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U S EXPORT-IMPORT BANK LOAN GUARANTEE FOR RUSSIA

A CASE STUDY OF BUREAUCRATIC POLITICS
AND NATIONAL SECURITY INTERESTS

CORE COURSE 3 ESSAY

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Course 3, The National Security Policy Process
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Introduction

Just as the Armageddon clock at Northwestern University was poised seconds from nuclear winter, an epochal change swept the cold war world. The fierce, maniacal Soviet bear suddenly lay down like a lap dog, panting with belly exposed and eyes begging for entrance into the warm house of free enterprise.

In response to this upwelling in world order, the Clinton Administration reshaped national security strategy in order to engage the world's nations and enlarge the community of democracies. Central to the Administration's strategy of engagement and enlargement is expanding the global marketplace. Intertwining the economies of the world is aimed at pacifying the planet by reducing the utility of the military instrument of foreign policy. A key priority in the Administration's foreign policy is to stabilize and transform Russia's economy in order to avoid another Armageddon death watch.

Just a few years ago it was inconceivable that a US vendor of high-tech, war transferable wares could do business with the Soviet evil empire, but the new national security strategy not only beats our swords into plowshares, but it then sells them to our former adversary. One case is the pending sale of US-built jet engines and avionics to Russia for the Ilyushin Design Bureau's IL-96M, their first commercial jumbo jet. From a national security policy perspective, the venture is vital to bolstering Russian stability. All that is required to pluck this historically ripe opportunity is for the Export-Import Bank of the United States to provide a loan guarantee for the \$1 billion deal.

A decision to consummate the loan guarantee seems simple enough, being both rational and synchronized with the Clinton Administration's national security strategy. However, competing interests in the public bureaucracy precludes a rational decision purely to advance national security interests. This paper examines how action on a national security issue is affected by competing interests in and around the government bureaucracy. To this end, the paper analyses Pratt and Whitney's loan guarantee request. The analysis is made in the context of Graham T. Allison's bureaucratic politics model to show that policy is a product of compromise resulting from competition among organizations, rather than a product

of monolithic decision makers. First, the paper describes Allison's bureaucratic politics model. Next, the story of the Pratt-Illusion venture is unfolded to inspect the players who took an active interest in the outcome. The paper then offers several observations, conclusions, and lessons from the case at hand concerning the effect of bureaucratic politics on national security interests.

The Bureaucratic Politics Model

Like the Clausewitz dictum that in war "simple things are difficult," Graham Allison presents a parallel for the peaceful workings of the public bureaucracy. A simple decision to provide a loan guarantee is difficult. Allison explains that organizational leaders who provide policy for such decisions are not a monolithic group but separate players in a competitive game. Their behavior produces outcomes in bargaining games. Policy is therefore not the product of rational decision making but rather the result of compromise, coalition, confusion, and competition. Importantly, the players are not unified by a single set of aims. Instead their behavior varies according to individual conceptions of national, organizational, and personal goals (69). Morton Halperin explains that organizational self-interest dominates behavior. In negotiations among organizations, each prefers an agreement which allows it to pursue its own interests even if the policy outcome is inefficient or uncoordinated. (Halperin 53). Finally, Allison points out that the players are also people. Each player comes to the table with baggage, including sensitivities, commitments, personal standing, and debts. All influence bargaining and the blend of policy comprising the outcome (Allison 72).

As we now turn to our case analysis, the background discussion searches for the elements of the Allison Model. In order to understand the bureaucratic political nature of the outcome, each player's position is illuminated according to six categories of related interests: national security, domestic economic, business, labor, existing policy, and political.

Background on the Pratt-Ilyushin Venture

Westernization of the Russian aircraft industry began in 1989 during the period of Glasnost prior to the collapse of the Soviet Union. Armand Hammer gathered a team of experts to advise the Russians

They began with the IL-96M, an Ilyushin Design Bureau project to produce a commercial jumbojet. Although Russian airframe design and integration are generally good, engine and avionics technology is not. In 1991, Pratt and Whitney, a US engine producer, joined the venture after competitively displacing British producer Rolls-Royce. Soon after, Rockwell Collins, another US company, signed on to provide avionics. At that time, Aeroflot Russian International Airlines signed for 20 of the IL-96M aircraft (Duffy, 166). In 1992, after Pratt reaffirmed its commitment to the venture, the IL-96M venture became one of the most visible signs of expanding opportunities for Western aerospace companies in the CIS (Lenorovitz). The durable venture survived Russian economic and constitutional crises.

In October 1994, on behalf of approximately 20 US providers to the project, Pratt applied to the Export Import Bank of the United States (Ex-Im Bank) to guarantee a \$1 billion loan for Aeroflot's purchase of the IL-96M. Although the Ex-Im Bank was set to decide in April, strong opposition by Boeing placed the decision in limbo. The US aircraft manufacturer complained that the loan guarantee would help produce an Airbus-like rival in Russia. Ex-Im Bank felt it needed outside analysis to make an informed decision and asked the National Economic Council to review the case (Blissen 10). Since April, the National Economic Council (NEC) has functioned as an interagency broker to produce policy to guide Ex-Im Bank's decision. During this time, the policy was chiseled into a compromise, but not before new conditions wedged into the negotiations. Presently, Vice President Gore is negotiating with the Russian Prime Minister to resolve trade issues on behalf of Boeing in order to obtain a policy on the loan guarantee acceptable to all players in the game.

Analyzing the Drama: Three Acts and Many Actor-Players

In order to examine the workings of bureaucratic politics in this case, this analysis divides the competition for shaping a policy to guide Ex-Im Bank's decision into three acts or phases. Phase one began with the Pratt loan guarantee request to Ex-Im Bank in October 1994, and it ended when the interagency process informally led by the US Trade Representative (USTR) failed to produce a policy consensus. This occurred when USTR took a sudden hard line against the loan guarantee in March 1995.

Here, phase two began as the NEC became the honest broker over interagency negotiations. The third phase began around October 1995 coinciding with an agreement to grant the loan guarantee with unresolved qualifications. In this phase, the Vice President pursued certain concessions from the Russian Prime Minister in order to satisfy Boeing and reach an acceptable outcome on the policy. Phase three continues to the present as final negotiations are underway.

Act I. Actor-Players and their Interests

At the point where Pratt sought the loan guarantee, ten key players took an active interest in the venture. First, Pratt and Boeing held private business interests. Next, Ex-Im Bank's interest was dominated by its charter to foster US exports, but it was constrained by previous policy guidance indirectly related to the Pratt-Ilyushin deal. Both the State Department and the National Security Council held strong interests from their national security/foreign policy perspective. Although a minor player in this issue, the Defense Department had a related national security interest in supporting the venture. The US Commerce Department and USTR played for domestic economic interests, that is, advancing US economic interests through the expansion of international trade and the opening of a potential market in Russia. Finally, two chapters of the International Association of Machinists (IAM) held competing labor interests.

National Security Interests

The position of the NSC and State was deeply rooted in the Administration's National Security Strategy of Engagement and Enlargement. The strategy document signed by President Clinton states, "All of America's strategic interests are served by enlarging the community of democratic and free market nations" (22). The strategy maintains that "Russia is a key state in this regard" and that "we serve our own prosperity and our security by helping new market reforms in the new democracies in Europe's East" (27). The global economic dimension of Clinton's strategy permeates the document as a lineament for all global ills including stability, trust, prosperity, human rights, and environment. Accordingly, NSC and State enthusiastically supported the loan guarantee. They believed the venture

would help stabilize the Russian economy through the survival of high-technology industries that have strong export potential for Russia. The deal would also play a role in Russia's transition from a state-controlled economy (Sparaco 34)

Although not a major player in this case, the Defense Department supported the venture as having two additional benefits to national security. First, as defense business plummeted for US engine producers, Defense was interested in the viability of the industrial base, in this case its providers of engines and avionics for combat aircraft. Secondly, Defense saw international sales as necessary to reduce research, development, and production costs. Most important was the C-17 engine program. The C-17 engine is nearly identical to the PW2337 engine destined for the IL-96M venture. The defense department was buying the remaining engine contract for its C-17 program, and Pratt's business with Russia would reduce unit cost to the C-17 program. Also, the Russian deal would keep the production line open longer in the event more C-17s were procured in the future (Interviews A, B, and C)

Business Interests

In actuality, Pratt represented approximately 20 US companies providing components for the IL-96, but Pratt's dollar share in the deal was nearly half. From a strategic business perspective, Pratt took the initiative and risk since 1989 to wedge open a door to Russia. The short-term benefit was a half billion dollars, but Pratt managers viewed the IL-96M venture as a first step toward an extensive penetration of the Russian/CIS market (Lenorovitz 20). The potential of the market is substantial. Estimates showed that nearly 80 percent of medium and long haul transports operated by former Soviet airlines exceeded their service life. Data from Russia's State Research Institute of Civil Aviation showed that 50 percent of the Soviet-built operational fleet should be retired by the year 2000 (Rybak 31). Consequently, business opportunity drove Pratt's interest.

On the other hand, Boeing was vehemently against the loan guarantee for the sake of its own business interests. Boeing saw the loan guarantee as helping to create a foreign competitor in the image of Airbus. Airbus is a heavily subsidized manufacturer that caught Boeing off guard when it rose to the

rank of global competitor in a fraction of Boeing's corporate lifetime. Boeing pointed to the fact that the IL-96M would compete directly with Boeing's 767 and 777 market niche at approximately half the cost of Boeing jets. (US Airframers 41)

Ex-Im Bank Charter and Existing Policy Interests

The Ex-Im Bank operates as an independent agency and can grant or deny the loan guarantee without outside consultation. During phase one of this analysis, the bank was in favor of granting the loan guarantee as a natural output of its organizational charter--to promote US exports. Because of the Russian economy, loan guarantees are essential for companies that want to secure financing for projects in Russia. (Blishen 11)

However, several factors motivated the bank to deliberate the matter at length. First, Boeing's complaints caused a dilemma in what was good for Pratt's exports today were bad for Boeing exports in the future. Naturally, Pratt argued the reverse. Secondly, a roughly parallel argument concerning American jobs came from labor interests. (Remez) Thirdly, the Bank considered Boeing a strategic US industry drifting toward a natural monopoly, and the trend should be protected. (Interview D) The final factor was existing policy that prevented the Bank from supporting foreign-built airframes that contain US components. This policy is referred to as the Airbus policy, established in the 1970's to help Boeing compete with the heavily subsidized Airbus. Although the Bank didn't believe the Airbus policy applied to the loan guarantee, the opposing corporate perspectives motivated the Bank's board to examine the applicability of the Airbus policy through an interagency review. (Interview D and E)

Domestic Economic Interests

Commerce and USTR quickly endorsed the loan guarantee. Shortly afterward in November 1994, Commerce led the way in media-blitzing the venture by staging a visit of the prototype IL-96M to Andrews Air Force Base. In opening remarks at the ceremony, the Deputy Secretary of Commerce called the Russian-US venture an historic partnership "one example of the Administration's commitment to creating a new market opportunity for both US and Russian industry." (Russia 33) The

support of Commerce and USTR was consistent with their organizational mission and associated strategy of increasing international trade as a means to increase US economic prosperity and global competitiveness. (Interview D)

Labor Interests

The venture had a jobs impact either way the Ex-Im Bank's decision fell Pratt estimated that the deal was worth 2500 jobs mostly in the Hartford, Connecticut area. Boeing estimated a more dramatic impact on the west coast, albeit in the future, if Ilyushin became a global competitor. As a result, each supporting chapter of the IAH lobbied strongly for its geographic side of the issue (Interview F)

Political Interests

In a sudden reversal, and a demarcation line into a new phase of the analysis, Mickey Kantor at USTR turned strongly against the loan guarantee His reversal immediately followed White House discussions Government and private sources supportive of the guarantee indicate that a political interest emerged in the bureaucratic political process (Maggs 1A and Interview F)

Act II New and Altered Players and Interests

In the second phase of the analysis, Mickey Kantor's reversal significantly altered the bargaining process Kantor now conflicted with Ron Brown at Commerce and Indians in Kantor's own backyard, and players moved to reinforce their positions Consequently, Kantor's position derailed the interagency process that USTR led earlier in the year (Interview G) Overnight, the high probability of a favorable outcome for Pratt deflated, and after five months, the loan guarantee was still in limbo

Political Interests

Some pro-guarantee sources state that Kantor's reversal was politically driven by the White House Boeing's political muscle on the west coast is vital to the 1996 Presidential campaign, and California is a strategic objective As a result, Kantor received pressure unrelated to the mission of his organization namely responsibility for the California vote (Interview F)

With Kantor's reversal, congressional players became more visible as competitors in phase two. California's republican-strong delegation was opposed ineffectively, though loudly, by Connecticut's senators, both minority party democrats. (Interview F) Connecticut Representative Barbara Kennelly railed at USTR's reversal appealing both to Kantor and the President. Her comments highlight the confusion that the Allison model predicts. "We thought Pratt and UTC were doing exactly what the President wanted them to do" by helping the Russian economy, boosting vital Russian business, and providing work for US aerospace companies. (Remez A1)

Ex-Im Interests

Realizing the failure of the interagency process, Ex-Im Bank asked for assistance from the NEC. Having its own organizational interest in promoting the global marketplace, NEC became the honest broker of the interagency process. (Interviews D and E)

National Security Interests and Domestic Economic Interests

The NSC, Commerce, and State entered the new interagency process with some sensitivity to USTR's new position. As a government source involved in the process noted, "The Clinton Administration places great value on collegiality, which means we try not to oppose each other in public, but the delay means we still want the loan guarantee to go through for good reasons." (Interview D)

Labor

Having been lobbied by both chapters for a national position on the issue, the IAM decided not to take a position on the loan guarantee. However, it reaffirmed the right of the two chapters to have opposing views on the issue. (Interview F)

Act III: Concessions, Negotiations, and Elevated Political Interests

Kantor's position and Boeing's apparent electoral muscle drove an unexpected wedge between collective collegiality and individual player interests. As a result, phase two lasted approximately six months with little progress toward a policy outcome. While pro-guarantee forces remained strong, the NEC worked to broker a win-win outcome. (Interview D)

Phase three began around October 1995 as the NEC sorted the interagency bargaining into two possible outcomes both approving the loan guarantee but with differing qualifications. The one most favorable to Boeing's interests called the guarantee a "one-time deal" unrelated to the Airbus policy, but it would take advantage of the occasion to reaffirm the Airbus policy in Boeing's interest. The alternative qualification was more to Pratt's liking. It would acknowledge that the guarantee is covered by the Airbus policy, but it is "highly exceptional" and would not set a precedent either way. This language gave Pratt some hope of additional exceptions in the future to access the Russian marketplace (Interview D and Private Sources)

National Security Interests

The principles of the NSC, State, and DOD were increasingly diverted by foreign policy pressures such as Bosnia, but from a deputy level, interests were strongly advocated. In particular, State became increasingly anxious as Russian government authorities and Ilyushin began to chafe at the year-long freeze. Approaching elections in Russia, the US troop deployment to Bosnia, and Russian stability intensified State's interest in the loan guarantee. Added to this was a general feeling of embarrassment after the US government had popped champagne a year earlier with the Russians over their prototype IL-96M at Andrews Air Force Base (Interview G and H)

Labor and Domestic Economic Interests

Labor interests remained unchanged, while domestic economic interests were advocated from a deputy level in Commerce. Sources indicate that Ron Brown's lower profile was in deference to Mickey Kantor's White House interests and for the sake of public collegiality (Interview D and F)

Political Interests

As the NEC crept within inches of brokering an outcome through the interagency process, Boeing convulsed the process to obtain a better result. Boeing introduced a walloping condition for accepting a "one-time deal" for Pratt. They demanded that US-Russian trade negotiations obtain Russian Presidential Decrees guaranteeing that no tariffs will be levied on any Boeing-built aircraft sold in

Russia The size of this demand is substantial For example, such an agreement means that Russia would agree to conduct itself as if a GATT participant while not receiving the advantages of GATT membership (Interview F)

Despite the scope of the demand, Vice President Gore agreed to negotiate the terms with the Russian Prime Minister The negotiations are in progress as this analysis is being written Private business sources believe that the Vice President's participation is further evidence of the political leverage Boeing is effectively using to influence the Administration

The Unfinished Act III

At the writing of this paper, the Vice President is negotiating Boeing's trade conditions with the Russian Prime Minister However, the outcome of the game appears well defined regardless of the outcome of the negotiations The loan guarantee will be a one-time deal, and the Airbus policy will be reaffirmed to assist Boeing's global competitiveness Following nearly 14 months of bargaining, Boeing's interests appear to dominate the closing minutes of the game In reality, bureaucratic politics has dominated all the minutes of the game as predicted by Allison's model.

Observations

Although Ex-Im Bank is an independent agency and not a bargaining player, its decision to seek external policy guidance subjected the Bank to the effects of bureaucratic politics As a result, its efficient internal decision process was obviated by deferring to the interagency process on matters clearly within its own action channels In the end, the Ex-Im Bank will provide the loan guarantee, but it will not receive policy to incorporate into standard operating procedures Instead, the bank has unintentionally set the precedent that all similar ventures in the future (predictably many) will require a similarly derived policy decree Additionally, the long delay has tarnished Russian-US relations, a side-effect that works directly against the Bank's charter and national security interests

Although Boeing's concerns are legitimate in the context of its business interests, the extreme delay in resolving the issue has reached a point of negative return for Boeing Ironically, as Boeing

fight to reserve a future marketplace for itself, the vast Russian marketplace is becoming biased against Boeing as it suffers the long punishing delay of the bureaucratic political process. In a similar manner, foreign policy and associated relationships have not profited from the process.

National security planning models, such as the Deibel framework, provide a rational and systematic architecture to assist in formulating strategy. However, the preceding analysis suggests that frameworks cannot adequately model the dynamic of bureaucratic politics. It attenuates progress toward national security objectives. For example, strategists rationally plan to capture opportunities like the Pratt-Russia venture, but execution of the plan is much less rational, resulting in unexpected results and unexpected delays.

Conclusion

Using Allison's model as a framework for analysis, the Pratt-Russia case shows how national security interests were affected by competing interests in and around the government bureaucracy. Clearly, the process through which the Ex-Im Bank received policy to guide its decision was not monolithic and rational. As Allison's model predicted, the policy was the result of compromise, coalition, and competition among players who acted according to their individual and organizational interests.

Just one strategic business venture has taken over a year to run the bargaining game of the public bureaucracy. In the end, Pratt will sell its engines, but the struggle and lost time has transformed the opportunity. Several conclusions are offered. First, skill in bureaucratic politics appears crucial to optimizing the outcome for the sake of national security interests. Secondly, opportunities need to be plucked before they are ripe. That is, the bargaining process consumes time, and time can transform the issue just as the delayed loan guarantee soured Russian attitudes. Finally, the interagency process is crucial to reaching an outcome and squeezing efficiency from the process. National security players can look to the NEC in this case as an example of skill in the role of honest broker, considering they were called into the drama in mid-play. In total, the lessons of the Pratt-Russia venture suggest that beating

our swords into plowshares may be an unexpectedly tough task for national security strategists in the post cold war era Ignoring bureaucratic politics will only aggravate the task

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