign aid is administered through four channels: the Agency for International Development (A.I.D.), the Peace Corps, the Export-Import Bank (Eximbank), and the Food for Peace program (P.L. 480).

Program Evolution

From 1948 to 1952, the Economic Cooperation Administration (E.C.A.) administered U.S. foreign aid. The Mutual Security Act was passed in 1951 and reported on aid transactions through 1953. The Foreign Operations Administration (F.O.A.) was the official agency from 1953 to 1955. Thence, the International Cooperation Administration (I.C.A) was organized and operated until 1961. The Development Loan Fund was established and operated concurrently from 1957 to 1961. In 1961, all predecessor agency functions were taken over by the present Agency for International Development (A.I.D.).

Public Law 480, the Agricultural Trade Development and Assistance Act, was passed in 1954, and administered surplus agricultural commodities under the Food for Freedom program. In 1966, Public Law 808 was passed, giving rise to the Food for Peace Act. (The program is still commonly referred to as P.L. 480 in spite of the legislative change.)

The Peace Corps was created in 1961.

The Export-Import Bank has existed since 1934. This institution,
to promote U.S. exports, is not financed by the Federal budget. Although Eximbank has the possibility of borrowing on favorable terms from the U.S. Treasury, its resources are obtained mainly through loan repayments.

Agency for International Development

A.I.D. administers funds under the following categories:

(a) Development Loans: Loans are offered in both dollars (donor country's currency) and local (recipient country's) currency. They are authorized on the basis of project, program, and sector loans.

(b) Supporting Assistance: This category is granted primarily to combat economic or political instability in countries engaged in major defense efforts, and in the 1950's was termed Defense Support. Approximately 10 percent of supporting assistance is termed counterpart funds.25 This portion, designated for U.S.-use in the recipient country, constitutes an exchange element and is therefore excluded as grant.

(c) Technical Cooperation (also termed Technical Assistance): This type of aid is considered 100 percent grant and consists of (i) students, trainees, experts, and volunteers sent to foreign countries, (ii) the supply of equipment for research or training, and (iii) the support of educational programs. (The Peace Corps is considered a special form of technical assistance.)

(d) Multinational Assistance: Two types of aid are covered by this category: (i) contributions to the development effort of the United Nations and its associative organizations, and (ii) capital subscriptions to multilateral financial institutions. These funds are treated as full grants.

(e) Contingency Fund: These appropriations are reserved for emer-
gency situations resulting from economic or political crises. They are treated as full grants.

(f) Administrative Expenses: These appropriations, considered as part of the cost of assistance, are treated as full grants.

Peace Corps

See (c) Technical Cooperation above.

Export-Import Bank

Eximbank is in a sense two institutions: one issues insurance and guarantees, and the other authorizes various types of loans. The former transactions are not considered foreign aid. The latter consists of (i) long term loans, (ii) commodity credits, (iii) exporter credits, (iv) special foreign trade (emergency) credits, and (v) discount credits. Within our present context, only long term loans and exporter credits are considered as foreign aid, while the others are not. The distinction is made because emergency credits are used primarily for direct military purposes (which is outside of our scope of consideration) or for stabilizing local currency crises, with the credits for the latter usually being cancelled before utilization; commodity credits, designated for the exportation of raw cotton, are exchange transactions; so are discount credits, initiated in 1966, which are made available to U.S. commercial banks at or near private interest rates against their holding of export debt obligations.

Food for Peace

In 1954, P.L. 480 consisted of three aid categories: Title I (sales for local currencies), Title II (donations for emergency relief and economic assistance), and Title III (donations to U.S. voluntary
agencies). Title IV (sales for dollars) was introduced in 1959. In 1966, the earlier programs were replaced by P.L. 808 which provided two categories: Title I (sales for dollars and local currencies) and Title II (donations). Barter is also included and consists of the exchange of agricultural commodities for (i) materials for which the U.S. is a consistent net importer, (ii) commodities required for foreign aid programs, and (iii) materials or equipment required for off-shore construction programs.

We treat sales for dollars and local currencies as foreign aid loans, and all donations as 100 percent grants. As regards barter, 25.67 percent of all P.L. 480 agreements from 1954 to mid-1969 are earmarked for U.S.-use, constituting an exchange element. Deducting this percentage, the remainder is treated as full grants. 27

Computations

In computing the grant ratios and grant equivalents, the following stipulations are made:

(a) A comparative (i.e., opportunity) rate of discount 10 percent is utilized throughout the analysis which represents the rate of return private investors expect to earn in developing countries. This rate is also used in O.E.C.D. calculations and, therefore, provides a basis for comparison. 28

(b) All data are presented on the basis of aid commitments rather than actual deliveries, for which data are often difficult to come by. Commitments, defined as firm obligations, are the best means to assess comparatively donor aid policies and are a useful indication of the direction the programs may be expected to take.

(c) Prior to 1964, due to the absence of detailed information,
yearly averages are used for the loan terms applied to the respective total loan figures.

(d) In local currency P.L. 480 sales and local currency development loans, a percentage of the exchange equivalent is designated for U.S.-use (in the recipient country) with the remainder, termed country-use funds, returned to the recipient in the form of loans and grants. The percentage designated for U.S.-use from P.L. 480 sales is applied for development loans also.\textsuperscript{29}

The results\textsuperscript{30} of our computer-programmed computations are summarized and presented in Tables 1-3.

IV. FINDINGS AND CONCLUSIONS

An Assessment of the Grant Components

Yearly U.S. aid commitments, respective grant equivalents, and grant ratios are shown in Table 1. For the period of 1953-1969 the total aid commitment is $65.9 billion, the total grant equivalent is $47.9 billion, and the corresponding weighted average grant ratio is 0.7269. Table 2 reveals the comprehensive grant ratios. The ratios have been fairly constant with the exception of the last three years considered. During the full period analyzed, the figures have varied from a high of 0.8542 in 1953 to a low of 0.4996 in 1967. The effect of \( g_1 \) (aid tying) has varied from zero in base year 1953 to -9.67\% in 1968. This trading factor's effect has been increasing, although fluctuations occurred. The effect of \( g_2 \) (soft currency loans), with minor variations, has been relatively negligible; below one-half percent on the average. The trend of the comprehensive grant ratio has shown a slow decline. This can be seen graphically in Graph 1, which also de-
picts the increasing trend of total official aid. Official aid reached an all time peak of $6.191 billion in 1967.

A glance at Graph 1 reveals that major fluctuations in the comprehensive grant ratio occurred in four periods: 1955-56, +0.0934; 1956-57, -0.1244; 1959-60, +0.0818; and 1966-67, -0.1382. In the 1955-56 period, the increase is due primarily to two factors: (a) the Food for Peace commitments (having, in general, high grant ratios), increased approximately three-fold, and (b) Eximbank funds (which have low grant ratios) decreased by roughly one-third. Eximbank fluctuations are also the prime influence in the remaining three periods. In the 1956-57 grant ratio increase, Eximbank funds increased roughly five-fold; in the 1959-60 decrease, Eximbank funds were cut by approximately one-half; and in the 1966-67 decrease, Eximbank funds were decreased by a factor of nearly two and one-half. Decreases in the comprehensive grant ratio reflect a widening gap between total official aid and the grant equivalent.

Table 3 contains grant ratios of the various types of dollar and local currency loans. The local currency loans generally have higher grant ratios than dollar loans. While the terms of repayment usually are harder in the local currency loans, the majority of their repayments are re-lent or granted back to the recipient country, raising significantly the grant ratio. Yet, in 1961-1964, the grant ratio is higher for dollar development loans than for local currency development loans. The main factor in this interesting paradox is that, in these years, U.S.-use funds constitute more than the actual exchange equivalent recovered from the local currency loans and even "borrowed" temporarily a portion of the grant equivalent, thus reducing the total grant equivalent in the original loan terms. The Table 3 also indi-
cates the decreasing trend of local currency development loans and local currency P.L. 480 sales, while P.L. 480 dollar sales are climbing.31

Furthermore, the computed grant ratios reflect the perennial overhaul of foreign aid policies.32 Development loans and surplus commodity sales were offered during the 1950's at interest rates slightly over 3%, which was reduced to 0.75% in 1961. From this extremely generous condition, interest rates slowly have grown harder until the levels of 2% during grace years and 3% during nongrace years were reached in 1969. Another feature of the reduction in concessionary terms is that from completely untied aid prior to 1959 (except for Eximbank loans), the percent of U.S. aid-financed and domestically purchased commodities reached 98.94% in 1969.

Other Conclusions

Three principal conclusions are drawn from the subject analysis.

1. While total official U.S. aid generally has increased during the 1953-1969 period, the comprehensive grant ratio has experienced a slow decreasing trend. In only three fiscal years during the period analyzed, 1967, 1968, and 1969, has the ratio dropped below 60 percent. However, a significant point is to be made here. The huge increase of Eximbank loans is the prime factor in this recent grant ratio decrease. For example, in 1965, the grant ratio is 0.792 and, in 1967, it is 0.586. The exclusion of Eximbank loans from the calculations results in grant ratios of 0.856 and 0.240, respectively, thus reversing the apparent total grant ratio decrease.

2. The effects of tied aid have been estimated to average approximately 10 to 20 percent, with individual cases as high as 49.3 percent.33
The World Export Index (see the Appendix) has shown this figure to average 10.72% from 1953 through 1969 (14.25% during the last decade). The eroding effect on the grant ratio during the period analyzed has averaged -3.69% (-4.59% during the last decade).

3. The grant ratio of local currency development loans and local currency P.L. 480 sales during 1953-1969 is 0.7611 and 0.7588, respectively. In this connection, Pincus's initial estimate of 80 percent grant and 20 percent loan is substantiated as quite accurate.
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<th>Fiscal Year</th>
<th>Total Aid Commitment (Millions of Dollars)</th>
<th>Total Grant Equivalent (Millions of Dollars)</th>
<th>Grant Ratio (g)</th>
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<td><strong>47,903.5</strong></td>
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Sources:


U.S. Department of Agriculture, P.L. 430 Congressional Sales, September, 1970;

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<th>Fiscal Year</th>
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Weighted Average: .7269, -.0369, +.0035, .6935

Source: Refer to Table 1.
## Table 3

**GRANT RATIOS OF U.S. FOREIGN AID LOAN PROGRAMS**

(Percentages and ratios)

Fiscal Year | Dollar loans |  | Local currency loans |  |
------------|--------------|---|----------------------|---|
            | Development  | Grant | PL 480 | Grant | Development | Grant | PL 480 | Grant |
1969        | 722.2        | .6831 | 411.0   | .6099 | -           | -     | 337.0   | .7709 |
1968        | 1,044.0      | .7244 | 306.0   | .6099 | -           | -     | 723.0   | .8076 |
1967        | 1,108.6      | .7234 | 178.0   | .6138 | -           | -     | 803.0   | .7839 |
1966        | 1,207.8      | .7330 | 181.0   | .6138 | 24.6        | .7927 | 866.0   | .7917 |
1965        | 1,128.0      | .7641 | 158.0   | .6138 | 34.9        | .7937 | 1,142.0 | .8517 |
1964        | 1,249.0      | .8299 | 46.0    | .6547 | 65.7        | .7991 | 1,056.0 | .8193 |
1963        | 1,159.2      | .8172 | 58.0    | .6956 | 128.8       | .7997 | 1,088.0 | .8416 |
1962        | 877.1        | .8172 | 19.0    | .7366 | 219.3       | .7998 | 1,030.0 | .8181 |
1961        | 261.8        | .8092 | -       | -     | 392.7       | .8001 | 951.0   | .7368 |
1960        | 177.1        | .5052 | -       | -     | 343.9       | .7174 | 824.0   | .6831 |
1959        | 15.6         | .5441 | -       | -     | 505.6       | .7559 | 724.0   | .4927 |
1958        | 7.6          | .5164 | -       | -     | 244.5       | .7517 | 658.0   | .6960 |
1957        | -            | -     | -       | -     | 332.7       | .7520 | 908.0   | .6960 |
1956        | 8.4          | .4904 | -       | -     | 202.4       | .7446 | 439.0   | .6877 |
1955        | -            | -     | -       | -     | 209.5       | .7913 | 73.0    | .6877 |
1954        | -            | -     | -       | -     | 100.0       | .7330 | -       | -     |
1953        | -            | -     | -       | -     | 16.4        | .7317 | -       | -     |

8,966.4     | .7601        | 1,357.0 | .6182   | 2,821.0 | .7611 | 1,622.0 | .7588 |

---

Source: Refer to Table 1.
Graph 1. U.S. Grant Equivalent and Comprehensive Grant Ratio, 1953-1969

Source: Tables 1, 2, and 3.
Appendix: INDEX COMPUTATIONS

Two indices are required in the trading factor analysis: one to measure the relationship of United States versus world market export prices and the other to reflect the difference between official versus market currency exchange rates. The former is used in the aid tying calculations to indicate the loss of exports had aid been offered on an untied basis, while the latter is utilized in shadow exchange rate calculations for local currency loans.

U.S. versus World Export Price Index

The index figures in Table A of this Appendix, which represent the value of U.S. export prices, are assumed to reflect a "basket of goods" commodity mix similar to actual aid-financed domestic commodity expenditures. The United Kingdom, France, Germany, Italy, Canada, and Japan are regarded as the countries which could effectively compete with the United States for these commodity expenditures. Thus, the U.S. export price index is compared with the average price index of the competing countries and the percent difference is shown. This derived ratio reflects the loss of exports attributable to foreign aid due to the price differential had aid been offered untied.35

Official versus Market Currency Exchange Rate Index

Due to limited availability of data, three countries, India, Pakistan, and Brazil, are used in the calculation of the shadow exchange rate index. These countries represent approximately 65% of the 1954-1969 P.L. 480 sales and approximately 47% of other local currency sales during this period. The weighting of these countries, which reflects the flow
of financial resources in both categories, are: India 65%, Pakistan 21%, and Brazil 14%. The index calculated in Table B of this Appendix is assumed to approximate the data for the remaining countries in the group. The exchange rate considered for each year is the rate as of June 30.

To calculate the index, the average local currency units per U.S. dollar from Table B are utilized in the following manner:

\[
\text{India} = \frac{5.26}{7.56} = 0.696 \text{ at } 65\% \text{ weighting} = 0.452
\]

\[
\text{Pakistan} = \frac{4.41}{8.44} = 0.523 \text{ at } 21\% \text{ weighting} = 0.110
\]

\[
\text{Brazil} = \frac{75.76}{158.73} = 0.477 \text{ at } 14\% \text{ weighting} = 0.067
\]

\[
\text{100\%} \quad 0.629
\]

Accordingly, 0.629 reflects the market value of local currency repayments, while its complement \((1 - 0.629)\), 0.371, indicates the grant proportion which is to be utilized in the shadow exchange rate calculations for trading factor \(g_2\).
### Table A. EXPORT TRADE INDEX: 1953 = 100

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\[
\left( \frac{P_{\text{world}} - P_{\text{U.S.}}}{P_{\text{world}}} \right) = \begin{array}{cccccccc}
-0.175 & -0.0309 & -0.0328 & -0.0388 & -0.0474 & -0.1010
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### Appendix: Table B

**OFFICIAL VERSUS MARKET CURRENCY EXCHANGE RATES**

(U.S. dollars per unit of foreign currency)

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Average: .1919 .1323 .2266 .1185 .0132 .0063

Average per U.S. dollar: 5.26 7.56 4.41 8.44 75.76 158.73


a Selling prices for bank transfers in the U.S. for payments abroad.

b Market prices for foreign banknotes.

c Since July 6, 1948, the official exchange rate was 5.40541 cents per cruzeiro. On February 13, 1967, new cruzeiros were issued at the ratio of 1 to 1000 old cruzeiros.

d Not available.
Thanks are due to the International Development Research Center of Indiana University for their cooperation and assistance in the production of this paper.

1. In addition to the official U.S. aid program, the private sector of the U.S. economy extends export credits and investments, accounting for approximately one-third of net global financial resource movements. As these financial flows are in the mainstream of the exchange economy, primarily motivated by profit considerations, we have not included them within the grants economy framework of this study.


4. The grants (or transfer) economy "consists of all one-way transfers of exchangeables. In an act of exchange between two parties, A and B, A gives something to B and B gives something to A. In a grant, A gives something to B and B gives nothing in the way of a clearly identifiable exchangeable to A. Exchange involves therefore bilateral or multilateral transfers whereas grants consist of unilateral transfers of exchangeables. This view of grants does not preclude the possibility that a grant from A to B may be accompanied by certain intangible transfers from B to A in the way of prestige or status, and so on, but these are not usually classified as exchangeables. The distinction between a grant and an exchange, therefore, is subject to some ambiguity but the fact that we have a fairly clear concept of an exchangeable makes the distinction workable: In an exchange of equal values, the net
worth of the parties is not changed; in a grant, however, the net worth of the grantor is always diminished and that the the grantee is increased. A grant or gift, moreover, is sometimes a sacrifice to the grantor."


5. Export-Import Bank of the United States.


7. Even primary effects often meet with problems of valuation, leading to the making of certain arbitrary assumptions. For example, an aid flow consisting of a Public Law 480 (P.L. 480) dollar sale contains the following grant element considerations:

a. The aid cost to the U.S. is valued at supported domestic prices; if it is valued at competitive world market rates, the grant ratio would be reduced. Also, the surplus goods sold were not produced for the aid program originally, but constituted a part of the U.S. exchange economy during initial economic transactions. Their cost to the government would therefore be affected. If the surplus commodities merely were being stored, giving them away to save storage costs might be economically advantageous if the prospect of domestic usage was quite dim, resulting in a grant ratio perhaps close to 0.

b. From a benefit-to-the-recipient standpoint, the surplus commodities could be valued at the recipient country's prices, thus reducing, or possibly increasing, the grant ratio. A decrease also may
occur if the recipient is not able to utilize the surplus commodities in an efficient manner. In addition, the commodities could upset the balance of the recipient economy's agricultural price structure, creating a negative "trading factor" effect (considered later).

c. Finally, computing the grant ratio with different arbitrarily chosen market rates of discount within the range of the interest rate structure in either the donor or the recipient economy would produce different magnitudes.


9. Ibid. (An assumption is made that the principal is repaid in equal installments.)


12. The U.N. Conference on Trade and Development Secretariat has estimated that the reduction in the value of a loan due to tying is at least 10-20 percent.

13. For details in calculating the indexes used in the tied aid factor, see the Appendix, Table A.


16. In some cases, the borrower can be a public agency or a private enterprise within the recipient country. The loan then may involve repayment by the non-governmental borrower to the recipient
country government in local currency. The recipient government, in turn, repays the U.S. Agency for International Development in dollars. These loans are termed "two-step loans."


19. U.S. Department of Agriculture, P.L. 480 Concessional Sales, Economic Research Service, Foreign Agricultural Economic Report No. 65, September, 1970, p. 36. From 1956 to 1969, of $5.2 billion lent, the purchasing power depreciated by $0.8 billion. The local currency development loans are assumed to be reduced by approximately the same percentage.

20. Horvath, op.cit.


23. Pincus, op.cit., p. 363, analyzed surplus agricultural commodity aid with three methods: (1) valued at U.S. prices, (2) valued at export market prices, and (3) valued at world market prices using estimates of elasticity of demand for U.S. exports.

24. For a thorough mathematical discussion of additional factors and refinements to the comprehensive grant ratio formula, see Janos Horvath and Donald P. Minassian, "A Mathematical Exposition of International
Grant... Also see: Janos Horvath and Donald P. Minassian, "Grant Erosion Due to Aid Tying," American Statistical Association 1971 Proceedings, Business and Economic Statistics Section (Washington).


26. Some conflict of definition is inevitable in this connection. For example, Mexico excludes any Eximbank transaction as foreign aid. (See I.M.D. Little and J.M. Clifford, op.cit., p. 233.)

27. P.L. 480 Concessional Sales, op.cit., p. 32.

28. Pincus, op.cit., p. 361. Pincus also used 5 and 5 3/4 percent to approximate the domestic opportunity cost and the World Bank lending rate, respectively. The change in grant elements attributable to the consideration of varying opportunity costs (above in our formula, the comparative rate of discount, q), is the subject of another ongoing research. This latter also embraces the trade-off coefficients which result from the alteration of concessionary terms within the contracts. Preliminary results are available from the senior author.

29. This procedure is followed because detailed information is published regarding the country-use of funds from P.L. 480 sales, and the bulk of countries receiving surplus commodities also receive development loans repayable in local currency.

30. Year-by-year and country-by-country computations for 1964-1969 have also been made, and the results may be obtained from the authors upon request.

31. By 1971, all P.L. 480 sales will be on a dollar basis.

32. For an assessment of policy considerations, see: Lester B. Pearson (ed.), Partners in Development (New York: Praeger, 1969); Robert E. Asher, Foreign Aid: The Postwar Record and Targets for the

