Special Relationships, Dollars, and Development:
U.S. Foreign Aid and State-Building in Egypt, Jordan, South Korea, and Taiwan

Chapter 2

FOREIGN AID AND THE PRIMACY OF COALITION POLITICS

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Abstract

The very different institutional contributions of large-scale American aid to Egypt, Jordan, South Korea, and Taiwan are best explained by different authoritarian coalitions in each aid recipient. Rulers in Egypt and Jordan have based their rule on highly disparate, distributive coalition strategies and have thus incorporated foreign aid into institutions of patronage, while donor-financed parallel institutions also provide public goods and thereby allow central patronage institutions to remain in place. By contrast, rulers in South Korea and Taiwan relied upon narrow, developmental coalitions and used American financial and technical assistance to create new, more efficient institutions. As a geopolitically-concerned donor, the U.S. was acutely aware of coalition pressures in each recipient and configured aid as such.

Introduction

The cases of Egypt, Jordan, South Korea, and Taiwan are often-cited empirical discrepancies in the grand theories of the aid literature. Egypt and Jordan have received massive quantities of assistance from the U.S. and other sources over a prolonged period of time. Jordan has displayed "surprisingly poor growth coincident with having relatively good economic policies and inflows of aid (Burnside and Dollar 2004, 783)," while "high levels of assistance often seem to be inversely related to Egypt's ability to use the aid effectively or wisely (Weinbaum 1986, 2)." Egypt and Jordan have incorporated foreign aid into institutions of patronage and distribution that undermine economic development more broadly, consistent with theories of aid-induced rentierism, while donor-financed parallel institutions within these countries provide public goods and thereby allow central patronage institutions to remain in place. Yet South Korea and Taiwan, also recipients of large-scale American assistance after the Second World War, are cited as rare success stories, where U.S. aid contributed to savings and investment, made the bureaucracy more meritocratic and insular, provided growth incentives for a rising capitalist class, and did not undermine revenue collection (Jacoby 1967; Amsden 1989; Wade 1990; Woo 1991; Kohli 2004).

All four countries were of geostrategic interest to their major donor, the U.S., which was extremely unwilling to use conditionality that might destabilize pro-American regimes. Nevertheless, the East Asian countries utilized U.S. aid more effectively than those in the Middle East. This divergence in outcomes indicates that aid might contribute to or produce very different institutional patterns independently of its volume or donor intent. Why has foreign aid fueled highly distributive, inefficient states in Egypt and Jordan while making positive contributions to developmental states in South Korea and Taiwan? This project describes the impact of U.S. foreign assistance upon state institutions in each of these four countries and tries to account for its variable impact.

Authoritarian rulers were subject to the constraints imposed by the preferences of coalition members, compelling them to use aid in different ways. In Egypt and Jordan, rulers were bound by disparate and costly coalitions consisting of business groups and subaltern classes. These coalitions emerged independently of foreign aid and resulted in distributive spending, minimal extraction, a politicized bureaucracy, rent-satisfying modes of state economic intervention, and collusive state-capitalist relations. The cost of maintaining a disparate coalition introduced a major structural deficit into the state budget, and these countries became reliant on various sources of external rent, including foreign aid, to meet coalition demands. In these cases, U.S. aid had two effects. First, it sustained inefficient distributive institutions beyond the period of time that normal economic conditions would have permitted. Second, because the U.S. has been willing to commit large amounts of aid over the long term to ensure regime stability in these two countries, it has used its aid to establish and maintain "parallel institutions" that provide essential public goods outside of the central patronage state, thus allowing distributive institutions to remain in place and domestic politics to remain stable.

In Taiwan and South Korea (though more so under Park Chung-Hee than under Syngman Rhee), rulers were freed by unified and inexpensive coalitions. To some extent, aid was diverted to coalition members, but since the coalition was relatively small, aid could also be used to establish new, more efficient bureaucracies and to discipline rent-seeking capitalists. Many of these institutions, such as a pilot agency that coordinates development efforts and formulates policy, started out as U.S.-supported parallel institutions that would aid in post-war reconstruction. By contrast to the Middle Eastern cases, parallel institutions in South Korea and Taiwan were short-lived. They were quickly incorporated into the central state as governments assumed responsibility for providing public goods to their respective societies.

The goal of this chapter, and the broader project of which it is a part, is to stress the primacy of coalition politics in explaining the impact of aid upon state institutions; this is done through description and, at most, mid-range theory. The project integrates abstract tenets from three different literatures (foreign aid, rentier state, and comparative political economy) with a close examination of U.S. aid to Egypt, Jordan, South Korea, and Taiwan, four key cases that have otherwise been classified as outliers in the broader work on foreign aid. Observations regarding coalition politics, aid effectiveness, and institutions in these four countries have the potential to coalesce into a more general theory, and, as such, this project carefully defines foreign aid, coalition strategies, and institutional contributions in anticipation that these could become antecedent, independent, and dependent variables, respectively, in a general theory. These will need to be supplemented by a derivation of actor preferences and the delineation of institutional constraints to produce a more general utility function, whether formally or informally. This can be a future project.

The chapter proceeds in five parts. It first provides a brief summary of theoretical holes in the aid literature, which were more extensively detailed in Chapter 1, and makes a case for a new approach centered on domestic politics. The second section provides a rationale for case selection and a discussion of the project's qualitative methodology. The third section outlines a new argument centered on the domestic coalition politics of aid recipients. The fourth section briefly summarizes the cases, which will be fleshed out in subsequent chapters. The fifth and final section summarizes the theoretical and empirical contributions of the project, and provides a chapter layout for the rest of the dissertation.

The Insufficiency of the "Supply Side"

The important empirical discrepancies provided by Egypt, Jordan, South Korea, and Taiwan reveal greater theoretical weaknesses in existing approaches to the study of foreign aid and economic development. These problems are evident in both econometric studies that are championed by development economists and qualitative studies on the Middle Eastern "rentier state" that are usually the purview of political scientists. Econometric studies concerned purely with aid and per capita GDP growth have failed to produce strong empirical evidence supporting this relationship in either direction (Rajan and Subramanian 2006; Easterly 2006), and a number of studies have challenged the mechanisms of the "Big Push" to which aid has traditionally been believed to contribute (Boone 1995, 1996; Kraay and Radatz 2005; Easterly 2006). Scholars have subsequently modified this research agenda by examining conditions under which aid is more or less effective, such as regime type or the nature of macroeconomic policy (Burnside and Dollar 2000; Bearce 2008). This is a step in the right direction, yet these studies employ a very thin consideration of institutions that precludes an understanding of exceptional cases like Egypt and Jordan. They have also been challenged on methodological and empirical grounds (McPherson 2000; Dalgaard and Hansen 2001; Hansen and Tarp 2000, 2001; Lensink and White 2001; Easterly et al 2004). Work that posits a negative relationship between aid and taxation/extraction has generally been more statistically sound (Heller 1975; Kimbrough 1980; Khan and Hoshino 1992; Khiliji and Zampelli 1994; Feyzioglu et al 1998; Brautigam and Knack 2004; Remmer 2004). Yet, like the "Big Push" literature, there are important exceptions for which these models cannot account—namely, South Korea and Taiwan, which continued to tax their populations even as they received massive American assistance. The assumption that aid inherently alters fiscal policy is highly contestable yet it is evident in all of these studies.

The fundamental problem in the aid literature to date is an overemphasis on the volume of aid, or the "supply side," as the principal causal variable in explaining institutional and economic development (Peters and Moore 2009). In this sense, the scholarship on foreign aid shares many of the detractions evident in the broader literature on external rents, particularly oil revenues. Foreign aid and oil revenues both fall under the category of "external rent," or unearned income, that accrues directly to the state. Both are typically presented as structural variables that exert uniform, independent, and generally negative effects on state institutions, politics, and economics in any context.

The literature on the "rentier state," for instance, claims that external rents undermine developmental institutions through two principal means. First, different societal groups forfeit participation in the policy process in exchange for protected markets, subsidies, public employment, and tax breaks. This concession breaks important channels of communication between the state and the private sector, and many of the institutions used to "buy" support of different social groups can be harmful to sustainable economic growth. Second, external rents relieve the state of extracting domestic revenue as a means of regenerating itself. To the extent that the state relies on taxes, there may be little incentive to develop the domestic economy as a means of cultivating a taxable domestic surplus (Luciani 1987). Without an extractive bureaucracy, there is little incentive or capability to centralize the fiscal apparatus, obtain information on producers and generate economic data, set fiscal priorities, and establish effective private sector regulation (Chaudhry 1997). Regime elites can avoid the politically painful process of constructing developmental institutions—leaving in place those rent-seeking practices that undermine economic activity.

Supply side theories produce few explanations relevant to the four cases considered here. Rather, it is the "demand side" of external rents that is most illuminating—those domestic political conditions that greet rents as they enter a recipient and condition their use. Extant approaches to the study of foreign aid overlook this very political side of economy, which a large and robust literature credits with determining important institutional outcomes, such as fiscal practices, the nature of the bureaucracy, state-capitalist relations, and modes of state economic intervention (Bates 1981, 2001; Olson 1982; Anderson 1986; Migdal 1988; Crystal 1989; Barnett 1992; Tilly 1992; Geddes 1994; Chaudhry 1997; Ertman 1997; Waldner 1999; Herbst 2000; Kang 2002; Centeno 2003; Kohli 2004; Doner et al 2005). Firmly rooted in comparative political economy, this largely qualitative literature utilizes coalition politics, colonial legacies, and domestic and international political competition to explain institutional development. Although some of these scholars insert *ad hoc* descriptive accounts of external rents into pertinent cases, few integrate external rents, let alone foreign aid, into their theoretical frameworks. Indeed, many of the same institutions are found in countries with and without access to foreign aid.

The least common denominator in much of this literature is what Migdal (1988) terms the "politics of survival" in late developing countries. The concept of late development is rooted in the notion that additional state intervention is necessary for a country to industrialize in a world economy already populated with industrialized states (Gerschenkron 1962). Smith (2007, 3) defines late industrialization as

> a set of policies in which 'the state explicitly nurtures the development of private sector capital and labor, relying on a variety of means—financial, social, political, and infrastructural (Bellin 2002, 3-4)' as well as more directly interventionist policies such as the creation of state-owned industrial enterprises and state-granted monopolies in key sectors.

The process of late industrialization is important because it entails a complete restructuring of production and consumption, the creation of new institutions, and the destruction of old ones in a very short period of time. These processes can affect the distribution of power in the state and society and produce substantial political conflict. Leaders prefer to implement late development in the least costly way and, as such, the means by which a ruler survives during this period fundamentally affect state economic institutions and policies.

External rents, including foreign aid, are an important resource available to rulers during late development. Any account of external rent distribution should make some attempt to explain the distributional politics of external rents. Which groups seek rents and why, and what factors condition their success? Why does the recipient regime accommodate their preferences? Does the implementation of these preferences have institutional implications? Taking the politics of coalition maintenance seriously--particularly in a non-democratic context--means abandoning crude arguments that rent distribution buys policy autonomy (Peters and Moore 2009).

In the past five years, a revisionist literature on the rentier state has tried to answer many of these questions. Drawing on empirical discrepancies in most-similar cases, this literature abandons the notion that external rents are structural variables that carry inherent distributional incentives. Rather, external rents are either an antecedent condition or an intervening variable, and their institutional effects are the result of interaction with domestic politics and/or institutions that have been addressed by the broader CPE literature. Herb (1999), for example, argues that the durability of petromonarchies in Saudi Arabia and Kuwait is the result of institutionalized mechanisms for succession being in place before the oil boom. Smith (2007) finds that oil revenues were used for improving institutions of extraction and local governance in Indonesia because they arrived after the rise of a powerful opposition party, whereas in Iran, a typical "rentier state," they did not. Peters and Moore (2009) argue that aid-based rentierism in Jordan is the result of a "disparate coalition" that is extraordinarily expensive to maintain, compelling rulers to route foreign aid to its various constituent parts. What is now needed is a study that systematically integrates the study of foreign aid with the theoretical contributions of comparative political economy. How does aid interact with regime maintenance, state-building processes, and late development? How do these processes matter for institutional outcomes?

Figure 1
Approaches to the Study of External Rents, Domestic Politics, and Institutions

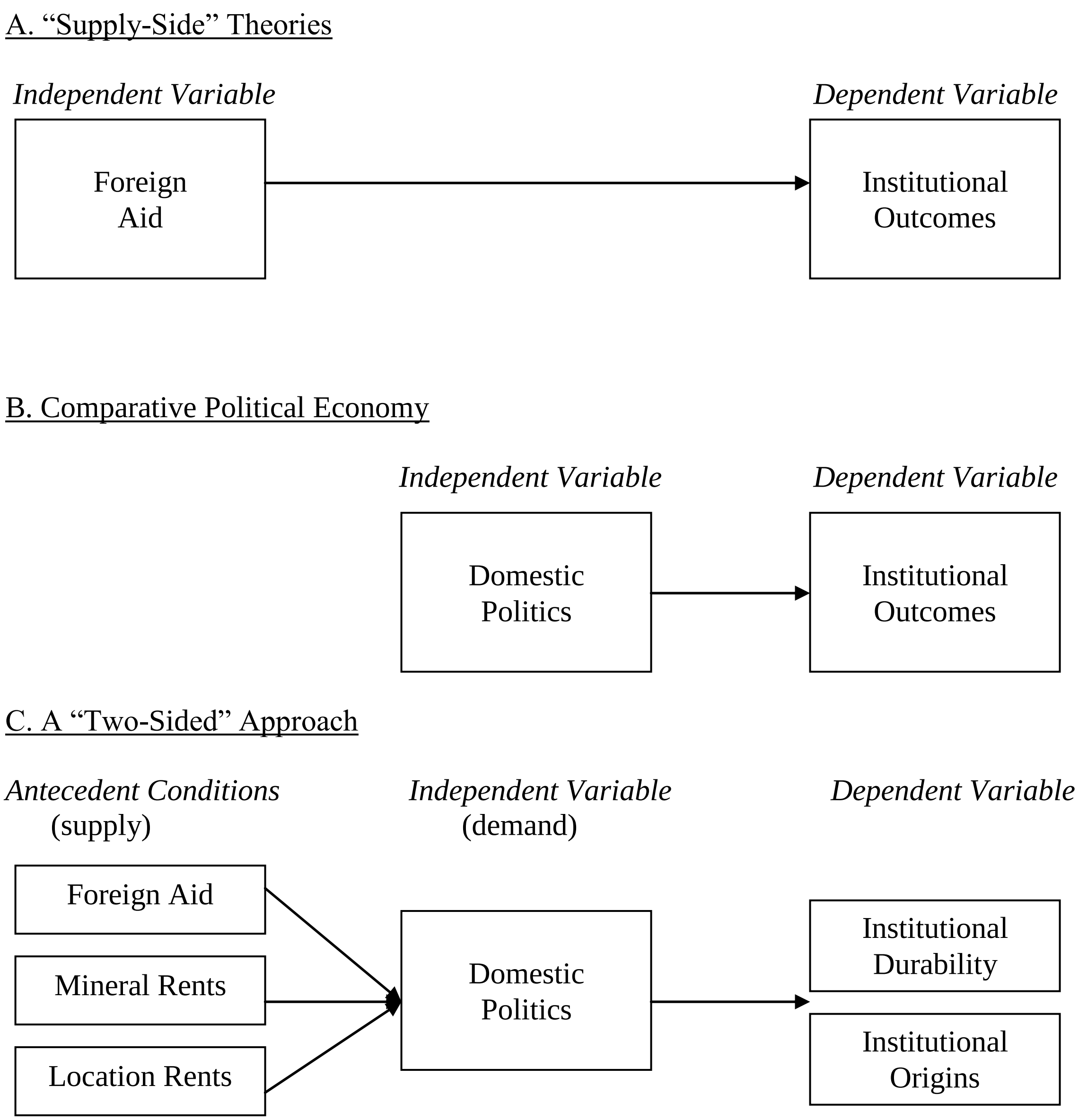

Figure 1 contains three diagrams. Diagram A depicts the traditional "supply-side" approach towards the study of aid and institutions. Diagram B depicts the general approach of the comparative political economy literature. Diagram C combines the two, reducing aid (along with other categories of external rent) to an antecedent condition and elevating domestic politics to the position of an independent variable. Distributive institutions, such as those found in Egypt, are also found in countries without such bountiful access to foreign aid, but which do experience similar domestic political pressures. Waldner, for instance, finds that the inclusion of subaltern classes in regime coalitions is a sufficient condition for highly distributional "precocious Keynesian" states in Syria and Turkey. Waldner concedes that aid may have helped to sustain distributive institutions, but had no causal role in their formation. This is to say that we should pretty well be able to predict the nature of state institutions by examining coalition composition. These institutions may come to rely on foreign aid for their durability, but they were not created by foreign aid itself. By designating foreign aid as an antecedent condition and incorporating domestic politics as an independent variable, a theory along the lines of Diagram C can account for both the (often dynamic) nature of the domestic demands on aid and the continued supply of it by donors—a "two-sided" approach (Peters and Moore 2009).

Depending on context, the dependent variable in a theory modeled on Diagram C can be designated as either institutional origins and/or durability. Although this project will occasionally refer to these outcomes collectively as "institutional contributions," it is important to distinguish between these two concepts. Utilizing institutional durability as a dependent variable will generate more modest claims. It refers to the contributions that aid makes to institutions that originated independently of donor financial and technical assistance. For example, rulers may initiate patronage-based public employment in the absence of foreign aid, even though foreign aid may provide some of the financial fuel for this relationship. It would be a mistake to attribute the emergence of this collusive relationship solely to the filtering of aid through domestic politics. Rather, aid contributed to the durability of an existing institution. It may even have done so alongside other sources of external rent.

However, there are some situations in which one might claim that the interaction between aid and politics is a sufficient condition for institutional origins. This can occur in two situations. The first is where the recipient displays exclusive fiscal or technical dependence on foreign aid for the genesis of the institution. Institutions require financial fuel and technical expertise. If it can be shown that a significant portion of these finances or expertise (ideally, a theoretical cutoff point that distinguishes institutional maintenance or genesis from collapse or nonexistence) are derived from foreign aid, we can legitimately state that foreign aid interacting with domestic politics produces an institution. The second situation, drawing upon a similar logic, occurs when foreign aid constitutes an institutional outcome in itself. The most notable examples are "parallel institutions" which are financed and staffed by donor organizations. In either of these two scenarios, the counterfactual is that without the financial and technical expertise provided by foreign aid, these institutions would not exist. Most institutional origins identified in this project are parallel institutions, generally due to the difficulty of locating the point at which aid becomes necessary for institutional genesis.[1]

[1] Luciani claims that rentier states are produced when greater than 40 percent of domestic revenues being provided by external rent. However, this baseline has no theoretical justification and can account for neither the necessity of technical assistance nor aid's necessity in the case of individual institutions.

Case Selection and Method

Egypt, Jordan, South Korea, and Taiwan have been included in this project based on their conduciveness to existing tools of qualitative methods, as well their ability to remedy gaps in the descriptive and theoretical literature on foreign aid. Egypt and Jordan have topped the list of U.S. aid recipients in the past fifty years, yet we still know little about aid's interaction with domestic politics and institutions in these countries. Scholarly accounts of Egypt and Jordan limit their focus to aid volume or individual projects while official reports frequently measure aid outcomes in terms of aid inputs. We know much more about U.S. aid in South Korea and Taiwan through a large secondary literature, as well as more frank accounts of these missions that were written by American policymakers and subsequently declassified. South Korea and Taiwan are thus included in this study less for the purpose of description and more for the necessary variation that they introduce on the dependent variable.

This project utilizes a two-stage qualitative framework that employs Mill's Methods and causal process tracing/ congruency tests. The goal of this methodology is to combine causal accounts with the elimination of rival hypotheses. Mill's Methods of Agreement and Difference allow for the deductive elimination of relevant monocausal and deterministic causal variables from the explanation. Then causal process-tracing allows for the delineation of causal mechanisms, thereby enhancing the internal quality of theory, and congruence-testing allows for the inductive elimination of rival causal claims by demonstrating that they do not operate in particular cases (George and McKeown 1985; Waldner 1999, 234-235). Given the paucity of good theory on foreign aid and development, as well as the lack of solid descriptive accounts of U.S. aid in Egypt and Jordan, this methodology is strategic. Qualitative analysis allows us to unpack the long-unpacked black box of domestic politics in a way that statistical analysis does not, maximizing the internal validity of theory and providing focused historical accounts of the cases in question.

Mill's Method of Difference allows for the elimination of possible causal variables by observing cases with similar initial conditions and different outcomes: "Nothing can be the cause of a phenomenon if the phenomenon does not take place when the supposed cause does (Cohen and Nagel 1934, 259)." The Middle Eastern and East Asian cases display very different institutional outcomes even though they share similar initial conditions, many of which past accounts have designated as causal determinants of the effects of foreign aid. Although the universe of rival hypotheses is infinite, I focus on these variables for elimination.

<u>Large scale foreign aid</u>. Following the lead of scholars writing on oil-based rentier states, several studies of Middle Eastern aid recipients designate large-scale aid as a sufficient condition for the emergence of distributive institutions (Lavy and Sheffer 1991; Knowles 2005). Although levels of U.S. aid, or foreign aid in general, are not exactly equivalent in terms of population, GDP, investment, or government expenditures, there is no question that all four countries have been the recipients of large-scale U.S. assistance.

Between 1947 and 1986 South Korea received $68.6 billion in total economic and military assistance, with economic assistance averaging roughly $1.06 billion until 1976 (USAID

2007).[2] By 1949, the ECA office in Seoul dwarfed its counterparts in Greece and Turkey; the Korean Military Advisory Group (KMAG) employed 500 people; and the U.S. Embassy in Seoul was the largest in the world. From 1953 to 1960, U.S. aid was equivalent to 10 percent of GDP per year on average, financing 70 percent of imports and 74 percent of total investment (Kohli 2004, 76).

Between 1946 and 1976, Taiwan received $37.8 billion in total U.S. aid, with economic aid averaging about $777 million per year through 1965 (USAID 2007). During the 1950s, U.S. aid constituted about 6 percent of Taiwan's GDP on average, and until the mid-1960s, the U.S. financed about 40 percent of gross investment (Ranis 1979, 244-246; Wade 1990, 81-82; Wu 2005, 56). As it had in South Korea, the U.S. also helped to finance and administer the Kuomintang's (KMT) land reform project in the early 1950s (Wade 1990, 76, 83).

Between 1957 and 2006, Jordan received $17 billion in total U.S. aid, with economic aid averaging about $189 million per year. Total U.S. aid was equivalent to about 5.5 percent of annual GDP on average (USAID 2007, World Bank 2007). U.S. leadership in IFIs has also resulted in additional rents for Jordan. The Paris Club forgave $830 million and extended payments on $2.2 billion of Jordan's foreign debt through 1997; the IMF has continually allowed Jordan to sidestep conditionality; and the World Bank has provided several hundred million dollars in loans to implement IMF structural adjustment programs.

The largest and most consistent volume of U.S. aid to Egypt has been delivered since President Anwar Sadat's 1974 rapprochement with the West. Egypt received $94.1 billion in U.S. aid between 1975 and 2006, and is one of the most widely studied cases of U.S. foreign assistance in the world (Abdel Khalek 1982; Burns 1985; Weinbaum 1986; Handoussa 1990; Bangura 1995; Alterman 2002; Mitchell 2002). After signing the Egypt-Israel peace treaty in 1979, Egypt was informally committed about $2 billion per year, $815 million in economic assistance and $1.3 billion in military aid.[3] This arrangement lasted until 1998, when the American and Egyptian governments agreed to reduce economic assistance by 50 percent over ten years, leaving the economic component of the 2008 aid package at roughly $450 million. After Egypt's participation in 1991's Operation Desert Storm, the U.S. and her Paris Club counterparts forgave half of Egypt's external debt contingent on deep reforms and a sharp reduction in the deficit.

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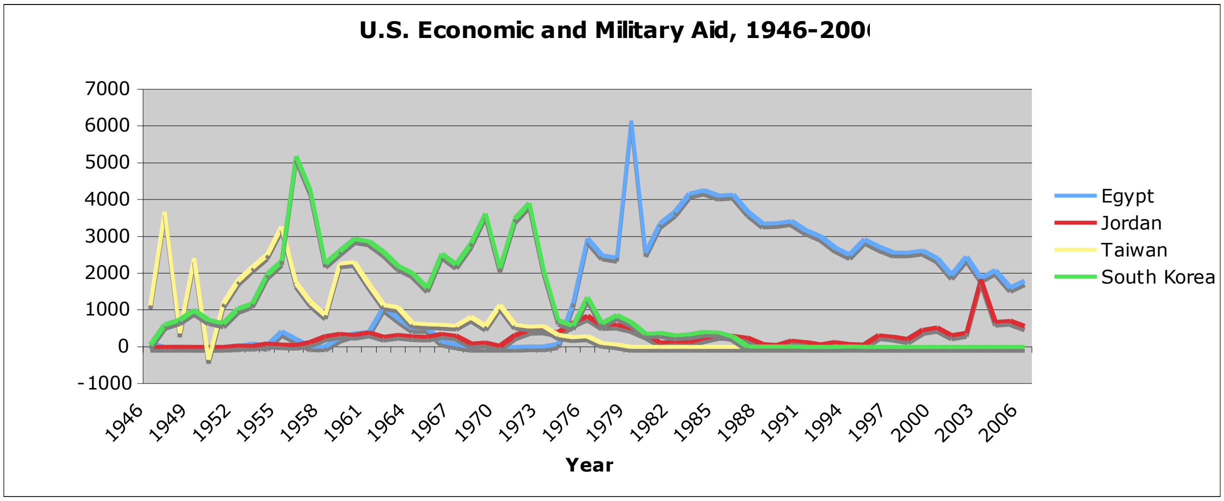
[2] Unless otherwise noted, figures are in constant 2006 dollars to adjust for inflation, allowing a comparison among the four cases, which received the majority of their aid in different periods.

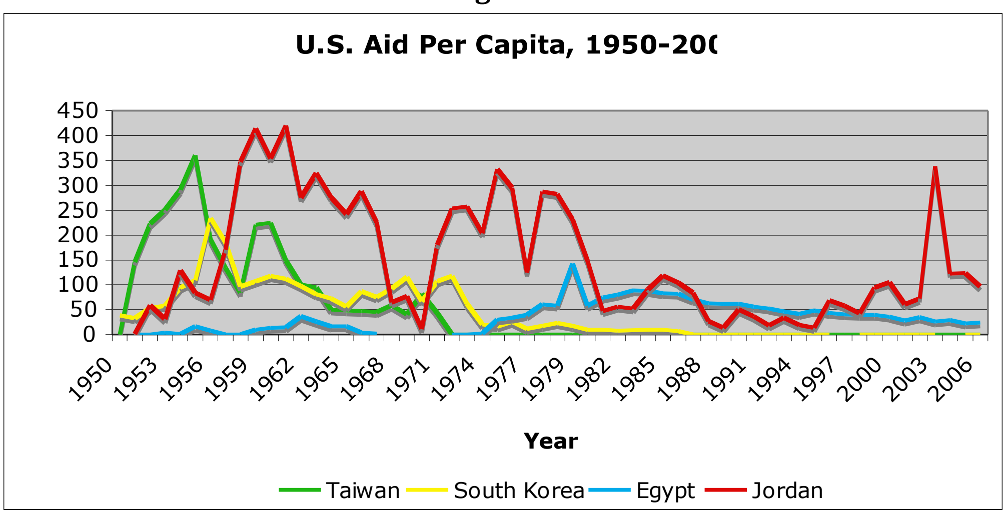
[3] These figures are cited in historic dollars, as the U.S. aid package to Egypt is not adjusted annually for inflation.

Figure 2



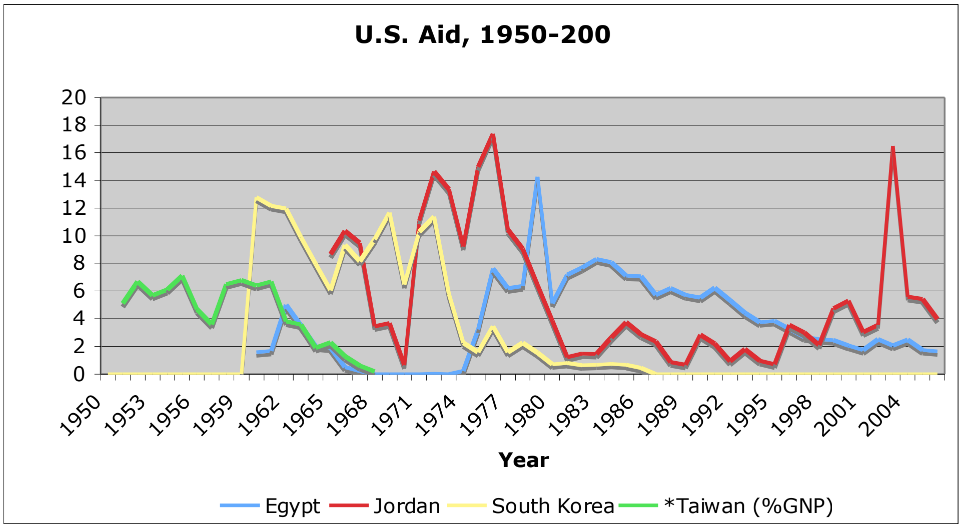
Source: USAID, 2007.

Figure 3



Source: Kuznets 1979; USAID Greenbook, 2007

Figure 4



Source: Scott, 1979; USAID Greenbook, 2008 (*Taiwan figure as percent GNP)

Geopolitical Relevance. Some scholars have suggested that economic and institutional development will be stunted in U.S. allies because of a non-developmental donor agenda (McKinlay and Little 1977, 1978; Maizels and Nissanke 1984; Frey and Schneider 1986; Trumbull and Wall 1994; Alesina and Dollar 2000; Burnside and Dollar 2000, 848; Bearce and Tirone 2007). Continued geopolitical centrality ensures a continued supply of unconditional aid, which allows regime elites to placate rent-seekers and avoid the politically painful process of establishing productive institutions meant to discipline rent-seekers and develop the economy.

From 1947 onwards Korea and Taiwan were vital components of the Truman Doctrine alongside Greece and Turkey, and South Korea's geopolitical salience increased further with the commencement of the Vietnam War. As the largest Arab power, Egypt has played a key role in nearly all aspects of Arab affairs, making it a valuable U.S. ally in terms of the Arab-Israeli conflict and the recent U.S.-led invasions of Afghanistan and Iraq. Jordan's geopolitical relevance has spanned the longest of the four cases, beginning first with its strong stance against pan-Arab socialism in the 1950s to containing the PLO in the 1960s and 1970s to signing a peace treaty with Israel and serving as a partner in the "War on Terror" in the 1990s and 2000s.

By designating four of the top U.S. allies of the past sixty years for comparison and demonstrating that the manner in which their leaders used aid drastically varied, this study negates geopolitical relevance as a central causal variable. Geopolitical relevance is only of secondary importance in that supplies a large volume of aid that is biased in favor of serving coalition requirements for the purposes of domestic stability. Yet it cannot be assumed that all regimes must distribute aid in the short term to a large number of rent-seekers, or that the construction of developmental institutions exerts the same level of political pain in all countries. The manner in which geopolitical relevance influences aid formulation depends on demand side conditions.

Regime Type. Numerous studies have found a statistically significant relationship between democracy and development (see Diamond 1992 for an overview), and the presence of greater accountability and transparency in democracies might lead one to hypothesize that democracies would use aid in a more efficient fashion than authoritarian dictatorships. Alternatively, Bearce (2008) finds that foreign aid provides greater incentive for economic reform in authoritarian regimes.

All four countries, however, were ruled by repressive authoritarian dictatorships during the period in question. South Korea was ruled by a U.S.-installed Korean exile, Syngman Rhee, from 1948 to 1960, and then by General Park Chung Hee from 1961 to 1979. Under U.S. pressure, Park held elections in 1963 under a highly constraining election law, then declared martial law in 1972 (Kang 2004, 22, 99). The KMT, initially headed by the Chiang family, has continuously ruled Taiwan since 1949, and the first democratic election of a president occurred only in 1988, long after U.S. aid ended. Both South Korea and Taiwan maintained large internal security apparatuses that engaged in repressive measures against labor. Since 1952, Egypt has been ruled by a mass political party underpinned by the support of the military.[4] Since the coming to power in 1921, the Hashemite family has ruled Jordan through hereditary succession. Both Egypt and Jordan are highly repressive security states with histories of restricted speech, physical coercion, and internal surveillance. Although national parliamentary elections have occurred in Egypt and Jordan since the 1980s, these elections should not be viewed as segues to democratization (Lust-Okar 2005; Brownlee 2007). The power of Egyptian and Jordanian parliaments is largely restricted to reviewing legislation originated by the executive, and elections are highly distorted in favor of incumbent regimes.

The United States has openly supported each of these authoritarian regimes during the period in question. Despite American officials' complaints of corruption, economic misdirection, and sometimes an intense personal dislike of many of these rulers, the U.S. provided financial and political support on the basis that incumbent regimes would maintain policies conducive to U.S. interests in their respective regions. Authoritarian governments in South Korea and Taiwan used aid for institutional upgrading, while authoritarian governments in Egypt and Jordan frittered it away on distributive institutions. Authoritarianism, then, cannot be sufficient to explain the relationship between aid and institutional outcomes. Rather, authoritarian rulers respond to different coalitions with different preferences.

<u>Neoliberal Conditionality</u>. Drawing upon state-centered theories of late development (Rosenstein-Rodan 1961; Gerschenkron 1962), many political scientists and economists emphasize the detrimental impact of conditionality that requires state retrenchment from the economy (Chaudhry 1994). USAID, supported by embassies and the Foreign Commercial Service (FCS), has actively promoted a neoliberal agenda of state retrenchment in both Egypt and Jordan, which have received the bulk of their aid since 1980. Following this lead, some critiques of aid to developing countries have criticized the inappropriateness of the neoliberal orthodoxy that donors have increasingly propagated (Abdel Khalek 1982; Handoussa 1990). However, three points are worth noting. First, the development agendas pursued by the U.S. in

[4] This party was first known as the Liberation Rally and Arab Socialist Union under Gamal Abdel Nasser (1952-1970), then the National Democratic Party under Sadat (1970-1981) and Muhammad Hosni Mubarak (1981-present).

South Korea and Taiwan in the 1950s and 1960s were more in line with the neoliberal orthodox policies advanced by the IMF and World Bank in later years than with the statist approaches of the time (Amsden 1989, 43). Second, although Egypt and Jordan have entered into structural adjustment programs with the IMF, due to their geopolitical centrality these agreements are often more lax or left unfulfilled (Harrigan, El-Said, and Wang 2006). Third and finally, despite early pressure for state retrenchment, USAID has devoted substantial technical assistance for institutional capacity-building to Egypt and Jordan.

Having eliminated some important possible explanations through the Method of Difference, we can also do the same through the Method of Agreement: "Nothing can be the cause of a phenomenon which is not a common circumstance in all the instances of the phenomenon (Cohen and Nagel 1934, 255)." Aid to Egypt and Jordan has resulted in similar outcomes in that both display some degree of distribution, and likewise South Korea and Taiwan are similar in that they exhibit degrees of developmentalism. Yet one important initial condition differs *within* these pairs:

<u>Market Orientation.</u> South Korea and Jordan, while pursuing highly interventionist strategies, remained fundamentally committed to the private sector as a driving force for late development, while Egypt and Taiwan launched into late development with large public sectors and, in the case of Egypt, full-blown socialism. As such, general market orientation (public or private sector) can also be eliminated as a causal variable.

Mill's Methods thus allow for the elimination of variables that have been employed to explain aid inefficiency in the past: aid volume, geopolitics, neoliberal strategy, regime type, and market orientation. However, the Methods of Similarity and Difference also assume that all variables are accounted for, which cannot be the case in a non-experimental setting. They are therefore only a rough cut at deductive elimination, and need to be supplemented with causal process-tracing and congruency tests, which allow us to delineate causal mechanisms (maximizing internal validity) and compare actual outcomes with rival theoretical predictions (reducing overdetermination), respectively (Waldner 1999, 230-232). These procedures will be carried out in the case study analyses of subsequent chapters.

Aid, Coalition Politics, and Institutional Contributions

This project examines the institutional contributions of U.S. aid to Egypt, Jordan, South Korea, and Taiwan from both the demand and supply sides. The supply side of the argument accounts for how large-scale economic and military assistance from one major donor, the United States, has met coalitional requirements and exerted specific institutional effects within this domestic political framework. The project focuses on the United States because the nature of aid is often donor-specific. The U.S. is the donor most commonly cited as concerned with geopolitics. For each case study the project will demonstrate that U.S. officials were acutely aware of coalition pressures in geostrategic aid recipients, and configured aid to meet these demands.

On the demand side, the composition of authoritarian coalitions has determined the extent to which aid is used for upgrading or distribution. Leaders that based their rule on highly disparate coalitions, such as the Hashemites in Jordan, established institutions of weak domestic extraction, patronage-based public employment, and economic protectionism independent of foreign aid. U.S. aid has contributed to the durability of these institutions, while also creating donor-financed "parallel states" that provide expensive public goods and allow the patronage state to remain in place. Unified and narrow coalitions, however, allow elites remain in power with minimal distribution, thus allowing rulers to use U.S. aid to establish new and efficient institutions. This was the case in Park-era South Korea and Taiwan. Egypt and Rhee-era South Korea fall between these two extremes, exhibiting varying degrees of distribution and developmentalism.

Following the work of Robert Bates (1981, 2001), a fundamental proposition of this project is that rational political action often results in suboptimal institutional outcomes. Identifying a clear set of political conditions that have underpinned aid ineffectiveness helps us move beyond surface-level explanations of "good governance," "corruption," and "the right" macroeconomic policies that plague the field of development economics (Burnside and Dollar 2000; Easterly 2006). It also challenges base claims of "policy autonomy" emanating from the literature on the rentier state. Different authoritarian regimes face different budgetary demands that arise from different coalitions. As a source of state revenue and expertise, foreign aid is incorporated into regime survival strategies. If regimes are politically able to pursue a developmental strategy, they will use aid to upgrade institutions. If regimes must distribute to remain in power, aid will be funneled to distributive institutions at the expense of economic development; it will also be used to build parallel institutions that provide necessary public goods and allow the recipient regime to avoid politically painful institutional reforms.

Independent Variable: Coalition Disparity

Although coercion is an important component of authoritarian regime durability, all rulers depend on the support of a coalition to maintain their rule (Riker 1962; Crystal 1989; Geddes 1994; Chaudhry 1997; Waldner 1999; Bueno de Mesquita et al 2003; Brownlee 2007; Smith 2007). A coalition is comprised of a group of constituencies, which this project conceptualizes as class-based societal actors. The system of mechanisms by which ruling elites maintain coalition support is called a coalition strategy. Coalition strategies are based upon the provision of selective benefits to coalition members and the exclusion of non-members (Waldner 1999). Selective benefits can be delivered on a personal, ad-hoc basis, but in terms of explaining institutional outcomes, it is institutionalized, class-based benefits delivered through constituency clientelism that are the most salient.

The preferences of ruling coalitions engaged in late development have exerted a significant influence on state institutions in the developing world. Although territorial control, extractive capacity, and central bureaucracies were well developed in many Western states before the onset of industrialization, most states in the post-colonial world did not enter late industrialization with these attributes. Institutionalized benefits to coalition members have become part of the overall structure of the state in the realms of fiscal practices, modes of state economic intervention, the nature of the bureaucracy, and state-capitalist relations. Civil and military employment, for example, is a vital kickback to regime supporters in much of the developing world (Geddes 1994). These institutions influence economic outcomes by defining the autonomy of state elites to pursue policies for development, the instruments available to pursue these policies, and the ability of social groups to influence policy (Waldner 1999, 5).

Waldner (1999) finds that the most important feature of a coalition with regards to institutional outcomes is coalition disparity, the degree to which economic policy preferences of class-based coalition members are not unified. If the ruling coalition is large in size and diverse in preferences, the preferences of one coalition member will impose costs upon the other. This necessitates compensation to each coalition member through side-payments, or payoffs delivered for the purpose of maintaining a coalition. Side-payments can be delivered on an ad-hoc, personal basis or through constituency clientelism, whereby institutions are set up to funnel benefits to entire classes. The more disparate the coalition, the more side-payments required for coalitional cohesiveness, and the more costly the coalition is to maintain.

A disparate coalition is usually comprised of a pro-business group, such as merchants or industrialists, and one or more subaltern classes, such as urban or rural labor. Labor prefers higher wages, secure employment, and social protection, which raise factor costs and taxes for business. Business prefers to maximize profits on goods and services and favors state protectionism that raises costs for consumers. While affecting consumers in general, the effects of business preferences are particularly acute for laborers, who spend a relatively large portion of their incomes on consumption. Disparate coalitions like these have been in place in Egypt since 1974 and in Jordan since 1921, requiring elites to dispense large, class-based institutional side-payments as a means of regime preservation. Common side-payments for a disparate coalition include heightened public employment and subsidies for popular classes combined with market protectionism and tax breaks for the business class. These side-payments exert large demands on the budget, and if the domestic tax base is not sufficient, regime elites tend to turn to foreign aid or borrowing—rendering these regimes structurally dependent on foreign aid for survival.[5]

Alternatively, members of unified coalitions have relatively similar preferences and require minimal to no side-payments. Regime elites thus have greater freedom to pursue efficient state-building and economic development with aid. The most common unified coalition, and the type exemplified in this study, is an alliance between industry and a state technocratic elite. Industry can be represented by either state managers in an economy dominated by state-owned industries (SOEs) (Taiwan) or by organized private industrialists (South Korea). In Taiwan, this alliance was held together by a powerful party that oversaw a partnership between technocrats and the managers in the state-owned sector—though this was not the case in South Korea, where Rhee and Park personally cultivated alliances between technocrats and a small number of private conglomerates.

Since the existing work on the rentier state tends to extrapolate coalition size from the sheer presence of external rents, it is important to demonstrate that coalitions originate independently of them. The size of ruling coalitions could be a product of several factors. Waldner (1999) attributes coalition size to elite conflict, claiming that disagreements between elites over integration into the global economy caused them to expand their coalitions as a means of competing with each other. Another perspective, echoed in Kohli (2004) and Peters and

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[5] Another type of disparate coalition could occur between a pro-business faction and landowners hostile to industrialization, though this coalition does not appear in any of the cases in this study.

Moore (2009), charges that coalition strategies are conditioned by the strength of institutional legacies, many of which were left behind by colonial powers. Rulers presiding over weak institutional legacies may need to ally themselves with social groups that can help establish territorial authority, generate revenue, and staff a central state. Both arguments are relevant to the cases examined here.

The Hashemite regime coalition in Jordan is highly disparate and composed of East Bank tribes and merchant-industrialists. This coalition was greatly shaped by the Ottoman institutional legacy—namely, weak to non-existent extractive institutions and exceedingly well-armed Bedouin tribes in the periphery accustomed to a lifestyle of raiding and receiving protection rents. Abdullah I co-opted the Bedouins with civilian and military employment, cash, tax breaks, and land. However, because extractive institutions were so weak, he lacked the financial means to continue delivering tribal kickbacks (Vatikiotis 1967; Aruri 1972, 4; Moaddel 2002, 30-31). Having exhausted his British subsidy, Abdullah allied himself with the East Bank merchant community, which provided him with out of pocket "loans" in exchange for low to minimal income tax, protected markets, import licenses, and monopoly rights (Amawi 1992, 412; Moaddel 2002, 68; Moore 2004, 60-61). Tribal employees in the military and civil service routinely complained of the rise in prices brought about by import monopolies (Amawi 1992, 505-506), while merchants continued to pay high luxury import taxes, dispense "loans" to Abdullah, and be saddled with higher factor costs arising from public employment to tribes. The Hashemites increased benefits to both groups to maintain the coalition and by the late 1950s, the Jordanian state had all of the features of a traditional rentier state, consisting of weak institutions of taxation, a distributive state apparatus, a bloated bureaucracy, economic protectionism, and collusive ties between the state and merchant-industrialists.

The ruling coalition in Egypt under Anwar Sadat and Hosni Mubarak consists of urban labor and an urban bourgeoisie closely linked to foreign capital (Waterbury 1983, 1985, 1993). Their predecessor, Gamal Abdel Nasser, expelled landowners and the urban bourgeoisie from power in the early 1960s and initiated a massive employment scheme for workers in the civil service, military, and bureaucracy. Nasser's populism so inclusionary that it undermined accumulation of surplus for industrial investment, and while Sadat and Mubarak were no more willing to exploit the working class, they reconfigured economic policy so that accumulation would occur through foreign investment, borrowing, and deficit financing, with an alleged focus on export-led growth (ELG). This required a re-incorporation of the urban bourgeoisie into the ruling coalition, which was largely fueled by the use of tax exemptions and special import rights. The urban working class was forced to bear the disproportionate burden of taxation and also paid higher prices as a result of demand-driven inflation wrought by the rapid influx of foreign capital. This prompted additional side-payments to urban labor, such as large subsidy schemes and increases in public sector wages throughout the 1970s and 1980s.

In South Korea, Syngman Rhee presided over a narrow coalition of business elites and bureaucrats, much like his successor, Park, but was known for his collusion with local capitalists and patronage staffing of the bureaucracy. Rhee's problem was that he had little institutional means to implement a developmental agenda in the aftermath of the Second World War, Japanese colonial withdrawal, and the Korean War. Given the weakness of the postwar state (most civil servants under the Japanese colonial state had fled or were persecuted as collaborators) and his reliance on this small elite to reconstruct the economy, Rhee could not expect to curb their rent-seeking and expect to remain in power. However, Rhee kept the coalition narrow by precluding the rise of subaltern classes through land reform and labor repression. The most direct implication of a demobilized peasantry and a nonexistent labor movement was that Rhee was neither compelled to find state employment for lower classes nor to subsidize their consumption. Rhee was thus able to isolate important sections of the bureaucracy from patronage appointments, including the Ministry of Finance, the Ministry of Industry and Trade, and the Bureau of the Budget (BOB) (Woo 1991, Kang 2002, 2004).

Coalitions under the Park regime in South Korea and the KMT in Taiwan were highly unified business-technocrat alliances. Park presided over the same coalition as Rhee and continued to repress subaltern classes, keeping the coalition narrow. Yet Park, unlike Rhee, was able to discipline capitalists. This was done in three ways. First, Park's initially hostility towards business demonstrated to business leaders that they did rely on the state for their livelihoods, and that Park was willing to take it away if business did not provide political support or meet economic performance goals (Woo 1991, 82-84; Kang 2002, 2004).[6] Second, the Korean economy had largely been reconstructed by 1957, rendering Park less dependent on business for reconstruction. Third, the bureaucracy had matured throughout the Rhee era, and the insertion of junta members into management positions injected a common ideology and background into the bureaucracy (Evans 1995, 52).

As an émigré single-party regime, the KMT's coalition was highly unified. When the KMT migrated to Taiwan, it left behind a problematic landlord class that had interfered with state-building on the Mainland and, building on Japanese coercive institutions, established direct control over Taiwanese peasants in the countryside (Waldner 1999, 128-129). The KMT also precluded the emergence of a large native business class; it inherited all former Japanese assets and did not sell, instantly generating the largest public sector in the Free World. With no landlord class to interfere with industrialization plans, few ties to existing social classes, and the thwarting of rival power centers made possible by retaining Japanese property, the KMT thus had fairly wide room to maneuver (Wade 1990, 75, 109). Although alien to Taiwan, the KMT brought a high level of organization and ideological coherence with it from the Mainland, allowing it to insinuate itself into Taiwanese institutions quite rapidly.

Antecedent Condition: Large-Scale Foreign Aid

In the greater body of literature foreign aid is classified as an independent variable. Without severing dialogue with the mainstream literature, this study departs from this practice: it considers aid to be an antecedent rather than an independent variable. Across all four cases I make the stylized claim that the level of U.S. foreign aid is "large-scale," a rough categorization that does not allow for variation in the volume of aid received. U.S. foreign aid is conceptualized in three ways:

[6] In 1961, Park arrested many of the industrialists who had benefited from Rhee's policies under the charge that they had accumulated "illicit wealth." The businessmen were publicly humiliated as they were marched through the street carrying placards. Rhee later struck a bargain with the businessmen whereby they would be released in exchange for meeting output targets and providing political contributions to the ruling party.

Bilateral government-to-government assistance in grants and concessionary loans, economic and military. Economic aid need not be provided for developmental purposes nor even be classified as developmental. Since all four cases faced significant geopolitical threats and would likely have displayed large defense expenditures even in the absence of aid, we can view military aid as fungible to an extent. In addition, military aid is important because it enables exclusion of non-coalition members and, in some cases, supports military involvement in the economy.

International Financial Institution (IFI)-to-Government Assistance. This includes International Monetary Fund (IMF)/ World Bank grants and concessionary loans and Paris Club debt write-offs in cases where U.S. involvement can be shown to be the driving factor behind the aid allocation. As the largest shareholder and the home base of both the World Bank and the IMF, the U.S. exercises significant leverage in these institutions and therefore also indirectly influences Paris Club debt rescheduling and forgiveness (see Krueger 1992, Woods 2006, 15-38).[7] These qualify as cases of single-transfer, large-scale budget support.

Preferential economic transactions. These transactions with the recipient, typically donor government-to-recipient business or donor business-to-recipient business under government intervention, would not occur under normal market conditions, and include donor government procurement of goods and services and private investment.

Existing studies of foreign aid are heavily focused on aid's numerical value, thereby conceptualizing it as direct budget support. Yet in moving the level of analysis to domestic politics and coalition maintenance it is necessary to reconceptualize foreign aid as an input. Foreign aid rarely surpasses the volumes of external rent afforded by oil, yet it is a more diverse resource upon which elites in late developing countries can draw and can far outmatch resources available to the opposition. In this sense, the study of foreign aid is a much more difficult and complex process than the study of oil revenues.

Aid comes from multiple sources. Bilateral, multilateral, and non-governmental donors may have different goals in allocating aid, and may configure aid in ways that best pursue these goals. Some donors provide aid for humanitarian (Lumsdaine 1993; Noel and Therien 1995), ideological, or commercial (Schraeder, Hook, and Taylor 1998) reasons rather than on the basis of geopolitical imperative (Alesina and Dollar 2000). Geopolitically-motivated aid implies donor preoccupation with the maintenance of friendly regimes, and this aid can generally be viewed as highly fungible and disbursed with minimal conditionality, much like oil rents. The fungible nature of this aid allows regimes to meet coalition demands easily. By contrast, European and Japanese donors have configured aid for more developmental goals, tying aid to specific projects that generate little direct budget support.

As such, aid also comes in many forms, and should be examined in terms of both its volume and its constituent parts. Aid can be delivered as government-to-government budget support, much like oil revenues; as a program, which creates a group of beneficiaries over the long-term; or a project, such as building infrastructure or providing targeted sectoral support in the short-term. Unlike oil revenues, aid also comes hand-in-hand with organizations and the

[7] The Paris Club requires recipients to reach an agreement with the IMF before it will reschedule or forgive debt.

people that staff them. Aid provides not only financial but also technical resources that might not be available in the recipient country. Recipient governments are thus empowered to allocate or withhold diverse sources of technical assistance. The manner in which they do so has important institutional implications.

Dependent Variable: Institutional Contributions

The dependent variable, broadly defined, is "institutional contributions." This is an umbrella term for two distinct dependent variables, institutional origins and institutional durability. With reference to these four cases, this project is interested how and why U.S. aid has sustained and/or created state institutions that are key to economic development. Borrowing from Waldner (1999), there are four categories of institution with which this project is concerned:

Fiscal practices. These are government taxing and spending practices. Taxes can be broken into direct revenue, which taxes internal economic activities, and indirect revenue, which taxes trade. Spending can be broken into current and capital expenditures. Current expenditures include subsidies and other welfare transfers, as well as the salaries of public employees.

Modes of State Economic Intervention. While fiscal practices exhibit the financial means by which states interfere in the economy, this category expresses the broader frameworks by which they do so. State economic intervention can be conceptualized as national industrial policies or sectoral promotion policies and their corresponding implements, such as ownership (private or public), trade policy (tariffs, licenses, quotas, tax breaks, preferential trade), monetary policy (interest rates, money supply, and exchange rates), and property rights.

Nature of the Bureaucracy. This refers to the organization of the state, particularly at the national level. Most important are the "autonomy" of the state from rent-seekers, such as business or labor, and, relatedly, the manner in which bureaucrats are appointed and promoted. Developmental states, such as those in East Asia, display bureaucratic organization close to the Weberian ideal-type. They are, to a degree, autonomous from different societal groups, which are assumed to be rent-seeking (Krueger 1974; Bhagwati 1982; Olson 1982). Qualified technocrats that are hired and promoted based on merit, and compensated with salaries competitive with the private sector, staff the civil service. Sanctions for corruption are clear and well-enforced. A pilot agency tends to spearhead and coordinate most development efforts. Most notably, a state elite is singularly devoted to the pursuit of economic development, and it directs a fiscal policy that is based upon capital accumulation and production, not redistribution (Waldner 1999, 144).

State-Capitalist Relations. This refers to the nature of the relationship between capitalists and the state, encompassing information flows between the two parties as well as the relative balance of power between them. As Evans (1995) has pointed out, states that are fully autonomous from society cannot be developmental: they lack vital exchanges of information with the private sector, as well as the ability to decentralize implementation (Evans 1995, 158; Schneider and Maxfield 1997, 5). Developmental states, then, also have intensely close linkages with capitalists, a phenomenon known as "embedded autonomy." While business is still assumed to be rent-seeking, developmental states carve out autonomy through their ability to discipline business, particularly industry.

The fundamental link between aid and institutional contributions is the notion that foreign aid is incorporated into a broader framework by which institutions are constructed to deliver benefits to coalition members. Aid can make institutional contributions in two different ways. First, to the extent that it can be considered fungible (or that it is actually delivered as direct budget support), aid supports the general budget and its various political priorities ("budget support"). For example, if a recipient receives $200 million for a water project that the state would have undertaken anyway, $200 million of other revenues can be freed up for expanding the civil service or supporting an inefficient state-owned enterprise (SOE). The $200 million in project aid is therefore equivalent to $200 million in cash budget support. Second, aid can be tied to specific programs or projects ("targeted aid"). For example, USAID might provide the funds and staff for a special economic zone, support a microfinance project, or provide technical expertise for a trade agreement. Some aid encapsulates both targeted aid and budget support, especially more complex, multi-component programs like the Commodity Import Program in Egypt or the cash transfer programs in Egypt and Jordan.

Table 1 provides a summary of potential institutional contributions in fiscal policy, modes of state economic intervention, business-state relations, and the nature of the bureaucracy. The institutional contributions are divided by whether or not aid was used for upgrading (white) or for distribution (gray); whether or not the specific institutional contribution is an instance of genesis or durability will vary by case. Table 1 demonstrates the same types of aid can make different institutional contributions depending on the coalition strategy of the recipient regime, particularly in the case of budget support.

Table 1
Foreign Aid and Institutional Contributions

	Type of Aid	
Type of Institution	Budget Support	Targeted Aid
Fiscal Policy	• Reduce domestic revenues by reducing the need to tax various segments of the population.	• Donor-financed project aid, particularly in infrastructure, relieves the state from extraction.
	• Tax policy remains unaffected while additional foreign revenue is used for long-term developmental projects, such as infrastructure,	• Adjust levels of taxing and spending towards optimal levels through conditionality. • Meet optimal levels of taxing and spending based on technical assistance
Modes of State Economic Intervention	• Support inefficient state-owned enterprises. • Allow for preferential tax breaks and subsidization of industry and consumers.	• .
	• Support efficient state-owned enterprises. • Allow the state to invest in large-scale infrastructure, health, and	• Trade liberalization or structural adjustment through conditionality and/or technical assistance. • Empower local stakeholders in favor of

	education as a public good.	economic reform with financial and/or technical assistance
Nature of the Bureaucracy	• Provide funds for superfluous public employment, possibly based on patronage. • Cause taxation and information-collecting institutions to decay by reducing incentives to tax.	•
	• Provide funds for higher salaries, allowing the state to hire a limited number of qualified applicants.	• Engender civil service reform or other bureaucratic change through conditionality and/or technical assistance. • Enrich local bureaucracy through sustained collaboration and knowledge transfer between donor and recipient • Train local experts that are absorbed into the recipient bureaucracy. • Create "pockets of efficiency" within local bureaucracy through unsustainable hiring practices and donor-funded technical units.
State-Capitalist Relations	• Discourage institutionalized interaction between the state and capitalists by providing disincentives for taxation of capital. • Discourage development of domestic industry as a means of funding state revenue by providing external revenue.	• Undermine credibility of local business associations through conflicting aid projects and programs. •
	• Elevate state as a provider of capital to business, giving it leverage over business actions.	• Strengthen communication between the state and business by providing technical and financial assistance for peak and sectoral business associations. • Strengthen local capital by helping it forge alliances with foreign capital. • Strengthen position of state vis-à-vis rent-seekers in the private sector. • Suppress popular classes through assistance to police forces.

A final type of institutional contribution is not fully captured in Table 1. Rentiers and semi-rentiers experience severe coalition demands that result in state inefficiency, most importantly limited domestic extraction and an unqualified and bloated bureaucracy. These institutional traits seriously circumscribe the ability of the central patronage state to provide a range of public goods to society, including infrastructure, which is expensive to build and maintain and requires a competent set of engineers for planning, building, and maintenance, as well as a reliable system of property rights and regulations that impose minimal transaction costs on business. Infrastructure and certain categories of public goods are absolutely necessary in all countries, yet states governed by disparate coalitions would be unable to provide them without rulers risking political demise by altering their existing coalition strategies.

Geopolitically-motivated donors, such as the U.S., are acutely aware of coalitional pressures and configure aid as such. This “two-way” effect affects many aspects of aid formulation, but it is most evident in the willingness of the U.S. Agency for International Development (USAID) to set up in geopolitical allies “parallel institutions” that provide necessary public goods while allowing the politically vital patronage state to remain in place. Parallel institutions require longstanding commitments for financial and technical resources that geopolitically irrelevant states would be unable to extract. These are instances where U.S. aid interacting with domestic politics can account for the origination of a specific institution. *In these cases the United States as a donor provides the institution*.

One type of parallel institution provides infrastructure. Putnam (1993) and Brautigam (1996) designate level of service provided by the government, such as percentage of the population with access to electricity, as an indicator of state capacity. Yet as Kamel (1999, 4) points out, in many LDCs these functions are provided by donors. Donor provision of infrastructure is thus an important focus in this study, as this practice indirectly supports the patronage state by allowing aid recipients the luxury of maintaining it.

Bureaucracies must originate, coordinate, and monitor development projects and make sure that they are sustainable. Yet many developing country bureaucracies face what Kahler has coined “the orthodox paradox,” whereby a bureaucracy that is the root of many economic woes is ultimately the entity tasked with fixing them (Evans 1992, 140). Bureaucracies are not self-reforming, and reform efforts can be constrained by domestic politics and resource requirements. These obstacles render the presence of an external agent (i.e., a donor) important (Kame1 1999, 8).

A second type of parallel institution thus serves as a “pocket of efficiency (Evans 1995)” that services businesspeople. Pockets of efficiency are primarily donor-financed and staffed, semiautonomous government agencies that provide first-world service in a third-world environment. They enforce property rights, cut through red tape, and may even preside over entire parallel segments of the economy, essentially running a liberal market operation in an otherwise state-dominated economy. These institutions are part of the recipient’s state, being embedded in local ministries and employing local staff. After agreeing on the uses of the money (number of staff to be hired, office equipment, transportation costs, etc), the donor makes a large lump-sum transfer to the recipient government, which then uses the money to hire qualified personnel at market-competitive salaries, as well as to provide them with any necessary office and logistical support. These local hires may be supported by massive, open order technical assistance projects supplied by the same donor. Pockets of efficiency may also be supported constituencies within society that benefit from their services and support their continued existence. In many cases, the donor may even help strengthen these constituencies through work with local business associations, providing them with greater institutionalized access to the state (Schamis 1999; Ozel 2003) and greater organizational capacity and resources.

The significance of parallel states in the larger aid literature has yet to be recognized, and within the scholarship on political development they have passed entirely under the radar. Although the term “parallel state” is new, great powers, both as modern donors and historical colonial powers, have engaged in the construction of these institutions at varying points in time and across a diverse geography; the four cases in this study are simply prominent examples.[8] These practices are widespread and they have important implications. Not only are large swathes of state functions being performed by external entities in many countries, the presence of parallel states allows distributive regimes to avoid politically-painful institutional reforms at the national level. In one sense, parallel institutions represent an efficient use of aid. Yet in another sense they allow inefficient, distributive practices to persist (and in many cases, aid also contributes to the durability of these institutions as well).

Case Summaries

South Korea (Rhee)

Syngman Rhee's rule is usually described as a brief respot between the efficient and strong Japanese colonial state that fell in 1945 and its resurrection under Park in 1961. Although Rhee did try to exact large amounts of U.S aid, employ patronage to staff large sections of the bureaucracy, and allocate project aid on a highly personal basis, his rule should not be measured with a neoliberal stick. Rhee was able to make some real institutional advances because he presided over a narrow coalition of business elites and bureaucrats that was not much different from that of Park. The most direct implication of a demobilized peasantry and a nonexistent labor movement was that Rhee was not compelled to find state employment for lower classes, nor did he have to distribute aid to them as a side-payment. Rhee was thus able to isolate important sections of the bureaucracy from patronage appointments, including the Ministry of Finance, the Ministry of Industry and Trade, and the Bureau of the Budget (BOB). U.S. advisers trained employees in the BOB, which was linked to the U.S. mission through the Combined Economic Board, and also worked in conjunction with Japanese advisers to fill most bureaucratic positions with qualified Koreans who had taken the Japanese civil service exam (Kohli 2004, 64). While Rhee did not retain former Korean managers from the Japanese colonial period (as they were seen as collaborators), he did leave them in state bodies related to taxation. During Rhee's rule, direct taxes constituted between 25 and 34 percent of domestic revenues, substantially more than other developing countries at the time (Kohli 2004, 60).

Additionally, because he did not have to respond to demand for side-payments from a broad coalition, Rhee was free to devote full attention—and significant quantities of U.S. aid-- to a small number of Korean industrialists, using preferential allocation of former Japanese holdings and U.S. project loan aid to build up a concentrated domestic industrial base. This occurred most notably in the textile industry, which was used to jumpstart export-led growth under Park (see Amsden 1989). Rhee maximized recipient benefits of the American loans by maintaining an overvalued official exchange rate, and profits could be made from exchange rate differentials on ICA project loans (Woo 1991, 68). In return, these businessmen made substantial donations to Rhee's Liberal Party (Woo 1991, 68-69). It was Rhee, then, who created the *tri-pé* role for the state as a mediator between foreign capital and a small number of local industrialists.

Finally, Rhee was able to avoid or delay persistent American efforts to impose liberal policies that would retrench the state's role in the economy. Rhee saw that the U.S., for

[8] Brazil's National Bank for Economic Development (BNDE), a semiautonomous state investment vehicle, was formed as a result of recommendations from the Joint Brazil-United States Mission (1950-1952), and in the 1960s received a great deal of its revenue from PL 480 counterpart funds (Baer and Villela 1980).

geopolitical reasons, wanted to re-integrate South Korea as a subordinate member into a resurrected Greater Asian Co-prosperity Sphere led by the Japanese (Woo 1991, 52-55; Cumings 1987, 307). He resisted. By maintaining an overvalued exchange rate and a policy of industrial protectionism towards a small number of businessmen, Rhee advanced a program of import-substitution industrialization (ISI) in the face of staunch American opposition.[9] Economic aid peaked in 1956 at $322 million, and was gradually reduced upon the basis that (1) reconstruction was coming to an end; and (2) aid was supporting ISI (Davenport 1960, 2). The fact that Rhee took these risks (and that the U.S. saw a reduction in aid as politically feasible) indicates that, relative to Egypt and Jordan, Rhee's regime was not structurally dependent on aid for survival—he did not need large volumes of aid to meet coalitional demands.

South Korea (Park) and Taiwan

Freed by unified coalitions, Park-era South Korea and Taiwan used U.S. aid to establish new, more efficient institutions. Technical assistance was assimilated into powerful, home-grown pilot agencies that coordinated the development agenda. Loans and grants were used to elevate the state to the position of a powerful intermediary between local business and foreign capital, allowing the state to punish rent-seeking and reward good performance through the power of the purse. Financial assistance was devoted to long-term capital expenditures such as education and agricultural extension services, though attention was also paid to cultivating domestic funding for these projects. Aid was used to suppress popular classes in order to keep the coalition narrow and factor costs down. Finally, developmental regimes were not highly dependent on the immediate and widespread distribution of foreign aid for political survival, and were able to reject donor conditionality that they perceived as antithetical to their political or economic interests.

However, the timing and extent of U.S.-backed economic reform varies slightly between the two cases. Although Park eventually pushed through several exchange rate devaluations and trade liberalization upon American recommendations, there were some aspects of state intervention that he refused to relinquish, namely the personalistic distribution of foreign capital and aid projects, as well as export subsidization. As a result, U.S. economic aid dropped from $234.5 million in 1969 to $36.7 million in 1975, then was phased out completely in 1982. As economic aid was reduced, the U.S. mission came strongly behind the IMF and even threatened to withhold Development Loan Funds and PL 480 aid until the Korean government adopted the IMF policy reform package. The recommendations included currency devaluation, abandoning export subsidies, and placing ceilings on foreign loans (Woo 1991, 110). With the exception of reducing export subsidies, the Koreans eventually "swallowed the IMF pill (Woo 1991, 110)," causing a major uproar from the *chaebol*. In 1971, the Federation of Korean Industries (FKI) appealed to Park to freeze the curb on foreign loans, decrease interest rates, and reduce corporate tax. When Park did not act, the FKI became aggressive, telling Park that he would have to slash the government budget by half unless he acceded to their demands (Woo 1991, 111-112). Park eventually orchestrated a massive bail-out in 1972.

[9] Whatever liberal policies Rhee did enact, such as two exchange rate devaluations and a short-lived privatization of the banking sector, were delayed and the product of much struggle between Rhee and the U.S. mission (Amsden 1989, 44-48).

U.S. pressure for economic reform in Taiwan was much more successful. The advice of U.S. consultants is widely credited for Taiwan's 1958-1962 move towards export-led growth (Little 1979, 174; Cumings 1987, 71). Between 1958 and 1961, the exchange rate system was dismantled and replaced with a significantly devalued unitary rate. Tariffs were reduced and import controls eased. In 1960, the government enacted the famous Nineteen Point Policy Reform, which contained a number of recommendations from the U.S. and the IMF intended to reduce inflation, decrease the budget deficit, and control the money supply (Wade 1990, 84, 88, 94).[10] These liberal policies were not forced by conditionality, but couched by political support from the highest levels of the regime (Lundberg 1979, 269).

The general consensus is that Taiwan was "more dependent" on American aid and thus had to follow recommendations to a greater extent than did Korea. However, there is substantial evidence that Chiang and his technocrats sided with the Americans at the outset rather than having conditionality hoisted upon them. Since the KMT party was highly unified around Chiang, who favored reform in pursuit of growth, and the party controlled the vast majority of the productive sector, reform policies faced little opposition. In South Korea, by contrast, there was a great deal more opposition to the policy reform package, chiefly because the Park regime had allied itself with a small group of capitalists that benefited from ISI policies under Rhee and which would be hurt by liberalization measures. Park was ultimately able to implement the policy reforms, but they were much-delayed and followed by a massive corporate bailout. Narrow coalitions ultimately allowed both regimes to push through the major reform schemes being advocated by their countries' respective U.S. aid mission; had these regimes also incorporated popular sectors there is no way that reforms reducing market protectionism and a reduction in state spending would have been feasible.

Jordan

U.S. aid to Jordan has been delivered mostly in the form of budget support and infrastructure projects. Jordan has used U.S. aid to sustain distributive institutions that deliver side-payments to tribes and the East Bank economic elite, including public employment, weak extraction, state-owned industries, and consumer subsidies. Between 1961 and 1975, military employment tripled and civil employment increased by two-thirds (Tal 2002, 75; Moore 2004, 68). The state grew even larger during the 1970s, when U.S. aid was briefly overtaken by that of the Gulf petromonarchies. Between 1970 and 1985 the size of the civil service increased by 300 percent, and by the mid-1980s, the state employed 50 percent of the labor force, the equivalent of one public servant for every ten children in Jordan (Piro 1998, 66-67). During this time aid constituted as much as 86 percent of central government revenues (Bint Talal 2004: 59; Carroll 2003: 35; Moore 2004: 104; World Bank 2007). When the U.S. re-assumed the role of major donor in the mid-1980s, aid conditionality had become the norm, yet the U.S. continued to provide aid free of conditionality. Even after a massive financial crisis in 1989, when Jordan was forced to begin a long string of agreements with the IMF, USAID did not significantly re-focus

[10] At the same time, however, state involvement in export promotion grew. Exports were promoted through customs rebates on intermediate goods to be used in export production, tax incentives, cheap credit, and direct subsidies. Additionally, regime imperatives to preclude the development of alternative power centers in private industry trumped any American recommendations in favor of large-scale privatization. We thus should not over-exaggerate the success of American free-market pressure (Wade 1990, 52; Waldner 1999, 130).

its strategy toward structural adjustment and bolstering the private sector, which had been weakened by decades of collusion between the state and a small elite.

Even after the accession of Abdullah II, widely considered to be a reformer, larger and larger portions of U.S. aid have been committed to the cash transfer program, which provides budget support for various regime priorities. These priorities remain distributive. Although down from 69 percent in 2001, in 2006 compensation of employees still accounted for 40 percent of government expenditures. Subsidies have risen from around 12 percent of expenditure in the mid-1990s to 38 percent in 2005 and 31 percent in 2006. Many of these subsidies and transfers apply only to civil service or military employees, an effort to protect them from a general retrenchment of food and energy subsidies, roaring inflation, and the imposition of a value-added tax. Jordan still remains highly dependent on foreign aid, which financed 42 percent of government expenditures in 2003 and 12 percent in 2006.

While the local bureaucracy was used as a means of political patronage and public largesse, the Point Four/ USAID and U.N Refugee and Works Agency (UNRWA) bureaucracies grew in parallel to the Jordanian rentier state, performing essential state functions but never making an attempt to engage Jordanian institutions in meaningful reform (Kingston 2001).[11] Point Four built a significant portion of Jordanian infrastructure in the 1950s and 1960s, including transport networks, hydraulic infrastructure, and basic institutions in health and education. This practice was continued by Point Four's successor, USAID, and has freed Jordanian elites from undertaking politically painful institutional reforms to expand domestic revenue and rationalize the bureaucracy, but it has also rendered Jordan practically dependent on donors for infrastructure. To this day, USAID has funded the maintenance of infrastructure, particularly in the water sector, because the Jordanian state cannot do so itself. More recently, USAID has assisted in the establishment of "pockets of efficiency," such as the Jordan Investment Board (JIB) and the Aqaba Special Economic Zone Authority (ASEZA) around Jordan's only port. Both institutions help investors cut through red tape and are staffed with qualified technocrats earning market-competitive salaries. They service narrow slivers of the economy that either (1) attract more rents for the state, such as port areas; and/or (2) benefit a segment of the East Bank economic elite that has developed ties to Gulf capital.

Egypt

As in Jordan. Egyptian rulers have had to answer to a disparate coalition of labor and business. Yet while Jordan's East Bank industrialists are inward looking and have few links to foreign capital, Egypt's post-1974 "infitah" bourgeoisie has intimate connections with multinationals. Since the 1970s, U.S. economic aid has helped the Egyptian regime maintain a dual system: an inflated public sector whose institutions deliver side-payments to lower and middle classes, and a parallel set of institutions aimed at a small number of capitalists in the private sector.

These dual needs were met from 1975 to 1992 through the Public Sector Commodity Import Program (CIP), which allowed public *and* a small number of private sector parties to

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[11] UNRWA is considered here due to the central role of the U.S. in its creation and relatively large U.S. contributions to the organization. U.S. policymakers viewed UNRWA as an explicit vehicle by which infrastructure could be provided to Palestinian refugees without encroaching on East Bank patronage networks.

contract low-interest loans for the purchase of American commodities and capital goods. The loans were then paid back to the Egyptian government in local currency as a form of budget support. From 1975 to 1992, the Public Sector CIP accounted for $7.6 billion of total economic aid, and had nourished a small capitalist class with collusive ties to the state (Weinbaum 1986, 42). Once the CIP became increasingly oriented to the private sector in 1986, and totally exclusive to it in 1992, it extended to a broader group of beneficiaries. By the time the Private Sector CIP was terminated in 2008, it had provided $3.6 billion in financing to over 1,850 Egyptian private companies over a series of more than 12,000 individual transactions ("Private Sector CIP"). Known as the "*infitah* class" or *hitan* ("whales"), this small group of businessmen still forms the core of the capitalist class today, and many of their needs have continued to be serviced by U.S. project aid (Sfakianakis 2004). Most notably, USAID has also provided support to the American Chamber of Commerce in Egypt and the Federation of Egyptian Industries, the former of which has served as an informal rallying point for the formulation of economic policy—particularly economic reforms. A quick survey of American Chamber of Commerce members, key economic ministers of the past fifteen years, and businessmen that have utilized the CIP reveals a striking overlap (Anonymous Interview, 12/23/2007).

Much like its use of the CIP in the pre-1991 period, USAID has continued to provide assistance to the private sector while also supporting the Egyptian budget—and therefore a large public sector. No other USAID program better exemplifies this principle than the cash transfer program, which commenced in 1984.[12] Beginning in 1992, USAID started attaching formal "benchmarks" to the cash transfer program; over the years, these benchmarks have touched on all aspects of economic reform, ranging from privatization to regulatory reform to feasibility studies. While there is little evidence that benchmarks force reforms through a conditionality mechanism, the program has two other benefits. First, the cash transfer operates in conjunction with various technical assistance projects that help the Egyptian ministries in implementing reform benchmarks. Second, the cash transfer program is a stealthy vehicle for direct budget support. Thus, while the cash transfer supports economic reform in theory, it also supports Egyptian budget priorities in favor of the public sector.

By 2000, the GOE had privatized only 29 percent of SOEs, a number of which were bought up a rock-bottom prices by well-connected businessmen within the NDP (Sfakianakis 2004, 85-86). Patterns in public sector largesse have also exhibited very little change. In 1997, the government instituted an optional early retirement scheme for public sector employees, but only 182,000 bought into it (IBM Consulting 2004, 17). Compensation of employees, which has averaged roughly 30 percent of expenditures, has shown no general decline between 1990 and 2006. Subsidies have actually increased from 12 percent of expense in 1991 to 33 percent in 2006 (World Bank 2007). Facing rising inflation, the proposed FY 2008-2009 budget included a 30 percent increase in public sector wages and subsidies (Abdel-Razek 2008).

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[12] Roughly $200 million per year is set aside annually for the cash transfer, whose share of economic aid has risen as funding for project aid and CIP has drawn down. The cash transfer program has been assumed under a number of titles: Sector Policy Reform I, II, and II (1992-1994, 1995-1997, 1996-1998, respectively); Development Support Program I and II (1999-2002, 2001-2009) ("USAID Status Report," 1990, 1998). For an excellent overview of each program and its associated benchmarks see Salim (2006).

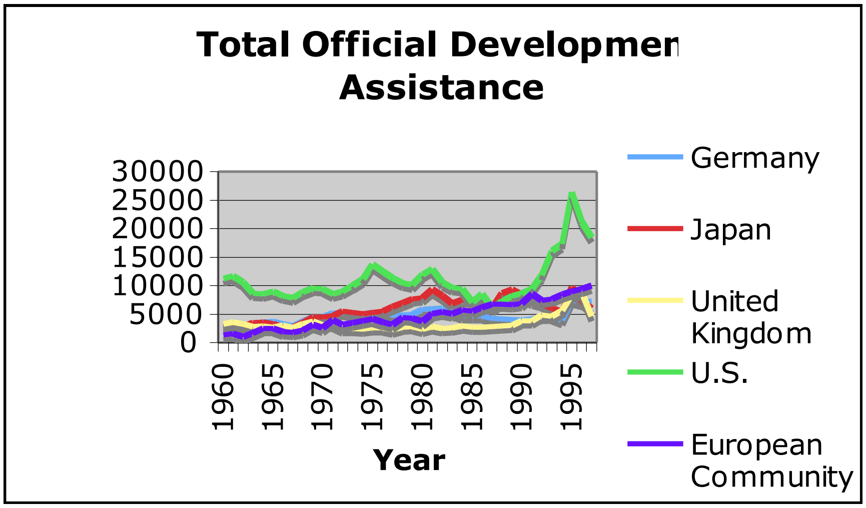
To implement the highly technical economic reform benchmarks without addressing the political dynamite of civil service reform, the U.S. and other donors have worked outside of the system. In the late 1990s USAID adopted an Implementation Letter Mechanism (ILM) by which salaries of employees in special "technical units" at key economic ministries would be indirectly financed by USAID at private sector rates. In 2007, American ILMs financed the salaries of twenty to twenty-five staff at the Central Bank and almost all of the sub-governors, ten to twelve senior advisers at the Ministry of Finance, thirty staff at the Ministry of Investment (distributed primarily among the Capital Markets, Insurance, and Mortgage authorities), and seven to eight staff at the Ministry of Industry and Trade through (Anonymous Interview, 5/10/2007). Americans consultants contracted by USAID—namely the behemoth Technical Assistance for Policy Reform Activity I and II projects implemented by Chemonics International and Bearing Point, respectively—provide additional support to the technical units. As one technical unit head claimed of regular civil servants, "Leave them to drink their coffee, read their newspaper, and catch the bus before 1 o'clock (Anonymous Interview, 12/12/2007)."

Chapter Layout

The case studies set forth in subsequent chapters will demonstrate that the composition of recipient coalitions best explains the institutional contributions of U.S. aid to Egypt, Jordan, South Korea, and Taiwan. Chapter 3 discusses the rise of unified conservative coalitions in South Korea and Taiwan against Japanese institutional legacies and, in the case of South Korea, U.S. military occupation. It then explains how these narrow coalitions used U.S. aid for institutional upgrading yet were able to buck American conditionality at times. Chapter 4 discusses the origins of disparate coalitions and their preferences in Jordan and Egypt; this chapter does not include a discussion of U.S. aid. Rather, the purpose of this chapter is to both demonstrate that these coalitions did not emerge as a result of access to external rents as is posited by rentier theory, as well as to explain the origins of institutions that aid perpetuated in future years. Chapters 5 and 6 discuss the role of U.S. aid in maintaining disparate coalitions and corresponding distributive institutions in Egypt and Jordan, with additional detail into parallel institutions that provided infrastructure for both countries. Chapter 7 addresses the impact of U.S. aid during the period of neoliberal economic reform in Egypt and Jordan. It examines how neoliberal conditionality has affected Egyptian and Jordanian institutional side-payments in the context of continued geopolitical centrality and access to U.S. aid, arguing that aid has served two purposes. First, it has maintained old distributive institutions, and in some cases, helped regimes court new sources of rent that might replace foreign aid and loans. Second, it has established "pockets of efficiency" that manage limited economic reforms that benefit a small group of winners from these policy changes while imposing minimal costs on potential losers within the coalition.

Focusing on such a highly clientelistic relationship between donor and recipient may hinder the argument's generalizability, an issue that I address in the final chapter. However, given that the U.S. is still the world's largest bilateral donor in raw terms (see Figure 5), these four recipients and the highly fungible nature of their aid are likely not unique. Israel, as well as the more contemporary cases of Afghanistan, Iraq, and Pakistan are high-profile, policy-relevant cases that surely share a similar relationship with the United States and its foreign aid programs.

Figure 5



Source: Organization for Economic Cooperation and Development, 2008.

This project makes two major contributions to the study of foreign aid and institutions. First, it adds additional layers to the literature of the "rentier state." By tracing the route of U.S. aid from donor to coalition member, highlighting institutional contributions along the way, the project challenges the traditional notion that access to unfettered external rents elevates the state to a position of autonomy relative to society. Rather, aid accrues to specific coalition members who, for various reasons, have been able to see their economic policy preferences become reality. Furthermore, the project explicitly attributes the origins of recipient coalitions to factors other than the presence of foreign aid. Second, the project generates new information on the origins and functions of parallel states in aid recipients. These states allow patronage institutions to remain in place, yet provide infrastructure and minimal transaction costs for limited sectors of the economy. The study of parallel institutions could spur a new and exciting research agenda, particularly within the literature on economic reform.

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