Examining the Marshall Plan Analogy

"What the President has requested is a $20 billion investment in the future of Iraq. To put that in context, the Marshall plan after World War II cost roughly $90 billion in today's dollars"

Donald Rumsfeld, Secretary of Defense, 9/30/03

Baghdad 2003

Berlin 1945

A Report by the Minority Staff of
The House Appropriations Committee

Iraq Aid Package has No Precedent in the Marshall Plan

On September 15, 2003, the Bush Administration asked the Congress to appropriate $20.3 billion for the "reconstruction" of Iraq. In arguing that Congress should approve these funds the President, the Administrator of the Iraq Coalition Provisional Authority (Ambassador Bremer) and the Secretary of Defense have all argued that this is a relatively small investment compared to the effort that the United States made in launching the Marshall Plan in 1948.

On September 30th, Secretary of Defense Donald Rumsfeld testified before the House Appropriations Committee "What the President has requested is a $20 billion investment in the future of Iraq. To put that in context, the Marshall plan after World War II cost roughly $90 billion in to today's dollars."

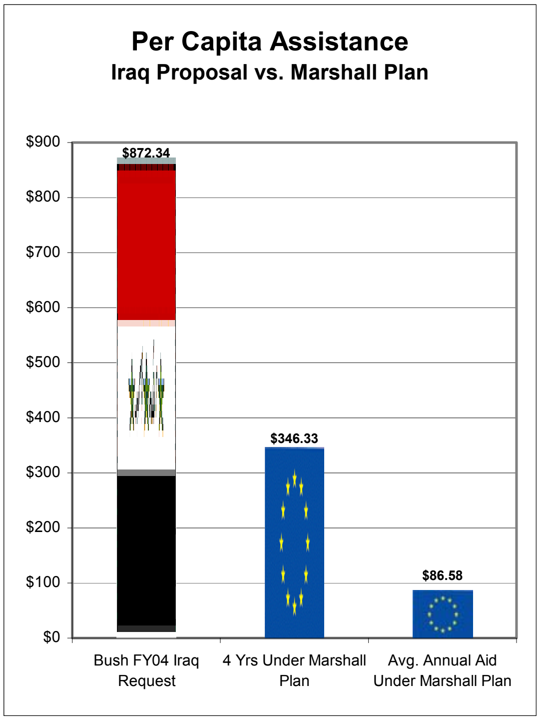
The Marshall Plan was first enunciated by Secretary of State George Marshall at Harvard in June of 1947. The Economic Cooperation Act of 1948 cleared the Congress on April 2nd of 1948 and was signed into law by President Truman on the following day. It authorized $5.3 billion in first year funding (equal to about $40 billion in inflation adjusted dollars) and required the money to be disbursed by an "autonomous independent organization" known as the Economic Cooperation Administration to insure that funds were not dispensed based on cronyism within the Truman Administration. The plan has traditionally been viewed as one of the most generous acts of international assistance in World history.

Parallels between the Administration's current proposal for $20.3 billion in reconstruction assistance to Iraq and the Marshall Plan are troubling in a number of respects.

Iraq Aid Far More Generous Than Aid Under Marshall Plan

Under the four years of the Marshall Plan (1948 through 1952) a total of $11.8 billion in grants were dispersed. In 2003 dollars to would be worth approximately $89.2 billion. Those funds, however, were directed at a total of 16 nations with a combined population of 257 million people compared to Iraq's population of 23.5 million. Four of the 16 nations receiving Marshall Fund assistance had populations approximately twice the size of Iraq's current population.

The average per capita assistance level over the four years of the plan was about $46 and the average assistance level per year was about $11. Even after adjusting for inflation the levels of assistance were a fraction of the levels that President Bush has requested for Iraq. Under the four years of the plan



assistance levels were $346 per capita and annual assistance levels were about $86.

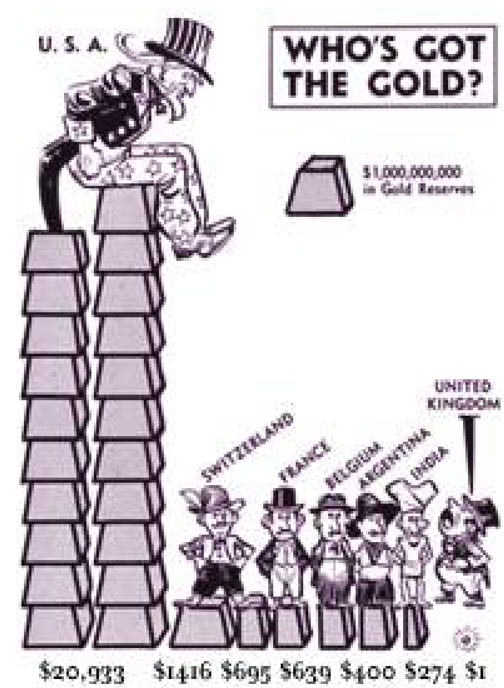
Iraq with an estimated population of 23.5 million will receive $20.3 billion in fiscal 2004 or a one-year assistance level of $872 or more than ten times the average annual per capita level of assistance under the Marshall Plan.

Marshall Plan Addressed Imbalances That Threatened Growth of Global Trade—Iraq Plan Exacerbates Imbalances

While the Marshall Plan is often viewed as simply another assistance program conducted on a grander scale, it was actually directed at resolving critical imbalances that would have prevented restoration of U.S. global markets. Because economic conditions have reversed over the last 55 years, the Iraq assistance program will actually exacerbate current imbalances in the global trading system.

The world economy faced an extraordinary set of conditions at the time of the Marshall Plan. The U.S. economy had experienced rapid expansion during the war while the other major economies had been largely devastated. Nearly all of Europe, Russia, China and Japan had borrowed heavily to finance the cost of war and subsequently seen much or all of their industrial capacity obliterated by the War.

In 1947, the United States with less than a tenth of the world's population had a majority of the world's industrial capacity and an even larger share of its assets. During the late 1940s Seventy percent of the world's gold reserves were held in U.S. banks and the United



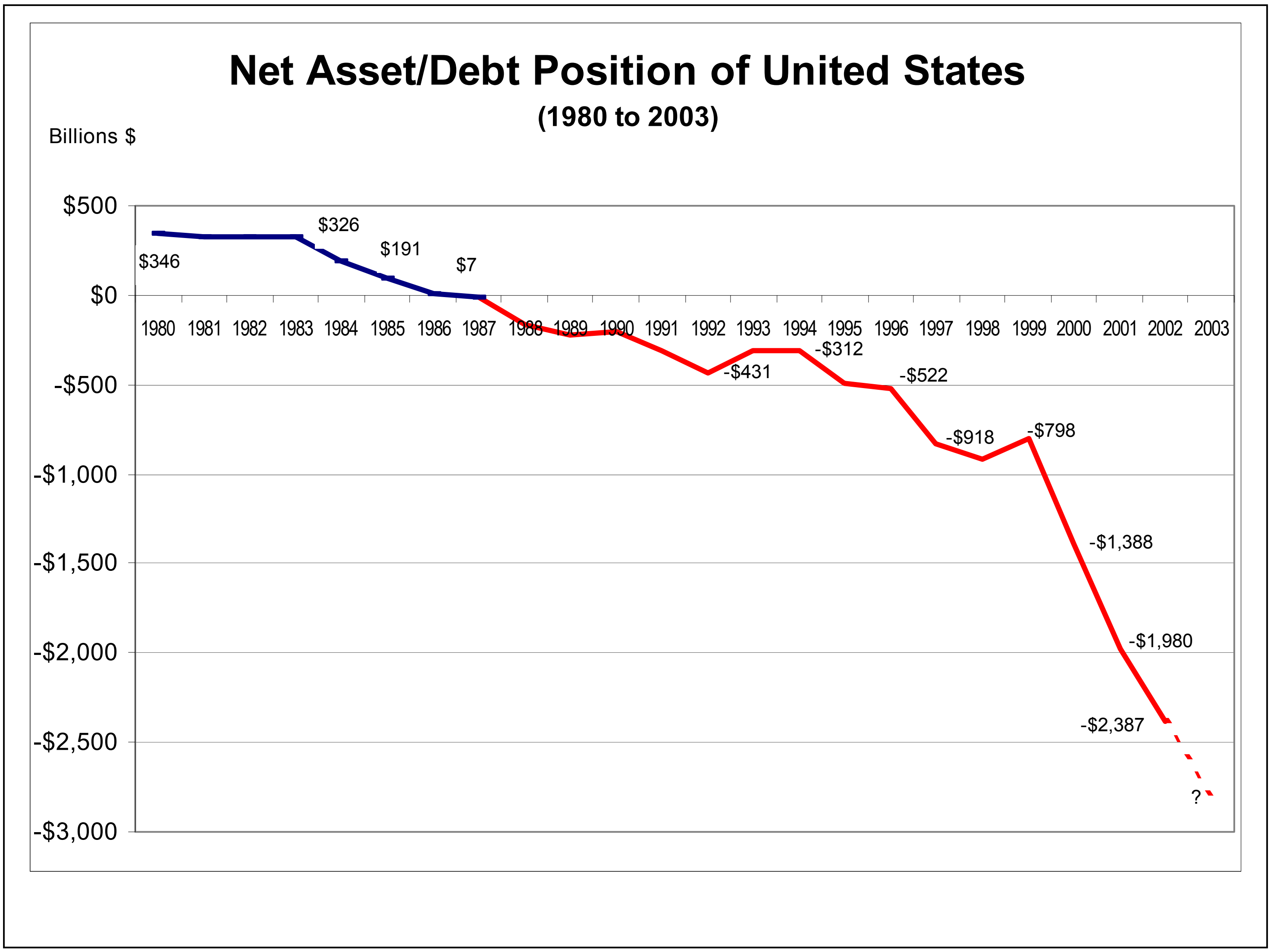
1947 Cartoon Illustration of U.S. Dominance of World Gold Reserves, *Corbis/United Press International*

States ran enormous and persistent trade surpluses with virtually all of its trading partners.

The world economy during that period was similar to a Monopoly game in which one player has won nearly all of the cash, properties, hotels and "*get out of jail free*" cards. But unlike the Monopoly players, who can quit their board game and go to dinner, players in the world economy are part of a game that must never stop or there will be no dinner. The U.S. had to redistribute a share of its capital in order to let the *"game"* go forward and protect its own prospects for future economic growth.

Today the United States remains the largest and most powerful economy in the world but it is only one of many strong and prosperous economies. Some of America's former benefactors now enjoy per capita income levels higher than those in the United States.

But the most dramatic change has occurred in the area of international finance. In the years during and immediately following the Marshall Plan, the United States continued to enjoy large trade surpluses. The accumulated savings from those overseas sales meant that foreigners owed Americans far more than we collectively owed individuals, businesses



or governments overseas. Through the 1950s, 1960s and 1970s the United States remained the largest creditor nation in the world although the concentration of world capital in the U.S. declined as the economies of other nations expanded.

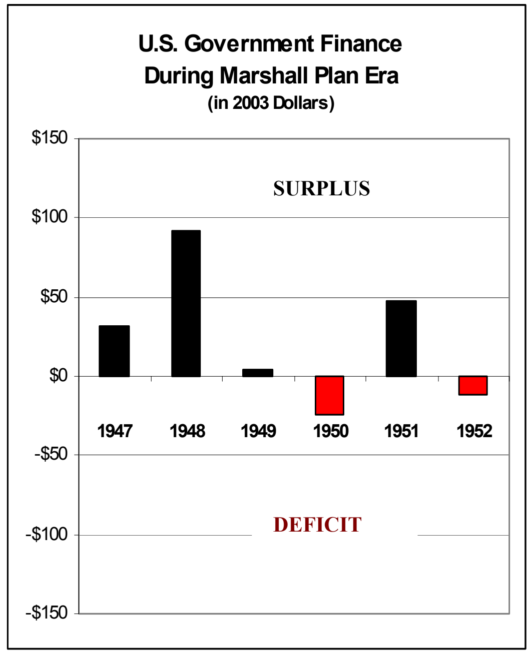
During the 1980s, however, a combination of factors caused the United States to move rapidly from being the world's largest creditor nation to being the world's largest debtor.

The chronic trade deficits of the 1980s continued into the 1990s as American businesses increasingly sought opportunities to move manufacturing operations to Asia and Latin America in order to benefit from lower wage costs.

The Commerce Department's Bureau of Economic Affairs reported in June that the nation's net debtor position had deteriorated further in 2002 and that we owed foreigners $2.4 trillion dollars more than they owed us by the end of the year. The massive trade deficits we experienced so far in 2003 indicate that our debt position is likely to push closer to $3.0 trillion by the end of 2003.

U.S. Treasury issues represent a large portion of the American debt held by foreigners. The Treasury Department estimates that $1.3 trillion or about 46% of our total federal debt *(debt held by public)* is owned by individuals and institutions outside the United States. The Japanese alone own $444 billion in U.S. Treasury Bonds.

Sudden large budget deficits have forced increased reliance on foreign borrowers since projected deficits exceeding $500 billion cannot be financed with domestic

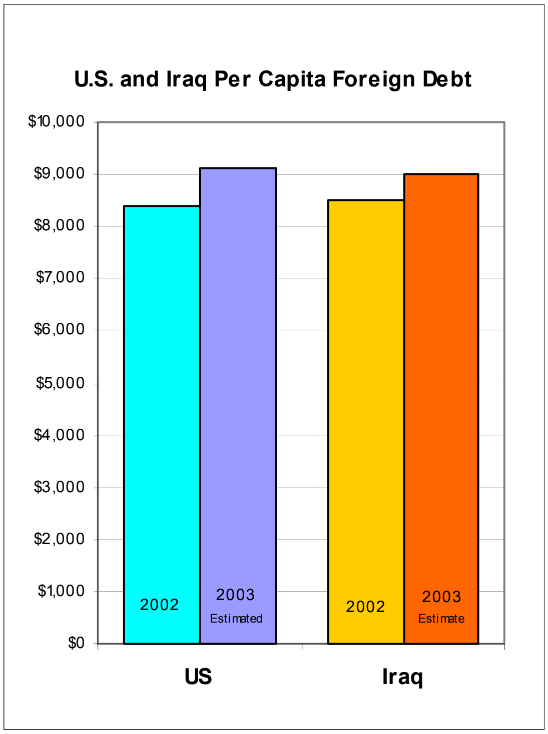


private savings, which is expected to remain in the neighborhood of about $300 billion in the coming year.

So unlike the Truman era in which the Marshall Plan was launched, the world is not suffering from an excessive concentration of global capital in the United States. Nearly eighty percent of global economic activity occurs outside the United States and there is a far broader base of wealth and income available to shoulder global and regional problems created by wars, political upheavals and natural disasters.

Furthermore, unlike the Truman era in which federal government spending was relatively in line with revenues, the huge deficits which now face the federal government mean that any effort to assist a particular foreign nation must in effect be borrowed from other foreign nations.

Recent reports indicate a growing uneasiness among foreign holders of



U.S. Treasuries over the size and rapid increase in the rate of U.S. government borrowing. Already the spread between the yield on U.S. Treasuries and corporate bond issues has declined from about 1.3% (or 130 basis points) last spring to only about .3% (30 basis points) today. That is in effect a downgrading of U.S. debt and the credit worthiness of the federal government.

IRAQ'S FOREIGN DEBT

Arguments over whether U.S. assistance to Iraq should be made in the form of grants or loans has evolved around the issue of Iraq foreign debt. Iraq as a nation has traditionally been free of foreign debt. In 1980 its foreign reserves exceeded $35 billion. But during the 1980s Saddam Hussein borrowed heavily (most from other Arab nations in the Persian Gulf to finance his war against Iran).

Figures vary widely as to both the extent and composition of Iraq's debt. At the end of the first Gulf War, Iraq told the United Nations that its foreign debt equaled $42 billion. The Organization for Economic Cooperation and Development estimated that the bilateral debt to OECD nations in 2001 was no more than $18.4 billion. The Economist Intelligence Unit estimates Iraq's total debt in 2002 to be $64.3 billion. The Center for Strategic and International Studies has produced an estimate of Iraqi debt that totals $108.1 billion.

In addition to this debt there are also reparation claims. Some of these claims appear to be enforceable under international law and some appear to be highly inflated and poorly founded. In total the reparation claims exceed several hundred billion dollars. Official estimates of Iraq's total external liabilities have therefore been very roughly estimated at $200 billion.

While there is no question that Saddam's irresponsible borrowing presents a problem for efforts to speed Iraq's economic recovery it should also be noted that on a per capita basis Iraq's external debt is similar to and by next year may actually be somewhat smaller than the per capita foreign debt of the United States.

While Iraq's economy is much smaller than that of the United States**, foreign debts cannot be paid with domestic production but must instead be paid through export earnings**. No matter how large a nation's domestic economy is it can only reduce its foreign debts by running trade surpluses. The United States suffers from persistent trade deficits that show no signs of reversing themselves in the foreseeable future and it's huge foreign debt will continue to increase as long as it continues to run those surpluses. Iraq on the other hand has the capacity to generate significant trade surpluses through oil sales. **Iraq, therefore is in a much stronger position than the U.S. to eventually repay its foreign debts.**

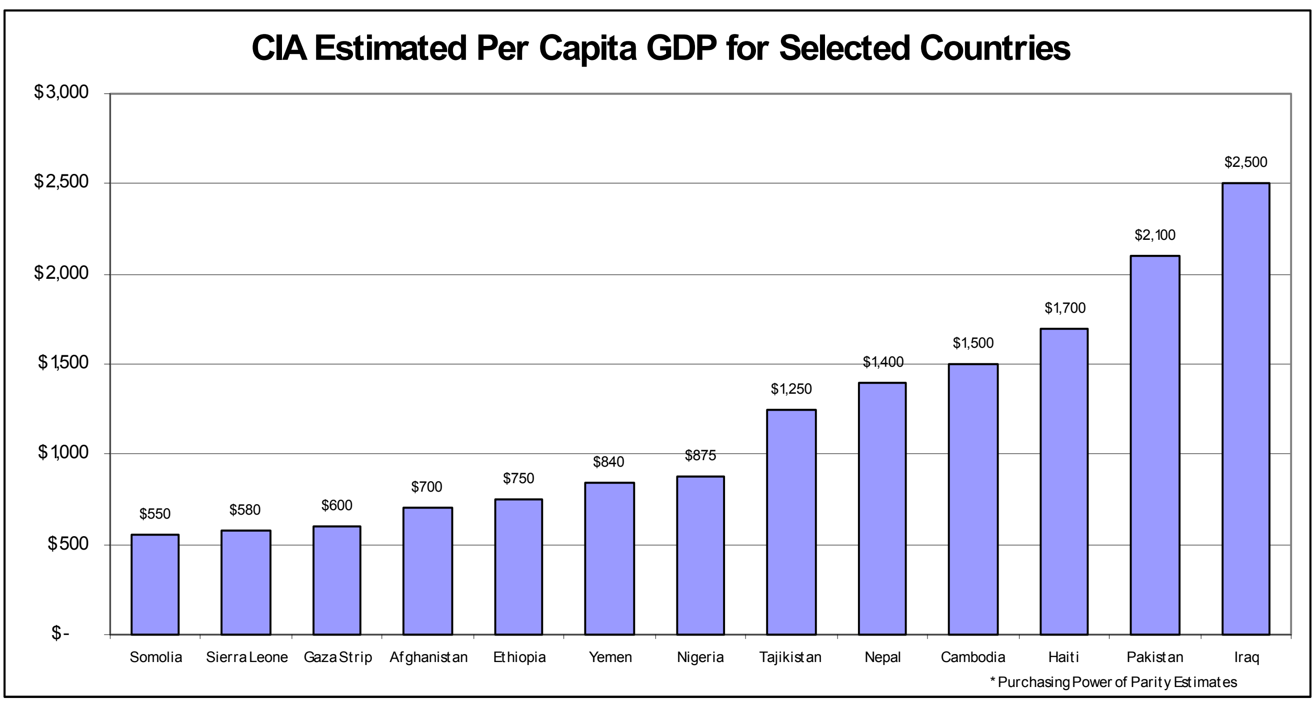
Iraq has 112 billion barrels of proven oil reserves and in addition probable and possible reserves that may amount to another 220 billion barrels. At current world prices the value of proven reserves would be in the range of $2.8 trillion and the value of the probable and possible reserves would be an additional $5.5 trillion.

Clearly, the political problems created by the lack of international support for the coalition invasion and occupation of Iraq make the use of loans reconstruction awkward. While the continuing international discord over Iraq's reconstruction may make grants an easier option than loans they are not easily justified on economic grounds.

IRAQ PROPOSAL IS ALSO DIFFICULT TO JUSTIFY ON PURELY HUMANITARIAN GROUNDS

While the Administration's Iraqi assistance plan fails to serve the kind of global macro economic objectives addressed by the Marshall Plan it is also difficult to justify simply on the grounds of traditional humanitarian assistance. To argue for this massive aid package on humanitarian grounds necessarily raises the question of how do the humanitarian problems in Iraq compare to those elsewhere in the world?

Because of the repressive nature of Saddam's regime and the chaos that persists in the aftermath of the coalition



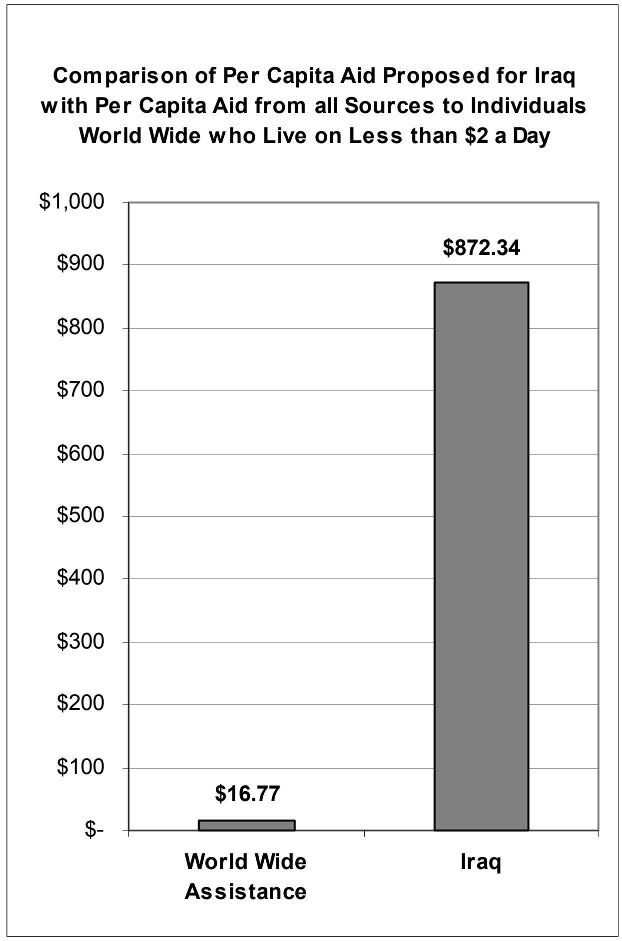
CIA Estimated Per Capita GDP for Selected Countries invasion, it is difficult to get accurate data or even a reasonable approximation of humanitarian conditions on a nationwide basis.

The World Factbook for 2002 published by the CIA, estimates Iraq's purchasing power per capita GDP to be a $2500. That is about four times the estimate for the Gaza Strip, Sierra Leone, or Somalia; about three times the estimate for Afghanistan Ethiopia, Yemen, Madagascar, Nigeria and Mozambique; about twice the estimate for Angola, Nepal, Rwanda and Tajikistan and about 50% greater than the estimate for Haiti, Cambodia, Bangladesh and Senegal and somewhat larger or about the same size as the estimate for Pakistan, India, Nicaragua, Bolivia and Viet Nam.

Iraq is also reported to have significantly higher life expectancy rates than many countries in the world. The CIA estimates life expectancy at birth in Iraq to be 67.4 years compared with 44 years in Ethiopia, 47 years in Afghanistan, 50 years in Haiti, 54 years in El Salvador, 58 years in Nepal, 63 years in India and 64 years in Bolivia. Worldwide, life expectancy at birth is 64 years.

But what is most striking about the administration's proposed assistance package to Iraq is the proportionality of the assistance relative to aid provided to people in other troubled portions of the globe.

The Development Assistance Committee of the Organization of Economically Developed Countries monitors international assistance provided to all nations for developmental purposes. In 2001 such assistance totaled $52.3 billion, a slight decline from the previous year. The $20.3 billion which the administration is proposing for Iraq would represent a 40% increase in world wide assistance and nearly 200% increase in the level of U.S. assistance.



If one ignores other assistance activities in Iraq and assumes for a moment that the only assistance that Iraq would receive would be that provided by the Bush Administration's $20.3 billion package, the concentration of world developmental resources on that nation would still be staggering.

The World Summit on Sustainable Development which met in Johannesburg, South Africa in 2002 estimated the number of people in the world living on less than a dollar a day at 1.2 billion. The number living on less than $2 a day was estimated at half the world population or 3.1 billion people. The $2 dollar a day living standard ($730 a year) would be a little less than one third of the CIA's $2,500 estimate of per capita purchasing power GDP in Iraq.

If we were to assume, however, that all Iraqis fell in the category of people in the world living on less than $2 a day we would have a situation in which less than one percent of the world's desperately poor people are receiving more than 28% of the worlds total assistance funds. Iraqi poor, assuming all Iraqis are poor will be getting assistance at a level of $870 per capita while the other poor people in the world will be getting less than $17.

CONCLUSIONS

While the Administration has attempted to compare the $20.3 billion it has requested for Iraq with the Marshall Plan, it is dramatically different in a number of respects. First **it provides about ten times the annual per capita level of assistance provided under the Marshall Plan** even after adjusting Marshall Plan aid levels for inflation.

Secondly, **it does not correct global financial imbalances**, which was a principal objective of the Marshall Plan. In fact, it exacerbates both the serious current account and budget deficits which the United States is now experiencing.

Lastly, the Iraq proposal is also difficult to defend from the perspective of humanitarian assistance because **Iraqis will be receiving more than 50 times the assistance levels directed toward the rest of the underdeveloped world** despite evidence that Iraqis are less poor than the vast majority of people who will be receiving far lower levels of assistance.