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(Foreign Affairs: Twenty-Two Nation Summit, 10/21/1981-10/23/1981 Cancun, Mexico)
Case File Number(s): 044849 (1 of 4)
Box: 16

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FO006-02

MEMORANDUM

5913

NATIONAL SECURITY COUNCIL

WS

ACTION

October 7, 1981

OBE per Carlson 11/13/81

MEMORANDUM FOR RICHARD V. ALLEN

FROM: NORMAN A. BAILEY

SUBJECT: Cancun Summit

Richard Darman has requested NSC Staff comments on Roger Porter's memo on the Cancun Summit (Tab A) by 3:00 p.m. today.

Attached at Tab I is a memorandum from you to Darman indicating that the NSC Staff has no comment on the paper except to recommend that a follow-up working group be established after Cancun to examine carefully all tax alternatives.

Henry Nau concurs. Roger Fontaine has no comment.

RECOMMENDATION

That you sign the memorandum to Darman at Tab I.

Approve ________ Disapprove ________

Attachments

Tab I Memo to Darman
Tab A Porter Memo to Darman

NSC #8105913

MEMORANDUM 5913

THE WHITE HOUSE

WASHINGTON

MEMORANDUM FOR DICK DARMAN

FROM: DICK ALLEN

SUBJECT: Cancun Summit

The NSC Staff has no comment on the attached paper (Tab A) except that we recommend that a follow-up working group be established after Cancun to examine carefully all tax alternatives.

Attachment

Tab A Porter Memo of October 3 to Deaver

5913

Document No. ____________

WHITE HOUSE STAFFING MEMORANDUM

DATE: 10/6/81 ACTION/CONCURRENCE/COMMENT DUE BY: 10/7/81 3:00pm

SUBJECT: CANCUN SUMMIT

	ACTION	FYI		ACTION	FYI
VICE PRESIDENT	☐	☐	HARPER	☐	☐
MEESE	☐	☐	JAMES	☐	☐
BAKER	☐	☐	MURPHY	☐	☐
DEAVER	☐	☐	NOFZIGER	☐	☐
STOCKMAN	☐	☐	WILLIAMSON	☐	☐
ALLEN	☑	☐	WEIDENBAUM	☑	☐
ANDERSON	☑	☐	HICKEY	☐	☐
BRADY/SPEAKES	☐	☐	MC COY	☐	☐
CANZERI	☐	☐	CEQ	☐	☐
DOLE	☐	☐	OSTP	☐	☐
FIELDING	☐	☐	USTP	☐	☐
FRIEDERSDORF	☑	☐	ROGERS	☐	☐
FULLER *(For Cabinet)*	☐	☐	____________	☐	☐
GARRICK	☐	☐	____________	☐	☐
GERGEN	☑	☐	____________	☐	☐

Remarks:

You will recall that we discussed these briefly on Monday -- and agreed to be prepared to present these to the President for decision by Wednesday. Could you please provide comments by 3:00 p.m. Wednesday.

Thank you.

Richard G. Darman
Assistant to the President
and
Deputy to the Chief of Staff
(x-2702)

THE WHITE HOUSE

WASHINGTON

October 3, 1981

MEMORANDUM FOR MICHAEL K. DEAVER

FROM: ROGER B. PORTER RBP

SUBJECT: Cancun Summit

At its Thursday, October 1 meeting, the Cabinet Council on Economic Affairs reviewed, as requested, a series of possible initiatives for the Cancun Summit. The central strategic issue facing the President as he prepares for Cancun is the position he should take on the calls for Global Negotiations. While the Cabinet Council's review did not directly address what approach we should take to Global Negotiations, our review of possible initiatives should prove helpful in developing the next steps in preparing for Cancun.

Our review concentrated on what basic approach the U.S. should pursue in its relations with developing countries and on what policies were most likely to produce lasting mutual benefits for both developed and developing nations. We considered a number of ideas and proposals, some more promising than others.

General Conclusions

In our discussion of possible proposals or initiatives, we reached several general conclusions:

1. The U.S. should identify with the developing countries' aspirations for greater economic growth and prosperity and show sympathy for their needs and problems.

2. We need to articulate better the U.S. record in aiding developing countries.

3. The most important step that both developed and developing nations can take is to put their domestic economic houses in order. International cooperation and economic growth depend on sound domestic policies.

4. Recommending a long list of specific initiatives or substantive proposals is unlikely to "win the hearts" of the developing nations at Cancun.

5. We should emphasize that we have a development strategy that can bring practical benefits to both the developed and developing world — one that we have found can succeed.

6. The institutional framework for what is needed is already in place but improvements can be made. We are prepared to join with others in making those improvements.

7. Our development strategy rests not on a single program or establishing a single forum. Rather it rests on an integrated approach that emphasizes trade, investment, and foreign assistance.

8. Neither government to government assistance nor massive income transfers from the developed to the developing world will bring sustained economic growth and prosperity. Lasting progress will occur only as the developing nations increase their capacity to produce goods and services and as there are markets for their products.

9. Thus, a successful development strategy must rest on an integrated approach that helps build productive capacity (through investment and technical assistance) and expand markets (through reducing barriers to trade).

Investment

The Cabinet Council examined three principal avenues for improving the investment climate in less developed countries thereby increasing the flow of private capital.

1. Multilateral Investment Insurance Arrangements.

A major constraint to the flow of direct investment to the LDC's is investors' perceptions of high political risk. Political risk insurance currently available from public and private sources is insufficient to support adequate flows of investment to the developing world, especially for high-risk, high-cost energy and minerals exploration projects.

A multilateral insurance arrangement, such as an International Investment Insurance Agency (IIIA), within the framework of the World Bank or its affiliate, the International Finance Corporation (IFC), could substantially reduce a major disincentive to investment in LDC's. Tying such an insurance arrangement to the World Bank could significantly increase its effectiveness since the potential loss of World Bank funding should prove a powerful deterrent to expropriation.

Several details such as dispute settlement and arbitration mechanisms, financial obligations, and control mechanisms (weighted versus non-weighted voting rights) require further development.

2. Expanding Cofinancing Programs.

Multilateral development institutions can play an important role as catalysts in generating greater private investment in LDC's through cofinancing programs with commercial banks. Such programs are relatively modest now. (In the past two years, private lenders have participated with the World Bank in some 40 projects committing a total of about $3.5 billion.) The U.S. can actively support increasing substantially the level of private cofinancing activities of the World Bank and the IFC.

3. Incentives under Bilateral Tax Agreements for Investment in Developing Countries.

Under current arrangements, when foreign governments in developing countries reduce or "spare" taxes for investors through tax holiday incentive laws, these have little effect on U.S. investors who simply end up replacing the foreign taxes they are spared with additional U.S. taxes because they receive a U.S. foreign tax credit only for taxes actually paid abroad.

One alternative examined by the Cabinet Council was allowing a U.S. foreign tax credit to U.S. investors not only for taxes actually paid to the developing country but also for taxes which would have been paid but which were "spared" under the tax holidary incentive law.

Other alternatives considered included extending a 10 percent investment tax credit to investments in developing countries, and allowing tax sparing credits only if the developing country reduced by treaty its statutory withholding tax on dividends, interest, and royalties paid to U.S. investors.

The Cabinet Council felt it was premature to endorse any of these specific tax proposals for several reasons. The current budget situation makes any near-term revenue losses extremely unattractive. Moreover, congressional agreement to support such tax changes is uncertain. There is widespread agreement that the President should not propose specific tax treaty changes on which he could not deliver. Rather, the Council felt that we could express a willingness to discuss new arrangements without supporting any specific changes in advance.

Foreign Assistance

A second major element of our development approach is foreign assistance programs. The underlying theme behind the Council's consideration of our economic assistance strategy is the need to build productive capacity in developing countries. Increased technical assistance in its many forms, including greater involvement by the U.S. private sector in technical assistance programs, is needed. "If you give a man a fish you feed him for a day; if you teach a man to fish you feed him for a lifetime."

The Council's review of this area produced agreement on the need to:

- Encourage sound LDC policies that promote development and that strengthen the private sector emphasizing the important role of market forces, especially in pricing policies. Governmental controls on agricultural and energy prices in many developing countries constrain development in those sectors;

- Continue to support existing multilateral institutions and to honor our commitments to them;

- Refocus our bilateral aid on programs which:

  a. provide technical assistance and

  b. concentrate on training;

  (Most U.S. bilateral assistance focuses on agriculture and energy.)

- Place increased emphasis in agricultural programs on expanding food production, primarily through small farms and raising incomes by strengthening productive enterprises;

- Place increased emphasis in energy programs on technical assistance for energy assessment and training, reforestation, and research and development where our aid complements the private sector.

Trade

Developing nations must not only increase their capacity to produce goods and services by sound domestic economic policies, greater foreign investment, and expanded technical assistance and training; they also must have adequate markets for their products.

Five measures illustrate the absolute and comparative U.S. contribution to providing markets for LDC exports.

1. The U.S. absorbs approximately one-half of all the manufactured goods that the LDCs export to the industrialized countries.

2. In 1980, 51 percent of U.S. imports from developing countries entered duty free. Our average tariff on all dutiable imports was 5.5 percent.

3. The U.S. maintains very few quantitative restrictions and U.S. customs procedures are highly transparent and predictable.

4. Our Generalized System of Preferences (GSP) program is the most open and responsive of all the donors' programs. GSP duty-free imports have increased threefold since 1976 and are expected to reach $9 billion in 1981.

5. In the past two years alone, the non-OPEC LDCs earned more from exports to the U.S. ($114.5 billion) than the entire Third World has received from the World Bank in 36 years.

Among the developed nations, the U.S. has a superior record with respect to lowering both quantitative and qualitative trade barriers to LDC products.

Building on this record, the U.S. can challenge other developed nations to join in strengthening the GATT in ways that encourage the further adoption of market-oriented, outward-looking policies by developed and developing countries.

Specific potential initiatives include:

- o Support the extention of the Generalized System of Preferences, in some form, beyond its scheduled termination in 1985.

- o Seek at a 1982 GATT Ministerial a reduction in the barriers against LDC goods and services.

- o Press for strong discipline on safeguard actions to reduce arbitrary, secretive, inter-industry trade restraints.

cc: Donald T. Regan
Edwin Meese III
James A. Baker III
Richard G. Darman
Craig L. Fuller
Martin C. Anderson
Richard V. Allen

MULTILATERAL INVESTMENT INSURANCE ARRANGEMENTS

Overview:

A major constraint to the flow of direct investment to the LDC's is investor perception of higher political risk in these countries. Political risk insurance currently available from public and private sources is insufficient to support adequate flows of investment to the developing world, especially for high-risk, high-cost energy and minerals exploration projects. A multilateral insurance arrangement drawing together the resources of developed and perhaps developing countries could provide a mechanism to help meet these needs.

Pros:

-- Risk on major projects could be spread so that high value projects could be covered more easily.

-- Capital-exporting countries could act mutilaterally in cases of expropriation, raising the inherent cost of hostile action against the property of citizens of any one state.

Cons :

-- LDCs have been reluctant to support past multilateral insurance proposals, which could reduce their leverage in dealing with developed countries or limit their control over foreign enterprise. Some leaders of the G-77 opposed arbitration obligations or other limits to national sovereignty.

-- Western European countries were uninterested in past schemes as well, preferring to exert greater control through national programs which can be tailored more closely to the pursuit of their own domestic objectives. (Europeans also tend to view such programs as benefiting us more than them, especially in Latin America, where the bulk of foreign investors are U.S.)

-- Previous plans were dropped when participants were unable to agree on: dispute settlement and arbitration mechanisms; financial obligation (including at least a token contribution from the LDCs); control mechanisms (weighted versus non-weighted voting rights). Any new program would also have to deal with these issues.

Most Forthcoming Alternative: A multilateral insurance arrangement within the framework of the World Bank or International Finance Corporation (IFC).

World Bank President William Clausen has already privately expressed his interest in launching a multilateral insurance program within the World Bank. However, strong U.S. support would be needed to begin such a program. We would prefer an insurance mechanism established through the IFC, similar to the International Investment Insurance Agency (IIIA) advanced on a number of occasions by the U.S. between 1961 and 1972. (The IIIA would have been a new international agency which insured private developmental investment in member LDCs against specific political risks and reinsured investment insurance contracts made under domestic programs such as OPIC.)

Pros:

-- Would create a large insurer capable of providing low-cost insurance against political risk and loan guarantees for major investments.

-- IIIA would be fiscally sound and credible to investors.

-- The framework for consultation is already in place, and general principles have been set out in the IFC Charter.

-- It would be a multilateral program with a link to the IFC, which should deter expropriation.

-- The program could possibly be put in place without additional funding. The IFC already has a guarantee program; changes in reserve ratio requirements could permit the IFC to leverage existing funds to support many more projects through insurance rather than direct loans.

Cons:

-- The IFC's Charter does not specifically allow or prohibit it to issue insurance. A Charter amendment would be needed to permit the IFC to issue insurance on reasonable terms.

-- The LDCs will have the same objections they had to previous IIIA proposals. The prospects for a successful negotiation are thus not good.

-- LDCs oppose the involvement of a major multilateral lending agency. They fear that a World Bank-linked mechanism would have additional leverage, since the Bank must look at a country's expropriation record before approving new loans.

-- We would have limitd control over the design of an IFC proposal.

-- A sound facility would require reserves, funded in all probability by paid-in capital. The USG might have problems if we had to seek an appropriation.

Moderately Forthcoming Option: A U.S.-led, developed country multilateral initiative.

The U.S. could propose a multilateral insurance program within an existing developed country mechanism such as the Direct Assistance Committee of the OECD, similar to the International Investment Reinsurance Agency (IIRA), a plan raised in the Investment Insurance Committee of the Berne Union in the mid-70's. The group would provide reinsurance on political risk coverage; risk would be shared among countries in proportion to their contribution to the insurance pool.

Pros:

-- LDC approval is not needed to implement the program.

-- Greater national control is retained over insurance issued.

Cons:

-- Such a mechanism would probably not draw in non-Western (e.g., OPEC) participants.

-- Previously, Western Europeans have been unenthusiastic.

Least Forthcoming Alternative: Greater U.S. public-private sector insurance cooperation.

The Overseas Private Investment Corporation (OPIC) could work more closely with private sector insurance companies on a project-by-project or regional basis. Private insurers are increasingly interested in entering the political risk field, and could benefit from OPIC experience and cooperation.

Pros:

-- The program would be easy to implement, and would in fact only expand current OPIC efforts.

-- This program would re-emphasize our commitment to the private sector, and help interested private sector insurers to expand their activities in the political risk field.

Cons:

-- There would be little expansion of coverage available. Private sector firms could not be expected to accept too large a portion of the total risk.

-- There would be only limited psychological impact from announcing such a program.

-- Limitations which keep OPIC from insuring projects (e.g., country exposure limits, employment-impact, Calvo clause) would

Incentives under Bilateral Tax Agreements for Investment in Developing Countries

U.S. tax treaties with developing countries can include investment incentives. Such benefits should be provided only by treaty because: (1) the incentive can be targeted to particular countries where it is likely to be most effective and where it conforms to overall U.S. foreign policy objectives; (2) it can be targeted to certain industries which are important to the development of the partner; (3) the U.S. would be able to receive reciprocal consessions, particularly exchange of information; and (4) the greater incentive thereby created for developing countries to enter into treaties with the U.S. would further enhance the ability of these countries to attract U.S. investment.

Last Forthcoming Alternative: Tax Sparing Credits Only for Reduction under the Treaty in Treaty Partner Taxes

If the treaty partner reduces by treaty its statutory withholding tax on dividends, interest and royalties paid to U.S. investors, the U.S. would allow a foreign tax credit for the full statutory tax.

Pro:

- It will benefit U.S. investors and encourage investment.
- Developing countries would probably agree to greater treaty reductions in their statutory withholding rates.
- Because it is more limited than full tax sparing, it would probably engender less opposition.

Con:

- It would violate the policy of not giving U.S. treaty benefits to U.S. citizens and residents.
- It will encourage repatriation.
- The impact will be uneven, depending on the partner's level of statutory withholding rates.
- It will provide windfall benefits to those who would have receive the income in any event.
- The Senate would be likely to object.

Moderately Forthcoming Alternative: Investment Tax Credit

A 10 percent investment tax credit would be extended to investment (and reinvestment) in developing countries.

Pro:

-- Most developing countries would consider this a satisfactory alternative to tax sparing.

-- It would afford an immediate benefit to U.S. investors, whether or not the venture proved profitable.

-- It would be a move toward capital export neutrality.

-- It would not encourage repatriation and, if structured to cover reinvestment, would encourage retention.

-- It would permit a broadening of the U.S. treaty network with developing countries.

-- The U.S. would retain control over the incentive.

Con:

-- It would violate the purpose of the domestic credit -- to encourage investment in the United States.

-- It would give U.S. treaty benefits to U.S. persons.

-- It would be uneven in impact, giving greater benefit to capital intensive investments, which are, typically, not those most needed by developing countries.

-- It has previously been rejected by the Senate.

Most Forthcoming Alternative: Tax Sparing Credits for Developing Country Tax Holidays

A U.S. foreign tax credit would be granted to U.S. investors not only for taxes actually paid to the developing country, but also for the taxes which would have been paid but which were "spared" under tax holiday incentive laws in the developing country.

Pro:

-- Developing countries consider this very important.

-- It would attract some additional U.S. investment.

-- It would permit a broadening of the U.S. network of treaties with developing countries.

<u>Con</u>:

-- The assertion that tax sparing is needed to avoid neutralization of developing country tax holidays by the U.S. foreign tax credit is an over-simplification. Provisions of U.S. tax law, particularly deferral and the overall foreign tax credit limitation, offset much of the neutralizing effect.

-- It would give U.S. tax benefits to U.S. persons.

-- It would move away from capital export neutrality.

-- The partner's tax policies control, not the U.S.

-- It would be uneven in impact. Countries with high tax rates but generous tax holidays would benefit; those with low rates and no tax holidays would not.

-- It would encourage rapid repatriation.

-- Investors who would have invested anyway would receive windfall benefits.

-- It has previously been rejected by the Senate.

TALKING POINTS ON CANCUN TRADE OPTIONS

I. The U.S. objective in the trade discussions at Cancun should be (1) to demonstrate the leadership role that the U.S. plays in liberalizing the international trading system, (2) to push North-South discussions on trade in the direction of pragmatic steps to strengthen the GATT system in ways that encourage the further adoption of market-oriented, outward-looking policies by developed and developi[ng] countries.

II. The U.S. has an excellent record of providing market access to the exports of developing countries. We should not hesitate to point out that record. For example:

- In 1980, 51 percent of U.S. imports from the developing countries entered duty-free.

- Our GSP program is the most open and responsive of all the donors' programs. GSP duty-free imports have increased three-fold since 1976 and are expected to reach $9 billion in 1981.

- The U.S. absorbs half of all the manufactured goods that are shipped to the industrialized countries from LDCs.

- In the past two years alone, the non-OPEC LDCs earned more from exports to the U.S. ($114.5 billion) than the entire Third World has received from the World Bank in 36 years.

III. A strengthening of the GATT, including its continued adaptation to the growing participation of developing countries in international trade, is the most meaningful action that can be taken on behalf of LDC trade in the early 1980s.

- The establishment of a strong discipline on safeguard actions would provide major, concrete encouragement to LDCs that outward-looking trade policies will not be undermined by arbitrary protectionist actions by developed countries. The U.S. position on safeguards is closer to the LDC position than are the positions of other developed countries. We should push on this at Cancun.

- Further liberalization of industrial nations' trade regimes is most likely to be achieved in the context of reciprocal, multilateral negotiations within GATT.

- Increased South-South trade depends upon further trade liberalization by developing countries, especially the advanced developing countries. The GATT provides an opportunity for such LDC trade liberalization in developed countries, thereby increasing the incentives for both groups to liberalize.

- The proposed GATT Ministerial offers an excellent opportunity in the immediate future to promote system-strengthening steps of special interest to developing countries (e.g., safeguards). The U.S. could seize the initiative at Cancun by proposing that free and open trade be the focus of the GATT Ministerial and by announcing that the U.S. will launch an extensive round of consultations with all countries, including developing countries, in preparation for the Ministerial's agenda.

- The U.S. could assert its leadership role even more vigorously at Cancun by announcing that the Administration will support the extension of GSP in some form beyond its scheduled termination date in 1985.

- Ability to deliver on our commitments is essential to maintaining our credibility on trade leadership. For this reason, it would be very dangerous to make commitments at Cancun on issues having extremely high domestic political sensitivity which might prove impossible to fulfill. Significant changes in the MFA, for example, would conflict with President Reagan's campaign pledge not to relax the existing degree of protection on textiles.

- Trade's contribution to development can be intensified by complementary private investment, development assistance and technology sharing. At Cancun we should point out that we are prepared to cooperate with other developed nations and with developing countries in such an integrated approach. In fact, we already have begun such an effort in the Caribbean region.

IV. Pro and Con of Suggested Approach

Pro:

- The approach offers pragmatic initiatives that are in the economic interests of both developing countries and developed countries.

- The Administration can fulfill these commitments at an acceptable domestic political cost.

- The proposed GATT Ministerial provides a relatively short time-frame within which the LDCs can judge the responsiveness of the developed countries.

Con:

- The developing country bloc is skeptical about the GATT's responsiveness to LDC trade concerns.

- The nature of the proposed trade initiatives does not lend itself to quantifying the additional resources that the LDCs will earn as a result of strengthening the GATT.

U.S. Economic Assistance Strategy

Context

The developing countries face economic problems which have been aggravated by high oil prices, high inflation and slow economic growth in the developed world. These problems can be overcome by: (1) strong economic growth in the U.S. and other developed countries; (2) freer trade; (3) sound economic policies in the Third World; (4) strengthening the role of market forces; and (5) development and adaptation of technology to raise productivity in agriculture and industry.

The primary responsibility in promoting development rests with the LDCs themselves. However, foreign aid is a significant factor. Both the U.S. foreign aid program and the multilateral development banks play important roles. We continue to support the multilateral institutions and to honor our commitments to them, but the U.S. will emphasize bilateral over multilateral assistance.

Assistance Priorities

--Encourage sound LDC policies that promote development, and strengthen the private sector.

--Build LDC institutions so that these countries can help themselves.

--Develop and transfer technology to the Third World using the unique resources of U.S. universities and corporations for training and R and D.

Countries of Concentration

--The primary focus of economic aid is on the poorer countries.

--Aid is concentrated among the poorer countries which pursue sound economic policies.

--Aid is provided within overall U.S. security and foreign policy objectives.

Fields of Concentration

U.S. bilateral assistance focuses primarily on agriculture and energy. Our agriculture programs stress increasing food production, primarily through small farms and raising incomes by strengthening productive enterprises.

In energy, our programs emphasize technical assistance for energy assessment and training, reforestation and R and D in areas where our aid complements the private sector.

Assistance: Agriculture

Contributing to the Third World's capacity to feed itself is an important U.S. commitment.

U.S. assistance to agricultural production should give priority to (1) better developing country policies, e.g., farmers won't produce much if the government holds down the prices paid to them; (2) developing human and institutional LDC capabilities, e.g., training and building experiment stations; (3) expanding the role of the private sector in agribusiness; and (4) generating and adapting technology.

The U.S. foreign aid program reflects these priorities. In 1982 over half of our development assistance will be focused on agriculture.

The Green Revolution of the past decade is the best example of the contribution of science and technology to food production. Underpinned by U.S. financial and scientific support, high-yielding varieties of wheat and rice were developed. They were critical to staving off famines in the 1970's and 1980's in several parts of the Third World. Indeed, some countries have become self-sufficient in food as a result of these crop breakthroughs. (The new variety of wheat was developed in a research center located in Mexico and the Mexicans are proud of their contribution).

Examples of scientific and technological activities supported by the U.S. include work to develop (1) a variety of plants that will tolerate a wide-range of soil and climate conditions, insects, and diseases; (2) more efficient irrigation systems (80% of the land under irrigation is in Aisa); (3) production of several crops per year on the same land in the humid tropics; and (4) methods of human and animal disease control to include such serious problems as the Tsetse Fly in Africa. The Tsetse bars agriculture production on vast areas of potentially-productive lands and other areas.

The U.S. also supports the strong efforts by the multilateral banks in agricultural assistance.

Free trade is important for agriculture as well as other sectors. This is detailed in the Trade paper.

Assistance: Energy

The U.S. recognizes the significance of energy problems--dependence on imported oil, and dwindling fuelwood supplies--confronting developing countries.

The U.S. believes domestic policies of developing country governments are critical to effective energy development. Energy pricing in particular must be realistic. Subsidies and price controls inhibit efforts to increase production. Sound government policies also are indispensible to the creation of a climate favorable to foreign and domestic private investment in energy production and improved energy efficiency.

Reflecting LDC concerns and our capabilities, the U.S. bilateral assistance program in energy--which primarily involves technical assistance--will place its major emphasis on renewable energy sources, e.g., reforestation, training, and in helping stimulate greater private sector involvement in conventional fuels development. Funding for renewable energy programs, especially fuelwood, will double in the next fiscal year to $70 million. (This is a reallocation; no additional monies are being requested.)

In particular, AID will expand (or initiate) the following energy assistance programs:

--Mobilizing Private Sector Support--Trade and Development Program feasibility studies for energy; the adaptation of private sector technology to developing country situations; and providing financing for developing country internships in U.S. energy companies.

--Support for the Program of Action of the United Nations Conference on New and Renewable Sources of Energy--The Conference identified specific actions to better utilize new and renewable sources of energy. In support of the Conference program the U.S. policy emphasizes the following: new fuelwood/reforestation programs; an evaluation network to help determine the most attractive applications of the new technologies; and active participation in consultative group meetings to foster increased international cooperation.

--Training--Plans for intensified energy training program for technicians from developing countries are being examined.

The U.S. also supports energy lending by multilateral institutions. Such lending can generate considerable increases in LDC energy development by catalyzing private investment in energy development, through joint project planning, co-financing, multilateral insurance and other innovative methods. We believe these institutions can reorient their lending to have a more positive impact on the private sector and we will suggest means to achieve this. The U.S. does not support the creation of a new energy affiliate because it believes that the same results can be accomplished by the existing institutional arrangements with their existing and expected funds.

Assistance: Private Sector

Private sector resources and expertise are a critical complement to foreign aid for economic growth in the Third World. AID's programs will place increased emphasis on stimulating LDC private sector development and on mobilizing U.S. private sector resources and expertise.

For this purpose AID will:

- -- Significantly expand co-financing and parallel financing with private commercial banks and venture capital firms both U.S. and LDC in developmental projects in developing countries.

- -- Work in close cooperation with the IFC and other appropriate institutions in providing advisory services to developing countries in the following areas: market development; investment policy; and industrial and agri-business policy. These advisory services would help to provide the incentives and financing for expanded private sector investments.

- -- Increase support for managerial and technical training.

NATIONAL SECURITY COUNCIL

October 7, 1981

MEMO FOR: JANET COLSON

FROM: CAROL CLEVELAND

Do you have any problems with my signing the attached memo for Mr. Lenz?

Sign ____________

Redo for Mr. Allen's sig ________

MEMORANDUM

5913

NATIONAL SECURITY COUNCIL

September 7, 1981

ACTION

MEMORANDUM FOR ALLEN J. LENZ

FROM: NORMAN A. BAILEY NB

SUBJECT: Cancun Summit

Richard Darman has requested NSC staff comments on Roger Porter's memo on the Cancun Summit (Tab A) by 3 p.m. today.

Attached at Tab I is a memorandum from you to Darman indicating that the NSC staff has no comment on the paper except to recommend that a follow-up working group be established after Cancun to examine carefully all tax alternatives.

Henry Nau concurs. Roger Fontaine has no comment.

RECOMMENDATION:

That you sign the memorandum to Richard Darman at Tab I.

Approve ________ Disapprove ________

Attachments
Tab I Memo to Darman
Tab A Porter Memo to Deaver

MEMORANDUM

5913

NATIONAL SECURITY COUNCIL

INFORMATION

MEMORANDUM FOR RICHARD G. DARMAN

FROM: ALLEN J. LENZ

SUBJECT: Cancun Summit

The NSC staff has no comment on the attached paper (Tab A) except that we recommend that a follow-up working group be established after Cancun to examine carefully all tax alternatives.

Attachment
Tab A Porter Memo of October 3 to Deaver

NSC/S PROFILE UNCLASSIFIED ID 8105913

RECEIVED 06 OCT 81 15

TO ALLEN FROM DARMAN, R DOCDATE 06 OCT 81

PORTER, R 03 OCT 81

KEYWORDS: CABINET COUNCIL MEXICO

CANCUN SUMMIT ECONOMICS

DARMAN REFERRAL

SUBJECT: CABINET COUNCIL MTG RE ECONOMIC SUMMIT IN CANCUN

ACTION: PREPARE MEMO LENZ TO DARMAN DUE: 07 OCT 81 STATUS S FILES

FOR ACTION	FOR CONCURRENCE		FOR INFO
BAILEY	FONTAINE	NAU	LENZ
			WEISS

COMMENTS ** COMMENTS DUE BY 3:00 PM WED.

REF# LOG NSCIFID (M / B

ACTION OFFICER (S)	ASSIGNED		ACTION REQUIRED	DUE	COPIES TO
RA	4	10/7	for Signature	10/8	
	C	11/13	OBE per Calvo		

DISPATCH W/ATTCH FILE WH (C)

WS

C.F.

04484955 Document No. ___________

FO006-02

WHITE HOUSE STAFFING MEMORANDUM

DATE: 10/6/81 ACTION/CONCURRENCE/COMMENT DUE BY: 10/7/81 3:00pm

SUBJECT: CANCUN SUMMIT

	ACTION	FYI		ACTION	FYI
VICE PRESIDENT	☐	☐	HARPER	☐	☐
MEESE	☐	☐	JAMES	☐	☐
BAKER	☐	☐	MURPHY	☐	☐
DEAVER	☐	☐	NOFZIGER	☐	☐
STOCKMAN	☐	☐	WILLIAMSON	☐	☐
ALLEN	☑	☐	WEIDENBAUM see comments	☑	☐
ANDERSON	☑	☐	HICKEY	☐	☐
BRADY/SPEAKES	☐	☐	MC COY	☐	☐
CANZERI	☐	☐	CEQ	☐	☐
DOLE	☐	☐	OSTP	☐	☐
FIELDING	☐	☐	USTP	☐	☐
FRIEDERSDORF 10/6 - see comments	☑	☐	ROGERS	☐	☐
FULLER *(For Cabinet)*	☐	☐	___	☐	☐
GARRICK	☐	☐	___	☐	☐
GERGEN	☑	☐	___	☐	☐

Remarks:

You will recall that we discussed these briefly on Monday -- and agreed to be prepared to present these to the President for decision by Wednesday. Could you please provide comments by 3:00 p.m. Wednesday.

Thank you.

Richard G. Darman
Assistant to the President
and
Deputy to the Chief of Staff
(x-2702)

THE WHITE HOUSE

WASHINGTON

October 3, 1981

MEMORANDUM FOR MICHAEL K. DEAVER

FROM: ROGER B. PORTER RBP

SUBJECT: Cancun Summit

At its Thursday, October 1 meeting, the Cabinet Council on Economic Affairs reviewed, as requested, a series of possible initiatives for the Cancun Summit. The central strategic issue facing the President as he prepares for Cancun is the position he should take on the calls for Global Negotiations. While the Cabinet Council's review did not directly address what approach we should take to Global Negotiations, our review of possible initiatives should prove helpful in developing the next steps in preparing for Cancun.

Our review concentrated on what basic approach the U.S. should pursue in its relations with developing countries and on what policies were most likely to produce lasting mutual benefits for both developed and developing nations. We considered a number of ideas and proposals, some more promising than others.

General Conclusions

In our discussion of possible proposals or initiatives, we reached several general conclusions:

1. The U.S. should identify with the developing countries' aspirations for greater economic growth and prosperity and show sympathy for their needs and problems.

2. We need to articulate better the U.S. record in aiding developing countries.

3. The most important step that both developed and developing nations can take is to put their domestic economic houses in order. International cooperation and economic growth depend on sound domestic policies.

4. Recommending a long list of specific initiatives or substantive proposals is unlikely to "win the hearts" of the developing nations at Cancun.

5. We should emphasize that we have a development strategy that can bring practical benefits to both the developed and developing world — one that we have found can succeed.

6. The institutional framework for what is needed is already in place but improvements can be made. We are prepared to join with others in making those improvements.

7. Our development strategy rests not on a single program or establishing a single forum. Rather it rests on an integrated approach that emphasizes trade, investment, and foreign assistance.

8. Neither government to government assistance nor massive income transfers from the developed to the developing world will bring sustained economic growth and prosperity. Lasting progress will occur only as the developing nations increase their capacity to produce goods and services and as there are markets for their products.

9. Thus, a successful development strategy must rest on an integrated approach that helps build productive capacity (through investment and technical assistance) and expand markets (through reducing barriers to trade).

<u>Investment</u>

The Cabinet Council examined three principal avenues for improving the investment climate in less developed countries thereby increasing the flow of private capital.

1. <u>Multilateral Investment Insurance Arrangements</u>.

A major constraint to the flow of direct investment to the LDC's is investors' perceptions of high political risk. Political risk insurance currently available from public and private sources is insufficient to support adequate flows of investment to the developing world, especially for high-risk, high-cost energy and minerals exploration projects.

A multilateral insurance arrangement, such as an International Investment Insurance Agency (IIIA), within the framework of the World Bank or its affiliate, the International Finance Corporation (IFC), could substantially reduce a major disincentive to investment in LDC's. Tying such an insurance arrangement to the World Bank could significantly increase its effectiveness since the potential loss of World Bank funding should prove a powerful deterrent to expropriation.

Several details such as dispute settlement and arbitration mechanisms, financial obligations, and control mechanisms (weighted versus non-weighted voting rights) require further development.

2. Expanding Cofinancing Programs.

Multilateral development institutions can play an important role as catalysts in generating greater private investment in LDC's through cofinancing programs with commercial banks. Such programs are relatively modest now. (In the past two years, private lenders have participated with the World Bank in some 40 projects committing a total of about $3.5 billion.) The U.S. can actively support increasing substantially the level of private cofinancing activities of the World Bank and the IFC.

3. Incentives under Bilateral Tax Agreements for Investment in Developing Countries.

Under current arrangements, when foreign governments in developing countries reduce or "spare" taxes for investors through tax holiday incentive laws, these have little effect on U.S. investors who simply end up replacing the foreign taxes they are spared with additional U.S. taxes because they receive a U.S. foreign tax credit only for taxes actually paid abroad.

One alternative examined by the Cabinet Council was allowing a U.S. foreign tax credit to U.S. investors not only for taxes actually paid to the developing country but also for taxes which would have been paid but which were "spared" under the tax holidary incentive law.

Other alternatives considered included extending a 10 percent investment tax credit to investments in developing countries, and allowing tax sparing credits only if the developing country reduced by treaty its statutory withholding tax on dividends, interest, and royalties paid to U.S. investors.

The Cabinet Council felt it was premature to endorse any of these specific tax proposals for several reasons. The current budget situation makes any near-term revenue losses extremely unattractive. Moreover, congressional agreement to support such tax changes is uncertain. There is widespread agreement that the President should not propose specific tax treaty changes on which he could not deliver. Rather, the Council felt that we could express a willingness to discuss new arrangements without supporting any specific changes in advance.

Foreign Assistance

A second major element of our development approach is foreign assistance programs. The underlying theme behind the Council's consideration of our economic assistance strategy is the need to build productive capacity in developing countries. Increased technical assistance in its many forms, including greater involvement by the U.S. private sector in technical assistance programs, is needed. "If you give a man a fish you feed him for a day; if you teach a man to fish you feed him for a lifetime."

The Council's review of this area produced agreement on the need to:

- o Encourage sound LDC policies that promote development and that strengthen the private sector emphasizing the important role of market forces, especially in pricing policies. Governmental controls on agricultural and energy prices in many developing countries constrain development in those sectors;

- o Continue to support existing multilateral institutions and to honor our commitments to them;

- o Refocus our bilateral aid on programs which:

  a. provide technical assistance and

  b. concentrate on training;

  (Most U.S. bilateral assistance focuses on agriculture and energy.)

- o Place increased emphasis in agricultural programs on expanding food production, primarily through small farms and raising incomes by strengthening productive enterprises;

- o Place increased emphasis in energy programs on technical assistance for energy assessment and training, reforestation, and research and development where our aid complements the private sector.

Trade

Developing nations must not only increase their capacity to produce goods and services by sound domestic economic policies, greater foreign investment, and expanded technical assistance and training; they also must have adequate markets for their products.

Five measures illustrate the absolute and comparative U.S. contribution to providing markets for LDC exports.

1. The U.S. absorbs approximately one-half of all the manufactured goods that the LDCs export to the industrialized countries.

2. In 1980, 51 percent of U.S. imports from developing countries entered duty free. Our average tariff on all dutiable imports was 5.5 percent.

3. The U.S. maintains very few quantitative restrictions and U.S. customs procedures are highly transparent and predictable.

4. Our Generalized System of Preferences (GSP) program is the most open and responsive of all the donors' programs. GSP duty-free imports have increased threefold since 1976 and are expected to reach $9 billion in 1981.

5. In the past two years alone, the non-OPEC LDCs earned more from exports to the U.S. ($114.5 billion) than the entire Third World has received from the World Bank in 36 years.

Among the developed nations, the U.S. has a superior record with respect to lowering both quantitative and qualitative trade barriers to LDC products.

Building on this record, the U.S. can challenge other developed nations to join in strengthening the GATT in ways that encourage the further adoption of market-oriented, outward-looking policies by developed and developing countries.

Specific potential initiatives include:

- o Support the extention of the Generalized System of Preferences, in some form, beyond its scheduled termination in 1985.

- o Seek at a 1982 GATT Ministerial a reduction in the barriers against LDC goods and services.

- o Press for strong discipline on safeguard actions to reduce arbitrary, secretive, inter-industry trade restraints.

cc: Donald T. Regan
Edwin Meese III
James A. Baker III
Richard G. Darman
Craig L. Fuller
Martin C. Anderson
Richard V. Allen

MULTILATERAL INVESTMENT INSURANCE ARRANGEMENTS

Overview:

A major constraint to the flow of direct investment to the LDC's is investor perception of higher political risk in these countries. Political risk insurance currently available from public and private sources is insufficient to support adequate flows of investment to the developing world, especially for high-risk, high-cost energy and minerals exploration projects. A multilateral insurance arrangement drawing together the resources of developed and perhaps developing countries could provide a mechanism to help meet these needs.

Pros:

-- Risk on major projects could be spread so that high value projects could be covered more easily.

-- Capital-exporting countries could act mutilaterally in cases of expropriation, raising the inherent cost of hostile action against the property of citizens of any one state.

Cons :

-- LDCs have been reluctant to support past multilateral insurance proposals, which could reduce their leverage in dealing with developed countries or limit their control over foreign enterprise. Some leaders of the G-77 opposed arbitration obligations or other limits to national sovereignty.

-- Western European countries were uninterested in past schemes as well, preferring to exert greater control through national programs which can be tailored more closely to the pursuit of their own domestic objectives. (Europeans also tend to view such programs as benefiting us more than them, especially in Latin America, where the bulk of foreign investors are U.S.)

-- Previous plans were dropped when participants were unable to agree on: dispute settlement and arbitration mechanisms; financial obligation (including at least a token contribution from the LDCs); control mechanisms (weighted versus non-weighted voting rights). Any new program would also have to deal with these issues.

Most Forthcoming Alternative: A multilateral insurance arrangement within the framework of the World Bank or International Finance Corporation (IFC).

World Bank President William Clausen has already privately expressed his interest in launching a multilateral insurance program within the World Bank. However, strong U.S. support would be needed to begin such a program. We would prefer an insurance mechanism established through the IFC, similar to the International Investment Insurance Agency (IIIA) advanced on a number of occasions by the U.S. between 1961 and 1972. (The IIIA would have been a new international agency which insured private developmental investment in member LDCs against specific political risks and reinsured investment insurance contracts made under domestic programs such as OPIC.)

Pros:

-- Would create a large insurer capable of providing low-cost insurance against political risk and loan guarantees for major investments.

-- IIIA would be fiscally sound and credible to investors.

-- The framework for consultation is already in place, and general principles have been set out in the IFC Charter.

-- It would be a multilateral program with a link to the IFC, which should deter expropriation.

-- The program could possibly be put in place without additional funding. The IFC already has a guarantee program; changes in reserve ratio requirements could permit the IFC to leverage existing funds to support many more projects through insurance rather than direct loans.

Cons:

-- The IFC's Charter does not specifically allow or prohibit it to issue insurance. A Charter amendment would be needed to permit the IFC to issue insurance on reasonable terms.

-- The LDCs will have the same objections they had to previous IIIA proposals. The prospects for a successful negotiation are thus not good.

-- LDCs oppose the involvement of a major multilateral lending agency. They fear that a World Bank-linked mechanism would have additional leverage, since the Bank must look at a country's expropriation record before approving new loans.

-- We would have limitd control over the design of an IFC proposal.

-- A sound facility would require reserves, funded in all probability by paid-in capital. The USG might have problems if we had to seek an appropriation.

<u>Moderately Forthcoming Option</u>: A U.S.-led, developed country multilateral initiative.

The U.S. could propose a multilateral insurance program within an existing developed country mechanism such as the Direct Assistance Committee of the OECD, similar to the International Investment Reinsurance Agency (IIRA), a plan raised in the Investment Insurance Committee of the Berne Union in the mid-70's. The group would provide reinsurance on political risk coverage; risk would be shared among countries in proportion to their contribution to the insurance pool.

<u>Pros</u>:

-- LDC approval is not needed to implement the program.

-- Greater national control is retained over insurance issued.

<u>Cons</u>:

-- Such a mechanism would probably not draw in non-Western (e.g., OPEC) participants.

-- Previously, Western Europeans have been unenthusiastic.

<u>Least Forthcoming Alternative</u>: Greater U.S. public-private sector insurance cooperation.

The Overseas Private Investment Corporation (OPIC) could work more closely with private sector insurance companies on a project-by-project or regional basis. Private insurers are increasingly interested in entering the political risk field, and could benefit from OPIC experience and cooperation.

<u>Pros</u>:

-- The program would be easy to implement, and would in fact only expand current OPIC efforts.

-- This program would re-emphasize our commitment to the private sector, and help interested private sector insurers to expand their activities in the political risk field.

<u>Cons</u>:

-- There would be little expansion of coverage available. Private sector firms could not be expected to accept too large a portion of the total risk.

-- There would be only limited psychological impact from announcing such a program.

-- Limitations which keep OPIC from insuring projects (e.g., country exposure limits, employment-impact, Calvo clause) would also limit joint activities.

Incentives under Bilateral Tax Agreements for Investment in Developing Countries

U.S. tax treaties with developing countries can include investment incentives. Such benefits should be provided only by treaty because: (1) the incentive can be targeted to particular countries where it is likely to be most effective and where it conforms to overall U.S. foreign policy objectives; (2) it can be targeted to certain industries which are important to the development of the partner; (3) the U.S. would be able to receive reciprocal consessions, particularly exchange of information; and (4) the greater incentive thereby created for developing countries to enter into treaties with the U.S. would further enhance the ability of these countries to attract U.S. investment.

Last Forthcoming Alternative: Tax Sparing Credits Only for Reduction under the Treaty in Treaty Partner Taxes

If the treaty partner reduces by treaty its statutory withholding tax on dividends, interest and royalties paid to U.S. investors, the U.S. would allow a foreign tax credit for the full statutory tax.

Pro:

-- It will benefit U.S. investors and encourage investment.

-- Developing countries would probably agree to greater treaty reductions in their statutory withholding rates.

-- Because it is more limited than full tax sparing, it would probably engender less opposition.

Con:

-- It would violate the policy of not giving U.S. treaty benefits to U.S. citizens and residents.

-- It will encourage repatriation.

-- The impact will be uneven, depending on the partner's level of statutory withholding rates.

-- It will provide windfall benefits to those who would have receive the income in any event.

-- The Senate would be likely to object.

Moderately Forthcoming Alternative: Investment Tax Credit

A 10 percent investment tax credit would be extended to investment (and reinvestment) in developing countries.

Pro:

-- Most developing countries would consider this a satisfactory alternative to tax sparing.

-- It would afford an immediate benefit to U.S. investors, whether or not the venture proved profitable.

-- It would be a move toward capital export neutrality.

-- It would not encourage repatriation and, if structured to cover reinvestment, would encourage retention.

-- It would permit a broadening of the U.S. treaty network with developing countries.

-- The U.S. would retain control over the incentive.

Con:

-- It would violate the purpose of the domestic credit -- to encourage investment in the United States.

-- It would give U.S. treaty benefits to U.S. persons.

-- It would be uneven in impact, giving greater benefit to capital intensive investments, which are, typically, not those most needed by developing countries.

-- It has previously been rejected by the Senate.

Most Forthcoming Alternative: Tax Sparing Credits for Developing Country Tax Holidays

A U.S. foreign tax credit would be granted to U.S. investors not only for taxes actually paid to the developing country, but also for the taxes which would have been paid but which were "spared" under tax holiday incentive laws in the developing country.

Pro:

-- Developing countries consider this very important.

-- It would attract some additional U.S. investment.

-- It would permit a broadening of the U.S. network of treaties with developing countries.

Con:

-- The assertion that tax sparing is needed to avoid neutralization of developing country tax holidays by the U.S. foreign tax credit is an over-simplification. Provisions of U.S. tax law, particularly deferral and the overall foreign tax credit limitation, offset much of the neutralizing effect.

-- It would give U.S. tax benefits to U.S. persons.

-- It would move away from capital export neutrality.

-- The partner's tax policies control, not the U.S.

-- It would be uneven in impact. Countries with high tax rates but generous tax holidays would benefit; those with low rates and no tax holidays would not.

-- It would encourage rapid repatriation.

-- Investors who would have invested anyway would receive windfall benefits.

-- It has previously been rejected by the Senate.

TALKING POINTS ON CANCUN TRADE OPTIONS

I. The U.S. objective in the trade discussions at Cancun should be (1) to demonstrate the leadership role that the U.S. plays in liberalizing the international trading system, (2) to push North-South discussions on trade in the direction of pragmatic steps to strengthen the GATT system in ways that encourage the further adoption of market-oriented, outward-looking policies by developed and developing countries.

II. The U.S. has an excellent record of providing market access to the exports of developing countries. We should not hesitate to point out that record. For example:

- In 1980, 51 percent of U.S. imports from the developing countries entered duty-free.

- Our GSP program is the most open and responsive of all the donors' programs. GSP duty-free imports have increased three-fold since 1976 and are expected to reach $9 billion in 1981.

- The U.S. absorbs half of all the manufactured goods that are shipped to the industrialized countries from LDCs.

- In the past two years alone, the non-OPEC LDCs earned more from exports to the U.S. ($114.5 billion) than the entire Third World has received from the World Bank in 36 years.

III. A strengthening of the GATT, including its continued adaptation to the growing participation of developing countries in international trade, is the most meaningful action that can be taken on behalf of LDC trade in the early 1980s.

- The establishment of a strong discipline on safeguard actions would provide major, concrete encouragement to LDCs that outward-looking trade policies will not be undermined by arbitrary protectionist actions by developed countries. The U.S. position on safeguards is closer to the LDC position than are the positions of other developed countries. We should push on this at Cancun.

- Further liberalization of industrial nations' trade regimes is most likely to be achieved in the context of reciprocal, multilateral negotiations within GATT.

- Increased South-South trade depends upon further trade liberalization by developing countries, especially the advanced developing countries. The GATT provides an opportunity for such LDC trade liberalization in developed countries, thereby increasing the incentives for both groups to liberalize.

- The proposed GATT Ministerial offers an excellent opportunity in the immediate future to promote system-strengthening steps of special interest to developing countries (e.g., safeguards). The U.S. could seize the initiative at Cancun by proposing that free and open trade be the focus of the GATT Ministerial and by announcing that the U.S. will launch an extensive round of consultations with all countries, including developing countries, in preparation for the Ministerial's agenda.

- The U.S. could assert its leadership role even more vigorously at Cancun by announcing that the Administration will support the extension of GSP in some form beyond its scheduled termination date in 1985.

- Ability to deliver on our commitments is essential to maintaining our credibility on trade leadership. For this reason, it would be very dangerous to make commitments at Cancun on issues having extremely high domestic political sensitivity which might prove impossible to fulfill. Significant changes in the MFA, for example, would conflict with President Reagan's campaign pledge not to relax the existing degree of protection on textiles.

- Trade's contribution to development can be intensified by complementary private investment, development assistance and technology sharing. At Cancun we should point out that we are prepared to cooperate with other developed nations and with developing countries in such an integrated approach. In fact, we already have begun such an effort in the Caribbean region.

IV. Pro and Con of Suggested Approach

Pro:

- The approach offers pragmatic initiatives that are in the economic interests of both developing countries and developed countries.

- The Administration can fulfill these commitments at an acceptable domestic political cost.

- The proposed GATT Ministerial provides a relatively short time-frame within which the LDCs can judge the responsiveness of the developed countries.

Con:

- The developing country bloc is skeptical about the GATT's responsiveness to LDC trade concerns.

- The nature of the proposed trade initiatives does not lend itself to quantifying the additional resources that the LDCs will earn as a result of strengthening the GATT.

U.S. Economic Assistance Strategy

Context

The developing countries face economic problems which have been aggravated by high oil prices, high inflation and slow economic growth in the developed world. These problems can be overcome by: (1) strong economic growth in the U.S. and other developed countries; (2) freer trade; (3) sound economic policies in the Third World; (4) strengthening the role of market forces; and (5) development and adaptation of technology to raise productivity in agriculture and industry.

The primary responsibility in promoting development rests with the LDCs themselves. However, foreign aid is a significant factor. Both the U.S. foreign aid program and the multilateral development banks play important roles. We continue to support the multilateral institutions and to honor our commitments to them, but the U.S. will emphasize bilateral over multilateral assistance.

Assistance Priorities

--Encourage sound LDC policies that promote development, and strengthen the private sector.

--Build LDC institutions so that these countries can help themselves.

--Develop and transfer technology to the Third World using the unique resources of U.S. universities and corporations for training and R and D.

Countries of Concentration

--The primary focus of economic aid is on the poorer countries.

--Aid is concentrated among the poorer countries which pursue sound economic policies.

--Aid is provided within overall U.S. security and foreign policy objectives.

Fields of Concentration

U.S. bilateral assistance focuses primarily on agriculture and energy. Our agriculture programs stress increasing food production, primarily through small farms and raising incomes by strengthening productive enterprises.

In energy, our programs emphasize technical assistance for energy assessment and training, reforestation and R and D in areas where our aid complements the private sector.

Assistance: Agriculture

Contributing to the Third World's capacity to feed itself is an important U.S. commitment.

U.S. assistance to agricultural production should give priority to (1) better developing country policies, e.g., farmers won't produce much if the government holds down the prices paid to them; (2) developing human and institutional LDC capabilities, e.g., training and building experiment stations; (3) expanding the role of the private sector in agribusiness; and (4) generating and adapting technology.

The U.S. foreign aid program reflects these priorities. In 1982 over half of our development assistance will be focused on agriculture.

The Green Revolution of the past decade is the best example of the contribution of science and technology to food production. Underpinned by U.S. financial and scientific support, high-yielding varieties of wheat and rice were developed. They were critical to staving off famines in the 1970's and 1980's in several parts of the Third World. Indeed, some countries have become self-sufficient in food as a result of these crop breakthroughs. (The new variety of wheat was developed in a research center located in Mexico and the Mexicans are proud of their contribution).

Examples of scientific and technological activities supported by the U.S. include work to develop (1) a variety of plants that will tolerate a wide-range of soil and climate conditions, insects, and diseases; (2) more efficient irrigation systems (80% of the land under irrigation is in Aisa); (3) production of several crops per year on the same land in the humid tropics; and (4) methods of human and animal disease control to include such serious problems as the Tsetse Fly in Africa. The Tsetse bars agriculture production on vast areas of potentially-productive lands and other areas.

The U.S. also supports the strong efforts by the multilateral banks in agricultural assistance.

Free trade is important for agriculture as well as other sectors. This is detailed in the Trade paper.

Assistance: Energy

The U.S. recognizes the significance of energy problems--dependence on imported oil, and dwindling fuelwood supplies--confronting developing countries.

The U.S. believes domestic policies of developing country governments are critical to effective energy development. Energy pricing in particular must be realistic. Subsidies and price controls inhibit efforts to increase production. Sound government policies also are indispensible to the creation of a climate favorable to foreign and domestic private investment in energy production and improved energy efficiency.

Reflecting LDC concerns and our capabilities, the U.S. bilateral assistance program in energy--which primarily involves technical assistance--will place its major emphasis on renewable energy sources, e.g., reforestation, training, and in helping stimulate greater private sector involvement in conventional fuels development. Funding for renewable energy programs, especially fuelwood, will double in the next fiscal year to $70 million. (This is a reallocation; no additional monies are being requested.)

In particular, AID will expand (or initiate) the following energy assistance programs:

--Mobilizing Private Sector Support--Trade and Development Program feasibility studies for energy; the adaptation of private sector technology to developing country situations; and providing financing for developing country internships in U.S. energy companies.

--Support for the Program of Action of the United Nations Conference on New and Renewable Sources of Energy--The Conference identified specific actions to better utilize new and renewable sources of energy. In support of the Conference program the U.S. policy emphasizes the following: new fuelwood/reforestation programs; an evaluation network to help determine the most attractive applications of the new technologies; and active participation in consultative group meetings to foster increased international cooperation.

--Training--Plans for intensified energy training program for technicians from developing countries are being examined.

The U.S. also supports energy lending by multilateral institutions. Such lending can generate considerable increases in LDC energy development by catalyzing private investment in energy development, through joint project planning, co-financing, multilateral insurance and other innovative methods. We believe these institutions can reorient their lending to have a more positive impact on the private sector and we will suggest means to achieve this. The U.S. does not support the creation of a new energy affiliate because it believes that the same results can be accomplished by the existing institutional arrangements with their existing and expected funds.

Assistance: Private Sector

Private sector resources and expertise are a critical complement to foreign aid for economic growth in the Third World. AID's programs will place increased emphasis on stimulating LDC private sector development and on mobilizing U.S. private sector resources and expertise.

For this purpose AID will:

-- Significantly expand co-financing and parallel financing with private commercial banks and venture capital firms both U.S. and LDC in developmental projects in developing countries.

-- Work in close cooperation with the IFC and other appropriate institutions in providing advisory services to developing countries in the following areas: market development; investment policy; and industrial and agri-business policy. These advisory services would help to provide the incentives and financing for expanded private sector investments.

-- Increase support for managerial and technical training.