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A NEW APPROACH TO FOREIGN AID: THE INTERNATIONAL DEVELOPMENT ASSOCIATION

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CHAPTER I

INTRODUCTION

Objectives

This study has a number of objectives. The first is to trace the history of the idea of an International Development Association. It is fascinating to observe the route that this proposal followed, especially in the United Nations and in the United States of America. In fact, it may have set a precedent in foreign policy making in the United States. At least one author has maintained that the Monroney Resolution concerning the International Development Association represented a significant departure from the traditional role of the United States Congress in the foreign policy field.[1]

What was the role of the United States Government in establishing IDA? This study presents the attitude of the American Administration, as it developed, toward this agency. Apparently there were some significant changes of attitude concerning the necessity for a new international financial institution. What caused these changes?

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[1]James A. Robinson, The Monroney Resolution: Congressional Initiative in Foreign Policy Making (Eagleton Institute Cases in Practical Politics, Case 8; McGraw-Hill, 1960).

We look for proof for the view that the United States endorsed the recommendation for IDA only to offset the drive for SUNFED, that is, the Special United Nations Fund for Economic Development. In IDA, the United States has 30 per cent of the votes, whereas in SUNFED it would have had only one vote. It might be reasonable to assume that the United States Government would prefer an IDA-type arrangement to the SUNFED proposal, but was this, in fact, the choice? The argument that the spectre of SUNFED caused United States' policy to favor IDA has been widely circulated.

In addition to determining the view of the United States Government toward IDA, we also want to determine the attitude of the International Bank for Reconstruction and Development toward such an innovation. A certain school of thought holds that the Bank was coming around to the position that something similar to IDA was needed long before the Monroney Resolution saw the light of day. There is the contrary view that the Bank not only failed to recognize the need for IDA but actually opposed the idea. Andrew Shonfield has reported that Mr. Eugene Black, then President of the World Bank, said, during the early stages of the discussions on IDA, that "he had never liked the idea of 'soft loans,' but if they had to come he was going to make certain that he was the man who handled them."[1] There have been those who have suggested that the Bank captured IDA in order to kill it or at least to dilute its effectiveness. Those persons who were strongly in favor of soft loans can point to the small scale of IDA operations

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[1] Andrew Shonfield, The Attack on World Poverty (New York: Vintage Books, 1960), p. 156.

to date and feel reinforced in this view. One goal of the study is to clarify the attitude of World Bank officials to the establishment of a soft loan agency under Bank supervision.

In tracing the history of IDA's birth, we want to examine three issues which arose. First to be considered is the question of soft loans. There was, in 1958, and still is significant opposition to the whole idea of soft loans to underdeveloped countries. And yet the member governments of the World Bank have put up a billion dollars for just such soft loans. What were their reasons? What were the arguments that went on concerning this issue? The second significant issue which arose was the proposal to use the local currencies of the less developed countries to finance development. This was a crucial part of Senator Monroney's proposal and yet the International Development Association has not loaned any local currency to anyone. What were the problems of using local currencies and could these problems be overcome? The third issue to be considered is the question of bilateral as opposed to multilateral aid. Some of the support for the Association came out of frustration with bilateral aid programs and out of the feeling that something better was possible.

A second major objective of the study is to outline the manner in which the Association is organized; its relationship with the International Bank; its method of operation; and its major problems. In particular, we are interested in the allocation problem that has arisen in disbursing the billion dollars entrusted to this organization. Previously, the World Bank had been able to finance any sound project, presented by a creditworthy country--by selling bonds in the financial markets of the world. However, the funds allocated to the International Development Association have finite limits. Which projects should get loans from the Bank and which from IDA? What should be the basis for deciding--the situation of the country concerned or the type of project involved? What criteria have been established for making these decisions?

The third major objective is to test two hypotheses. The first hypothesis to be tested is that, on the basis of the first two years experience of the International Development Association, universally applicable criteria can be developed for evaluating projects in underdeveloped countries. On the basis of such evaluations, loan decisions can be made. We will look at the techniques IDA uses in appraising projects in testing this hypothesis. Secondly, it is hypothesized that the International Development Association is a significant new approach to foreign aid. In order to test this hypothesis, we look at total IDA investment as a component of all foreign investment in less developed countries and as a component of all soft loans to these countries. We also examine bilateral lending programs to see if IDA has had any influence on the approach taken in these programs.

Limitations

This is not a study of the desirability of foreign aid as such. The need for such aid is assumed. Neither is this a weighing of the arguments for multilateral as opposed to bilateral aid, although some of these arguments will be given as historical background. The very existence of the International Development Association is evidence of widespread support for the idea of multilateral aid to underdeveloped countries.

The need for soft loans is not treated in an exhaustive fashion although many of the arguments favoring establishment of the International Development Association rest upon the need for funds in addition to hard loans attainable from the International Bank for Reconstruction and Development and conventional loan institutions. But just what is meant by the expression "hard loan"? A hard loan is traditionally defined as one which the lending country can finance out of its own borrowing. Hard loans contain no element of subsidy to the underdeveloped countries. They usually have a duration of less than 30 years. Soft loans are defined as loans which cannot be financed out of borrowing in the market, and are normally made for something over 15 years. Grants are, of course, in a different category altogether. For whatever reasons, grants seem to have been rejected as a foreign aid device by both the donor and recipient countries. Grants will, therefore, not be considered in this study. Much of the case for a Development Association rests on the inadequacy of hard loans alone to meet the development task. Certainly this is the basis of the World Bank's support and they have conducted elaborate and sophisticated studies to show just how vitally necessary soft loans are.[1,2]

It has not been possible to report the arguments that have taken

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[1]Dragoslav Avramovic, Debt Servicing Capacity and Postwar Growth in International Indebtedness (Baltimore: The Johns Hopkins Press, 1958).

[2]Dragoslav Avramovic and Ravi Gulhati, Debt Servicing Problems of Low-Income Countries, 1956-1958 (Baltimore: The Johns Hopkins Press, 1960).

place in the world press concerning the International Development Association. It would have been interesting to have studied the reactions to IDA in the press of the Soviet Union, India, Ghana, West Germany, and all the other countries of the world. Unfortunately, this was not possible. We have had to rely on speeches made by the Governors of the International Bank in order to capture most countries' reactions to the establishment and operation of the International Development Association. The debate that took place in the United States is given fuller coverage because of the accessibility of the data. The reactions of a few other countries were obtained through personal interviews.

Just what is an underdeveloped country? Fortunately the problem of definition does not concern us here. We limit our discussion to those countries that are members of the International Development Association and have been allowed to put up 90 per cent of their initial subscription in their own currency (the Part II countries); a total of 52 countries as of September 30, 1962. These 52 countries were located in North, Central, and South America, Western Europe, Asia, and Africa. One Eastern European country (Yugoslavia) is included.

The operations of IDA are studied from September 24, 1960, when the Articles of Agreement entered into force, to September 30, 1962. This covers the early formative period, the period in which the basic policy decisions were made, and ends with the September, 1962 meetings of the Board of Governors of the Association, at which time it was proposed that IDA's resources be considerably enlarged.

Perhaps the largest disclaimer to be made for this study concerns a theory of economic development. Although there most certainly is a theory of economic development underlying the operations of the International Development Association, it is not the purpose of this study to delineate that theory. Such a task has perhaps already been undertaken[1] and a further elaboration is a challenging task for another occasion.

Sources

The chief source for the study is the International Development Association. Much of the material that was used has been published; however, considerable reliance is placed on unpublished materials and personal interviews and correspondence with staff members. While tracing the history of the proposal for IDA in the United States considerable use is made of public documents of the United States Congress, the National Advisory Council on International Monetary and Financial Problems, and various boards and committees. Interviews with officials in the legislative and executive branches of the United States Government provided helpful information.

In assessing the significance of the International Development Association as a new approach to foreign aid, the opinions of some leading development economists are presented. These opinions were solicited in personal letters which are in the author's possession. In attempting to measure the impact of IDA, representatives of some countries were contacted in Washington, D. C. In addition, a number of references

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[1]Eugene R. Black, The Diplomacy of Economic Development (Cambridge: Harvard University Press, 1960).

are made to the works of academic observers of the organization.

Method

Chapters II through VII are essentially historical in nature. From the sources previously mentioned, the history of the idea of an International Development Association is traced. These chapters contain a rather complete account of the important forces that shaped the creation of this institution. In Chapters II through VII, the author does not attempt to evaluate the arguments, the proposals and the policies that were put forth, although some few of the author's judgements are expressed where deemed appropriate.

Chapters VIII through XII contain an analysis of the problems that have confronted IDA and of the solutions that have been found. An analysis is made of the criteria being used in making loans. The crucial factors in decision-making are isolated and patterns in the types of projects approved are highlighted. These chapters are concerned with the allocation problem that has arisen. Some of the significant criticisms of IDA are examined. We study some proposals for IDA's future.

Chapter XIII contains the summary and conclusions. Can IDA's success be measured after only 2 years operation? What was hoped for when it was established? Has this been achieved? Does the past two years experience suggest any need for expansion of the organization? What are the major criticisms of IDA? These are some of the questions which the author attempts to answer in this chapter. It is not possible to test IDA in a controlled experiment, by setting up a different type agency, to see if another approach would have been better. So, ultimately, a subjective judgement must be made as to past effectiveness and as to significance for the future.

CHAPTER II

THE UNITED NATIONS AND THE INTERNATIONAL DEVELOPMENT ASSOCIATION[1]

The Proposed United Nations Economic Development Administration

The debate concerning the establishment of an International Development Association was very long and wide-ranging. Very early in the life of the United Nations, proposals were made for the establishment of such an institution. The ninth session of the Economic and Social Council, held in 1949, heard a report favoring a United Nations Economic Development Administration or "UNEDA." This proposal was put forth by the Third Session of the Sub-Commission on Economic Development. The idea came from the Chairman of the Sub-Commission, Mr. V. K. R. V. Rao of India.

The Sub-Commission pointed out that the economic development of underdeveloped countries involves large-scale investments over a

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[1]Background information for this chapter has been obtained from two sources not otherwise mentioned. The first, B. E. Matecki, Establishment of the International Finance Corporation and United States Policy (New York: Frederick A. Praeger, 1957), describes the establishment of a sister organization of the International Development Association, within the World Bank group. This study also contains a discussion of proposals for IDA within the United Nations. The second, John G. Hadwen and Johan Kaufmann, How United Nations Decisions Are Made (Leyden: A. W. Sythoff, 1961), discusses proposals for SUNFED and the United Nations Special Fund.

long period of time and that not all of these investments would yield the immediate returns which would be demanded by commercial investors. Yet, some of these projects were more essential to development than commercial investments in mining and manufacturing.

This group noted that the International Bank for Reconstruction and Development had indicated its willingness to expand its activities in financing economic development projects. But,

> on a realistic assessment it cannot be assumed that the Bank could, in the foreseeable future, be able to make a significant contribution to the massive investments required for economic development involved over a long period. Moreover, even if the finance available through the Bank could be increased . . . the terms on which it would be available under the policy established by the Bank limit the effectiveness of this financing to underdeveloped countries. There are fields and types of investment required for economic development which can neither satisfy the preconditions required by the Bank, nor carry the interest charges involved, nor be liquidated within the period required.[1]

After having written off the International Bank, the Sub-Commission turned to the proposal by its Chairman, Mr. Rao. This proposal was deemed to be deserving of consideration and it was commended to the attention of the Economic and Social Council.

What was the Rao proposal? After having surveyed the field of international financial agencies, Rao concluded that there was no international agency for: (1) Financing projects which were not bankable; (2) Aiding underdeveloped countries in the preparation and execution of development programs; (3) Co-ordinating technical assistance activities; (4) Promoting projects that extended over more than one national frontier. He, therefore, suggested that such

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[1]United Nations, Economic and Social Council, Sub-Commission on Economic Development, Report of the Third Session of the Sub-Commission on Economic Development (E/CN.1/65, April 12, 1949) (New York, 1949), p. 18.

an agency be established.[1]

The functions of the United Nations Economic Development Administration would be: (1) To make technical assistance available; (2) To co-ordinate technical assistance activities of the specialized agencies of the United Nations; (3) To assist underdeveloped countries in the procurement of needed materials; (4) To finance such schemes as could not be financed through normal banking institutions; (5) To promote regional developmental projects.[2]

Rao proposed that UNEDA be financed through the contributions of member governments. These would be in the currencies of the countries concerned and expenditures would be subject to the approval of the country whose currency was used. Rao stated that, for the time being, the bulk of the resources would have to come from the United States of America. No definite figure was indicated for the total budget or for the United States' contribution.

Assistance would be given in the form of loans and not of grants, although the terms of repayment would be liberal and the interest rate would only be nominal. All assistance would be conditional on the receiving country providing a share (as much as 50 per cent) of the costs of projects financed.

Projects would have to meet an economic test, "in the sense that their completion will result in raising the productivity of the underdeveloped areas and the standard of living of their people."[3] Rao saw UNEDA as a complement to the existing channels of international finance and not as a substitute or alternative to these channels. He

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[1] *Ibid.*, p. 22. [2] *Ibid.* [3] *Ibid.*, p. 14.

was particularly insistent that the agency would be expected to operate in a business-like manner and that no new bureaucracy be set up to administer the program. To accomplish these goals, he urged that most of the projects undertaken be carried out through the specialized agencies of the United Nations, that is, the Food and Agricultural Organization, the World Health Organization, the International Labor Organization, the United Nations Educational, Scientific and Cultural Organization and the World Bank.

The United States member of the Sub-Commission, Mr. E. G. Collado, took rather strong exception to Mr. Rao's proposal. The gist of his dissent follows:

> I believe sincerely that the most effective and desirable pattern of organization of the domestic economy from the economic and social points of view is that which gives greatest emphasis to free private enterprise and institutions guided and even regulated and supplemented by government where necessary in the broadest interests of the people and the nation. This is the pattern which has brought great benefits to my own country and, I believe, to many other . . . nations in various stages of economic development. . . . I therefore believe strongly that the United States should co-operate fully in sound economic development of under-developed countries, that it should look primarily to American private enterprise to provide abroad investment of capital and technique, and that it should rely fundamentally on the International Bank for Reconstruction and Development for financing or collaborating in financing closely circumscribed types of project basic to development not readily susceptible of implementation by purely private financing.[1]

This position of the United States, enunciated clearly in 1949, was to continue throughout the Administration of President Truman and most of the Eisenhower years. This policy, of primary reliance on private enterprise for economic development--aided and abetted when absolutely necessary by the World Bank, was used in

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[1] Ibid.

opposition to Rao's proposal for UNEDA and for all the subsequent proposals for a Special United Nations Fund for Economic Development or for a United Nations Capital Development Fund.

The United States, with its Tennessee Valley Authority, Reconstruction Finance Corporation, Federal Housing Administration, and Federal Land Bank, insisted that the developing countries of the world rely on private capital for their own economic development. The United States seemed to have demanded a purer practice in others than deemed necessary for its own economy. Or, as one observer put it, a Democratic Administration acted abroad as though Robert Taft were really President.

Without United States support, Rao's proposal had no chance of acceptance. He had foreseen that United States support was crucial for the success of UNEDA. And when the United States withheld support, the proposal went no further. The report of the Sub-Commission on Economic Development was, however, circulated to the specialized agencies of the United Nations for their comments.

The Food and Agricultural Organization was impressed with the limitations of the International Bank which the report had described.

> It has only recently made its first loans for outright development purposes, and these largely to relatively prosperous countries.
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> . . . .
>
> It is limited in its loans for agricultural purposes because of the shortage of development projects adequately prepared and planned, and because of the inability of many agricultural projects to earn foreign exchange to repay them.[1]

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[1]United Nations, Department of Economic Affairs, Methods of Financing Economic Development in Under-Developed Countries (1949.II. B.4) (Lake Success, 1949), pp. 78-79.

This same organization revealed an under-consumptionist bias when it called for the United States to contribute heavily to economic development abroad in its own interest.

> Looking further ahead, the recent exceptionally high domestic investment rates in the United States and other developed countries are unlikely to be long sustained. So long as the United States maintains its present general economic institutions, including the structure of taxes, business and government finance, and distribution of income among its population, a large and sustained outflow of funds for foreign investment might well be helpful in assuring sustained high levels of domestic employment and economic activity.[1]

As can be surmised, the Food and Agricultural Organization gave the Sub-Commission report quite sympathetic consideration.

The International Bank for Reconstruction and Development viewed the report with antipathy.

> The Sub-Commission considers it unrealistic to assume "that the Bank could, in the forseeable future, be able to make a significant contribution to the massive investments required for economic development involved over a long period". The magnitude of the task cannot be denied, but magnitude alone cannot determine the pace at which it is undertaken. The report itself admits the dearth of soundly conceived projects and this agrees with the Bank's experience. Rash expenditure now would prejudice the flow of investment in the future; for in the last resort development relies on the savings of the world, which can hardly be expected to be forthcoming if they are misused. Eventually more sound projects may be presented to the Bank than it can finance, but that time is not yet in sight.[2]

The Bank went on to point out that underdevelopment itself implied an insufficiency of skills with which to make development plans and implement them. And in addition to being short of skills, the underdeveloped countries were pictured as being short of the most rudimentary data necessary for planning purposes. In addition, the Bank pointed out that the necessary political and social foundations

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[1] _Ibid._, p. 80. [2] _Ibid._, p. 141.

for development had to be built gradually. Low productivity and living standards were pictured as being just as much the result of bad government, bad health, unsound finance and lack of education as of inadequate resources or the lack of productive facilities.

The Bank statement expressed an unwillingness to be deflected from its determination to make loans only for sound and productive projects. And any organization which lowered its standards in that respect would be guilty of waste for the sake of ostensibly humanitarian objectives.

> The proposal for the so-called United Nations Economic Development Administration . . . is based on an alleged need for a new international agency . . . [for] "financing projects of economically under-developed countries which are not financially productive in a banking sense".......The Bank itself was established to finance development projects for which private capital is not available.[1]

The Bank pointed out that its own interest rates were not designed to make any profit, so that loans which were made at lower rates would be simply disguised intergovernmental grants. Four of the functions of the proposed UNEDA were examined and each of them was found to be a present function of the Bank or one of some existing agency.

The Bank argued that its experience suggested that for the immediate future it would be able to acquire sufficient resources to finance all sound development projects in member countries that were ready for execution and that could appropriately be financed by foreign loans which were expected to be paid. This did not mean that the Bank's resources were adequate for all the world's development

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[1]Ibid., p. 143.

needs. "There is . . . a vast difference between the amount of money which can usefully be employed and the amount of additional external debt which the underdeveloped countries can properly assume."[1] In many cases, these countries did not have very good prospects of being able to repay foreign debt. And since Bank financing must necessarily take the form of external debt, it could only provide a part of the foreign capital necessary for development.

The Bank agreed that there are capital requirements for health, sanitation and other social purposes which are indispensable for economic development yet which could not yield a direct return. In some of the poorer countries such basic projects as highway construction, irrigation, and land clearing might also be non-bankable projects because the burden of servicing such debt would be too heavy. However, the Bank did not feel it proper to comment on the various proposals that had been made to extend assistance for such projects on a grant basis. The decision on such proposals was felt to be a matter for the governments of the donor countries to make.

The Committee of Experts

After this discussion of the Rao proposal, nothing significant occurred until 1950, when the Secretary General was asked to appoint a group of experts to study this problem. This request was made by the Economic and Social Council in resolution 290 (XI). Mr. Trygve Lie appointed five well-known experts to make recommendations as to what could be done to help the developing countries. The experts were

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[1] Ibid., p. 99.

W. Arthur Lewis, Theodore W. Schultz, Alberto Baltra Cortez, D. R. Gadgil, and George Hakim, who served as chairman of the group. The experts' report was presented to the General Assembly in May, 1951.[1]

This group concluded that a minimum 2 per cent increase in the per capita national income of the developing countries was necessary. And in order to achieve this 2 per cent, they figured that an annual capital import of well over $10 billion would be required.

They turned to the existing agencies to see if they might meet the need. The International Bank, at that time, was loaning to the underdeveloped countries at a rate well below $300 million annually. Thus, the experts decided that the Bank was not beginning to meet the challenge presented. And there was a significant obstacle in the way of increasing Bank lending. According to its charter, the Bank had to charge rates of interest which would attract funds in the financial markets.

> The amount that can profitably be invested at a 4 per cent rate of interest depends on the amount which is being spent at the same time on improving social capital; and especially on public health, on education and on roads and communications. There is much to be done in this way in the under-developed countries before they will be in a position to absorb large amounts of loan capital.[2]

The underdeveloped countries obviously did not have the money needed for improving their social overhead capital. And they, just as obviously, could not borrow the amount of money

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[1]United Nations, Department of Economic Affairs, Measures for the Economic Development of Under-Developed Countries (E/1986/ST/ECA/10, 3 May 1951) (New York: 1951).

[2]*Ibid.*, p. 84.

necessary for such purposes. Yet, without these basic facilities, economic development was extremely difficult.

To meet this problem, the experts proposed that some mechanism be established for transferring grants-in-aid of about $3 billion a year to the developing countries. This was considerably less than 1 per cent of the national incomes of Western Europe, Australasia, the United States, and Canada.

> The principle that the better off should help to pay for the education, the medical services and other public services received by the poorer classes of the community is now well established within every Member nation of the United Nations. The idea that this principle should also be applied as between rich and poor nations is relatively new. It has, however, been put into practice on several occasions.[1]

The experts cautioned that they were not proposing unconditional aid handed out like alms. What they wanted was grants linked to a specific function with international verification that the funds were used properly. And to oversee such a program, the experts took note of a proposal which had been put forward in the United States by the International Development Advisory Board. This Board had urged the establishment of an International Development Authority under World Bank auspices. The United Nations experts recommended establishment of an International Development Authority under United Nations auspices.

The experts took note of the fact that some countries might prefer to set up bilateral programs for development assistance. However, they felt that international administration had definite advantages over such bilateral approaches. For one thing, international

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[1] Ibid.

verification of expenditure would be more acceptable to the receiving countries. Secondly, some of the Scandinavian and Australasian countries' traditions were more in keeping with international cooperation and such an organization would save them the expense of setting up separate organizations of their own.

The functions of the Authority would be as follows: (1) To decide upon and administer grants-in-aid for specific purposes and to verify their utilization; (2) To cooperate with developing countries in preparation and coordination of plans for economic development; (3) To help in implementing development plans--by procuring technical personnel and equipment; (4) To make reports on the progress of the underdeveloped countries and recommendations for further action.[1]

The types of projects that would be eligible for grants would be: research and education, public health programs, subsidation of farm credit, and improvement of public works. The Authority would also be authorized to cooperate with the International Bank in undertaking projects. In cases where social overhead projects could not meet the Bank's standards for the full cost of the project, the Bank might loan the part that was bankable while the Development Authority would make a grant for the remainder.

The experts were unimpressed by the arguments of many persons that the underdeveloped countries were unready to absorb large amounts of capital. They were "impressed by the results achieved during the Second World War by programmes of rapid and intensive training of industrial workers and technicians."[2] There were no bottlenecks

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[1] _Ibid._, pp. 85-86. [2] _Ibid._, p. 87.

which could not be overcome, if enough money and effort were devoted to the task.

The President of the Bank, Mr. Eugene Black, took note of the proposal of the experts in his speech to the Board of Governors in 1951.

> It is my opinion, which I think the record adequately supports, that unless the international situation deteriorates further, we will be able to meet all the capital needs of economic development in our member states, to the extent that those needs ought properly to be met on a long-term loan basis.
> In view of the record, it seems strange indeed that suggestions are still heard that new ways must be found to increase many times over the amount of intergovernmental loans for development purposes. Such suggestions, in my experience, are usually based on large but hazy calculations of what is available and what really can be used in the form of loan capital for development. . . .
> I would like to record my emphatic disagreement with suggestions of this kind. . . .
> That is not to say that there may not be other useful instruments in the field of providing capital, on an international basis, for economic growth. The idea has been advanced, for instance, of an international authority to allocate grants for development. Under present world conditions, it does not appear likely that any significant amount of grant capital will be provided on a truly international basis; but the idea has merits that might well be considered in a later and happier day.[1]

Black was referring to the International Development Authority which had been proposed by Nelson Rockefeller's International Development Advisory Board.

He returned to this theme in his 1952 speech to the Governors. He was, throughout the discussion on new institutions, arguing that the Bank was ready to play a larger role.

> Some of the proposals which recently have been made envisage the creation of a new financing institution. If new

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[1] Summary Proceedings of the 1951 Meeting of the Board of Governors of the International Bank for Reconstruction and Development (Washington: IBRD, 1951), p. 6.

> arrangements come into existence, the Bank would, of course, cooperate with them. But let me point out that new institutions themselves do not create savings. Fundamentally we must work with what we have. I myself believe very strongly that the Bank itself could operate effectively as an instrument for mobilizing European capital, and I doubt that sufficient consideration has yet been given to the role we might play in this respect.[1]

The statement that "new institutions themselves do not create savings" came back to haunt Black as it was used again and again in opposition to the establishment of the International Development Association almost a decade later.

It was Black's position that the International Bank had been established as an international organization, a specialized agency of the United Nations, for the purpose of reconstructing and developing the war-ravaged world. Why not use it for that purpose? In one of the most eloquent passages from Black's many speeches and writings he argued his case for the Bank.

> Economic development is an important objective for the entire community of nations. It is important to less developed countries in terms of production, of standards of living and of continuing national growth. It is not less important to countries that already have reached a high stage of development. Their own livelihood and their own future depend on the progressive expansion of world production and commerce.
> . . . Not long ago, the world emerged from a great war which made it necessary, in many areas, to suspend normal processes of economic growth. The nations have had to engage in tremendous effort and to spend enormous sums of money to repair the loss of those years. Surely we would now court disaster if economic development were again to be treated as a secondary problem and more years were to be lost.
> . . . .
> Let me conclude by restating what, as I see it, we are all seeking in this process of economic development. Expanding world commerce and higher living standards are phrases that mean

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[1] Summary Proceedings of the 1952 Meeting of the Board of Governors of the International Bank for Reconstruction and Development (Washington: IBRD, 1952), p. 9.

> something important, but they may obscure the fact that both the source and the object of our efforts is the individual human being. In him is the motive power of what we can do, and for him are the rewards of what we can accomplish.
>
> More clearly today than ever before, we know what happens when men live and are treated as masses, as statistics, as servants of priviledged classes or as creatures of the state. All during our lifetimes, we have seen them erupt in riot and bloodshed; we have seen them hypnotized and driven to self-destruction in war. The threat that faces us today does not lie in the willfullness of a few men; it lies in their ability to control people in masses, and to appeal to other masses who may be willing to exchange one form of subjugation for another.
>
> In that perspective, economic development can be one of the most significant and constructive activities of our time. Through development, we can help give men a chance to satisfy their aspirations not as a mob but as individuals. For one of the striking characteristics of a developed society is the great variety of choice it can offer to individuals; a choice not merely of one 20th century convenience over another; but a choice of work, of careers, of living places, of ideas and of leadership.
>
> Variety of choice is one of the things we are talking about when we talk about freedom. In far too much of the world today, this element of freedom does not exist. Men are likely to think they have a choice only between extremes; between slow starvation and quick revolution; between complete inertia and regimented obedience to political leaders who themselves may represent extremes.[1]

Black was speaking for a middle road between slow starvation and quick revolution. He had seen the results of revolutionary economic development in Germany, Japan and Russia. He and those who agreed with him wanted to give countries another alternative--so that they might, with outside aid, develop quickly but peacefully. Black saw economic development as a process that should be carefully planned, soundly financed, and competently guided. People of this persuasion are convinced that outside capital can have a very beneficial effect on the process of economic growth, if such outside capital is soundly administered. They put economic considerations ahead of short-run political advantages because they believe that a prosperous world is

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[1] Summary Proceedings of the 1951 Meeting . . ., pp. 7-10.

"far more stable and peaceful than the one around us today."[1]

Despite the pleas of Black and those who agreed with him, however, there was continuing pressure from the developing nations to bypass the International Bank and set up a new United Nations agency.

The Origin of SUNFED

The seventh session of the General Assembly passed resolution 622 A on December 21, 1952 which endorsed a request of the Economic and Social Council for a detailed plan for a special fund for financing economic development. The Secretary General, Mr. Trygve Lie, appointed a committee of 9 composed of Mr. S. Amjad Ali of Pakistan; Mr. Fernand Baudhuin of Belgium; Mr. C. V. Bramsnaes of Denmark; Mr. Miguel Cuaderno of the Phillipines; Sir Cyril Jones of England; Mr. Leo Mates of Yugoslavia; Mr. Hernan Santa Cruz of Chile; Dr. Eduardo Suarez of Mexico; and Mr. Wayne C. Taylor of the United States.

The members of the Committee made no recommendation as to whether such a Fund should be established. They were merely interested in drawing a blueprint for a successful agency, should the United Nations decide to establish it. They were addressing the same problem faced by the Sub-Commission on Economic Development; that is, the need for non-commercial capital in the form of grants-in-aid, or long-term, low-interest loans.

The Committee recommended that the Fund should depend for its main budget on voluntary contributions on the part of governments.[2]

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[1] Ibid., p. 10.

[2] United Nations, Department of Economic Affairs, Report on a

However, they also recommended that the administrators of the Fund should be authorized to accept nongovernmental or private contributions in addition to contributions by governments. They encouraged the Fund to appeal for such contributions and made a plea for nations to declare such contributions tax deductible.[1]

In the author's opinion, it is unfortunate that such a provision has never been made in the establishment of any international aid agency. There is a possibility of a citizen response that has never been tapped in the drive for economic development. But those persons who are familiar with the enthusiasm generated by War Bond Drives, Bonds for Israel Campaigns, etc. can testify to the public's willingness to subscribe to respected causes. Member governments would want the right to refuse such solicitation--but this would probably not be an obstacle in the case of IDA.

There has been a proposal that the International Development Association should launch such a campaign. An English organization has made a proposal to set up projects for a Peace Investment Trust and to gather nickels and dimes--raised all over the world--which would be invested in bonds issued by the IDA.[2] The Charter allows the IDA to borrow funds but the organization could not pay interest on the funds borrowed since it does not collect interest on its loans. And there is no need to raise funds for the World Bank by collecting nickels and

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Special United Nations Fund for Economic Development--Submitted by a Committee Appointed by the Secretary-General (E/2381, 18 March 1953) (New York, 1953), p. 12.

[1] Ibid., p. 10.

[2] Interview with Mrs. Shirley Boskey, Development Services Staff, IBRD, January 24, 1963.

dimes because the Bank can raise all the funds it can prudently use, in the capital markets, in much more manageable operations. Thus, this idea proposed by the Committee of Nine a decade ago, has never yet been tried.

The Committee made recommendations about the structure of the Special Fund as follows: The Fund should not be established until at least $250 million had been pledged by at least 30 governments; the fund should make both long-term, low-interest loans and grants-in-aid; the Executive Board would be made up of an equal number of representatives from the major contributors and the other governments; and no mechanism of weighted voting should operate in the Board. This last recommendation has been a serious stumbling block in all attempts to set up a development fund under United Nations auspices. The rich nations of the world are asked to contribute funds to an agency whose policies they would not be able to determine as they now determine World Bank policy. This plan has been hailed with enthusiasm by all the underdeveloped nations but the United States has looked on it with considerably less fervor.

The Committee recommended that any investment projects which could not otherwise be financed should qualify for consideration by the Fund. They pointed out that although non-self-liquidating projects might well constitute a significant part of the Fund's operations, its scope should not be limited to such operations. The Committee went on to say that the Fund should be able to finance revenue producing projects.[1] This recommendation would seem to put the Special Fund in

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[1]United Nations Report on a Special United Nations Fund for Economic Development, p. 20.

competition with the International Bank and this is just the way many people saw it at the time.

The Scheyven Reports

The eighth session of the General Assembly, held in 1953, asked the member governments of the United Nations and the specialized agencies to comment on the proposal for SUNFED. Mr. Raymond Scheyven, of Belgium, was asked to prepare a report on the attitudes of governments toward establishment of a Special Fund. Mr. Scheyven presented his report in August, 1954.[1]

The report made quite a point of the World Bank's limitations in financing non-self-liquidating projects. By virtue of the fact that the Bank must evaluate a country's ability to repay debt in hard currency, there are many countries which are unable to meet banking standards. And this means that "many projects--even projects of very great importance from the point of view of economic development--cannot be financed by the Bank."[2]

There was general agreement on this point among the members of the United Nations. But there was a sharp split as to how this problem should be solved. One group of countries, those considered to be underdeveloped, urged immediate creation of a Special Fund. A second group of countries--including the Federal Republic of Germany, Canada, the United States of America, New Zealand, the United Kingdom, Sweden and Switzerland--maintained that progress must be made in disarmament before

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[1]United Nations, General Assembly, Special United Nations Fund for Economic Development (A/2728, August 10, 1954) (New York, 1954).

[2]*Ibid.*, p. 10.

any contribution could be made to financing a Special Fund. The third group of countries--which included Denmark, Italy, Norway, the Netherlands, Belgium, France, Japan, and Luxembourg--expressed the view that it would be regrettable to make the creation of SUNFED contingent upon a reduction in armament costs, and declared themselves ready to contribute to the Fund.[1]

The General Assembly adopted resolution 822 during its ninth session on December 11, 1954. This resolution requested that Mr. Scheyven prepare a further report on the establishment of SUNFED. This Mr. Scheyven did. His second report, dated May 23, 1955, contained some further recommendations as to the structure of the Fund. This report contained a clear statement that the Special Fund should only make investments which could not be financed by private capital or by the International Bank.[2] The Special Fund would provide grants or loans repayable in local currency, but would have no authority to make so-called "fuzzy" loans. This second report of Mr. Scheyven called for close cooperation between the International Bank and SUNFED. A proposal was made that the two agencies cooperate on the same project. The Bank could make a loan on conventional terms and the Special Fund could make a grant for the remainder. This is not unlike the arrangement that has been worked out between the International Bank and the IDA in several countries. All in all, this second Scheyven report was much more cognizant of the contribution of the World Bank than was the report prepared by the Committee of Nine.

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[1] Ibid., pp. 15-16.

[2] United Nations, General Assembly, Special United Nations Fund for Economic Development (A/2906, May 23, 1955) (New York, 1955), p. 4.

The Impact of SUNFED

Debate on the desirability of establishing SUNFED continues to this day. Critics have charged that if the United Nations established SUNFED it would have the Soviet Union in it and that this would ruin the operation from the beginning. It was felt that the United States Congress would be reluctant or unwilling to appropriate funds for any agency which would dispense aid to communist countries or have communist countries on its board. Officials in the United States were not too enthusiastic about the fact that the United States Government would have had to provide most all the money for SUNFED, because experience has been that the Russians have not contributed significantly to either the Technical Assistance Program of the United Nations or other such programs. There was also a feeling in the United States Government that the United Nations could not administer such a program. As one official in the Treasury Department put it, "If SUNFED had been established, it would have been one more organization created which would have spent money incompetently."[1]

The International Bank opposed the establishment of SUNFED because of its political administration--which it was felt would be poor administration. The United Nations is a political organization. Various aid-giving countries might put pressure on the administrators of SUNFED to favor certain countries in the granting of loans. Economic considerations might become unimportant in such a situation. However, the Bank's main objection to SUNFED was based on the fact that SUNFED was going to give lenient loans. Everybody would have gone to SUNFED

[1]Interview with an official of the U. S. Treasury Department, January 17, 1963.

for financing. The only way the Bank would agree to having another type of money available was to have it in the same building, with the same men making decisions on World Bank loans and the lenient loans.[1] This is the solution that was finally adopted with the establishment of the International Development Association.

There was considerable criticism of SUNFED on other points, also. One point of criticism was the plan to give each country one vote in the deliberations.

> This is plainly regarded as the ideal solution by the under-developed countries themselves. It is not unkind to suggest that they may be partly influenced by the thought that they would generally be able to command a majority of the votes in such an organization. They seem to envisage a complete specialization of functions, the donor nations solely concerned with the giving and the receiving nations with the disposal of the funds.[2]

Although the question of voting strength was important in the United States' position on SUNFED, it is the author's distinct impression that the United States' position was based more on competence than on voting strength. The United States' view is that the World Bank has competent people to do the work and that they overcome many problems by only taking on specific projects. Thus, if there had to be a new international agency, the United States would much prefer it under the Bank than under the United Nations.

Harlan Cleveland objected to SUNFED because the proposal did not contemplate a strong director. Cleveland feels that "the World Bank, which is essentially run, not by its Board, but by President Eugene Black and his staff"[3] was a better pattern to follow. Again,

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[1]Interview with Mr. Eugene R. Black, March 13, 1963.

[2]Shonfield, p. 100.

[3]Harlan Cleveland in an Introduction to Commander Sir Robert

he criticized the proposal that "SUNFED, like an international Community Chest, would be dependent on annual contributions by its members instead of starting life, as an investment organization should, with a nest-egg of contributed capital."[1]

Andrew Shonfield has elaborated a charge made earlier that the United Nations simply could not administer such a scheme.

> No doubt it would be able to dole out money to the poor countries each year on some simple criterion--e.g. equal shares for all or some system of weighting according to size of population, or even according to national income. But the United Nations as it now stands is not an executive organ which is capable of exercising discriminating and purposeful control over a development program of this magnitude. And if it were able to do so, the underdeveloped countries . . . would almost certainly like it no better than they like the World Bank or the International Development Association.[2]

Professor Benham gave a little more positive view of SUNFED. He argued that the most effective way of increasing economic aid would be to set up SUNFED. The underdeveloped countries liked the idea "partly because they would have had some voice in its affairs; they have no voice in the affairs of an institution such as the International Development Association. . . . They welcomed it also because its aid would have consisted partly of outright grants,"[3] whereas, IDA's charter specifically prohibits grants.

Although SUNFED was never established, the pressure for such an agency has had significant influence. Mr. Eugene Black has stated

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G. A. Jackson, The Case for an International Development Authority (Syracuse: Syracuse University Press, 1959), p.11.

[1] Ibid.

[2] Shonfield, p. 101.

[3] Frederic Benham, Economic Aid to Underdeveloped Countries (London: Oxford University Press, 1961), pp. 106-107.

that "the International Development Association was really an idea to offset the urge for SUNFED."[1] This view has also been expressed to the author by officials of the United States Treasury Department.

Benjamin Higgins believes that "the pressure for SUNFED had two results. First, in October 1958 the United Nations Special Fund was established.

. . . .

A more recent response . . . is the International Development Association."[2]

The establishment of these two new organizations, the United Nations Special Fund, under the leadership of Paul Hoffman, and the IDA, within the World Bank, have reduced but not eliminated the plea of the underdeveloped countries for SUNFED.

The proposal has never had much appeal to the United States of America where the International Development Association idea has been pictured as more realistic. It is to the discussion of IDA, in the United States, that we now turn.

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[1]Interview, March 13, 1963.

[2]Benjamin Higgins, United Nations and U. S. Foreign Economic Policy (Homewood, Illinois: Richard D. Irwin, Inc., 1962), pp. 89-90.

CHAPTER III

THE UNITED STATES AND THE INTERNATIONAL DEVELOPMENT ASSOCIATION

The Gordon Gray Report

On March 31, 1950, President Truman asked Mr. Gordon Gray to undertake a study of United States foreign economic policies and programs. In his report to the President, Mr. Gray pointed out that the Korean conflict and its drain on United States' resources had made it imperative that United States' aid be "channeled to those areas and for those purposes where reasonable performance in the political and economic fields can be achieved. It is important, from this standpoint as well as from others, to develop as far as possible, a cooperative and multilateral approach to foreign programs."[1] Gray recommended that the United Nations and its associated agencies be used as agents for United States' assistance, where possible.

The underdeveloped countries needed firm guidance in the use of outside aid. But, these countries feared such guidance from the United States because it smacked of intervention in their affairs.

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[1]Gordon Gray, Report to the President on Foreign Economic Policies (Washington: U. S. Government Printing Office, November 10, 1950), p. 17.

An international approach was the only practical way to have the guidance which was so essential and escape charges of imperialistic meddling.

Gray argued that there was a very great need for expansion of private investment in the developing areas. And private investment was considered to be the most desirable method of developing countries because it carries with it the technological and administrative skills necessary for success. However, there were very great obstacles to increasing private investment--the paramount one being the state of international tensions existing at the time. Also, the lack of basic facilities which typifies the underdeveloped country was considered a singularly important deterrent to increased private investment flows. And these basic facilities are not attractive to private enterprise because they do not yield a direct financial return or yield a return only over a long period of time.

Gray felt that, in view of the need for social overhead projects and the reluctance of private capital to undertake these projects, the United States should make public funds available for these crucial facilities. And, in light of the limitations inherent in bilateral assistance programs, Gray made quite a strong case for an international agency to handle such an undertaking. Thus, the groundwork was laid for the International Development Advisory Board which was to follow Gordon Gray's reasoning and recommendations and come up with a specific proposal for an International Development Authority. It is to the deliberations of the International Development Advisory Board that we now turn.

The International Development Advisory Board

Mr. Harlan Cleveland gives credit to Nelson Rockefeller and his International Development Advisory Board, a committee of citizens appointed by President Truman, for first suggesting an International Development Association. This Board pointed out that we had banks to make hard loans and foreign aid agencies to give funds away, but no machinery for employing the techniques which lay between pure loans and pure grants. And this group maintained that there were a great number of projects which could not demonstrate the pay-out necessary for a World Bank loan and which cost too much to be included in a grant program of technical assistance.[1]

President Truman had appointed this Board in November, 1950, to make recommendations in the field of foreign economic policy. Nelson Rockefeller served as chairman of the group. Other members were Robert P. Daniel, Harvey S. Firestone, Jr., James W. Gerard, John A. Hannah, Margaret Hickey, Lewis G. Hines, Bertha C. Joseph, Thomas Parran, Clarence Poe, Jacob S. Potofsky, John L. Savage, and Charles L. Wheeler. The group reached an unanimous decision that the United States should take the lead in establishing an International Development Authority.

The Board was led to this decision upon viewing the lack of social overhead facilities in the underdeveloped countries. And they felt that "progress in the production of food, raw materials, and

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[1] Harlan Cleveland in an Introduction to Commander Sir Robert G. A. Jackson, The Case for an International Development Authority, p. 7.

manufactures must move along with the construction of highways, the improvement of rail and port facilities, the expansion of electric power for factories, and irrigation to bring in new farm lands."[1] Unless these type projects were undertaken there would be no success in commercial ventures and attempts to raise living standards would be frustrated.

These improvements in transportation, power and irrigation were pictured as being so expensive that they were beyond the financial resources of the developing countries. Even with assistance from the then existing lending institutions, such projects were beyond the reach of many of the poor nations. And these projects were often such that no direct income was produced for many years and even if income was produced there was the problem of converting it into foreign exchange to repay overseas investors. By their very nature, these projects had no appeal for private capital and that presented the problem.

What would be the most efficient way of financing these public works? The Board recommended a stepped up bilateral loan program for some of these projects but warned that many of them could not be financed on a loan basis. "Our considered judgement is that such public works can be most effectively financed and developed through a well-managed international agency."[2]

The reasons given for favoring an international agency were

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[1] _Partners in Progress--A Report to the President by the International Development Advisory Board_ (Washington: U. S. Government Printing Office, March, 1951), p. 71.

[2] _Ibid._, p. 72.

as follows: (1) A United States agency would be subjected to diplomatic pressures to approve public works to serve political purposes. (2) Standards and procedures must be laid down in order to operate efficiently and it is difficult for one country to impose its standards upon other countries. And if the United States attempted to enforce such standards it would run the risk of engendering ill will and misunderstanding. An international agency could establish international standards which could be applied equally to all countries. (3) There was felt to be an urgent need to devise new financing tools which eliminate the emphasis on large-scale United States "giveaways". (4) It was not the United States' duty to singlehandedly finance the economic development of the world. The costs should be borne by many countries in a genuine pooling of effort among the free nations.[1]

The Board recommended that all the free nations be invited to participate in the new International Development Authority. The Authority would have its own board of directors to review projects submitted to it, however, the staff would be furnished by the World Bank through the use of a management contract. Thus, the Bank's staff could be used to evaluate projects and could also supervise grants that had been made.

Members of the Board discussed this proposal with the staff of the International Bank and concluded that the staff would give sympathetic consideration to such a proposal. This management link with the International Bank was considered to be a very important part of

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[1]*Ibid.*, pp. 72-75.

the proposal for the Development Authority. This was partly because this closeness would make the joint financing of projects possible. The Board felt that there were many sound projects around the world which could not meet the World Bank's requirements. However, if the Development Authority could make a grant for part of the funds, then the Bank could make a conventional loan for the remainder. In fact, the Board strongly urged that the new Authority not be authorized to make grants for the full cost of any project. This was insisted upon because the Board believed that all projects should be able to support at least a portion of the necessary financing on a loan basis and the borrowing country should match to some degree the outside funds provided. A second reason for tying the new Authority to the World Bank would be to gain the advantages of its several years experience in the field. The Board expressed great reluctance to recommend the establishment of a new agency, even under the Bank's aegis. But, "no existing agency is presently organized or has the authority to perform the functions which would be entrusted to the new Development Authority."[1]

Initial funds for the Authority would be $500 million which would be subscribed by the member nations in proportion to their subscriptions to the International Bank for Reconstruction and Development. Each nation would meet its subscription in its own currency. The United States' share was set at $200 million or 40 per cent of the total. The Board considered that the relatively small sum of $500 million should be used as a starter in order to subject the Authority to a thorough testing.

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[1]Ibid., p. 74.

The Board concluded its discussion of the new Authority with a warning.

> There are limits to which we can entrust our interests to new or partially tried international mechanisms. But it is also true that we must strive constantly to develop new international mechanisms which encourage the free participation of all free nations in mutually advantageous association. We must search for mechanisms which avoid the paternalistic approach, seeking instead those which build up a sense of responsibility and self-reliance among other nations and other peoples.[1]

In order to trace the origin of the idea of an International Development Authority, the author contacted Mr. Stacy May. Mr. May had served as Director of Research for the International Development Advisory Board and was known to have played a major role in its considerations. Mr. May reported that

> The Board's Chairman, Nelson A. Rockefeller was the proponent of this suggestion. He had a very strong conviction that if genuine progress was to be made upon development projects of certain types, it would be necessary to provide long-term financing upon terms that were far easier than those currently being offered by governmental lending agencies. As an example, he felt that on such proposals as multiple purpose water-impounding projects standard loans might be practical on the hydroelectric facilities only if grants or loans upon radically better than market terms could be offered to take care of the irrigation and flood control elements of the proposal.
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> I am not at all sure that Nelson Rockefeller originated the basic idea of loans upon terms that share at least some of the characteristics of grants, but I am very sure that it was his initiative and conviction upon this matter that persuaded the other members of the International Development Advisory Board to incorporate the recommendation that IDA be established.[1]

Citizens of the World

Certainly the most grandiose proposal for an International Development Association came from a private citizen in the United

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[1] Ibid., p. 75.

[2] Letter from Mr. Stacy May, May 14, 1963.

States, Mr. Stringfellow Barr. His book, Citizens of the World, which was published in 1952, contained a complete plan for such an Association under United Nations auspices.[1] Barr outlined the need for further assistance for the developing nations and reported the heated debates which had taken place in the United Nations over the establishment of a special fund for economic development.

> The poor countries want it set up. The rich countries, led by the United States, do not. . . . The most interesting detail of the fight is that one of the few things on which the United States and the Soviet Union now vote the same way is an International Development Authority; they both refuse it.[2]

Where would the money come from? How could the United States, at that time engaged in the Korean conflict, spare the resources? Barr suggested that the United States might be able to get the money in the same place it had gotten the $90 billion spent on defense since the time the Development Authority had first been proposed.

Barr rejected the World Bank as a satisfactory agency to deal with the world development problem.

> Since the World Bank . . . depends chiefly on the New York money market, it examines . . . projects primarily from the point of view of sound banking principles, not from the point of view of human need. Like most banks, it is most willing to lend money to those who least need it.[3]

Barr described the American president of the World Bank (Eugene Black) as being unimaginative and dismissed that agency from further consideration. What the world needed, he said, was a new Development Authority which would lend money to governments of

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[1](Garden City, New York: Doubleday & Company, Inc.)

[2]Ibid., p. 61.

[3]Ibid., p. 146.

underdeveloped countries for projects that were socially desirable. Conventional banking standards would not be applied. Outright grants might be made in some cases.

The Development Authority would be authorized by a new People's Assembly of popularly elected delegates from all over the world. One delegate would represent each million inhabitants of the world. The People's Assembly would appoint directors for the IDA.

Money would be raised by issuing bonds to people all over the world. Contributions should be made tax-deductible for individuals and corporations. Countries would be asked to make official donations, also. Every nation would contribute in its own currency; and if any nation was unable to contribute even in its own currency, its shares would go on the cuff until it could contribute. Some countries could give a lien on some of their natural resources. Barr thought it important that all countries of the world contribute either in their own money or in kind.

Attitudes of United States Government Officials

Nothing came of any of these proposals at the time they were made. The United States was involved in the Korean conflict for the first years of the 1950's and was not interested in establishing new international agencies. After 1953, the Secretary of the Treasury, Mr. George Humphrey, believed that economic development abroad should be accomplished through private investment. Any public funds made available should be used for development projects that would be put on a self-sustaining basis. He opposed anything which resembled a give-away and argued that everything should pay its own way. Any money extended to the developing countries should be a legitimate debt which the borrower expected to repay and the lender expected to receive. And the loan should be made at the going rate of interest. This type of foreign assistance meant that there was no burden on the United States taxpayers and the funds would revolve. Humphrey felt that, since the Treasury had to pay 3 or 4 per cent to borrow the money, the underdeveloped countries should pay that rate if the United States loaned them money. There was a distinct feeling that aid programs were international giveaways. And if the United States was going to give money away, it should give it away itself--and not let Gene Black do it. Humphrey was not enthusiastic about United States aid programs--much less about the international programs.[1]

There was a feeling upon the part of some Administration officials that the biggest mistake the United States had made after the Second World War was that it didn't put the Marshall Plan on a hard loan basis. For, it was not until after the Marshall Plan that the developing nations got the idea that they needed low-cost loans for development. The 4 to 5 per cent loans of the International Bank in 1946 were the cheapest international money that had ever been seen. Then the Marshall Plan changed all that and everybody got the idea that it was the United States' responsibility to pay for the economic development of the whole world. Some people in the Administration were doing their best to correct this view, which they considered to be erroneous. Their solution was to handle development assistance on a conventional loan basis through such institutions as

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[1] Interview with an official of the U. S. Treasury Department, January 17, 1963.

the Export-Import Bank.[1]

This view had a considerable following until Mr. Robert B. Anderson succeeded Mr. Humphrey as Secretary of the Treasury. "Although Secretary Anderson was a business type, also, he was not as hard boiled as Humphrey. Anderson was favorable to our aid program. Humphrey went along with it grudgingly."[2] By the time the Monroney Resolution was formally presented, Anderson was Secretary and a new attitude pervaded the Eisenhower Administration.

The Monroney Resolution

Senator A. S. Mike Monroney, Democrat of Oklahoma, was the author of the resolution that finally led to the establishment of the International Development Association. Senator Monroney attended the meeting of the Inter-Parliamentary Union in Bangkok less than a month after his re-election to the Senate in 1956. While he was attending this conference, he was given a guided tour of Thailand. What follows is his account of that tour. "The Thais had gotten a loan from the World Bank to build a low water dam 50 miles up the river from Bangkok which increased rice production something like 50 per cent. It was a $20 million project and they were extremely proud of it and took everyone to see it.

"The United States had provided $2 million for a highway to Cambodia--in the name of defense--and they couldn't even get the King or Prime Minister to come out and dedicate it. The Thais are a very proud people. They were proud of the responsibility of doing the

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[1] *Ibid.*

[2] *Ibid.*

dam project themselves."[1]

Monroney understood why the people of Thailand felt easier borrowing from the International Bank than they did about making bilateral loans from the United States. The Thais are historically neutralists and they didn't like being involved in the Cold War. And yet they needed outside capital for economic development.

It immediately struck the Senator that the Western nations ought to try to provide more funds like those of the World Bank. But, the trouble was that the Bank's terms were too high for many countries. Monroney thought that there ought to be some way to lower the terms by mixing hard currencies and local currencies. Part of a loan could be made in hard currencies at the going rate of interest. Part of the loan could be made in local currencies at much lower rates of interest. This would get the effective rate of interest down quite a bit and the United States would be able to use the local currencies that had been accumulated under the Public Law 480 program.

Title I of Public Law 480 of 1954 had established a program to dispose of surplus agricultural commodities to underdeveloped countries. Countries pay for these imports in inconvertible local currencies and the United States had acquired over $1 billion of these currencies by 1956. About 30 per cent of these currencies were available for United States' use over a period of years--to pay for embassy costs, etc. The remaining 70 per cent were available only for loans back to the country.

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[1] Interview with U. S. Senator A. S. Mike Monroney, January 25, 1963.

In addition to his desire to lower the rate of interest, Senator Monroney also desired to get a longer repayment period than the conventional 10 to 15 year loans made by the International Bank.

The possibility of transferring American-held foreign currencies to a new international association seemed a solution to the need for more outside capital on easier terms and without political strings attached. Monroney felt that the World Bank would be the logical place to locate such a new agency. This would put loaning on a multinational basis and would get some of the other countries of the world to share the responsibility. Also, it would give the borrowing countries a greater feeling of obligation to repay their loans since they came from an international agency of which they were members. The International Bank was known around the world as a soundly administered institution and Gene Black had won the respect of world leaders during his long term as president.

While in Bangkok, Monroney presented his ideas to the meeting of the Inter-Parliamentary Union. He called for "strengthening and enlarging the International Bank and the scope of its work." He suggested that some Marshall Plan counterpart funds were available to the United States which could be pooled with the funds of other nations to increase the capital of the bank. And he mentioned the Public Law 480 funds that were available.

He was of the opinion that the Marshall Plan countries probably had local currencies, also, that could be added to the World Bank and, thus, such nations might be able to re-cycle these original relief funds into doing double duty in reconstruction and development. Besides, the use of Marshall Plan counterpart funds would give a needed boost to Europe's exports.

On his way back from Bangkok the Senator visited Manila. He told the Manila Daily Bulletin that there was a feeling in Congress that the give-away basis of American foreign aid was losing, instead of winning friends for America. "Asian Countries," he said, "would rather have long-term, low-interest loans from rich countries to finance their economic development programs than aid given on a more or less free or counter-part basis. . . . America . . . should siphon her aid to this institution [the World Bank] instead of extending grants . . . [in] the nature of doles or charities."[1]

Senator Monroney and Gene Black are personal friends; so when the Senator got back to Washington he discussed his idea with Black. He also talked to Christian Herter, then Under Secretary of State; Douglas Dillon, then Deputy Under Secretary of State for Economic Affairs; and Senator J. William Fulbright, who was at that time Chairman of the Senate Committee on Banking and Currency. The discussions with Black were encouraging. Monroney's conversations with the State and Treasury Departments were also encouraging. In fact, he felt that he got a very enthusiastic reception at both departments. "Then it was rumored that Dulles came back from one of his trips and killed the whole thing."[2] However, Monroney was not discouraged by a rebuff from the State Department. Senator Fulbright thought the idea was worth further study and appointed Monroney chairman of the Subcommittee on International Finance which would give

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[1]Manila Daily Bulletin, November 24, 1956, p. 1.

[2]Interview with U. S. Senator A. S. Mike Monroney, January 25, 1963.

Monroney a platform from which to launch his proposal.[1]

Senator Monroney had originally thought that an international monetary conference would be an appropriate setting to initiate the International Development Association. He had presented this idea of a "second Bretton Woods Conference" to the Treasury and State Departments and to the President of the World Bank.

> I have suggested such a conference in the many, many conversations I have had with the State Department over the months that have elapsed. For reasons which I think are good and sufficient, on advice of people whose judgments we respect . . . I agreed to this resolution, although I originally thought that the other approach was probably better.[2]

Officials in the Treasury Department were aghast at the idea of a "second Bretton Woods Conference." One Treasury Department official went so far as to say that the Treasury finally came around to support the Monroney Resolution largely to head off the possibility of another monetary conference. This opposition to a conference was based on fear that "a group of people would get together who didn't know what they were talking about." This group of people might seriously weaken or even wreck the existing international financial organizations or re-orient those organizations in a direction that was not satisfactory to the United States.[3]

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[1]Information on the sequence of events leading up to the passage of the Monroney Resolution comes from James A. Robinson, The Monroney Resolution: Congressional Initiative in Foreign Policy Making (Eagleton Institute: Cases in Practical Politics, Case 8; McGraw-Hill Book Company, 1960).

[2]U.S., Congress, Senate, Subcommittee of the Committee on Banking and Currency, Hearings on S. Res. 264 (International Development Association), 85th Cong., 2d Sess., 1958, p. 167.

[3]Interview with an official of the U.S. Treasury Department, March 12, 1963.

The World Bank was just as opposed to another international financial conference as was the Treasury Department. And the opposition was based on much the same reason, that is, that the conference would get out of hand. They were afraid that the long years of work in establishing the reputation of the Bank would go down the drain in some wrangle among the Finance Ministers. So, the Senator came around to the view that a resolution expressing the sense of the Senate as favoring an International Development Association was the best plan of attack. Consequently, on March 24, 1958, Senator Monroney introduced the following resolution in the Senate.

> Resolved, That, recognizing the desirability of promoting a greater degree of international development by means of multilateral loans based on sound economic principles, rather than a system of unilateral grants or loans, it is the sense of the Senate that consideration should be given to the establishment of an International Development Association, in cooperation with the International Bank for Reconstruction and Development.
>
> In order to achieve greater international trade, development, and economic well-being, such an agency should promote the following objectives:
>
> 1. Provide long-term loans available at a low rate of interest and repayable in local currencies to supplement World Bank loans and thereby permit the prompt completion of worthwhile development projects which could not otherwise go forward.
>
> 2. Permit maximum use of foreign currencies available to the United States through the sale of agricultural surpluses and through other programs by devoting a portion of these currencies to such loans.
>
> 3. Insure that funds necessary for international economic development can be made available by a process which eliminates any possible implications of interference with national sovereignty.
>
> It is further the sense of the Senate that as a part of the United States economic aid program funds be subscribed to the capital stock of the International Development Association in cooperation with investments made by other participating countries.[1]

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[1]Senate Subcommittee on Banking and Currency, Hearings on S. 264, 1958, p. 1.

The resolution was immediately referred to the Committee on Banking and Currency. Hearings were held by the Subcommittee on International Finance on March 18, 19, and 20, 1958.

During these hearings, Monroney made a many-sided appeal for support for his resolution. His summation of the arguments in favor of establishing an International Development Association follow.

> Senator Monroney . . . . I believe that the proposed International Development Association would work better abroad than our present program because:
>
> (1) It removes the political stigma attached to loans from the United States alone by placing them under international banking facilities;
>
> (2) It insures to receiving nations a continuation of long-range project financing by removing the uncertainty of year-to-year appropriations for the annual aid bill in Congress;
>
> (3) It provides a further mechanism by which new nations can develop an international line of credit;
>
> (4) It places the responsibility of passing on the feasibility of projects and requests for loans in a genuine banking facility;
>
> (5) It encourages other nations whose recovery has been helped to assume their proper share of the common burden of the development of new nations; and
>
> (6) It facilitates the use in international trade of dozens of local currencies not now freely convertible.
>
> I believe it would work better at home because:
>
> (1) It takes the matter of economic development of underdeveloped countries out of the arena of domestic politics;
>
> (2) It reduces the cost of foreign economic development by the better use of soft currencies acquired in our program of surplus agricultural commodity disposal;
>
> (3) It reduces the cost of administration of foreign-aid programs; and
>
> (4) It enables the Congress to enact a long-range banking program and thereby remove this portion of our aid from year-to-year consideration on an emotional basis.[1]

In addition to these reasons, the Senator also pointed out the desirability of increasing foreign aid from our own selfish economic interest.

Mr. Monroney . . . . As more nations break through the development

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[1]*Ibid.*, pp. 5-6.

> barrier and are able to join that select group of countries with rising living standards and ability to carry out capital development from internal savings, the markets for western goods will simultaneously expand.[1]

He insisted that the United States was missing a bet in not getting the underdeveloped countries to help each other.

> In talking informally with representatives of foreign governments they have indicated to me that at various times they have expressed to the State Department a willingness to do more than we are now asking or permitting them to do.
>
> I am afraid that we are following a policy where we want to go it alone too much and not encouraging others to make a contribution to developing underdeveloped countries which they feel in their hearts they should do.[2]

In an appeal to liberals, Monroney recited the problems of bilateral assistance and the advantage of multilateral aid. "Direct aid by the United States is often viewed with suspicion. Some leaders play off Russia against the United States in an effort to milk the maximum from both."[3]

The Senator attempted to interject the Russian aid effort into the debate so as to present a challenge to the United States to do as well. In his speech to the Senate, when he introduced the resolution, he said, "The Russians have started an intense economic offensive by offering loans for development purposes that are a better deal than ours."[4]

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[1]Congressional Record, February 24, 1958, pp. 2261-7 as quoted in Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, p. 13.

[2]Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, p. 176.

[3]Ibid., p. 4.

[4]Congressional Record, February 24, 1958, pp. 2261-7 as quoted in Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, p. 8.

However, Senator Homer Capehart, ranking Republican on the Committee on Banking and Currency, didn't accept this argument that the United States had to go into the soft loan business because the Russians had.

> Senator Capehart. May I say--and I say it in the kindest spirit--aren't we losing the cold war and losing this battle, likewise, if we completely wreck the private enterprise system, the capitalistic system, by adopting the same kind of methods they do in trying to counteract them? Aren't we going to have to sometimes say this is the better of the two systems and we are going to make it work, and make it work on a practical basis, and we are not going to adopt your methods?[1]

Monroney was not going to let his project be tarred with the brush of communism. He replied to Senator Capehart as follows:

> The Senator was properly worried perhaps that we might be adopting the tools of communism in these low-interest, second-mortgage loans. But would it not be a fact . . . that the Communists have adopted grants and unilateral loans, while we are now moving to a capitalistic approach through international banking. We are abandoning the tools now being principally used by the Communists . . . .
>
> We are going to the capitalistic tools. No one can say that banking is communistic. It is the antithesis of communism.[2]

As to the mechanics of the new Association, the Senator was not too specific. He did have an idea of total funds needed to get the organization going.

> As a starter, it seems to me the International Development Association would need an original capital of $1 billion in dollars or hard currency. The United States would probably put up 30 percent of this amount or $300 million, based on our contribution to the establishment of the World Bank.[3]

After the Association had been established, the Senator had

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[1]Senate Subcommittee on Banking and Currency, <u>Hearings on S. Res. 264</u>, 1958, p. 78.

[2]<u>Ibid.</u>, p. 81.

[3]<u>Congressional Record</u>, February 24, 1958, pp. 2261-7 as quoted in Senate Subcommittee on Banking and Currency, <u>Hearings on S. Res. 264</u>, 1958, p. 11.

a painless plan for keeping it supplied with funds.

> It is likely that more hard currency capital might be needed for 2 or 3 years. If this should prove true, the Congress could commit the $75 million in annual dollar earnings from interest on foreign loans made under previous aid programs and thus meet additional requirements without new appropriations.[1]

It was on the subject of original financing that Senator Moroney aroused the Administration's opposition. For Secretary of State Dulles had just gotten the Congress to appropriate $300 million for the establishment of a Development Loan Fund which would dispense soft loans to underdeveloped nations. And now Monroney had the temerity to suggest that it might be possible to commit this $300 million to the International Development Association.

Monroney continuously presented the IDA as an attractive alternative to the Development Loan Fund because he felt that "We should not establish a permanent State Department bank which would have the possibility of turning our diplomats into bill collectors around the world. We would be using our public relations branch to say 'No' on development loans, and it will be defeating our diplomatic efforts."[2]

The Senator usually referred to the Development Loan Fund as "Mr. Dulles' bank". He insisted that "One of the most important points of this whole business is moving out of being the sole banker of the world--which Mr. Dulles' bank helps to make us become."[3] Senator Clifford Case cautioned Monroney that he would not succeed

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[1] Ibid.

[2] Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, p. 87.

[3] Ibid., p. 137.

in establishing IDA by attacking the present program. "I do have the feeling," Senator Case warned, "that it is unfortunate to attempt to gain these objectives by knocking down the present Development Fund and by attempting to show that it is of no value. With this I thoroughly disagree. I think you will not only fail to accomplish your objective, . . . which I share, by the process, by going at it in that way, but you will also very greatly hurt the whole cause of sound foreign aid."[1]

Senator Case was also concerned that Monroney was making it appear that IDA was somehow going to reduce American outlays for foreign aid. Monroney had cultivated this notion in trying to arouse support for IDA, particularly by his local currency ideas. Senator Case argued, however, that the local currency owned by the United States was already being used as well as it could be. "While this is a good idea it is largely being employed now, to the extent that it has value, and . . . it cannot and must not be allowed to appear in the mind of the American public particularly as any real way by which we can substantially cut down our own effort in the field of mutual aid and of foreign assistance."[2]

Senator Capehart was not at all enthusiastic about the establishment of the International Development Association. He could not understand why Senator Monroney and Eugene Black favored giving loans to countries which were not creditworthy. And Capehart was particularly incensed about the interest rate to be charged.

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[1] Ibid.

[2] Ibid., p. 177.

"I don't know why, if I am a good credit risk, I should be charged more to make a loan than if I were a bad credit risk."[1]

Monroney often described IDA as a second mortgage operation. The World Bank would take a first mortgage on a project and IDA would take a second mortgage for the unbankable portion of the loan. But, Senator Capehart insisted, "A second mortgage generally carries a higher rate of interest than a first."[2]

Senator Capehart insisted that the United States should loan money to the developing countries only at the going rate of interest in the respective countries. Monroney pointed out that fifteen per cent was the going rate of interest in most of those countries.[3]

To counteract adverse testimony by Secretary of the Treasury Anderson, Monroney invited Mr. Averill Harriman and Mr. Paul Hoffman to testify.

Harriman favored the establishment of the IDA and insisted that the Soviet Union should be invited to join and contribute substantially to it "in accordance with the country's obviously great capacity". Harriman expressed the view that one of the things that had made the Marshall Plan such a great success was that the Soviet Union was invited to join and refused. This had established the United States' good faith in undertaking this program and the bad faith of the Russians in opposing it.[4]

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[1] _Ibid._, p. 76.

[2] _Ibid._, p. 77.

[3] _Ibid._, pp. 80-81.

[4] _Ibid._, p. 145.

Hoffman, formerly head of the Marshall Plan program, introduced the need to counteract SUNFED into the hearings.

> Mr. Hoffman . . . . I don't believe we want to get ourselves in a position of competing with Russia, but Russia has become the principal backer of SUNFED, which is the United Nations Development Fund, about which many questions could be raised. However, we can't fight something with nothing.[1]

Mr. Hoffman expressed the view that IDA was the best alternative to SUNFED.

The three main issues that were raised by Monroney's proposal were: (1) the need for soft loans; (2) the possibility of using United States' holdings of local currencies in an international aid agency; and (3) the desirability of using a multilateral approach in economic assistance programs. These issues will be treated in the following three chapters.

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[1]*Ibid.*, p. 82.

CHAPTER IV

THE QUESTION OF SOFT LOANS

Debt Servicing Capacity of the Developing Countries

Is there a need for soft loans? What are the facts concerning the ability of the developing countries to service hard loans? As mentioned in Chapter I, two authoritative studies on debt servicing capacity were made by members of the staff of the International Bank for Reconstruction and Development.[1,2] These studies rely on information supplied to the Bank by debtor countries. The Development Assistance Committee of the Organization for Economic Co-operation and Development publishes statistics, on debt and debt servicing, which are provided by the creditor countries. There is some cross-checking in an attempt to gain reliable information. So far as the author could determine, the International Bank is the only source of statistics on the debt servicing capacity of low-income countries. For this reason, the author relies on these studies to a considerable extent.

The first study of debt servicing capacity, published by the Bank, covered the decade 1946-1955 and was, on the whole, an optimistic

[1]Avramovic, Debt-Servicing Capacity and Postwar Growth in International Indebtedness.

[2]Avramovic and Gulhati, Debt Servicing Problems of Low-Income Countries.

report. Avramovic pointed out that the size of postwar capital flows had been much above corresponding flows in the 1920's and that grants-in-aid had played a very substantial role in the post World War II period. Such grants had served to reduce the burden of debt that normally follows capital outflows.[1]

Avramovic defined external public debt as the

> Long-term debt owed or guaranteed by public bodies in debter countries. It includes debts of central and local governments, of public agencies and state-owned enterprises. External debt is taken to mean all debt which is contracted and payable externally. Grants-in-aid as well as loans granted by foreign governments but repayable in local currency are not treated as external loans. Short-term debts with a maturity of less than one year . . . are excluded.[2]

Avramovic estimated that the size of the return flow of service payments (public as well as private) of 36 low-income countries increased by 80 per cent in constant dollar prices from 1948-1955. Public debt service was reported to have risen considerably faster than the return flow on private account.[3] This 80 per cent increase was not viewed with alarm because of the relatively low base of debt service payments at the close of the Second World War. Avramovic concluded, on the basis of criteria to be discussed later, that there was plenty of room for further increases in indebtedness on the part of the developing nations.

How did he measure capacity to meet debt service payments? Primarily, he argued, debt service capacity depended upon two economic

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[1]Avramovic, p. 17.

[2]*Ibid.*, p. 20.

[3]*Ibid.*, p. 147.

factors. First, the debtor country must be able to do without enough domestic income and savings to make payment on the debt. Secondly, the country must be able to convert such savings into foreign exchange. These two are interdependent. "A high rate of over-all income growth, maintained over a long term, almost automatically implies an adequate rate of increase in the supply of commodities which either actually enter international trade or are capable of being internationally traded."[1] In order, thus, to measure debt-servicing capacity, one must look at the country's performance in the fields of income and savings and in the field of foreign trade. The most relevant ratio is the ratio of public debt service to current account receipts.

During the decade 1946-1955 the income of the developing countries grew at a rapid rate. However, Avramovic's statistical evidence indicated that aggregate service payments (expressed in constant prices) grew even faster.[2] In addition to income growth, the developing countries showed a rapid increase in gross savings during the decade under discussion. In the majority of countries considered the marginal savings rate was greater than the average rate, also.[3]

The crucial ratio, as pointed out earlier, is the relationship between service payments and current account receipts. In 36 developing countries, covered by the study, exports increased 62 per cent from 1948 to 1955. These same countries' debt service payments on public and private account rose by almost 90 per cent in the same period.[4] "As a consequence, the share of external earnings absorbed by service payments

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[1]*Ibid.*, p. 58.

[2]*Ibid.*, pp. 61-62.

[3]*Ibid.*, p. 79.

[4]*Ibid.*, p. 95.

increased from about 6.7% in 1948 to 7.7% in 1955. . . . The increase in the ratio of public debt service to external earnings was greater."[1] The statistics on debt service payments as a percentage of current account receipts for the 36 developing countries covered in Avramovic's study are shown in Table 1.

By the time that Senator Monroney's Resolution had borne fruit, and the International Development Association was being considered by the member governments of the World Bank, a second study on debt servicing capacity had been issued. The optimism evident in the study published in 1958 was missing in the 1960 report.

Although it was pointed out that the less developed countries had been receiving an increasing proportion of public funds transferred abroad, it was also noted that an increasing portion of these funds was taking the form of loans.[2] This phenomenon is accounted for by the fact that the United States gave Marshall Plan aid to the relatively rich nations of Western Europe on a grant basis whereas the aid to the poverty stricken countries of Asia, Latin America and Africa was mostly loans and mostly loans on conventional terms, i.e. Export-Import Bank operations.

In addition to the fact that capital was not extended on as favorable terms as before, it was pointed out that the export earnings of the primary producing countries had taken a nose-dive during the period of the second study, 1956-1958. And, while primary product prices fell, the prices of manufactured goods rose throughout the

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[1] *Ibid.*

[2] Avramovic and Gulhati, p. 10.

TABLE 1.--Relationship between service payments and current account receipts[a]

Country	Public Debt Service as Percentage of Current Account Receipts		Private Service Payments as % of Current Account Receipts	Total Service Payments as % of Current Account Receipts
	Postwar Direction of Change in the Ratio	Current Ratio (1955)	Current Ratio (1955)	Current Ratio (1955)
Brazil	I	19.2	5.4	24.6
Israel	n.a.	16.8[c]	1.5[c]	18.3[c]
Yugoslavia	I	13.1	0.9	14.0
Haiti	I	9.5	2.8	12.3
Chile	I	8.0	13.6	21.6
Turkey	n.a.	7.1[c,d]	n.a.	n.a.
Mexico	I	7.1	6.4	13.5
Columbia	I	6.8	2.2	9.0
Lebanon	n.a.	6.7[e]	17.4[e]	24.1[e]
Pakistan	I	6.1	2.4	8.5
Burma	n.a.	5.9[f]	0.7[f]	6.6[f]
Peru	I	5.4	6.1	11.5
Uruguay	S	5.1	2.0	7.1
Nicaragua	I	4.9	8.9	13.8
Paraguay	D	4.9	1.4	6.3
Bolivia	n.a.	4.6	2.9	7.5
Indonesia	n.a.	3.6[g]	11.1[g]	14.7[g]
Ecuador	I	3.6	14.1	17.7
Fed. of Rhodesia and Nyasaland	I	2.8	18.2	21.0
Argentina	n.a.	2.5	1.8	4.3

TABLE 1--Continued

Country	Public Debt Service as Percentage of Current Account Receipts		Private Service Payments as % of Current Account Receipts	Total Service Payments as % of Current Account Receipts
	Postwar Direction of Change in the Ratio	Current Ratio (1955)	Current Ratio (1955)	Current Ratio (1955)
Philippines	n.a.	2.2	12.1	14.3
Cuba	n.a.	1.9[e]	5.2[e]	7.1[e]
Belgian Congo	I	1.6	11.4	13.0
Iceland	I	1.5	0.6	2.1
Costa Rica	n.a.	1.5[c]	11.8	13.3
Iraq	n.a.	1.4	35.9[c]	37.3
El Salvador	D	1.0	6.0	7.0
Thailand	S	1.0	1.9	2.9
Iran	n.a.	n.a.	20.4[h]	20.4
Panama	S	0.7	13.9	14.6
India	S	0.7	3.6	4.3
Guatemala	S	0.5	5.8	6.3
Ceylon	S	0.5	4.0	4.5
Ethiopia	I	0.4	2.3	2.7
Venezuela	n.a.	0.1	29.3	29.4
Dominican Republic	n.a.	0.0	9.6	9.6

Notes: I indicates that the public debt service ratio increased.
S indicates that the public debt service ratio remained stable.
D indicates that the public debt service ratio declined.

TABLE 1--Continued

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[a]Current Account Receipts is defined to include goods, services, and private remittances. Gross receipts are used.

[b]Repatriation of private investment is not included.

[c]1954.

[d]May include some private service payments. Probably incomplete.

[e]1953.

[f]Average for 1954-55.

[g]Ratio to commodity exports only.

[h]May include some public debt service payments.

Source: Data from International Bank for Reconstruction and Development, Economic Staff, Statistics Division, for public debt service; International Monetary Fund, Balance of Payments Yearbook, various issues, for investment income payments and for current account receipts. Adapted from Avramovic, Table XVI, pp. 98-99.

period.[1]

As a result of the deterioration in their terms of trade, the underdeveloped countries had to reduce their rate of capital good imports. It was estimated that these countries' imports were reduced \$2.2 billion from 1957 to 1958 or about 10 per cent of the 1957 level of imports.[2]

A third adverse factor had entered the picture during the 1956-1958 period. There was a sharp rise in interest rates on international loans. And there was a marked shortening of the average effective period of repayment.[3]

Table 2 shows the external public indebtedness of 32 developing countries (accounting for two-thirds of the population of the underdeveloped countries outside the Soviet bloc) at the close of 1955 and at the close of 1958. The total public indebtedness of these 32 countries had increased from \$6.2 billion to \$10.1 billion in a period of 3 years. This is a 63 per cent increase. For some of these countries the original indebtedness was so low that any new debt shows up as a high percentage increase. But, for others, notably Brazil, Argentina, and India, the original indebtedness was considerable.

As large as the public debt service burden is in these countries, we must not forget that service payments on private account are about twice as large. In 1955 public debt service payments of these 32 low-income countries were \$653 million while service payments on private

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[1] Ibid., p. 28.

[2] Ibid., pp. 40-44.

[3] Ibid., pp. 18-20.

TABLE 2.--External public indebtedness December 31, 1955 and December 31, 1958 (millions of U. S. dollar equivalent)

	December 31, 1955	December 31, 1958
Latin America	3,705	5,246
Brazil	1,204	1,509
Argentina	(600)	(1,430)
Mexico	500	599
Chile	354	459
Colombia	274	438
Peru	222	216
Uruguay	127	131
Bolivia	94	96
Ecuador	69	94
Cuba	65	58
Panama	21	42
Haiti	43	37
Costa Rica	36	34
El Salvador	28	26
Nicaragua	23	25
Guatemala	22	22
Paraguay	18	17
Honduras	5	13
Asia, Middle East and Africa	2,592	4,874
India	308	1,442
Israel	(360)	(556)
Fed. of Rhodesia and Nyasaland	371	526
Belgian Congo	316	516
Indonesia	(569)	(415)
Iran	230	377
United Arab Republic	5	291
Pakistan	148	200
Philippines	91	198
Thailand	73	143
Burma	17	84
Ethiopia	33	51
Ceylon	44	48
Lebanon	27	27
Total, non-European low-income countries	6,297	10,120

Note: Figures in parentheses are crude estimates.

Source: Data from IBRD Statistics Division. Adapted from Avramovic and Gulhati, Table II, pp. 13-14.

account were $1,117 million. In 1958 the ratio was much the same. Private service payments were $1,280 million and public debt service payments were $770 million.[1] Of course there is a degree of flexibility in service payments on private account that is not present in public debt service payments. Insofar as private service payments take the form of dividends, they may fluctuate with export earnings in such a way as to minimize the strain on the balance of payments.

Table 3 presents public debt service as a ratio of export earnings for 30 developing countries (for which such figures were available) in 1955, 1956, 1957 and 1958.

A drastic worsening of the ratio is evident in the case of Columbia (from 6.1 in 1955 to 21.4 in 1958), Chile (8.8 to 13.2) and Ecuador (4.0 to 9.8). The weighted average for all these countries rose from 4.9 per cent of current account receipts in 1955 to 5.8 per cent in 1958.[2]

The fact that the study ended in 1958 gives, perhaps, too favorable a picture of the position of some countries. It will be noticed from Table 3 that India's public debt service only required 1.7 per cent of current account receipts in 1958. This is not an alarming ratio. However, 1958 was the beginning of heavy borrowing for the Second Five Year Plan and this ratio changed considerably in a very short period.

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[1]Avramovic and Gulhati, Table III and Appendix Table XXI, p. 19 and p. 73.

[2]*Ibid.*, p. 54.

TABLE 3.--Ratio of public debt service to current account receipts

Country	1955	1956	1957	1958
Colombia	6.1	5.2	10.2	21.4*[a]
Chile	8.8	9.3	10.6	13.2*[a]
Brazil	19.7*	10.1	11.3	13.0[a]
Ecuador	4.0	5.7	6.1	9.8*[a]
Haiti	6.5	14.1*	6.5	9.3[a]
Mexico	7.7	7.0	8.8	9.0*
Peru	4.9	8.3*	6.7	7.6
Uruguay	5.6	5.0	6.9	7.1*
Iran	1.3	1.0	3.1	5.5*
Pakistan	2.3	4.1	4.4	5.3*[a]
Panama	0.7	0.7	0.6	4.9*[a]
Nicaragua	4.9	5.3	7.0*	4.7
Fed. of Rhodesia and Nyasaland	2.7	2.8	3.8	4.2*
Costa Rica	0.9	3.5	3.7	4.2*
Paraguay	4.3*	4.3*	3.9	4.2
Belgian Congo	1.7	2.7	3.5	4.0*
Bolivia	4.8*	3.9	2.3	4.0[a]
Indonesia	3.8*	2.9	2.6	3.5
Thailand	1.1	1.4	2.0	2.3*
Philippines	1.5	1.5	2.4*	2.1
Ethiopia	0.4	1.0	1.8	1.9*
Honduras	0.0	0.0	0.6	1.8*
Burma	0.5	0.6	0.5	1.5*
India	0.7	0.7	0.9	1.7*[a]
El Salvador	1.0	1.1	1.1	1.4*
Malaya[b]	0.3	0.6	0.7	1.0*
Guatemala	0.2	0.2	0.5	0.7*
Cuba	1.0*	0.7	0.6	0.6[a]
Ceylon	0.5	0.5	0.6*	0.5
United Arab Republic	0.2	0.2	0.2	0.2[a]

*Indicates peak ratio.

[a]Preliminary.

[b]Ratio of debt service to commodity exports.

Source: Data from IBRD Statistics Division; IMF Balance of Payments Yearbook, various issues. Adapted from Avramovic and Gulhati, Table VIII, p. 53.

Despite the greater than 60 per cent increase in public indebtedness of the 32 low-income countries, Ávramovic and Gulhati concluded that "the possibilities for further international lending are far from exhausted. There are a great number of countries which are still in a position to assume new long-run obligations."[1] However, this conclusion is tempered with a warning. "Recent experience suggests that at certain points in the growth process, some countries incur substantial amounts of debt in a very short period of time; and this experience may well be repeated in other cases in the future."[2] In some countries uncertain export prospects and already heavy debt burdens made further borrowing difficult if not impossible.[3]

Thus, this second estimate of debt-servicing capacity presented a mixed picture. Although some countries could still borrow safely, apparently there was a growing number that had passed their limit. It was this latter group of countries that particularly pressed for the establishment of some institution like the International Development Association.

The Plight of Certain Countries

Is there some formula which establishes the limit beyond which a country's ratio of indebtedness to export earnings cannot go with safety? Although the International Bank says there is no such formula, in practice, the Bank regards a country as being in trouble when more than 6 or 7 per cent of their external receipts is absorbed by financial obligations abroad. Beyond this point, a special study is

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[1] Ibid., p. 59. [2] Ibid. [3] Ibid.

necessary to justify granting of further assistance.[1]

What does it mean for a country to go beyond some such limit? The word goes out that that country is no longer creditworthy. "What this really means is that the bankers judge that such a country might in a crisis find the temptation to default on its foreign debt overwhelming."[2] Most observers agree that the danger point has been reached by several Latin American countries, particularly Brazil, and is just ahead for India and Pakistan.

The case of India deserves special consideration. This country contains approximately 400 million people or one-third of those people living in underdeveloped countries (outside the Soviet bloc) today. What happens in India may have a crucial impact on the hopes of other developing countries following a non-totalitarian path.

Shonfield cites India as the most dramatic case for soft loans.

> Consider, for example, the arithmetic of India's Third Five-Year Plan, beginning in 1961. Taking the most conservative estimate of what the Indians will need to carry out a substantial program . . . the foreign-trade deficit during this period will average an amount equal to roughly two-thirds of India's export earnings today.[3]

What are the chances of increasing India's export earnings? One observer of the Indian economy has said that "As far as 95% of the exports from India are concerned, there is thus little likelihood of any marked increase even over the next two decades. In the past three

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[1]Leonard Rist, "The Capacity to Service Foreign Debts"--A lecture presented to the Economic Development Institute of the International Bank for Reconstruction and Development (IBRD) July 9, 1962 (Washington: IBRD, 1962) p. 10. (Mimeographed.)

[2]Shonfield, p. 97.

[3]Shonfield, p. 30.

decades the volume of exports of these items has fallen, and the trend may continue."[1]

Even assuming that the Indians were able to increase exports to the point that the foreign trade deficit was equal to only half their export earnings, Shonfield points out that, "this would mean that by 1966 the debt accumulated over the Five-Year Plan would amount to two and a half times the value of the country's export trade."[2] And this indebtedness would, of course, be on top of the already large debt burden.

If India borrowed the funds necessary to finance the Third Five Year Plan at 5 per cent interest for a 20 year period, she "would have to find each year a sum in foreign exchange, for interest and principal repayments together, equal to 10 per cent of the total amount borrowed during the five-year period."[3] This would mean that the annual cost of servicing the Third Plan debt would take 25 per cent of export earnings.

But, this is only the beginning. "More than $1 billion will be required for the repayment of external debt . . . during the period covered by India's Third Five Year Plan."[4] And this amount equals about 10 per cent of India's foreign exchange earnings each year. So, that by 1966, when the Third Plan is completed, India would be requiring

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[1]S. J. Patel, "Export Prospects and Economic Growth: India," The Economic Journal, LXIX (September, 1959), 501.

[2]Shonfield, p. 30.

[3]Ibid.

[4]Robert E. Asher, Grants, Loans, and Local Currencies (Washington: The Brookings Institution, 1961), p. 97.

something in the nature of 35 per cent of her export earnings just to service foreign debt!

The problem plaguing India in her attempt to increase export earnings is that of many developing countries today. Even though the people save fiercely and limit consumption to a starvation level, there is great difficulty in turning the goods saved into export items. There has not been any substantial increase in world demand for India's traditional exports of tea and jute. Textiles served as a medium for entering the export field for Japan, and India is trying to emulate Japanese experience. But, here the Indians run up against not only tariffs but "voluntary quotas" on textile exports. Even a program of rampant price-cutting cannot overcome such restrictions.

It is important to remember, in considering the problems confronting the Indians, that they are attempting to raise per capita income by 3 per cent a year, starting from one of the lowest income bases in the world. But, the size of the population is such that just to increase per capita income one dollar each year requires an increase in national income of $400 million. Assuming a capital-output ratio of about 3:1, in order to increase national income $400 million an investment of something over $1 billion is required. We should, indeed, "consider the arithmetic of India's Third Five-Year Plan."

India is not alone in her plight. At the 1961 meeting of the Board of Governors of the International Bank, the Governor from Pakistan presented a very similar picture of his country. What are the alternatives for such countries? The Pakistani Governor said they have two. First, they could cut their development plans and programs back to the amount of soft loans available. Or, they could assume conventional obligations that they know they will not be able to repay, in the hope that someone will bail them out.[1] This is a rather unappealing set of alternatives for any government that is trying to win popular support at home and at the same time maintain international respectability.

The Governor of the Bank for Nepal presented a different case. His country is not overwhelmed with outstanding debt. But, the opportunities for investments of a commercial or quasi-commercial pattern are practically non-existent. This is true because the economy needs so many of the basic requirements which yield no direct return.[2]

Is it wise to saddle countries like Nepal and the newly independent African countries with a lot of conventional debt at this point in their struggle for survival? Maybe the West could learn something from the experience of trying to finance India's and Pakistan's development through the use of conventional loans. Dr. Robert Asher has estimated that because of India's past conventional borrowing, Indian "aid requirements will be nearly 25 per cent greater than the $4.4 billion believed necessary for the import of capital goods during 1961-1965."[3] Is it just making more trouble for the future if hard loans are used as the main source of development capital? For, hard loans must increase enough to allow these countries to repay principal

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[1]IBRD Board of Governors Press Release No. 5, September 19, 1961, pp. 2-3.

[2]IBRD Board of Governors Press Release No. 16, September 18, 1962, p. 2.

[3]Asher, p. 97.

plus interest or these countries are led into a very cynical default.

Alan Neale has suggested that the countries that have passed the sensible limits of debt servicing capacity--India, Pakistan, Brazil and some of the African countries--do have one other alternative. They can, of course, adopt the Communists' methods of forced savings in order to achieve capital formation quickly.[1]

The World Bank and Soft Loans

Mr. V. K. R. V. Rao, in giving the Montague Burton Lecture at the University of Leeds in 1960, conceded that his proposal for a United Nations Economic Development Administration was obviously premature in the world of 1949. He recalled the World Bank's comments on that proposal and noted the irony of the fact that the Bank would be concurring in the establishment of the International Development Association only a decade later.[2]

The Bank's management would not plead guilty to inconsistency in their policy. For, the staff of the Bank has had a long-standing policy of opposition to what they call "fuzzy" loans. From the time when Mr. John McCloy was president down to today, the opposition to "fuzzy" loans remains strong. And this is not without some reason.

Just what is a "fuzzy" loan? The Bank defined "fuzzy" loans quite early, as loans repayable in local currency or loans where the

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[1]Alan D. Neale, The Flow of Resources from Rich to Poor (Harvard University Center for International Affairs Occasional Papers in International Affairs Number 2; Cambridge: Harvard University, 1961), pp. 41-42.

[2]V. K. R. V. Rao, International Aid for Economic Development--Possibilities and Limitations (The University of Leeds Eighteenth Montague Burton Lecture on International Relations, 1960), pp. 15-16.

obligation to repay was not clear. The Bank felt that if loans were made at low rates of interest or with an uncertain duration (as proposed in SUNFED) that borrowers would not take the obligation to repay seriously and this attitude would carry over to the loans made by the Bank and other creditors. Loans repayable in local currency were considered to be nothing but disguised grants.

The staff continued to oppose "fuzzy" loans, but by 1950-51 there came the realization that something else was needed besides conventional loans. "We had to have some kind of soft money in order to carry out the bare minimum that had to be done."[1] Speaking on behalf of the Bank to the United Nations Economic, Employment and Development Commission on May 17, 1951, Mr. Richard H. Demuth said:

> We believe that, in some countries, the rate of development cannot be accelerated substantially if the only external capital they receive is in the form of loans which have a reasonable prospect of repayment. If additional assistance is to be given to these countries we believe strongly that it should be in the form of grants, rather than in the form of quasi-loans, and that the grants should preferably be administered through international channels.[2]

The President of the Bank, in evaluating the requirement for soft loans, said:

> There are some in the creditor countries who advocate putting foreign aid on a grant-in-aid basis in order to escape the eventual necessity of taking repayment in foreign goods. On the other hand, there are some who advocate putting all aid on a 100% hard loan basis, ignoring the virtually insuperable transfer problems which this would create. Even if the creditor country is prepared to continue lending and relending on a large scale indefinitely, so that its actual capital investment need never be repaid,

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[1] Interview with Mr. Eugene R. Black, March 13, 1963.

[2] Richard H. Demuth, "Statement on Behalf of the International Bank for Reconstruction and Development Before the Economic, Employment and Development Commission" (Washington: IBRD, 1951), p. 10. (Mimeographed.)

> the mounting burden of interest can itself become a formidable problem.
>
> It is with such thoughts in mind that I have often endorsed in principle the idea that a significant part of development aid should be extended on terms providing some relief from the transfer burden. I have repeatedly observed that the justifiable and really minimum needs for development capital in the underdeveloped countries are greater than can be met through conventional loans.[1]

This speech came after the proposal for an International Development Association had been made and represents the tenor of thinking in the Bank during the last half of the 1950's.

In a later address, Black argued that, to be successful, development aid must be accepted as a more or less permanent feature of Western policy with a separate and distinct status of its own.[2] "Conventional loans alone will not do the job. A developing country can reach very rapidly the prudent limit of its capacity to assume fixed foreign exchange obligations, as we are learning in the Bank."[3]

Black also had a warning for the world's bankers and politicians.

> To ignore this prudent limit and simply pile loan upon loan is to destroy the very order in international financial transactions which development diplomacy is in part designed to preserve. . . . We can no longer afford periodic wholsale defaults as a means of cleaning out the international financial system.[4]

In order to get around this business of wholesale defaults such as happened after World War I, Black urged the nations of the world to

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[1] Summary Proceedings of the 1959 Meeting of the Board of Governors of the International Bank for Reconstruction and Development (Washington, IBRD, 1959), p. 10.

[2] Eugene R. Black, The Diplomacy of Economic Development, pp. 44-45.

[3] Ibid., p. 55.

[4] Ibid., pp. 55-56.

devise a "whole variety of financial instruments, some quite new and novel, if we are to preserve order in the balance of payments of the new nations and to keep in constructive contact with them."[1]

There has been a considerable degree of disagreement on just what form these new and novel financial institutions should take. The second Scheyven Report to the United Nations had presented a proposal for loans repayable in local currency.[2] The Bank looked with considerably more favor on this idea than on the earlier indeterminate loan proposal. And, if properly administered, the Bank would have favored such local currency loans.[3] In 1957 the establishment of the United States Development Loan Fund made local currency loans legitimate and the Articles of Agreement of the International Development Association are clearly designed to permit loans repayable in local currency. The report of the Executive Directors which accompanied the Articles of Agreement specifically mentioned "loans repayable wholly or partly in local currency."[4] Even though such loans are authorized, to date, none has been made. The finance made available by IDA does have a foreign exchange burden even though repayment is spread over a very long period. But, the staff of the Bank is not willing to call even these loans.

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[1] *Ibid.*, p. 56.

[2] United Nations, General Assembly, *Special United Nations Fund for Economic Development* (A/2906, May 23, 1955) (New York, 1955), p. 18.

[3] Interview with an official of the International Bank for Reconstruction and Development, March 8, 1963.

[4] *Report of the Executive Directors of the International Bank for Reconstruction and Development on the Articles of Agreement of the International Development Association* (Washington: IBRD, 1960), p. 7.

They are referred to as "development credits" and Mr. Black feels that they are really disguised grants.[1]

How can a no-interest loan made repayable over a 50 year period be distinguished from a "fuzzy" loan? First, there is a definite repayment date set. Secondly, there is a foreign exchange burden. The staff of the Bank would have much preferred outright grants to such arrangements but both the developed and developing countries preferred the "development credit" approach.[2]

And the financial community much preferred no-interest loans to 3 per cent loans. A 3 per cent loan was a "fuzzy" loan--not really a loan and not really a grant. The financial world is full of biases, cliches, and symbols and they felt that there was something very real about this distinction. And since the Bank must rely upon the financial community to purchase its bonds, the Bank must attempt to conform to their expectations.[3]

As mentioned earlier, from 1950-1951 on, the Bank became increasingly aware of the need for more funds for economic development. There was considerable discussion about what should be done about it. As some countries moved into the category in which they could never borrow from the Bank and as more countries approached the end of their creditworthiness, there was no help to offer these countries at all, unless the Bank changed its nature altogether. And it couldn't do that under the Articles of Agreement drawn up at Bretton Woods. There were various proposals that the Bank simply extend the period of repayment

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[1]Interview with Mr. Eugene R. Black, March 13, 1963.

[2]*Ibid.*

[3]Interview with an official of the IBRD, March 15, 1963.

on outstanding loans. Shonfield argued that the Bank's reserves of $500 million should allow the bank to make such a concession.

> Granted, the institution must keep up a tough appearance and give a fair imitation of a hard-faced banker, if it is to keep its relations sweet with Wall Street and other money centers. But lengthening the term of a loan, by offering a country, say, an extra five years before it has to begin repaying the principal in annual installments, surely need not be interpreted as a dangerously soft and unbusinesslike act, when interest and other charges amounting to a total of over 6 percent per annum . . . are to be paid by the borrower right through the extra five years. . . . . Some people might regard this as rather a good investment. . . . No doubt some of the brokers and investment bankers would shake their heads a little at first, as they invariably do whenever some object on the fixed horizon of banking conventions shifts its position ever so slightly; but they would soon recognize that the security of this highly profitable investment in World Bank bonds had not been reduced, just because some of the loans were going to be left to earn interest for a few years longer.[1]

Such proposals have been dismissed by the Bank as a violation of the trust placed in the Bank by its investors. McCloy and Black have both spent a great deal of time going around the United States assuring the bankers and other investors that nothing would threaten the sanctity of the loans made. And any alteration in the terms is felt to be a dangerous violation of this pledge.

By the time Monroney made his proposal, involving the local currency question as it did, the Bank was ready to consider almost anything that did not involve a fundamental change in principles. The Thirteenth Annual Report of the International Bank for Reconstruction and Development, published in September 1958, expressed the opinion that the Monroney proposal, although involving complexities which would have to be resolved, was very interesting and deserving of further

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[1]Shonfield, p. 99.

study.[1]

In his speech to the Board of Governors in 1958, President Black said:

> It would be a sad setback to the efforts and achievements of the past decade if the flow of international development capital should stagnate just when governments in the underdeveloped world have made significant progress in persuading their people to accept the changes and to make the sacrifices necessary for future growth. I can think of no quicker way to destroy the hopes of hundreds of millions of expectant people than that we, to whom they look, should be unprepared and unequipped for new situations as they unfold.[2]

Later in the same speech he commented on the need for new supplies and sources of international development capital and the desirability of channeling it through international agencies.[3] This was about as strong support as Black felt he could give in view of his position as head of an international agency and in view of the fact that the Monroney proposal was, after all, only a resolution before the United States Senate--a purely domestic affair.

Views of Some Developed Countries Toward Soft Loans

The official view of the Eisenhower Administration toward soft loans was undergoing a considerable change during the last part of the 1950's. With the change in personnel at the Treasury Department--the replacement of George Humphrey by Robert B. Anderson--there was a noticeable thaw in the position toward non-conventional loans for

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[1](Washington: IBRD, 1958), p. 6.

[2]Summary Proceedings of the 1958 Annual Meeting of the Board of Governors of the International Bank for Reconstruction and Development (Washington: IBRD, 1958), p. 13.

[3]*Ibid.*, p. 14.

developing countries. Deputy Under Secretary of State for Economic Affairs Douglas Dillon reflected the new policy of the Administration in his testimony before the Monroney Committee.

He stated that the State Department had estimated the need for soft loans at about $750 million a year in addition to the sums being made available by Western Europe. This $750 million per year had been the goal of the Administration in setting up the Development Loan Fund. However, Dillon argued that if the United States switched this amount of funds from the Development Loan Fund to the International Development Association,

> It would require at least an equivalent annual contribution from the other developed countries. Otherwise, the International Development Association would lose its multinational character and become a mere instrument or tool of the United States. An annual contribution of any such magnitude by the other developed countries over and above their present effort is clearly out of the question for the foreseeable future.[1]

The Administration apparently felt that since the entire soft loan program could not be put on a multilateral basis, it was better not to put any of it on such a basis. Even though the Administration had been convinced of the necessity for soft loans, there was lingering doubt in the Congress.

Representative John Rhodes, of Arizona, was very greatly concerned about the impact of IDA loans on the moral fibre of the underdeveloped countries.

> Mr. Rhodes. Apparently the governing body of IDA has made a policy decision, for at least the time being, not to charge interest. I question the wisdom of it, not only because I think most people who borrow money expect to pay interest, but because it seems to me

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[1]Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, p. 141.

there is some virtue to charging interest.[1]

Not only was Mr. Rhodes concerned about the loss of virtue that follows not paying interest, he was also concerned about the morality of the United States in making such funds available.

> Mr. Rhodes. However, at some time in the future it seems to me that in the expectation of a normal borrower, he would, at some time start paying interest. I do not think that we are playing fair with the underdeveloped countries if we let them get into the habit of thinking that the moon is made of green cheese and I am afraid this is exactly what we are doing by making this type loan.[2]

Alan Neale has referred to this type argument as a

> more than usually nauseating line. . . . If the poor countries could increase their import capacity sufficiently by raising money on commercial terms, they would do so. This is just what they cannot do. In a capital-hungry world it is obvious that by and large new investment projects in the faster-growing advanced countries will tend to offer a safer and more attractive return than projects in underdeveloped countries and that in a free world market for capital the latter would be outbid nearly every time. This line is humbug and in reality asserts that underdeveloped countries should not get capital at all.[3]

In Europe, there is still considerable opposition to soft loans. Germany and the United Kingdom, in particular,

> have raised objections of principle against soft loans, especially with respect to interest rates. The German Government feels that loans at soft terms may impair the role of private capital, distort competitive positions and weaken the function of interest rates in allocating scarce capital among competing uses. Care must be taken, in the view of the German Government, to ensure that the granting of loans at soft terms does not constitute a substitute for monetary and financial discipline on the part of the recipient countries. The United Kingdom Government generally makes loans at the rate at which it can borrow plus a small management charge. It is concerned, in addition, that lending at soft rates might

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[1]U. S., Congress, House, Subcommittee of the Committee on Appropriations, <u>Hearings, Foreign Operations Appropriations for 1962</u>, 87th Cong., 1st Sess., 1961, p. 97.

[2]<u>Ibid.</u>, pp. 98-99.

[3]Neale, p. 39.

have repercussions on the terms of treasury lending to domestic borrowers, such as the nationalized industries. The United Kingdom Government tries to reduce the debt service burden by extending the period of repayment, now typically at 25 years, and by granting grace periods.[1]

Commander Sir Robert G. A. Jackson has presented an impressive argument against this plea "for the role of private capital."

> Many of us in the West feel that large movements of capital should be somehow automatic, with capital seeking the best areas of investment and responding to opportunities for profit. This would be the "natural" method and to those who reason thus governmental activities or action by international agencies are felt to be a disturbing departure from the old, free, liberal tradition. It is therefore relevant to ask how the movements of capital occurred in the past and whether "automatic" methods would still bring the same results. . . . . We can see that a number of essential elements in the earlier patterns of international investment are now lacking. In the first place, the world is much less secure. . . . Today the one-time prop of "law and order" in large parts of the world--the colonial control exercised by European powers--has vanished, and rightly so. . . .
>
> Furthermore, much automatic investment has vanished, or is vanishing, with the end of colonialism. . . .
>
> Another vital fact is that the whole outlook for private capital has changed. . . . Today the largest potential investor, America, has a vast prosperous internal market.[2]

Commander Jackson's wife, Lady Jackson, has added her voice to those who would argue for more soft loans.

> I do not believe we are thinking about development on anything like a large enough scale. Our sense of proportion in this whole question of economic assistance is still quite wrong. The most revealing figure is that the world can spend 100 billion dollars each year on defense, yet if we produce five billions in economic assistance, we think we are doing very well.[3]

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[1]Organization for Economic Co-operation and Development (OECD), Development Assistance Efforts and Policies in 1961 (Paris: OECD, September, 1962), p. 23.

[2]Commander Sir Robert G. A. Jackson, The Case for an International Development Authority (Syracuse: Syracuse University Press, 1959), pp. 41-42.

[3]Barbara Ward, "Imagination in Development," Restless Nations (New York: Dodd, Mead & Company, 1962), pp. 197-198.

> If morals have any meaning at all, they must entail that the hungry are fed, the naked clothed, the homeless sheltered, and all the sons of men given some little share in the world's great patrimony of knowledge and opportunity, of health and hope.[1]

Lady Jackson has given the Western world a large order and one that hard loans simply cannot fill. Some such vision of the world's need must have been in Senator Monroney's mind when he first conceived of the International Development Association in Bangkok in 1956. And along with this need, the Senator thought he saw a way to meet it--through the use of local currencies.

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[1]Barbara Ward, "New Perspectives," Restless Nations, p. 67.

CHAPTER V

THE LOCAL CURRENCY QUESTION

Monroney's Proposal

In Monroney's speech to the Inter-Parliamentary Union in 1956 there was a three-pronged proposal. One aspect concerned the need for more funds on easier terms. The second aspect concerned an international agency to administer these funds. And the third aspect of his proposal was the possibility of using counterpart funds left over from Marshall Plan days and local currencies acquired under Public Law 480 to finance the new agency. When the Senator returned to Washington, he discovered that there were few Marshall Plan counterpart funds still available. So, this idea was dropped. However, he discovered that the United States had around $1 billion in inconvertible currencies of the underdeveloped countries as a result of sales of surplus agricultural commodities. By the time the International Development Association was launched, in 1960, unutilized balances of foreign credits totalled $4 billion.[1]

Monroney wondered why this money couldn't be put to work. He had seen the obvious surpluses, of tea and jute in India, of rice in some of the Southeast Asian countries, of petroleum in the Middle East,

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[1] Semiannual Report of the National Advisory Council on International Monetary and Financial Problems for the Period January 1 through June 30, 1960 (Washington: U.S. Government Printing Office, 1961), Table C-9, p. 73.

of ores in Latin America. And yet, some of these commodities could be used by other developing countries.

One official in the United States Treasury Department suggested that Senator Monroney simply did not understand the use of local currencies. Secretary Anderson's statement to Monroney's committee was supposed to straighten him out on this matter by pointing out that what the underdeveloped countries needed was foreign exchange. This same official pointed out that, to date, the International Development Association has not loaned a peso of local currency--even that which was paid in on subscription. Why should a country put up a million pesos in capital, borrow it back from IDA and pay a service charge on it, when they could go to the printing press and print up the money and spend it? And most of the underdeveloped countries do just that. It was pointed out, however, that the Inter-American Development Bank has used local currency to make loans to a country in its own currency. And such countries have been willing to pay interest on the currencies which they themselves have subscribed.[1]

One of the executives of the World Bank has said that "Monroney thought that local currencies were 'real money'. Gene Black had breakfast with Monroney and luncheons and dinner parties to try to explain it, but he never did succeed."[2]

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[1]Interview with an official of the U. S. Treasury Department, January 17, 1963.

[2]Interview with an official of the IBRD, January 22, 1963.

Monroney's Publicity Campaign

Monroney had been a newspaperman before going to Congress and had a considerable respect for the influence of the press in getting an idea accepted by the public. He also had a number of friends in the newspaper business. He kept up a steady stream of ammunition to these people on the International Development Association and particularly on the local currency aspect. Several papers editorialized in favor of his proposal, including the New York Times, the Washington Post and the St. Louis Post Dispatch.

The Dayton (Ohio) Daily News editorialized on March 1, 1958 in support of Senator Monroney's resolution. The editorial strongly endorsed the local currency aspect of the proposal. "Such a bank could facilitate many three-way trade-and-loan deals such as Russia so easily arranges, with satellites handy for absorptive marketing, whereas free-world tariff barriers render them difficult for this country to make."[1]

The Des Moines Register was not optimistic about the local currency feature but felt that it might have some value.

> It would not do India much good for an international agency to lend back rupees for economic development. These rupees would represent a claim on Indian resources. What India needs is capital from abroad.
>
> Nevertheless, there is some value in the "local currency" loan feature. In some of the poorer countries, banking facilities are so inadequate, that the "Monroney bank" would serve a valuable function just in providing long-term financing machinery.[2]

A good many economists have pointed out the need to do something

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[1]Dayton Daily News, March 1, 1958 as quoted in Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, p. 35.

[2]Des Moines Register, March 24, 1958 as quoted in Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, p. 44.

about United States holdings of local currencies.

> These balances are already growing fast on account of our farm-surplus-disposal program. We will consequently acquire an embarrassing power over other countries. We will be the largest single holder of bank deposits, capable of upsetting monetary and fiscal policies abroad. To make matters worse, our hoards of foreign currencies must retard the elimination of exchange controls in Asia and Latin America. Other countries may hesitate to make their currencies convertible for fear that we may then demand dollars in exchange for our balances, denuding them of foreign exchange. This is an anomalous situation for the United States, because we extol currency convertibility.[1]

The Senator concluded that the reason the underdeveloped countries were not able to buy each other's surplus goods was a lack of usable currency. And here was the United States holding $1 billion in the currencies of these very countries and not making any use of it! It did seem like a most reasonable solution to transfer United States' holdings of these currencies to an international institution. It would be able to use them to purchase surplus commodities and transfer them to places where they were needed. This would mobilize wasted resources, and it would increase the tempo of economic development without costing the United States taxpayer one cent.

Monroney had another reason for wanting to put these local currencies to work. He could foresee that as this store of local currency mounted each year, there was going to be a powerful movement to cancel them out. "Sooner or later these currencies must be forgiven or written off or they must be used."[2] As a past member of the Banking

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[1]Peter B. Kenen, Giant Among Nations (Chicago: Rand McNally & Company, 1963), pp. 175-176.

[2]Congressional Record, February 24, 1958, pp. 2261-7 as quoted in Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, p. 11.

and Currency Committee of the House and a member of the Senate Committee on Banking and Currency, Monroney had come to believe in sound international financial operations. The idea of writing off all these currencies did not appeal to him as a move designed to engender respect for international obligations and a sense of responsibility for debts. It also would involve disillusionment for the United States taxpayers who supported Public Law 480 because they thought the United States was getting a quid pro quo for these surplus commodities.

Hearings on the Monroney Resolution

By the time the hearings on the Resolution had started, Monroney had acquired a considerable amount of ammunition on the local currency question. It was to become the central issue in the hearings.

Secretary Anderson came to the hearings laden with questions concerning the local currency aspect of IDA.

> Secretary Anderson. . . . (1) Is local currency available in countries that might have capital goods available for export to other areas?
> (2) If there are such holdings, would the countries permit their use for financing exports?
> (3) Would they be willing to have the currencies turned over to an international agency for this purpose?
> (4) Would financing through this agency within the country be favored by countries now receiving loans repayable in local currency from United States programs?[1]

In addition to his questions, the Secretary had a good many statements to make about the local currency issue. He pointed out that, "Although the United States holds title to large sums in local currencies, these have been acquired only under specific agreements with foreign countries that their use would be limited in various

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[1]Senate Subcommittee on Banking and Currency, Hearings on S. Res. 264, 1958, pp. 58-59.

specific ways, and generally these limitations do not permit their use for financing exports."[1] The Secretary also emphasized that local currencies loaned back to the developing countries would not add to these countries' real resources.

He made much of the fact that Public Law 480 had specifically authorized the financing of goods purchased in one country for the use of another country. This was exactly what Senator Monroney had in mind. And yet, the Secretary maintained that "only very small amounts of currencies generated under the program have to date been agreed upon for this purpose."[2] Mr. Anderson's interpretation of this experience was that such transactions were almost impossible to effect.

Mr. Douglas Dillon, Deputy Under Secretary of State for Economic Affairs, echoed the testimony that had been given by Anderson. Dillon argued that our stock of local currency could not be used to remove resources from the country whose local currency is concerned.

> We cannot, for example, use our holdings of Brazilian cruzeiros to buy up Brazilian coffee, cocoa, or cotton--Brazil has no capital goods for export--and ship that coffee, cocoa, or cotton to some other country. And even if we should do so with the consent of the Brazilian Government, we would be reducing by that much Brazil's export earnings in hard currencies and its capacity to pay for the capital resources needed for its economic development.[3]

Senator Monroney answered that he was not concerned with commodities that could be sold in world trade. His interest was in using surplus commodities of the underdeveloped countries and he was convinced then and is still convinced that exchanges of such commodities could be arranged. He used the expression that the developing countries should sell for "money, marbles, or chalk."

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[1] *Ibid.*, p. 59. [2] *Ibid.*, p. 60. [3] *Ibid.*, p. 143.

> I am talking about a worldwide operation where there are many kinds of surpluses that go unused, that rot on the ground because the neighboring country does not have the foreign exchange to buy the rotting crop except as it converts its local currencies to hard dollars.[1]

Monroney maintained that the United States Government had not really tried to effect transfers of surpluses between underdeveloped countries.

The State Department prepared a memorandum on local currencies for the use of the Committee. In this memorandum, it is pointed out that "unless they receive at least equivalent resources in return the less developed countries cannot provide resources to other countries without a setback to their own economic growth. If the United States were to use a less developed country's local currency to remove resources from it for use by other countries we would cause such a setback."[2]

This statement does no damage to Monroney's proposal because he did not propose taking resources from the less developed countries without putting anything back in. He was proposing an exchange of resources between countries with complementary needs. The State Department insisted that "To the extent that it is feasible, this sort of exchange is already going on through normal commercial channels.

. . . .

There is no present obstacle to trade between the less developed countries which would be removed by United States governmental action in lending these countries each other's local currencies."[3] Senator Monroney would not reconcile himself to a world where people starve in

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[1]*Ibid.*, p. 175. [2]*Ibid.*, p. 123. [3]*Ibid.*, p. 124.

one country while surplus food rots on the ground in an adjoining country. The State Department view, however, was that there was no solution to this problem.

Senator Monroney thought the Administration position on local currencies was contradictory. On the one hand, the Secretary of the Treasury insisted they were practically useless for economic development. They didn't add any real resources to the country they were loaned to. They could not be used in international trade. And yet, on the other hand, the Administration kept pushing Public Law 480 loans repayable in local currencies and had even established the Development Loan Fund to receive repayment in local currencies. During Deputy Undersecretary of State Dillon's testimony, Senator Monroney said: "You can't have it both ways. If your case is true--that these funds are of no use--then the repayments that the State Department gets back in these same local currencies also have no use and, therefore, we are adding to a stagnant pool of frozen currencies."[1]

Debate on Local Currencies

During the 1959 meeting of the Board of Governors of the Bank, local currencies became the subject of an extended debate. The developed countries, led by the Netherlands and the United Kingdom were particularly opposed to the local currency aspects of IDA.

The Governor from the Netherlands stated that his Government was

> not without concern about the possible monetary and commercial implications of the utilization of so-called local currencies for

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[1] *Ibid.*, p. 136.

> international investment purposes. We are particularly concerned about the inflationary consequences of the utilization of such currencies accumulated in the past, and about the distortion of international trade that may result from the limited usability of inconvertible local currencies if made available for foreign payments. We, therefore, want to stress that the financial operations of the IDA should in no way aggravate the problems of monetary instability and trade restrictions which in many countries continue to exist, despite the great--and to a certain extent successful--efforts of the International Monetary Fund and the GATT to reduce their significance. We would defeat our own purposes if the IDA were to become an institution creating or even stimulating the very tendencies the Fund and the GATT are opposing.[1]

The Netherlands Governor introduced the International Monetary Fund into the debate on local currencies and surely some mention must be made of the Fund's opposition to anything which smacks of bilateral trading arrangements or of barter. This is in line with the classical liberal tradition of free trade.

However, Andrew Shonfield has argued that it is not in line with the realities of the twentieth century.

> One way in which the underdeveloped countries could surely help to relieve the pressure on their balance of payments is by trading more among themselves. It is not just a matter of taking in each other's washing. Surplus production of a commodity runs to waste in one country, while in another people go short of it, because the mechanism of exchange fails to function efficiently. A lot more food could and would be grown in the great surplus agricultural area of Asia, which runs from Burma across the South-east-Asian peninsula, if there were an assured market for it. But it only needs one good rice harvest for Burma to be faced with the nightmare of surplus stocks. That is what has happened recently. There are no adequate storage facilities, the rice rots, the price falls; and next time, the peasant does not bother to grow so much or to bring it to market.
>
> The reason given for the Burmese failure to sell the rice to the Indians is simply that the Indians cannot afford it. That is true in the sense that the Indian government is not prepared to allocate anything out of its very inadequate reserves of foreign exchange to pay for additional imports of rice. . . . If Burma demands to be paid, like everyone else, in sterling or some other convertible currency, it will be left holding its surplus rice,

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[1]IBRD Board of Governors Press Release No. 10, September 30, 1959, p. 3.

> and everybody will be that much poorer.
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> Indeed, one would have thought it elementary that these nations should be encouraged to engage in barter trade wherever this helps them to put their actual or potential surpluses of production to some useful purpose. It came as a shock, therefore, when I was in India at the end of 1959, to run into a mission from the International Monetary Fund engaged in a vigorous effort to break up an Indo-Burmese barter agreement. The IMF started by hurling anathemas. What the Indians were doing was a sin against the principle of untrammeled multilateral trade, with equal freedom for all exporters to enter a market.[1]

Some persons have argued that Monroney's proposal to use local currencies to facilitate such barter arrangements merely put a mask on them. It was still essentially barter and was condemned as such by some of the member governments of the International Bank.

The United Kingdom joined in attacking the local currency proposal. "We have considerable doubts about the use of local currencies by IDA. . . . We shall want to be clear how such use could be arranged without resulting in distortions of normal trade."[2] The Governor from Canada participated in the debate, also. He echoed the speeches of the Governors from the Netherlands and the United Kingdom, in that he was concerned about contributing to inflation, aggravating the exchange problems of borrowing countries, and contributing to uneconomic trade diversion.[3]

The Governors from India and Pakistan also expressed opposition to the local currency aspects of IDA. The Governor from Pakistan said that

> It would be unrealistic to expect the less developed countries to

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[1]Shonfield, pp. 39-40.

[2]IBRD Board of Governors Press Release No. 60, September 30, 1959, p. 4.

[3]IBRD Board of Governors Press Release No. 68, September 30, 1959, pp. 2-3.

> . . . agree to the use of their local currencies, whether in the shape of counterpart funds or otherwise, in the form of unrequited exports. . . . I am sure that the option to determine the time when a less developed country will be in a position to spare some of its production for helping other developing countries must rest with the countries concerned and not with the institution.[1]

The Governor from India was in agreement with the Pakistani Governor on this issue. He presented a closely reasoned argument in opposition to widespread use of local currencies by IDA.

> The proposal before us has raised the question of the utilization of the accumulations by one country in the local currency of another. These accumulations cannot, obviously, be used in a manner that amounts to making that much exports available without corresponding payment. Nor can they be used as a source of additional internal finance without creating inflationary pressures in the process. These funds are a resource only notionally, the impact of the initial loan in real terms being represented by the imports financed from it. The subsequent transactions are only an accounting device. It is true that with the accretion of an external resource, a measure of domestic credit creation might be appropriate, but the measure and timing of this credit creation have to be judged in relation to the over-all economic situation rather than in terms of the apparent accumulations as such.[2]

Thus, it can be seen that not only the developed countries (especially the large trading nations), objected to the local currency aspects of IDA, but the countries that had received large quantities of agricultural surpluses under Public Law 480 objected also. Both groups of countries were afraid of a reduction in their exports brought about by three-cornered trade arrangements. It was a little strange, however, to attack Monroney's proposal as inimical to free multilateral trade, while supporting Public Law 480. The whole agricultural surplus disposal program, no matter what its merits, is an exception to the principles of free multilateral trade.

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[1]IBRD Board of Governors Press Release No. 47, September 30, 1959, p. 2.

[2]IBRD Board of Governors Press Release No. 65, September 30, 1959, pp. 4-5.

When the International Development Association was established the Articles of Agreement had a provision dealing with local currencies. Article III, Section 2 (a) states that

> The Association may enter into arrangements, on such terms and conditions consistent with the provisions of this Agreement as may be agreed upon, to receive from any member, in addition to the amounts payable by such member on account of its initial or any additional subscription, supplementary resources in the currency of another member, provided that the Association shall not enter into any such arrangement unless the Association is satisfied that the member whose currency is involved agrees to the use of such currency.[1]

Mr. J. Burke Knapp, Vice President of the International Bank, in discussing this provision with the author emphasized the phrase "as may be agreed upon." Knapp pointed out that the International Bank had been most reluctant to assume the responsibility for administering these local currencies. Thus, this provision in the Articles is extremely important. No government, including the government of the United States, could even donate local currencies to the International Development Association without the agreement of the Association.[2]

The local currency debate is coming back into the limelight in the present discussions concerning augmentation of the Development Association's funds. There is considerable pressure on the Executive Directors to accept local currencies as part of the subscriptions.

Some members of the staff of IDA feel that local currencies could be loaned to the underdeveloped countries. They argue that there is a great deal of sense to loaning these currencies so long as they represent real savings. If the money has not been obtained from

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[1]Articles of Agreement of the International Development Association (Washington: IDA, 1960), p. 7.

[2]Interview, January 22, 1963.

savings, then it is purely inflationary--that is just the same as printing it. But, if the country has taxed savings to contribute to the Association, why shouldn't they be loaned?

There is a question of workability in connection with IDA use of local currencies. Could the Association keep track of the currency as it worked its way through the country's financial system? Could IDA insure that the money really did represent savings?

> At first sight it might seem obvious that the release of monies obtained from savings would not be inflationary. There is, however, a very important question of timing. What could happen--and in fact often happens--is that funds are accumulated from genuine savings, but that during the period while this accumulation is exercising a deflationary effect, the local government is expanding the money supply through other channels. The immediate result is neutral, but if then in a subsequent period the impounded savings are released, the result can be a serious inflationary impetus despite the original source of the released funds.[1]

It would strike the author that these problems are no more difficult than others that the staff has solved. It is not unlikely that some use will be found for these currencies.

The United States has not transmitted any of its holdings of local currencies to the Association. The Treasury Department felt that Public Law 480 authorized such transmission but, nevertheless, included specific authority in a bill introduced in 1960. The bill was part of another matter and for an unrelated reason did not pass. The Administration has not proposed legislation since then on this matter.

Thus, it can be seen that one of Senator Monroney's ideas for the International Development Association has been abortive. He is

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[1]Personal letter from an official of the IBRD, June 25, 1963.

still optimistic that something can be done with these currencies and, meanwhile, his goal of putting more of the United States economic aid program on a multilateral basis has been realized.

CHAPTER VI

A MULTILATERAL APPROACH TO AID

Proponents of Multilateral Aid

When Senator Monroney proposed the International Development Association, his experience in Thailand was fresh in his memory. He had seen the enthusiasm with which the Thais regarded their dam that had been built with World Bank funds. And he had seen their reluctance to exhibit their new highway that had been paid for with United States' defense support funds. This experience made a lasting impression. It seemed quite obvious to the Senator that an international aid agency was more effective in encouraging economic development that was a bilateral program. In coming to this view, he was joining a number of economists who had been arguing along similar lines for years.

Alec Cairncross has pointed out the historical reasons why the Thais and others have viewed bilateral programs with suspicion.

> The export of capital has always been associated in the outlook of the under-developed countries with imperialistic influence and the improper exercise of power by lending countries in order to secure property rights or advance the commercial interests of investors. The setting up of the Bank was, from their point of view, a blow against imperialism of this kind. They were far more willing to welcome capital from an international institution than to rely either on private investment or on loans from friendly governments.[1]

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[1]Alec Cairncross, The International Bank for Reconstruction and Development (Princeton University Essays in International Finance No. 33, March, 1959), p. 27.

One does not have to look far to find persons from the developing countries that will agree with Cairncross. The Governor of the International Development Association from Sudan, at the 1961 meeting of the Board of Governors, pointed out that IDA's greatest strength was its international character. He urged the rich countries to look upon aid as a basic aim of foreign policy and not as an expedient for securing immediate diplomatic advantages.[1]

By channeling aid through an international agency, the United States tells the underdeveloped countries that it puts development ahead of diplomatic advantages. And there is a growing disenchantment with the possibility of using bilateral aid as a cementer of alliances and a feeling that the United States should have long-run development objectives rather than a desire for transitory alliances.

A number of people have pointed out the difficulties involved in administering a bilateral aid program. Perhaps none has done it better than Leonard Rist.

> The underdeveloped world is comprised of a great number of countries. Few among the industrialized nations can claim thorough knowledge of all of them; long standing relations are necessary to establish not only the climate of confidence but the basis for long-term judgments of the real needs of the developing country. It is not surprising, therefore, that some of the industrialized countries should feel hesitant when they make decisions on the type of assistance which they shall grant.
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> International organizations have, in this respect, a distinct advantage. Their political relationship with their own member countries is that of a cooperative organization with its members.[2]

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[1]IDA Board of Governors Press Release No. 32, September 19, 1961, p. 2.

[2]Leonard Rist, "International Cooperation in Development Aid," Address to the Fourth S E A N Z A Meeting, (Washington: IBRD, 1962), pp. 16-17. (Mimeographed.)

A very practical reason for turning development efforts over to an international agency was given, by the Maxwell Graduate School, to the United States Senate Committee on Foreign Relations. "Programs which induce change raise touchy political problems. There is consequently a strong case for multilateral management of such programs in the whole field of technical aid and investment loans for economic development."[1] This group pointed out that certain local special interests are bound to be adversely affected by the changes which come about as the result of development efforts. Why should the United States Government be blamed for such changes? An international agency is less bothered by such pressures.[2]

The plight of the underdeveloped countries in dealing with so many different aid programs has been demonstrated by the story of one country that applied for technical assistance from the United Nations. The technical assistance needed was learning how to apply for loans and grants from all the different aid-dispensing agencies.

In addition to the arguments given by economists and developing countries there is an argument put forward by an American businessman in favor of international channels for aid.

> I question, however, whether from a standpoint of either the lender or the borrower it is wise for one national government to borrow from another. Among the reasons in support of this view are, first, it is difficult for a lending national government to

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[1]U. S., Senate, Committee on Foreign Relations, United States Foreign Policy--Compilation of Studies, "The Operational Aspects of United States Foreign Policy" by Maxwell Graduate School of Citizenship and Public Affairs, Syracuse University (Washington: U. S. Government Printing Office, March 15, 1961), p. 565.

[2]*Ibid.*, pp. 598-599.

> put such a transaction on a thoroughly businesslike basis and, second, the collection of loans given by one country to another presents great difficulties. For these reasons I think that as rapidly as possible lending and borrowing among nations should be on an international basis.[1]

Raymond Mikesell has been able to detect a noticeable shift in United States public opinion in favor of multilateral aid. He gives three reasons for this shift. First, the relative deterioration of the United States' balance of payments has led to a desire to share the burden of economic assistance. Secondly, there is a changed attitude toward development assistance. Formerly it was tied to short-term objectives as part of the United States military program whereas it is now seen as a long-run process designed to assure national independence and democratic progress in the developing countries. Finally, Mikesell believes that a major factor in the change has been the influence of the World Bank and its President, Eugene R. Black. Confidence in Black and the Bank are credited with winning Congressional and Presidential support for the International Development Association. The change that has come about originated as much in the Congress as in the Administration, as evidenced by the Monroney Resolution.[2]

Reservations Concerning Multilateral Aid

Despite all the oratory and shifting of opinions, the Director of the Organization for Economic Cooperation and Development points

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[1]Paul G. Hoffman, "Priorities of Economic Development," Restless Nations, p. 96.

[2]Raymond F. Mikesell, "Problems and Policies in Public Lending for Economic Development," U. S. Private and Government Investment Abroad, ed. Raymond F. Mikesell (Eugene, Oregon: University of Oregon Books, 1962), p. 350.

out how really little progress has been made in this direction.

> I think it likely that in the years to come, true multilateral aid through the United Nations Special Fund, specialized agencies, and so on, might be increasing. Personally, I think this is desirable. However, it's a fact of life that the bulk of aid for the time being, as well as the bulk of private capital exports and the bulk of technical assistance, is given or lent or invested on a bilateral basis. We published a report some months ago on the flow of funds, including the economic value of technical assistance to less developed countries in the four years 1956-1959. It appeared from that report that no less than 93 per cent of the total flow of funds was on a bilateral basis. Only 7 per cent was coming through the World Bank, United Nations agencies, and the like. If you exclude private capital exports, its only 88 per cent, but still about nine-tenths of technical assistance and of capital flow of all sorts is, whether you like it or not, on a bilateral basis.[1]

Many people think that this is as it should be. Raymond Mikesell and Robert Loring Allen give three reasons why the United States should continue to provide the bulk of its development assistance on a bilateral basis. First, there is the traditional argument that foreign aid as a tool of foreign policy can be more flexibly employed on a bilateral basis. A second reason is that the United States can exert a leadership role in coordinating the assistance activities because of the size of its contribution. Thirdly, it is argued that it is easier to tie bilateral assistance to United States exports than in the case of multilateral assistance.[2]

Some economists would question the argument that bilateral aid is a flexible tool of foreign policy. Benjamin Higgins insists that

> The dilution of U. S. objectives is greater in the United States

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[1]Thorkil Kristensen, "The OECD and World Development," Restless Nations, p. 104.

[2]U. S., Congress, Joint Economic Committee, Economic Policies Toward Less Developed Countries, prepared by Raymond F. Mikesell and Robert Loring Allen 87th Cong., 1st Sess., 1961, pp. 34-36.

> program than in the United Nations program. The necessity for Congressional control of policy for foreign economic assistance, along with all other policies influencing the economic position of underdeveloped countries, results inevitably in a certain degree of inconsistency and instability of the short-run goals reflected in the legislation governing the U.S. economic assistance programs.[1]

Higgins is including the World Bank and the International Development Association when he refers to the "United Nations program."

Apparently a good many people subscribe to the view of one United States Government official. "The under-developed countries don't care where they get the money. Sure, State Department money is political. But let's not get around politics. Our aid money should be for political gain. Not for securing the election of someone we like in Ruritania - not that type. That doesn't get us anywhere. But, development loans should go where they will help us. Our political objectives are pretty important."[2]

There is fear in some quarters that multinational agencies might be governed by political forces in making loan decisions. And it is pointed out that in some countries, notably in South America, the World Bank is rather unpopular with large sections of the public.[3] These two caveats should be given along with the obvious advantages which multinational agencies have, although, it certainly seems unlikely that the International Development Association, with its weighted voting system, is in any immediate likelihood of being governed by political

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[1]Higgins, p. 145.

[2]Interview, January 17, 1963.

[3]Mikesell, "Problems and Policies in Public Lending for Economic Development," U. S. Private and Government Investment Abroad, pp. 351-352.

forces inimical to the West. And the Bank's unpopularity may be caused by its insistence on responsible governmental policy which is unpopular with many.

The Brookings Institution has enumerated two reasons why the United States might not wish to turn more economic aid over to the World Bank. First, it is argued that not all nations which the United States wishes to assist are members of the Bank. Secondly, some countries may not wish to submit their loan requirements to the scrutiny of the Bank, especially when its membership includes governments which are not on friendly terms with the applicant.[1]

There is a feeling in some countries that the World Bank and the IDA are dominated by the United States Government and reflect its policies. No one who has observed the operations could believe that the United States is without influence in these institutions. The United States does have almost a third of the voting power and can, with the countries of the Commonwealth, control a clear majority of the votes. Of course, the Commonwealth countries do not always vote with the United States. However, it is difficult to envision policies, to which the United States was violently opposed, continuing for any great length of time. On the other hand, there are items on which the developed countries sometimes split and the United States winds up in the minority position.

One of the reasons which some members of the staff of the Bank give for not wanting to accept any greater portion of the United

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[1]U. S., Congress, Senate, Special Committee to Study the Foreign Aid Program, Foreign Aid Program "Administrative Aspects of United States Foreign Assistance Programs," by the Brookings Institution, 85th Cong., 1st Sess., 1957, p. 501.

States aid effort is the fear of United States' attempts to dominate the Association. Of course if the United States and Western Europe increased their contributions to IDA pari passu this objection would disappear.

Importance of the Framework for Administering Aid

Roscoe Drummond summarized much of the thinking on multilateral aid in his summary of the 1961 Conference on Tensions in Development.

> Everyone realizes that responsible government must be the accountable custodian of tax revenues and must demonstrate to its citizens that it has not lost control of the uses of its tax money. This is why most economic aid is bilateral: a transaction directly between two governments. At the same time, experience shows that international agencies can insist upon firmer, better, more stringent conditions--even including internal economic reforms--in a contract between the donor agency and the recipient country.
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> The judgment of nearly all the experts present was that the best possible, the most exacting, and the most constructive conditions for giving and receiving economic assistance can be negotiated when the representatives of several nations are at the conference table. . . .
>
> Since the essential foundation for effective economic aid is to develop a relationship of trust and understanding between the less developed and the more developed countries, the following suggestion was advanced. The best means of bringing this relationship into being is for the under developed nations now, without delay, to become themselves donors of economic aid. They should devote part--however modest, however miniscule--of their national income to helping other underdeveloped countries. They will thus benefit and be benefited; through actual experience as donors, the largely recipient countries will be able to understand better the attitudes and problems of other donor countries. This will enhance the feeling of dignity and equality among nations in an economic partnership designed not to win a Cold War but to win the peace.[1]

Drummond is echoing a point made time and time again by Senator Monroney in his drive to get the International Development

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[1]Roscoe Drummond, "Partnership for Peace," Restless Nations, pp. 10-11.

Association established. The Senator felt the West was missing a real bet in not getting the underdeveloped countries to help each other. It would not only help them to see the problem from the donor's position. It would also give them a feeling of responsibility that the resources entrusted to them not be squandered. There is, for various reasons, a limited amount of resources that can be raised for economic assistance. When any nation wastes its portion it penalizes other nations in the growth process. IDA was an attempt to instill this idea into all the developing countries.

This will not be achieved by simply getting the nations of the West together to give their aid through consortia. Dag Hammarskjold pointed this out in a press conference after his return from Africa in 1960.

> I will not in this context repeat what is common knowledge. For those countries, it is infinitely easier to receive financial assistance and technical assistance by experts and so on through an international body than on a bilateral basis, and it is infinitely easier for them to receive it through an international body of which they are themselves members than through any other international body of which they are not members. That is to say, internationalization of aid is not achieved by switching from the system of one country giving another country aid to a system where one group of countries gives a country aid. The bilateral character is then maintained. It is not until and unless the receiving country feels that this is an act of solidarity within an organization where they have equal rights with the donors that you really reach the optimum point not only psychologically but politically and economically.[1]

Hammarskjold's argument is reinforced by Barbara Ward. She points out that the framework in which aid is given is almost as

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[1]From remarks made by the late Secretary General of the United Nations as quoted in Benjamin Higgins, United Nations and U. S. Foreign Economic Policy, p. 179.

important as the aid itself.

> On the side of the developing nations, friction and resentment spring inevitably from the fact that while political independence is now (save in parts of Africa) a fact, economic independence is not. The "Southern" areas of our planet have not yet the capital or the skills needed for the forced-draught development that is demanded by their relative backwardness and growth of population. They must still look to the North, and there is still an element of dependence inherent in their situation. It follows that the frame within which assistance is given is of immense political importance. If the Western powers give aid for practical purposes--to stop Communism, to make clients, or to back nations agreeing with their views--then the assisted countries feel they are being used as means, not ends. This is, after all, one definition of subordination or dependence. . . . The context of aid giving is of vital importance. If we see the transfer of capital and skills from the developed North to the underdeveloped South as part of a joint, world-wide effort to create a modernized world economy, the idea of <u>interdependence</u> is written in to what we do. But if we aim only at Cold War maneuvers, the subordination of the developing lands to our Western policies is inescapable.[1]

Senate Passage of the Monroney Resolution

Despite the urgings of economists, businessmen, and international civil servants, the Eisenhower Administration was not at all enthusiastic about the idea of rushing down to the International Bank and handing over the foreign aid funds. Deputy Under Secretary of State Dillon, in his testimony before Monroney's subcommittee, argued that the State Department had "found generally, with the exception of the Middle East where tensions are very high, that the countries concerned indicate at least to us that they would just as soon, if not prefer, deal with us directly rather than with a multilateral institution."[2] And Senator Capehart was not too impressed with the arguments

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[1]Barbara Ward, "Imagination in Development," <u>Restless Nations</u>, pp. 182-183.

[2]Senate Subcommittee on Banking and Currency, <u>Hearings on S. Res. 264</u>, 1958, pp. 170-171.

in favor of multilateral aid, either. He said that the "only thing I have heard about so far from you, Mr. Chairman, in favor of it is that people would like us better if we loaned our money in conjunction with some other country rather than loaning it to them directly, which to me is a silly argument. I do not think there is any truth to that statement at all."[1]

Despite the objections of Senators Capehart and Bricker, the Senate Committee on Banking and Currency accepted the arguments in favor of multilateral aid. In the report on Senate Resolution 264, the Committee gave three reasons for putting aid on a multilateral basis.

> First, because the advantages of development accrue to all members of the international political community, it seems only fair to share the costs of the development program among all who can participate. Second, a lending institution including both debtors and creditors gives a greater measure of assurance that the loans will be repaid. Third, governments may sometimes prefer international loans because they remove any possible implication of political interference in internal affairs.[2]

Senators Bricker and Capehart did not concur in this report. They condemned the "use of a Senate resolution to usurp the usual diplomatic procedure employed in negotiating the formation of a new international institution."[3] Furthermore, they argued that "The resolution does not urge any course of action that the State Department could not initiate itself through ordinary channels."[4] Thus, the only possible

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[1]*Ibid.*, p. 173.

[2]U. S., Congress, Senate, Committee on Banking and Currency, *Report on the International Development Association*, 85th Cong., 2d Sess., 1958, p. 6.

[3]*Ibid.*, p. 7.

[4]*Ibid.*

explanation was that "the purpose is to force the administration to adopt a policy that it has not deemed wise heretofore."[1] And the Senators were in hearty agreement with the State Department's lack of action in this sphere, because they were convinced that "there is no need for the proposed IDA."[2]

In addition to a majority of the Senate Committee on Banking and Currency, the Senator from Oklahoma was finally able to convince the Eisenhower Administration to support his resolution. There were several changes in the resolution, at the request of the State and Treasury Departments, but on May 20, 1958 the official position of the Administration became one favoring enactment.

The revised resolution reads as follows:

> Resolved, That recognizing the desirability of promoting a greater degree of international development by means of multilateral loans based on sound economic principles, it is the sense of the Senate that prompt study should be given by the National Advisory Council on International Monetary and Financial Problems with respect to the establishement of an International Development Association, as an affiliate of the International Bank for Reconstruction and Development.
>
> In order to achieve greater international trade, development, and economic well-being, such study should include consideration of the following objectives:
>
> (1) Providing a source of long-term loans available at a reasonable rate of interest and repayable in local currencies (or partly in local currencies) to supplement International Bank lending activities and thereby permit the prompt completion of worthwhile development projects which could not otherwise go forward.
>
> (2) Facilitating, in connection with such loans, the use of local and other foreign currencies, including those available to the United States through the sale of agricultural surpluses and through other programs.
>
> (3) Insuring that funds for international economic development can be made available by a process which would encourage multilateral contributions for this purpose.[3]

What brought about the change of policy on the part of the

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[1] Ibid. [2] Ibid., p. 9. [3] Ibid., p. 11.

Administration? One official in the Treasury Department has attributed the change in policy to all the favorable publicity Senator Monroney got for his resolution. "The Treasury would have held back on IDA until today unless Monroney had gotten all the publicity, the Senate Resolution, etc."[1] Monroney attributes the change, in large part, to the publicity and favorable editorial support. However, he points out the role of Eugene Black in getting the Resolution endorsed. "Black gave a dinner for a bunch of Republicans and told them it was alright and they decided to support it."[2]

The pressure for SUNFED was important, also. As Paul Hoffman had pointed out "You can't fight something with nothing." IDA appeared as a good, cheap alternative to the contribution the United States would have had to make to SUNFED. All these reasons and more contributed to changing the Administration's view of the matter. On July 23, 1958, with Administration support, the Resolution sailed through the Senate by a vote of 62-25. And, thus, the International Development Association was on its way.

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[1]Interview with an official of the U. S. Treasury Department, January 17, 1963.

[2]Interview with U. S. Senator A. S. Mike Monroney, January 25, 1963.

CHAPTER VII

THE INTERNATIONAL DEVELOPMENT ASSOCIATION IS ESTABLISHED

The United States Government Launches the International Development Association

The Monroney Resolution, as it had been passed by the Senate, requested the National Advisory Council on International Monetary and Financial Problems to study the possibility of establishing an International Development Association. The Council was established by the Bretton Woods Agreement legislation and consisted of the Secretary of the Treasury, the Secretary of State, the Secretary of Commerce, the Chairman of the Board of Governors of the Federal Reserve System, and the President of the Export-Import Bank. When other agencies are vitally concerned with the subject matter under discussion they are invited to the meetings. At times the Mutual Security Administration, the Agency for International Development and the other aid agencies have been regular members.

Before this Council made any reports and prior to the meeting of the Board of Governors of the International Bank in September, 1958, Secretary of the Treasury Anderson wrote President Eisenhower and proposed that informal discussions be undertaken during these meetings concerning the establishment of an International Development

Association. The President agreed to this proposal. Thereafter, Secretary Anderson and his party went on a trip around the world--on the way to and from the New Delhi meetings of the Board of Governors. They talked to the Chancellor of the Exchequer in the United Kingdom and the Finance Ministers of Germany, Italy and Japan. "Only Japan was enthusiastic. Germany and the United Kingdom definitely did not want it. They wound up supporting it as a result of a horse trading operation. They agreed to support IDA in exchange for some things they wanted. The United Kingdom and Germany still don't like it very much. We talked about using local currencies to the Finance Ministers--using Brazilian lumber to build a project in Greece because we have lots of Brazilian cruzeiros. All the underdeveloped countries actively supported the idea for IDA."[1]

Secretary Anderson dwelt on IDA at some length in his opening statement to the Board of Governors.

> We are now studying this proposal in my own Government. I have no blueprint to offer at this time for such an Association. Essentially, however, it would be an affiliate of the International Bank which would make long-term loans for economic development repayable in whole or in part in the currency of the borrowing country. As I have said, the United States Government is making its own studies of the feasibility and desirability of establishing an IDA. We hope that other countries will at the same time be giving thought to the matter, and we shall look forward to having informal conversations with you. If these informal studies and conversations lead to encouraging conclusions, it would be appropriate to undertake more formal study and negotiation, looking to the establishment of such an Association.[2]

It is interesting to note that Anderson emphasized that repayment would be made in local currencies rather than that loans would be made in

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[1]Interview with an official of the U. S. Treasury Department, March 12, 1963.

[2]IBRD Board of Governors Press Release No. 4, October 6, 1958, p. 3.

local currencies--as Monroney had planned.

The Secretary of the Treasury serves as Chairman of the National Advisory Council on International Monetary and Financial Problems. Thus, Anderson must be given a great deal of credit for pushing the proposal for IDA through the Council. The Council studied the Monroney Resolution from July, 1958 to January, 1959, when it submitted an interim report to the Chairman of the Senate Foreign Relations Committee. This report merely indicated that discussions had been held with foreign governments and that study was continuing.

On August 19, 1959, the Council submitted the report requested by Senate Resolution 264.[1] The language of this report is in marked contrast to the testimony of Administration witnesses on the Monroney Resolution. The report depicts the Council, if not bubbling with enthusiasm, at least reconciled to the idea of an International Development Association. It states that "On the basis of its studies thus far . . . the Council is convinced that the International Development Association would form a valuable adjunct to the International Bank, and would effectively extend the field of operations of the latter."[2]

The reasons given for support of IDA follow those adduced by Senator Monroney. First, the Association would allow the World Bank to loan to countries which could not assume the full foreign exchange obligation of a conventional loan. Secondly, it would allow countries to finance projects without providing all the local currency themselves. Thirdly, it would provide a multilateral agency with great flexibility

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[1]National Advisory Council on International Monetary and Financial Problems, Report on the Proposed International Development Association (Washington: U. S. Government Printing Office, 1959).

[2]*Ibid.*, p. 3.

in lending operations.[1]

The report indicates that there was reluctance on the part of some countries to accept the World Bank shares as appropriate for IDA. One proposal, to overcome this objection, would have those countries whose recent growth warranted it purchase debentures issued by IDA in addition to their prorated share.[2]

The underdeveloped countries had indicated, during the course of the 1958 conversations, a desire for more coordination of lending activities. The hope was held out that the Association might provide this coordination.[3]

The National Advisory Council concluded its report by saying that it considered the International Development Association as both feasible and desirable and that it would be in the best interest of the United States and the free world to proceed with efforts to establish such an organization.[4]

The Council decided that the best approach to establish IDA would be to have the Executive Directors of the Bank draw up a draft of the articles of agreement for submission to member governments. Consequently, Secretary Anderson proposed such a step to Mr. Eugene Black in a letter dated July 31, 1959. This letter is appended to the report of the National Advisory Council. In it, Secretary Anderson stated that he was convinced that a sufficiently broad base of support existed for the IDA among member governments so that a carefully worked out plan would meet with widespread acceptance. President Black

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[1] *Ibid.*, p. 8.

[2] *Ibid.*

[3] *Ibid.*, pp. 8-9.

[4] *Ibid.*

forwarded the Secretary's letter to all the member governments of the Bank. In his forwarding letter Mr. Black stated, "I am fully in accord with the suggestion of the Governor for the United States that our meeting in September should be the occasion for taking action looking toward its consideration and, as I would hope, toward the establishment of an International Development Association."[1]

Along with the letter, Secretary Anderson sent some guidelines for use by the International Bank's Executive Directors in drawing up articles of agreement for the International Development Association. These guidelines contained the following provisions: (1) The purpose of IDA would be to promote economic development of less-developed members whose needs could not be met by the International Bank. To this end, IDA should finance sound projects of high priority. (2) Membership in IDA should be available to any member of the Bank. IDA should be a separate financial entity, but should be manned by the staff of the International Bank. (3) Voting should be on a weighted basis, according to capital subscribed. (4) IDA should have an authorized capital of $1 billion. Members would pay half of their subscription immediately and the rest over a 5 year period. (5) The United States would contribute about $320 million. (6) IDA's resources should be reconsidered every 5 years. (7) Members would make their subscription partly in gold or convertible currency and partly in their own national currencies. (8) Twenty per cent of each country's quota would be freely disposable by IDA. IDA would have authority to suspend the obligation of the less developed countries to pay in convertible currency. (9) IDA

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[1] Ibid., p. 11.

would have authority to borrow from member governments and other sources. (10) Arrangements should be made for IDA to receive the currencies of one member from another member.[1] The staff of the International Bank had worked with officials of the Treasury Department in drawing up these guidelines.

The Board of Governors' Debate on the International Development Association

The Views of the Developed Countries

President Eisenhower, in welcoming the Board of Governors of the International Bank to Washington in 1959, stated the United States' view that the new Development Association must be closely integrated with the Bank. "Thus, there will be assured the wise expenditure of its funds and the effective coordination of its activities with other institutions. In our view, no other mechanism can perform this task for the free world as well as would the proposed IDA."[2] Treasury Secretary Anderson, following President Eisenhower, made a very strong case for establishing IDA.

The Governor from the Netherlands, Mr. J. Zijlstra, posed several interesting problems for the Governors. He stated the Netherlands' view that, although, they had accepted the decision to double their initial subscription in the capital of the Bank--this did not mean that they accepted this formula for apportioning shares in the future. Shares in IDA should be based on the members' capacity

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[1] _Ibid_., pp. 5-6.

[2] _Summary Proceedings of the 1959 Meeting of the Board of Governors of the International Bank for Reconstruction and Development_, (Washington: IBRD, 1959), p. 2.

to contribute. He proposed a charter allowing non-members of the Bank to be associated with IDA. The question of voting rights should be open to discussion. The forms of financial assistance to be made available by IDA should not be specified in advance--grants should not be excluded in the charter. The link with the International Bank should not be so close as to preclude close cooperation between IDA and the Special Fund and other United Nations activities. He attached great importance to the observance of certain rules with respect to fair behavior in debtor-creditor relationships and with respect to foreign interests. Without assurance that IDA would operate on the basis of such sound principles, the Netherlands would not be prepared to participate.[1]

Ludwig Erhard, the Governor of the Bank from Germany, expressed approval of the plan to allow IDA to provide funds on flexible terms. However, he warned that

> The very allowance for such flexibility would, however, commit the International Development Association and the recipient countries to observe a particularly high degree of discipline in their economic and monetary policies. Only such discipline will avoid the danger that unrealistic aspirations which will later be found to have been harmful are assisted by the new credit facilities.[2]

The theme of this speech of Erhard's would be repeated, by him, at every meeting of the Board of Governors following the establishment of IDA.

The Governor from the United Kingdom attached "great importance to the proviso that the subscription of industrialized countries should

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[1]IBRD Board of Governors Press Release No. 10, September 30, 1959, pp. 1-3.

[2]IBRD Board of Governors Press Release No. 44, September 30, 1959, p. 2.

be convertible, untied, and additional to the existing level of aid."[1] He echoed the argument made by the Governor from Germany that, although IDA funds should be made available on less stringent terms than is possible with the International Bank, nevertheless, the basis of sound international lending should not be undermined. "We do not ourselves much like the idea of concessionary rates of interest."[2]

The Governor from Canada, Mr. Donald Fleming, warned that, although there was need for funds on less onerous terms than those of the Bank, there was also need to maintain lending standards. "In our opinion, the distinction between grants and loans should not be blurred, and provisions regarding repayment, while properly less onerous than those which are available in commercial loans or through the International Bank, nevertheless should not be such as to store up trouble for the future."[3]

The Governor from South Africa expressed the view that debtor countries should be assessed for contributions to IDA on the basis of per capita gross national product rather than on the basis of the International Bank's subscription formula. South Africa injected a note of caution into the discussion of IDA.

> At the present time the demand for capital far exceeds the supply. The establishment of the IDA will not create new capital. At most it will mean the redistribution, within limits, of the available capital. Such diversion can and will make an important contribution to the economic advancement of the less developed countries but we must face the fact that there will still not be enough

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[1] IBRD Board of Governors Press Release No. 60, September 30, 1959, p. 3.

[2] *Ibid.*

[3] IBRD Board of Governors Press Release No. 68, September 30, 1959, p. 2.

capital to satisfy all the wants of all these countries. . . .
If we were to think that the IDA will provide the answer to all capital prayers of the less developed countries, that it will be the panacea for all economic ills and that it will solve all financial problems, we are bound to be disappointed.[1]

The Governor from Sweden interjected SUNFED into the debate.

We hold the view that there would have been considerable merits in a solution permitting also other member countries of the United Nations, besides those represented here, to assist in the task of creating a new financial institution of this kind. As you know, projects of a nature similar to IDA, among them the Special United Nations Fund for Economic Development, have been considered by the UN for several years, and the matter will come up again before this year's session of the General Assembly. I will make it clear, however, that we--since so many of the prospective recipient countries in the course of this meeting have spoken in favor of the IDA--shall not object to the proposed mandate to the Bank Directors. . . . An attempt should be made to coordinate the work being done in this field here and in New York.[2]

In Chapter XI, we shall see how Sweden's view has changed.

The Views of the Underdeveloped Countries

The Governor from Viet Nam proposed that

Instead of a single multilateral loan fund, several such development funds might be created within the framework of, or closely tied to, the International Development Association, with each loan fund adapted to conditions and needs of a particular region. Moreover, it could represent a vital step forward, so far as the countries of a specific region are concerned, toward greater regional cooperation in coordinating or harmonizing production plans, trade and payments--much the same as the Marshall Plan and subsequent institutions did in Europe.[3]

This proposal was made right after the Inter-American Development Bank had been proposed to meet the needs of Central and South America and the Arab and African Development Banks had been proposed for those areas.

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[1]IBRD Board of Governors Press Release No. 69, September 30, 1959, p. 3.

[2]IBRD Board of Governors Press Release No. 59, September 30, 1959, p. 3.

[3]IBRD Board of Governors Press Release No. 42, September 30, 1959, p. 3.

Some of the Asian countries felt as though they were being neglected and saw a possibility of remedying this through IDA. Nothing came of this proposal, however.

The Governor of the Bank from Libya, Mr. A. N. Aneizi, spoke quite frankly to the Governors. He pointed out that it might be desirable to modify the practices of the International Bank rather than to set up an entirely new institution. He was concerned with the undue proliferation of bodies with more or less the same aims and objectives. He urged that, if IDA be set up, it finance local currency expenditures so as to avoid undue emphasis on the balance of payments aspects of development programs. He also urged the Governors to modify the voting rights of members so as to enable the underdeveloped countries to have a more effective say in the affairs of IDA than in the affairs of the International Bank. And he pointed out that the underdeveloped countries have to incur substantial outlays for essential projects whose benefits transcend the narrow financial and economic criteria of either the World Bank or the proposed IDA.[1]

The Governor from Pakistan warned that it would be unrealistic to expect the underdeveloped countries to put up money in convertible currencies except in token amounts.[2]

The Governor from India had several points for the Governors to consider. He pointed out that

> A developing country finds inevitably that all its investment needs cannot be encompassed within what has come to be called a projects

[1]IBRD Board of Governors Press Release No. 45, September 30, 1959, pp. 1-2.

[2]IBRD Board ot Governors Press Release No. 47, September 30, 1959, p. 2.

> approach; its needs have to be viewed in their totality in terms of the entire program which it is implementing. I should suggest, therefore, that this wider approach should be stressed while framing the provisions of the IDA, and in this approach, I should add, an element of grants cannot be entirely ruled out.
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> Secondly, while it is recognized that an international institution should be a cooperative endeavor . . . there is no getting away, on a plane of practical reality, from the fact that the less developed countries are not in a position to assume any large responsibilities by way of subscription or repayment in terms of convertible currencies or of unrequited exports.[1]

The Governor from Ghana made an extremely straightforward address to the Governors. He expressed the view that IDA's

> working should be so ordered that loans can be made to all deserving underdeveloped countries on an equitable basis, not only for specific projects, but also for general development. . . .
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> . . . .
>
> I should like to conclude my contribution to this debate by stating what I am sure is the voice of the millions in Africa and the other areas with conditions of life similar to ours in Africa, and who like ourselves, are either only recently free or on the verge of nationhood. We have not had the chance to improve our lot as we would wish. In the world of today where the "haves" tend to have more and the "have-nots" to have less, unless we receive aid from the older and stronger nations, some of whom until a while ago were our rulers and ordered our lives for us, the future for us can be but bleak and desolate. May I say that these older and more developed nations, in helping the younger and weaker ones, will only be helping themselves. For us in Ghana, and I believe for all the others, too, whatever help we are given, we should like to feel, is intended primarily to help us stand on our feet and to make us strong economically. Anything less than this may not be welcome.[2]

Apparently the Ghanaian Governor was correct in his assessment that he spoke for other underdeveloped countries, because several spokesmen for other countries spoke approvingly of his address.

Mr. David Horowitz, the Governor from Israel, introduced the writings of one of the founders of the Bank, John Maynard Keynes, into

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[1]IBRD Board of Governors Press Release No. 65, September 30, 1959, p. 4.

[2]IBRD Board of Governors Press Release No. 71, September 30, 1959, p. 3.

the debate.

> "Assuming no important wars and no important increases of population, the economic problem may be solved--or at least within sight of solution--within a hundred years. This means that the economic problem is not--if we look into the future--the permanent problem of the human race."
>
> Keynes was vindicated by subsequent events in industrialized countries. What is needed now is a massive transfer of capital to underdeveloped areas, to vindicate his prediction in the underdeveloped areas of the world.
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> . . . .
>
> The underdeveloped countries cannot get the capital required, on the scale which is imperative, directly on the capital market. They are unable to compete with the credit capacity of developed countries on the free capital market. . . . No dogmatic adherence to "natural" capital movements only should mislead the world in its efforts to raise the standards of living and prevent grave and growing discrepancies.[1]

Horowitz was trying to counter the arguments presented by the West German and United Kingdom spokesmen in favor of natural capital movements as a device to allocate scarce capital.

Drafting the Articles of Agreement

After the debate, the Governors came to unanimous agreement on the resolution introduced by the United States Government and, on October 1, 1959, instructed the Executive Directors, "having regard to the views expressed by the Governors and considering the broad principles on which such an Association should be established and all other aspects of the matter, are requested to formulate articles of agreement of such an Association for submission to the member Governments of the Bank."[2]

When the Board of Governors instructed the Executive Directors

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[1] IBRD Board of Governors Press Release No. 51, September 30, 1959, p. 3.

[2] Summary Proceedings of the 1959 Meeting . . . , p. 30.

of the International Bank to draw up articles, they were giving them a large order. The Governors of the Bank are usually the finance ministers of each member country. Each member has one Governor on the Board and they meet annually, usually in September. For the day-to-day operations of the Bank there are Executive Directors. The best analogy is that of a corporation. The Governors are the stockholders and the Executive Directors correspond to the board of directors. Each of the five major members of the Bank, the United States, United Kingdom, France, Germany, and India appoint a Director. The other member countries elect 13 directors to represent their interests. Both the Governors and the Executive Directors have a weighted system of voting--with the number of votes corresponding to the number of shares held in the Bank.

After the meeting of the Governors in September, 1959, the Executive Directors began their task of drawing up IDA's Articles of Agreement. There ensued a process of debate based on draft papers prepared by the staff of the International Bank. The shape of IDA was outlined in these staff papers and was worked out in detail in meetings of the Executive Directors.

There weren't many controversies during this process of establishing IDA. The timing is important to remember. It was only proposed at the September, 1959 meetings that Articles be prepared. And by January, 1960, the approved text of the Articles was ready to go to the Governors. So, discussion only took place over a three-month period. The Executive Directors normally have monthly meetings, but they had special meetings to consider IDA. Everyone interviewed agreed that there were no tremendous battles over the Articles and the timing surely seems to corroborate this.

The chief concern during the drafting was to keep the Articles flexible. Everyone wanted as little to tie the Association's hands as possible. And they were very successful in this. As Gene Black has said, "The result is that we can do what we want to. The charter of IDA gives the management and staff the right to do almost anything."[1]

The attitude of the Bank's staff toward IDA is difficult to define. As mentioned in Chapter I, Mr. Andrew Shonfield stated that Mr. Black said, during the early discussions on IDA, "that he had never liked the idea of 'soft loans', but if they had to come he was going to make certain that he was the man who handled them."[2]

Mr. Michael Hoffman, of the Bank Staff, hotly disputed this statement. Hoffman argued that the idea for IDA really originated with Eugene Black and Richard Demuth. Black, in particular, is credited with inventing IDA--with taking the local currency idea of Monroney's and changing it into a plan for good project loans on extraordinary terms. Hoffman insisted that Black was very much behind IDA.[3] And, as mentioned earlier, Senator Monroney gave Black a great deal of the credit for getting the idea accepted.

However, there are people who dispute this view. Some members of the Bank staff have indicated that they thought Shonfield was probably right--that Black didn't want soft loans--but if anybody was going to

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[1]Interview, March 13, 1963.

[2]Shonfield, p. 156.

[3]Interview, January 22, 1963.

make them, he wanted to make sure that it was the Bank. This is not inconsistent with Black's own statements. He preferred giving outright grants to the underdeveloped countries. He never liked the idea of soft loans. But, he did realize that if you had soft loans being dispensed by another agency while the Bank was handing out conventional loans, that everyone would go to the other agency.[1] So, it may be that Shonfield and Hoffman are both right. Black recognized the need for money in addition to conventional loans, but he opposed soft loans. However, he recognized that soft loans were the only feasible way to get more money--grants were unacceptable to both the developing and developed countries--and he worked hard to get the soft loan agency tied in with the Bank.

Black discussed his views on this matter at the 1959 meeting of the Board of Governors. This was before the vote to prepare Articles of Agreement. "Should the underdeveloped countries simply want money and not development capital--that is, capital administered to achieve its development purpose--then I suggest this would be the wrong place to come."[2] He might have been intending his remarks for those nations that had been pushing for SUNFED.

At the 1960 meeting, Vice President W. A. B. Iliff stated that the staff realized that the Bank's administration of IDA would be watched carefully. "We have to demonstrate that a bank can handle monies soundly and effectively where an orthodox financial return is not a first consideration."[3] Some of the poorer countries have not yet

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[1]Interview, March 13, 1963.

[2]<u>Summary Proceedings of the 1959 Meeting</u> . . . , p. 11.

[3]<u>Summary Proceedings of the 1960 Meeting of the Board of</u>

been convinced that the staff has succeeded, as will be discussed in Chapter XI.

Some of the underdeveloped countries feel that the Bank captured IDA in order to kill it or dilute its effectiveness. There is a current of hostility toward the Bank in some of these countries. They see the rich nations as having given IDA to the Bank in order to offset SUNFED. And they don't expect the Bank to be enthusiastic in trying to expand the Association. The author did not find any basis for this charge.

During the negotiations, the views of the Bank staff prevailed on most questions. One of the things that did get changed was the nature of the new fund of easy money. The Bank did not want a new institution created. The United States insisted on a new institution. The staff only wanted a fund that could be administered by the Bank and there was some reason for this. The staff was afraid that if there was a separate institution it would get confused with the Bank in the eyes of the financial community. The Bank has a very good standing with the bankers of the world. If these bankers thought the Bank was putting out funds at no interest--they might be reluctant to buy any more Bank bonds. The United States felt that these bankers and investment dealers were sophisticated people and would be able to distinguish between the operations. The Monroney Resolution had called for a new institution. There was a good bit of popular support for a new institution. And so, on this particular point, the staff was apparently overruled.

Governors of the International Bank for Reconstruction and Development (Washington: IBRD, 1960), p. 11.

However, the distinction between the International Bank and the International Development Association is in some ways an imaginary one. Although the funds are kept separate and distinct, the management and staff are identical. Section 4 of Article VI specifies that the Executive Directors of the Association shall be composed ex officio of each Executive Director of the Bank who was appointed by a member of the Bank who is also a member of the Association, or elected by the votes of at least one country who was a member of the Association.

The President of the Bank is ex officio President of the Association and Chairman of the Executive Directors. The President of the Bank is the chief of the operating staff of the Association. He is responsible for the organization, appointment and dismissal of the officers and staff. The closeness of the relationship between the Bank and IDA has caused Dr. Robert Asher to say that although "legally an institution, the IDA appears in reality to be a fund administered by the World Bank."[1] As far as the practical effects are concerned, the Bank staff may not have been over-ruled even on this point.

On such broad questions as the membership and objectives of the Association, there was little dissent. Membership is open to all members of the Bank who desire it. The objectives of the Association are "to promote economic development, increase productivity and thus raise standards of living in the less-developed areas of the world included within the Association's membership, in particular by providing finance to meet their important developmental requirements on terms which are more flexible and bear less heavily on the balance of payments than

[1]Asher, p. 54.

those of conventional loans."[1]

As has been indicated earlier, there was some disagreement on whether the Association should make loans or grants. The staff of the Bank preferred grants, in line with their views on this subject dating back to 1951. However, both the poor and rich members, especially the United States, preferred loans. So, Article V, Section 2 reads as follows: "Financing by the Association shall take the form of loans."[2] There is a provision for other financing either out of funds subscribed after the initial subscription or, in special circumstances, out of supplementary resources furnished to the Association if these resources carry an authorization for such financing.

"The Association may provide financing in such forms and on such terms as it may deem appropriate, having regard to the economic position and prospects of the area . . . concerned and to the nature and requirements of the project."[3] In the report which the Executive Directors prepared to accompany the Articles for country consideration, they elucidate on this section. This section is intended, they explain, to permit the Association to make finance available in a number of ways. The Association could provide for lenient terms of repayment through the use of loans repayable in local currencies, it could make loans repayable in foreign exchange but having long grace periods, it could lend at no interest, or it could lend at a low rate of interest.

Loans are, as with the International Bank, tied to specific

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[1]Articles of Agreement of the International Development Association, pp. 3-4.

[2]Ibid., p. 11.

[3]Ibid.

projects and shall be for purposes of high developmental priority. The expression "specific projects" is given a broad interpretation, however, and can include such proposals as a railway program, an agricultural credit program, or a group of related projects. There is also provision for finance other than for specific projects in special circumstances.

Loans may be made to a member, a member's territory, a political subdivision of a member country, a public or private entity in the territory of a member, and to international or regional organizations. In the case of loans which are not made to member governments, the Association has discretion as to whether or not it will require a governmental guarantee, whereas the Bank's charter requires it to secure a governmental guarantee on such loans.

The Association cannot provide financing when such financing is available from private sources on terms which are reasonable or when a loan could be provided by the International Bank. The Association is barred from tying funds to purchases in any one of its member countries and is directed to give attention to considerations of economy, efficiency, and competitive international trade in using proceeds of its loans.

The Association has the authority to: borrow funds with the approval of the member in whose currency the loan is denominated; guarantee loans from other sources; and provide technical assistance and advisory services at the request of a member.

The Association is authorized to enter into a formal arrangement with the United Nations and may enter arrangements with other public international organizations having specialized responsibilities in related fields.

On the question of voting rights in the Association there were differences of opinion. The underdeveloped countries wished to have more weight than they have in the International Bank and to some extent they succeeded. When the quotas of the World Bank were doubled in 1958 the voting strength of the smaller countries was diluted somewhat. In the Articles of IDA, the old formula is brought back. Each original member gets 500 votes plus one additional vote for each $5,000 of its initial subscription. Countries joining after original membership get voting rights as decided by the Board of Governors. All additional funds given to IDA above the original subscription carry no voting rights.

The voting pattern works out as follows: as of June 30, 1961, the United States had put up 35 per cent of the money and had 31.25 per cent of the votes; the United Kingdom had put up 14.5 per cent of the money and had 12.94 per cent of the votes; France and Germany had the same quota which was 5.85 per cent of the money and 5.37 per cent of the votes; and no other country had as much as 5 per cent of the votes. As new countries come into the Association, these percentages change slightly.

The underdeveloped countries were not at all reconciled to the weighted voting arrangement. The Governor of the Bank from Burma, Thakin Tin, put the case rather bluntly at the 1961 meetings.

> The principle of voting and representation in the management on the basis of the size of stock held by members, though customary for profit-making associations, is hardly comforting to small stockholders in an institution like the Bank which has the avowed object of assisting underdeveloped countries. The latter cannot help feeling that they are excluded from deliberations vital to their future and what they get in the way of development loans is largess through the beneficience of large stockholders who dominate

the institution by virtue of their voting strength.[1]

On the question of local currencies there was some disagreement, also. As mentioned earlier, the staff of the Bank was not enthusiastic about receiving local currencies from the United States. However, the Articles contain provisions whereby countries may provide supplementary resources in the currency of another member, but IDA must agree before any local currencies can be contributed.

On the question of amendment of the Articles, the IDA procedure is a little simpler than in the Bank. Amendment of IDA Articles can be done by the Board ot Governors, whereas in the Bank, the amendment must go to the member governments.

The Articles direct that political considerations not be taken into account when deciding upon a loan. "Only economic considerations shall be relevant . . . and these considerations shall be weighed impartially in order to achieve the purposes stated in this Agreement."[2] Even though this Article is clear in its intent, it is difficult to think that Egypt would be impartial about approving loans for Israel or vice versa.

The two main issues which arose in the discussions were the shares to be contributed by the members and the form in which the member's contributions would be made. First, it was agreed that the total funds of the Association would be $1 billion. There was some argument against fixing such a total in view of the fact that new countries would be coming in and that some of the members of the Bank

[1]IDA Board of Directors Press Release No. 7, September 19, 1961, p. 2.

[2]Articles of Agreement of the International Development Association, p. 12.

might not choose to join IDA. But, a total was set. Then the apportioning of shares took place.

One possibility which was considered was contributions based on national income or gross national product. The gross national products of the industrial nations, which would have to subscribe the usable currency, were converted to United States currency on an exchange rate basis and totaled. On this basis, the United States has 57 per cent of the West's gross product, the United Kingdom has 8 per cent, the European Economic Community countries have 20 per cent, and the other industrial countries have a combined total of 8 per cent. On the basis of United States prices (using the formula devised by Milton Gilbert and Irving Kravis) the proportions are United States--47 per cent, United Kingdom--9 per cent, European Economic Community--25 per cent, and other countries--19 per cent.

Dr. Paul N. Rosenstein-Rodan established a formula for apportioning relative shares of foreign economic aid. He used both exchange rate and United States price formulae for his computations. On a straight gross national product basis, he concluded that the United States should contribute 60 per cent of the aid burden. By using United States prices to establish a figure for "real" gross national product, he computed the United States' share at 54 per cent. Applying the progressive income tax principle to the real gross national product he concluded that the United States share would be 65 per cent as shown in Table 4.[1]

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[1]P. N. Rosenstein-Rodan, "International Aid for Underdeveloped Countries," The Review of Economics and Statistics, XLIII (May, 1961), p. 111.

TABLE 4.--Sharing the burden of aid[a]

	Nominal GNP				"Real" GNP			
	GNP Per Family (dollars)	Number of Families (thous.)	Tax Per Family (dollars)	Contribution by Each (%)	Weights for "Real" GNP	"Real" GNP Per Family (dollars)	Tax Per Family (dollars)	Contribution by Each (%)
Belgium	5392	2303.2	495	1.1	1.23	6632	729	1.4
Canada	7954	4578.2	1002	4.3	1.00	7954	1002	3.7
Denmark	4774	1152.7	380	0.4	1.33	6349	676	0.6
Finland	3573	1128.5	164	0.2	1.44	5145	449	0.4
France	4815	11,478.0	389	4.2	1.20	5778	568	5.3
W. Germany	4452	14,072.0	326	4.3	1.43	6366	679	7.7
Italy	2491	12,385.7	0	0	1.44	3587	164	1.6
Luxemburg	6084	83.0	626	0.04	1.23	7483	900	0.06
Netherlands	3815	2910.5	209	0.6	1.55	5913	594	1.4
Norway	4895	906.7	398	0.3	1.29	6315	670	0.5
Oceania	4419	4023.7	317	1.2	1.33	5877	585	1.9
Sweden	6228	1889.7	653	1.2	1.30	8096	1033	1.6
Switzerland	6222	1343.5	652	0.8	1.25	7778	944	1.0
United Kingdom	5383	13,075.0	493	6.1	1.30	6998	799	8.4
U.S.A.	11,161	46,141.5	1728	75.2	1.00	11,161	1728	64.4

[a]On basis of progressive income tax schedule of U. S. A. Assumes a family consists of 4 members.

Source: Adapted from P. N. Rosenstein-Rodan, "International Aid for Underdeveloped Countries," The Review of Economics and Statistics, XLIII (May, 1961) p. 138.

The idea of progressivity of contributions was welcomed by some of the poorer countries. However, the richer countries saw little to commend such a proposition. No agreement on any formula based on gross national product could be reached. The other alternative was to use the quotas that had been established at Bretton Woods for contributions to the International Monetary Fund and the International Bank. The exact formula for these quotas was not available to the author but, it is known that it took account of the size of gross national product, the ratio of exports to gross national product, the fluctuations in export earnings, etc. All these considerations are more relevant for the International Monetary Fund than they are for the International Bank or the International Development Association (see Chapter XI).

The United Kingdom, Belgium, the Netherlands and other ex-colonial powers have been strikingly hit by this formula. At the time the Bretton Woods Agreement was drawn up the United Kingdom held great reserves for sterling area trade and had a large share of world exports and imports. By using exchange rates on gross national products, the United Kingdom would contribute 8 per cent and all the European Economic Community countries would contribute 20 per cent. However, by use of the Bretton Woods formula, the United Kingdom's share is 17 per cent and the European Community countries' share is 23 per cent. On a straight gross national product basis, the following countries are obviously contributing more than their share to the Bank; United Kingdom, Netherlands, Belgium, Norway, South Africa and Denmark. And the following countries are contributing less than their share; Italy, Sweden, Canada, Germany, France and the United States. However, the Bretton

Woods formula was the only basis on which any agreement could be reached and this was finally adopted.

The United Kingdom, Belgium and the Netherlands have been unhappy with this decision. They feel that the world situation has changed since Bretton Woods. The United Kingdom subscribed to the Association almost immediately, despite its objections. The Netherlands held off for a while and Belgium is not yet a member.

The second major issue involved the arrangements to be made for payment of subscriptions. Were all member nations going to have to subscribe in gold or convertible currencies? Or were the poor nations to be allowed to subscribe in their own currencies? Finally a very ingenious scheme was devised. The members of the Bank were divided into two parts. Part I countries are the industrial nations of the world and would be expected to make their contribution in convertible currency. Part II countries were underdeveloped countries who might expect to be eligible for assistance from IDA and would expect to make most of their contribution in their own currencies.

The decision on which countries would fall into Part I and which into Part II

> presented the Bank with an interesting and rather difficult question. A large number of economic criteria were made available by the Bank, the amount of capital exported by the country, the gross national product of the country, and various other things of that sort. These were reviewed by the Board of Directors. But in the ultimate analysis, the management of the Bank was invited to present a list of those countries which, in their opinion, and based on the background of the World Bank, should be in category I and those which should be in category II. The management presented this list, and the various executive directors who were negotiating the charter discussed it and agreed that this was an adequate list.[1]

[1]U. S., Senate, Committee on Foreign Relations, Hearings on S. 3074, 86th Cong., 2d Sess., 1960, pp. 22-23.

The Bank staff relied primarily on per capita income figures for their decision. But there were some negotiations. Most cases were fairly obvious but there were two cases that the staff could not decide--so they asked the countries concerned. Spain said they were flattered to be asked but they did not feel that they were Part I calibre. Finland accepted Part I membership.

Some countries (such as Iceland) came in as Part II countries feeling that they probably wouldn't be able to borrow from IDA because their per capita incomes were too high to justify IDA loans. Japan is an anomaly from a per capita income standpoint. Japan, however, does export capital so it was put in Part I. The decision was based partly on how a country sees itself. Israel, for instance, has a high per capita income but is a massive capital importer. Ireland came in as a Part II country but has a relatively high per capita income. One of the considerations which the Bank staff considered was the fact that Part I countries are required to put up all their subscription in gold or convertible currency, while the Part II countries only put up 10 per cent of their subscription in gold or convertible currency and 90 per cent in their own currency. So, some relatively well-off countries (Iceland again) wouldn't want to put up all their subscriptions in convertible currency due to their own needs. Table 5 shows the countries of Part I and Part II and their proposed initial subscriptions.

There has been little published criticism of the IDA for its policy of requiring the underdeveloped countries to contribute 10 per cent of their subscription in gold or convertible currencies. Ceylon expressed opposition to any further drain on the poorer countries in

TABLE 5.--Proposed initial subscriptions in the International Development Association
(millions of U. S. dollars)

Part I			
Australia	$20.18	Japan	33.59
Austria	5.04	Luxembourg	1.01
Belgium	22.70	Netherlands	27.74
Canada	37.83	Norway	6.72
Denmark	8.74	Sweden	10.09
Finland	3.83	Union of South Africa	10.09
France	52.96	United Kingdom	131.14
Germany	52.96	United States	320.29
Italy	18.16		763.07
Part II			
Afghanistan	1.01	Israel	1.68
Argentina	18.83	Jordan	0.30
Bolivia	1.06	Korea	1.26
Brazil	18.83	Lebanon	0.45
Burma	2.02	Libya	1.01
Ceylon	3.03	Malaya	2.52
Chile	3.53	Mexico	8.74
China	30.26	Morocco	3.53
Colombia	3.53	Nicaragua	0.30
Costa Rica	0.20	Pakistan	10.09
Cuba	4.71	Panama	0.02
Domininican Republic	0.40	Paraguay	0.30
Ecuador	0.65	Peru	1.77
El Salvador	0.30	Philippines	5.04
Ethiopia	0.50	Saudi Arabia	3.70
Ghana	2.36	Spain	10.09
Greece	2.52	Sudan	1.01
Guatemala	0.40	Thialand	3.03
Haiti	0.76	Tunisia	1.51
Honduras	0.30	Turkey	5.80
Iceland	0.10	United Arab Republic	6.03
India	40.35	Uruguay	1.06
Indonesia	11.10	Venezuela	7.06
Iran	4.54	Viet-Nam	1.51
Iraq	0.76	Yugoslavia	4.04
Ireland	3.03		236.93
		TOTAL	$1000.00

Source: Adapted from Articles of Agreement of the International Development Association (Washington: International Development Association, 1960), p. 29.

the event of a future expansion of IDA.[1]

Each country is given five years in which to pay in its original contribution. Currency of Part II countries may be used by the Association for administrative expenses incurred by the Association in the territories of such members; and insofar as it is consistent with sound monetary practices this currency may be used to pay for goods and services to be used for projects financed by the Association in such territories; and when the Association and the country agree on it the Association can use these currencies for projects outside the territories of the member. All members must take steps to maintain the value of their subscriptions. In the event of depreciation, countries must add enough currency to restore the original value and in case of appreciation, the Association will return currency to the member country.

The Articles charge the Association with reviewing the adequacy of its resources at such time as it deems appropriate and at five-year intervals thereafter. If it seems desirable, the Association shall authorize a general increase in subscriptions. When additional subscriptions are authorized, each member shall be given the opportunity to subscribe an amount which will enable it to maintain its relative voting power, but no member shall be obligated to subscribe. Any country may add to its subscription at any time.

The Executive Directors gave the member nations until December 31, 1960 to decide whether they desired membership. And the Articles were to enter into effect upon their acceptance by governments whose

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[1]IDA Board of Governors Press Release No. 57, September 19, 1961, p. 5.

subscriptions totaled 65 per cent of the total or $650 million. The completed Articles of Agreement and an accompanying report of the Executive Directors went out to the Governors of the Bank, by mail, on January 26, 1960.

Congressional Approval of the International Development Association

On February 18, 1960, the National Advisory Council submitted a special report on the International Development Association.[1] This report contained the Articles of Agreement for the Association and a statement of the Administration's reasons for favoring United States' participation. The arguments which were used in the debate on the Monroney Resolution were repeated but with some changes in emphasis. This report emphasized that the less developed countries themselves would be contributors to this new institution.[2] Much was made of the fact that other countries would provide a larger share of the total resources than would the United States.[3] The possibility of using local currency was still receiving emphasis, although the Council did point out that the magnitudes that would be involved could not be predicted.[4]

President Eisenhower wrote a letter of transmittal for the report in which he stated that "I am convinced that participation by

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[1]National Advisory Council on International Monetary and Financial Problems, Special Report to the President and to the Congress on the Proposed International Development Association (Washington: U. S. Government Printing Office, 1960).

[2]*Ibid.*, p. IV.

[3]*Ibid.*, p. 2.

[4]*Ibid.*, p. 9.

the United States is necessary."[1] Thus, since 1958, the Administration's reaction had run the gamut from determined opposition to IDA, through indifference, to lukewarm approval, until by February 18, 1960, membership had become necessary.

President Eisenhower's recommendation that the United States participate in the International Development Association went to the Congress in February and both houses of the Congress called early hearings on the proposal. There was the feeling that early United States action was necessary in view of the role of the United States in proposing IDA. And it was also thought that early United States approval would encourage the other nations to act speedily. Secretary of the Treasury Anderson and Under Secretary of State Dillon presented the Administration's case.

Secretary Anderson's testimony before Subcommittee No. 1 of the House Committee on Banking and Currency left no doubt concerning his stand on United States membership in IDA. He introduced his statement with this sentence. "I wholeheartedly support enactment of this bill."[2] He went on from there to reiterate arguments that had been made earlier in favor of the Association. However, he did introduce some new points of emphasis.

One of these concerned the fact that the underdeveloped countries themselves were putting in 10 per cent of their subscriptions in gold or convertible currencies.

> This, it seems to me, will give a sense of fiscal discipline, because all of them will be looking at the fund thinking in

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[1] _Ibid._, p. IV.

[2] _Hearings on H. R. 11001_, 86th Cong., 2d Sess., 1960, p. 3.

> terms that, when these hard resources have been exhausted, the borrowers as well as the lenders have to be putting back some hard currencies in order to maintain the activities of the International Development Association.[1]

This particular item became one of the crucial points upon which the United States was insistent. Anderson pressed for agreement on the principle that, not only must all countries make some contribution in gold or dollars on the first round, but, that any replenishment of capital would also involve a gold or dollar contribution by the debtor as well as the creditor countries.[2]

Some of the Representatives indicated concern that the establishment of the International Development Association might be detrimental to the United States' balance of payments. Secretary Anderson was reassuring on this point.

> We are contributing about 32 percent of the funds to this institution, and the normal practices of the World Bank indicate that about 29 percent of the identifiable purchases under World Bank loans on an international competition basis are made in the United States.[3]

He conceded that these figures would indicate that the establishment of IDA might lead to some temporary addition to the United States' balance of payments problem. However, he argued that IDA was a long run attempt to solve this problem "on the basis of establishing a world in which we can become larger exporters, and other people better customers."[4]

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[1]Ibid., p. 10.

[2]New York Times, May 19, 1959, p. 10.

[3]House Subcommittee 1 of the Committee on Banking and Currency, Hearings on H. R. 11001, 1960, p. 36.

[4]Ibid.

The strongest implied criticism came from a member of the committee who was not even at the hearings. Representative Wright Patman, of Texas, had sent a list of questions which he wanted Secretary Anderson to answer. The questions concerned the interest rates that had been charged by the Export-Import Bank and the International Bank from 1946 to 1958.

Tables 6 and 7 are taken from Secretary Anderson's reply to Representative Patman's questions. Patman was calling attention to the rise in interest rates on Export-Import Bank loans from 2.77 per cent in 1948 to 5.20 per cent in 1959 and on International Bank loans from 4.25 per cent in 1947 to 5.64 per cent in 1958. The Congressman was implying that it was the United States Government that was responsible for raising these rates and that this action was the reason that some such measure as the International Development Association was necessary.

Another line of criticism which came from the House Committee was based on the action of the International Bank in extending a loan to the United Arab Republic for the purpose of dredging the Suez Canal. This loan had come right at the time that the United Arab Republic had denied Israeli ships, or ships bound for Israel, access to the Canal. Some 25 per cent of the membership of the House of Representatives had objected to the Bank over this loan. The Bank had, nevertheless, granted the loan. This had considerably angered some Representatives and several of them expressed their unwillingness to establish IDA under World Bank management.

There was very little criticism or opposition in the Senate hearings. Most of the Committee on Foreign Relations was obviously

TABLE 6.--Total loan authorizations and average interest rates charged on foreign loans by U. S. Government lending agencies, fiscal years 1946-58

Fiscal Years	Export-Import Bank		Mutual Security Program		Public Law 480[a]		Development Loan Fund	
	Loan Authorizations	Average Interest Rates	Loan Authorizations	Average Interest Rates	Loan Authorizations	Average Interest Rates	Loan Authorizations	Average Interest Rates
	Millions	Percent	Millions	Percent	Millions	Percent	Millions	Percent
1946	$2,197.0	2.77						
1947	279.2	3.50						
1948	465.7	2.87	$2.3	2.50				
1949	173.8	3.73	965.8	2.50				
1950	405.5	3.53	73.2	2.50				
1951	395.3	3.81	296.7	2.57				
1952	550.9	3.19	222.4	2.57				
1953	571.0	3.78	25.6	2.68				
1954	250.4	3.99	2.2	3.00				
1955	488.4	4.52	270.2	3.78	$66.1	3.92		
1956	378.0	4.64	215.8	3.92	39.3	4.00		
1957	1,067.3	4.78	383.8	3.95	546.3	4.06		
1958	857.0	5.20	102.8	3.98	502.1	4.26	$102.1	4.36

[a]Includes only loans to foreign countries. Does not include loans to private enterprises under sec. 104(c) of Public Law 480.

Source: Adapted from House Subcommittee 1 of the Committee on Banking and Currency, Hearings on H. R. 11001, 1960, p. 24.

TABLE 7.--Total loan authorizations and average interest rates charged by international landing agencies, fiscal years 1947-58

Fiscal Years	International Bank		International Finance Corporation	
	Loan Authorizations	Average Interest Rates	Investments	Average Interest Rates[a]
	Millions	Percent	Millions	Percent
1947	$250.0	4.25		
1948	263.0	4.26		
1949	137.1	4.39		
1950	166.3	4.03		
1951	297.1	4.08		
1952	298.6	4.58		
1953	178.6	4.77		
1954	323.7	4.82		
1955	409.6	4.68		
1956	396.1	4.75		
1957	387.9	5.04	$2.0	6.00
1958	710.8	5.64	8.7	7.00

[a]Investment agreements usually provide in addition for payments contingent on profits and in most cases for options on shares of the borrowing company.

Based on data supplied by the International Bank and the International Finance Corporation.

Source: Adapted from House Subcommittee 1 of the Committee on Banking and Currency, Hearings on H. R. 11001, 1960, p. 25.

quite favorable to the establishment of IDA. There were some questions concerning coordination between IDA and United States' aid activities so that borrowers could not play off one against the other and so that duplication of effort could be avoided. The Administration spokesman assured the committee that the United States Executive Director of IDA would sit as a member of the Board of the Development Loan Fund so that such problems ought not arise.

A surprising degree of unanimity existed among the business and labor groups of the United States on the advisability of joining the International Develooment Association. Only three groups, the Farm Bureau, the National Foreign Trade Council, and the Merchant Marine Institute, expressed reservations concerning the IDA.

As far back as 1956, the Research and Policy Committee of the Committee for Economic Development had called for an expanded program of public investment in underdeveloped countries under World Bank leadership where an international approach was advantageous. This group favored giving the World Bank additional capital contributions and authority to make grants and development loans repayable in local currencies.[1]

The Chamber of Commerce of the United States supported the IDA from the start. The Chamber was anxious to have assurances that loan funds would not supplant private capital. The National Association of Manufacturers had no particular policy position with reference to IDA. The U. S. Council of the International Chamber of Commerce sent a representative to testify in favor of United States membership in the

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[1]Research and Policy Committee of the Committee for Economic Development, Economic Development Abroad and the Role of American Foreign Investment (New York: CED, 1956), p. 29.

Association.

The National Farmers Union made a strong statement before the House Committee on Banking and Currency favoring United States participation in IDA. The National Grange sent a letter of support as did the National Council of Farmer Cooperatives. The Farm Bureau actually did not oppose the establishment of IDA; they merely wanted to insure that if the United States joined IDA it be with the firm understanding that the United States Development Loan Fund's appropriation be reduced by the amount of the appropriation to IDA. For, as their letter pointed out, "there is a limit to the amount of capital funds the U. S. Government can provide to other countries."[1]

The bankers of the United States sent three spokesmen to welcome the establishment of IDA. Mr. John J. McCloy, Chairman of the Chase Manhattan Bank, Mr. James S. Saxon of the First National Bank of Chicago, and Mr. Tom B. Coughran, Executive Vice President of the Bank of America, served to represent the bankers as strongly in support of United States participation in IDA.

The American Federation of Labor-Congress of Industrial Organizations made a very strong case for United States participation in the International Development Association. The spokesman did have two reservations about the new Association. One was that, in turning IDA over to the World Bank, the influence of individuals with the traditional bankers' point of view might outweigh the views of those who recognize the need for flexible, nonbankable loans for economic

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[1]House Subcommittee No. 1 of the Committee on Banking and Currency, Hearings on H. R. 11001, 1960, p. 102.

development.[1]

The labor spokesman also questioned the size of the appropriation for IDA. The September, 1959 convention of the AFL-CIO had adopted a resolution which called upon Congress to authorize effective United States financial support for IDA. It did not appear to the AFL-CIO representative that a contribution of $320 million constituted effective support. He expressed the hope that Congress would expand the resources of IDA so that it would be assured of at least $1 billion a year.

> We must recognize that, unless the more fortunate, industrially advanced nations of the free world, and especially the United States, which is still by far the richest, are prepared to make available to the less developed countries economic assistance on a scale commensurate with their minimum needs, they will reluctantly, but inevitably, turn to the Soviet Union.
>
> This is an important reason for increasing the capitalization of the International Development Association substantially above the presently contemplated level, but it is by no means the only one.[2]

The Congress turned a deaf ear to this plea.

Other groups which endorsed United States entry into the Association were the National Council of the Churches of Christ in the U. S. A., the United Christian Missionary Society, and the Women's International League for Peace and Freedom.

The Merchant Marine Institute questioned the advisability of multilateral foreign aid because the United States would not be able to require that goods be shipped in American vessels. The National Foreign Trade Council passed resolutions at both its 1958 and 1959 meetings which questioned the need for another inter-governmental

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[1] Ibid., p. 55.

[2] Ibid., p. 56.

financial institution. The Council felt that any necessary aid should be given on a bilateral basis and that such aid should not be repayable in non-convertible funds. However, by the time the bill to establish IDA came before the Congress, the Council was reconciled to IDA and did not testify against United States membership. They did publish a statement which questioned the local currency aspects of IDA and which regretted that no reference was made in the articles of agreement to the need to prevent any financing which would be inimical or injurious to private enterprise.[1]

Why was there so little opposition to United States participation in IDA? Such participation will cost more than $300 million. At the same time that legislation establishing IDA was sailing through the Congress there was very bitter and determined opposition to smaller sums contained in the bilateral aid program. Some persons have suggested that the Congress is usually enthusiastic about any new aid program. All proposals for re-orienting the foreign aid program are seen as panaceas at their first introduction. Thus, the IDA merely slipped through on its newness as did the Inter-American Development Bank and the Development Loan Fund a few years earlier. These people would expect a good bit harder fight on additional funds for IDA than was made over the original authorization.

Another interpretation has attributed IDA's popularity to the intensive publicity campaign which Senator Monroney waged throughout 1958-1960. Editorials favoring IDA appeared in 40 newspapers around the

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[1]"Statement of the National Foreign Trade Council Concerning U. S. Participation in the International Development Association" (New York: National Foreign Trade Council, 1960), pp. 2-3. (Mimeographed.)

country during this period. All the major newspapers in the country carried extensive stories and articles on IDA, many in a friendly vein.

Certainly the fact that IDA was to be managed by the staff of the World Bank had considerable influence. Mr. Gene Black's reputation is quite phenomenal among United States lawmakers. They credit him with a wizard's touch when it comes to managing a difficult operation.

Congressional approval for United States participation came on June 30, 1960. An appropriation of $73 million for the first installment of the United States on its initial subscription was approved on July 14, 1960 and on August 9, 1960, the United States deposited its instrument of acceptance with the International Bank. The Articles of Agreement had specified that the Agreement would enter into force when it had been signed on behalf of governments whose subscriptions totaled not less than $650 million. This point was reached on September 24, 1960 and the International Development Association became a reality. Operations of the Association were begun on November 8, 1960 when the Executive Directors held their inaugural meeting.

CHAPTER VIII

FUNDAMENTAL POLICY DECISIONS

Basic Philosophy Underlying Policies

The First President of the Association, Mr. Eugene Black, has stamped the Association with his basic views on the development process. His views underlay the basic policy decisions made during the first two years IDA was in operation and these views have been expressed on many occasions (see Chapter II). He believes that economic development cannot be based on expediency.

> Political processes, of course, are the essence of democratic governments; and it is true that in a democratic society it is often difficult for a government to take the long-term view. Yet development is a long-term process. It cannot be carried out sporadically; it must be approached as a matter of broad and continuing public interest--not a means of promoting the interests of a particular area of the country, not a means of winning votes in a critical electoral district, not a means of satisfying the ego of political sponsors.
>
> The more developed nations, too, need to remind themselves continually that international aid for development ought not to be based on expediency. To be really effective, they should not relate their efforts to fever charts of international tension, but rather to the fundamental conditions of which the fever may be only a long-delayed symptom.[1]

For a man whose job has been to allocate capital, Black has a surprising attitude toward the role of capital in economic development.

Let me say that in my opinion too much emphasis is often placed on

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[1] _Summary Proceedings of the 1951 Meeting of the Board of Governors of the International Bank_ . . ., p. 8.

> capital, particularly foreign capital, as the prime ingredient of development.
>
> . . . .
>
> The social institutions of the country, the distribution of wealth and opportunity among the people, the effectiveness of the educational effort, the energy and competence of government administration, and the character of the policies governing the use of the country's resources--these are all factors which bear quite as directly as foreign capital on the rate of development.[1]

Black argues that quality is more important than quantity in economic aid.

> Even the most enthusiastic supporters of economic aid recognize that the outside world cannot provide more than a small margin of the resources needed; the really crucial economic and human resources must come from within. Therefore, it is only realistic, we think, to use economic aid primarily to promote proper standards in the art of managing a country's resources.[2]

The staff is fond of reminding the underdeveloped countries that many countries developed without huge inflows of external capital.

> We have become so accustomed to associate development with economic and financial aid from abroad, that we sometimes tend to forget that economic growth and industrialization have taken place in several parts of the world without important inflow of capital. The European countries are the outstanding example, although, of course, freedom of movements of capital was the rule in the XIXth century. The same is true of Japan before World War I; its remarkable development was based on internal savings. More recently, the Soviet Union has achieved both reconstruction and development without foreign assistance but at a tremendous cost in terms of standard of living.[3]

Black eschews, as far as efficiency permits, the ideological aspects of development.

> In the World Bank we concentrate on economic development as if its only end were higher comsumption and greater comfort. We try

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[1] Ibid.

[2] Eugene R. Black, "The Age of Economic Development," The Economic Journal, LXX (June, 1960), 269.

[3] Leonard Rist, "International Cooperation in Development Aid," Address to the Fourth S E A N Z A Meeting, p. 2.

> to remove the taint of ideology from the language of economics and then relate that language solely to the end of promoting higher material living standards.[1]

Black rejects the simple explanations for underdevelopment and the theories of growth which focus on one cure. He argues that it is not just a lack of capital per se, of savings per se, of education per se, or of entrepreneurship per se which stands in the way of growth.

> It is more useful, I think, to consider the problem in terms of how to achieve the kinds of decisions which are needed to make more of the potential for growth. For as there is a greater awareness of the possibilities for growth in society, many of the traditional obstacles appear much less formidable.[2]

None of Black's critics has attacked him because the Association has done too much. A number have claimed that it did much too little. His answer follows:

> If the meaning is that we should substitute our hearts for our heads in investing IDA resources, I could not disagree more completely. For the one lesson of experience that more than any other has been borne home to me over the years is that the surest way of defeating our ultimate development objective is to use carelessly or ineffectively the scarce resources which have been entrusted to us. . . . That is why we have insisted, and will continue to insist, on the same high standards of investment for projects financed with IDA funds as for those financed with Bank resources.[3]

Black does not deny the consideration which should be given to human suffering. He is certainly aware of the political pressures upon the governments of the developing countries. And he urges that economic aid can be dispensed sensibly, still taking these considerations into account.

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[1]Black, "The Age of Economic Development," p. 269.

[2]Black, The Diplomacy of Economic Development, p. 27.

[3]Summary Proceedings of the 1961 Meeting of the Board of Governors of the International Bank for Reconstruction and Development (Washington: IBRD, 1961), pp. 14-15.

> The claims of poverty appear so compelling that the outsider is tempted to conclude that all argument over the niceties of equality, or of regional "fairness" or of national prestige is really too much of a luxury to be tolerated. But such an attitude does less than justice to the governments of these countries; the political problems they face are excruciatingly difficult; they are the primary agents of change in societies undergoing a wholesale transformation to prepare for modern economic life. In Western societies the primary agents of change in the early stages of development were the entrepreneurs; governments could then confine themselves to ruling--to maintaining law and order. Now governments in the underdeveloped world are taking most of the development initiatives themselves, either because there is no entrepreneurial class of any significance or because only the Government can raise the necessary capital. They have to lead as well as rule. To help these governments perform their necessary development functions without generating extravagant forms of political injustice and cruelty is really the major objective of economic aid.[1]

Some Early Policies

With Black's philosophy forming the foundation for decisions, what fundamental policies did the Association choose? As to the terms of financing, it was decided that IDA would not make loans repayable in local currency. On this point there was general concensus among the Executive Directors, and the staff was opposed to local currency loans.

The terms that have been adopted for all "development credits" extended to date have been identical. The credits must be repaid in foreign exchange. They have a duration of 50 years, amortization is to begin after a 10 year grace period; thereafter, 1 per cent of the principal is repayable annually for 10 years and 3 per cent is repayable annually for the next 30 years. A service charge of 3/4 of 1 per cent per annum on the amounts withdrawn and outstanding is charged to pay IDA's administrative costs.

The second Annual Report of the Association dilated these

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[1]Black, "The Age of Economic Development," p. 271.

conditions. The staff did not intend that these concessionary terms should result in the extension of financial subsidies to the actual projects on which IDA funds were employed. So, in the case of revenue-producing projects, IDA requires that the credit be invested on a normal business-like basis and that the price of the goods or services produced by the project be fixed at levels which will make the project remunerative.[1]

If IDA should lend soft money for a project with a high rate of return inside the country--then IDA would be subsidizing the borrower vis-à-vis his competitors, which was no part of IDA's purpose. So, the policy has been that IDA credits for commercial projects are passed on to the government and from the government to the ultimate borrower at rates of interest comparable to the rates prevailing within the country. An attempt is made not to distort the interest rate structure of the country. An example of this policy is the $5 million credit to the China Development Corporation which was passed through the hands of the Republic of China. The Corporation is paying 12 per cent interest to the Chinese Government and the duration is 30 years. The reason for this policy is clear. Subsidizing revenue-producing activities would be very bad politics in the first place. It would be inequitable as between borrowers. And it could lead to a poor allocation of resources. Of course, one result of the policy is that the government concerned makes a profit from its "on-lending" of IDA funds. This technique is an innovation in international lending. Previously the terms of aid have been related to the project concerned rather than to the

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[1] Annual Report of the International Development Association 1961-62 (Washington: IDA, 1962), p. 6

circumstances of the recipient country. IDA is paying attention to both.

The First Annual Report carried the announcement that IDA had no policy of allocating its funds in advance. However, it was pointed out that an effort was being made to assure wide geographic distribution, taking account of the priority which should be given to the poorer countries. It was pointed out that it would be necessary to impose limits on credits to some countries which could absorb all the money very quickly.[1] Quite obviously the report was referring to India and Pakistan.

Very early a significant policy question had to be decided along this line. What would be the criterion of eligibility for IDA credits? Would it be based on the type of project or the condition of the borrowing country? It was decided to base decisions on IDA countries rather than IDA projects. Mr. Black's speech to the 1961 meeting of the Board of Governors made it clear that the same standards are applied to projects by both the Bank and IDA, although IDA does finance some projects of a more social nature than the Bank, e.g. schools, housing.

There was an early proposal that soft loans be made for some projects, where returns were slower in accruing, even though they were located in countries that were creditworthy. In addition, credits could be extended for quick-return projects in non-creditworthy countries. In practice, this would mean two types of operations. IDA would finance education, urban water supply, housing projects, etc. in countries that could borrow from the Bank. And, IDA would make credits available for

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[1]First Annual Report of the International Development Association 1960-1961 (Washington: IDA, 1961), pp. 4-5.

roads, hydroelectric plants, and irrigation projects in countries that had difficulty obtaining international credit.

This discussion was resolved in favor of IDA-countries. The Association only lends to countries which are not creditworthy or are exhausting their remaining margin of creditworthiness, and the Bank itself is moving into some projects with slow payback in countries which are creditworthy. The staff is the arbiter on what countries get what terms. The staff decides whether the loan should be made from the Bank, from IDA or not at all. Three criteria have been established for determining if a country is eligible for credits from the International Development Association.

The Creditworthiness Criterion

First, a country must be near the end of its rope so far as creditworthiness is concerned. Within this category there are two types of countries. The first group are those countries whose foreign exchange situation is such that the staff thinks that further hard loans involve a substantial risk of default. The second group consists of those whose burden of foreign debt service is so high that, while they can borrow on conventional terms some of the external capital which they require to carry out their priority programs, they cannot prudently borrow the whole of it. In these circumstances the World Bank and IDA may combine forces and this is, in fact, what has happened in India, Chile, Sudan and Columbia.[1] Decisions on creditworthiness or the blend of loans and credits are based essentially on judgment. Ratios of debt service to exports, or of debt service to local budgetary receipts or

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[1]IBRD Board of Governors Press Release No. 4, September 19,1961, pp. 5-6.

gross national product cannot be used as rigid criteria.[1]

Since the Association's funds are for countries with a balance of payments difficulty, it becomes necessary to draw up a balance of payments estimate for future years. If minus items cannot be offset by plus items, then the country must either default or reduce imports to a level which would seriously affect the continuity of the development process. Although the Association must have a view of the future balance of payments of its customers, the balance of payments really depends upon two items under the control of other lenders. First, how much are other lenders likely to lend in the years ahead? And, secondly, what debt service liability has accrued because of loans these institutions have already made? There are great dangers in projecting balance of payments situations 10 years ahead for this depends upon what assumptions are made about debt service liabilities the country will have acquired during the period and on what terms such liabilities are incurred. It is necessary to try to predict what other soft loan money is going to be made available and whether the industrial nations will keep their present bilateral programs going.[2]

There is an assumption underlying the need for IDA that the underdeveloped countries are going to continue to get capital mainly on conventional terms. It is, therefore, relevant for IDA policy to consider what everyone else is going to be doing. There is the prospect of the underdeveloped countries receiving all sorts of resources from all sorts of sources. What it boils down to is that IDA policy-makers

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[1] Ibid.

[2] Interview with Mr. J. P. Hayes, Economic Staff, IBRD, January 21, 1963.

must guess the other chap's intention.[1]

Despite these complexities, it has been decided that exhaustion or near-exhaustion of creditworthiness is a necessary condition before IDA money can be obtained. But, this ought not be enough. Exhaustion of creditworthiness could be due to improvident policies and IDA was not established to reward the improvident.

The Performance Criterion

So, a second criterion was established--that some element of good performance in the country should be postulated.

> A necessary condition in all cases is evidence that the borrowing government is making a real effort to mobilize its own resources and to gear its financial policies to development . . . IDA is prepared to assist . . . when the government can show a definite will to mobilize domestic resources and to avoid inflationary policies.[2]

Good performance is a very appealing criterion but it is also an ambiguous term which is difficult to quantify. It has been suggested that good performance could be measured in terms of the rate of growth of a country multiplied by the proportion of investment which had been financed domestically. This would reflect the incremental capital output ratios (ICOR) of the countries concerned as follows:

$$\text{ICOR} = \frac{\text{Average savings rate} \quad \text{(ASR)}}{\text{Average growth rate} \quad \text{(AGR)}}$$

$$\text{AGR} = \frac{\text{ASR}}{\text{ICOR}}$$

But, the incremental capital output ratio reflects a country's resource endowment, price structure, etc. This ratio also reflects previous

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[1] *Ibid.*

[2] IBRD Board of Governors Press Release No. 4, September 19, 1961, pp. 5-6.

investment inflows and would therefore penalize a country with heavy prior investment, if one assumed diminishing returns to investment. If one assumed complementarity of investment and increasing returns--then it might give benefit to the relative newcomer. Such calculations illustrate the difficulty of objectively measuring performance.

Some people stress the country's marginal savings rate in evaluating performance. It is argued that, if a serious effort at development is being made, the country will achieve a relatively high marginal savings rate. It has been hard to establish any standards here, though. There seems to be no correlation between average or marginal savings rates and per capita income levels--and there is no norm for any income level. This may be because it has not been approached in a sufficiently sophisticated way as yet.[1]

Another possible quantitative measure of performance has been the taxation performance of the underdeveloped countries. How much of the national income has the government been able to collect in the form of taxes for investment purposes? However, there is a low correlation between gross national products and tax levels, also. When exports and imports as a percentage of gross national product are added to a multiple correlation analysis, the fit is much better. The implication is that countries with a high level of exports and imports can tax them easily.[2]

Pre-investment studies of countries are, except in rare cases, based on investigations on the spot, because experience shows that

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[1] Interview with Mr. J. P. Hayes, January 21, 1963.

[2] Ibid.

> the scant and inadequate published data can only be supplemented in the field and that some judgment of the imponderables bearing on development can only be acquired through personal knowledge of the government and the way it operates, of business enterprise and of the farming classes.[1]

These studies of countries seek to analyze the existing structure of the economy, the structural changes that are taking place and the factors that are inhibiting or accelerating growth. Analysis is made of the magnitude of investment, savings, exports and imports, and external sources of capital. The staff tries to arrive at some judgment as to the rationality of policy and the efficiency and speed with which capital investment takes place. In all these assessments, limitations of data are serious. National accounts data may be wholly lacking. Information on savings are likely to be very unreliable.[2]

> Certainly many of the things which we in the Bank have for many years emphasized both in analysis and practice bears on the importance of "human resources" relative to capital. It is reflected in the attention given to institutional bottlenecks; to the existence or adequacy of initiative and enterprise both in the private and public sector; to the quality and organization of the civil service and the decision-making process of the government; to the degree to which a sense of purpose or an air of buoyancy pervades the country.[3]

Given the difficulty of quantifying good performance, the staff is driven to all kinds of non-quantifiable aspects. It is difficult to set uniform standards. Different countries require different norms. The newly independent nations cannot be expected to meet the same performance standards required for an older country. This calls for judgment as to

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[1]John C. de Wilde, "Research in the International Bank for Reconstruction and Development," a paper presented to the Annual Meeting of the American Economics Association, December 29, 1962 (Washington: IBRD, 1962), p. 6. (Mimeographed.)

[2]*Ibid.*, pp. 6-8.

[3]*Ibid.*, pp. 8-9.

which standards to apply.

In evaluating performances, a question arose. To what extent should this reflect good performance up to the present and to what extent should it rest on opinion or hope that performance is going to be good in the future? In some cases, performance has been poor in the past, but IDA money might be used to encourage better performance in the future (see Chapter X).

IDA uses its funds to exert pressure on countries to follow orthodox financial policies. There has, however, been a notable lack of success throughout South America. As President Black observed in 1961,

> The persistent inability of most South American governments to manage their economies wisely in recent years is easily the most discouraging fact about the continent. . . . When as in Brazil and Chile recently, the general price level rises more than 80% in a given year, it is not just a matter of one misguided policy; there is obviously something fundamentally wrong. There is obviously something fundamentally wrong, too, when . . . tax evasion becomes so commonplace that in many countries it amounts to 50% of income tax assessments.[1]

What can be done in such circumstances? Mr. Black admits that "there is little that outsiders can do about these shortcomings other than to withhold support until tolerable conditions exist. I consider that the major reason for the World Bank's existence is to underline the kind of orderliness in government that is absolutely essential anywhere that economic growth is desired."[2] He is not unduly optimistic about success in bringing this condition about. "No outsider can force orderly government on South America. The problem is one that

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[1]Eugene R. Black, Tales of Two Continents (University of Georgia Ferdinand Phinizy Lectures, 1961), p. 33.

[2]*Ibid.*, pp. 33-34.

South America must solve for itself."[1] Andrew Shonfield has warned against an over-emphasis on performance criteria in administering aid.

> While there is a shortage of funds for this purpose, it is essential that the operation shall be conducted with the minimum of waste, and the criterion to be applied in choosing countries worth investing in is that the "yield" on the capital put into them is not markedly below the standards set in countries which are already developed--the yield being measured in terms of the extra output which the investment produces, not the profit from it. All the same, while the main stream of economic aid must be guided by these businesslike criteria, it is to be hoped that we do not become so exclusively obsessed with the problem of economic growth that we forget about the ordinary demands of charity altogether. Poor people have to be helped, even if they refuse to grow.[2]

The countries that have been considered to meet the performance criterion are shown in Table 8.

The Poverty Criterion

The third criterion is poverty. The Articles state that IDA will "provide financing to further development in the less-developed areas of the world included within the Association's membership." Did the drafters intend this to mean loans only to the poorer of the Part II countries--or to any Part II country? The staff interprets it to mean that loans will only be made to the poorer Part II countries, because it is argued that IDA provides cheap money--tax money from the taxpayers of the rich countries. And, one cannot justify taking money from taxpayers to give subsidies to rich or even relatively rich countries. So, the richer Part II countries--Iceland, Ireland, Israel--have, for all practical purposes, been disqualified from borrowing from IDA. The estimates of per capita income, used by IDA, for the countries that have received credits are shown in Table 9.

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[1] *Ibid.*, p. 34.

[2] Shonfield, pp. 84-85.

TABLE 8.--International Development Association credits granted through September 30, 1962
(millions of U. S. dollars)

Member in Whose Territories Development Credits Have Been Made	Program or Project	Date of Development Credit Agreement	Original Principal Amount
CHILE	Road Construction	June 28, 1961	$19.0
CHINA	Harbor Dredging	August 30, 1961	2.2
	Ground Water Development	August 30, 1961	3.7
	Municipal Water Supply	September 6, 1961	4.4
	Development of Private Industry	December 1, 1961	5.0
			15.3
COLOMBIA	Road Project	August 28, 1961	19.5
COSTA RICA	Road Construction and Maintenance	October 13, 1961	5.5
HONDURAS	Western Highway Improvement	May 12, 1961	9.0
INDIA	Highway Construction and Improvement	June 21, 1961	60.0
	Tubewell Irrigation	September 6, 1961	6.0
	Shetrunji Irrigation Project	November 22, 1961	4.5
	Salandi Irrigation Project	November 22, 1961	8.0

TABLE 8--Continued

Member in Whose Territories Development Credits Have Been Made	Program or Project	Date of Development Credit Agreement	Original Principal Amount
	Punjab Flood Protection and Drainage	November 22, 1961	10.0
	Durgapur Power Extension	February 14, 1962	18.5
	Sone Irrigation Project	June 29, 1962	15.0
	Purna Irrigation Project	July 18, 1962	13.0
	Second Koyna Power Project	August 8, 1962	17.5
	Bombay Port Project	September 14, 1962	18.0
	Telecommunications	September 14, 1962	42.0
			212.5
JORDAN	Amman Water Supply Project	December 22, 1961	2.0
KOREA	Railway Development	August 17, 1962	14.0
NICARAGUA	Managua Water Supply Project	September 7, 1962	3.0
PAKISTAN	Dacca Irrigation Project	October 19, 1961	1.0
	Inland Ports Project	November 22, 1961	2.0
	Khairpur Irrigation Project	June 29, 1962	18.0
			21.0
PARAGUAY	Highway Inprovement and Maintenance	October 26, 1961	6.0

TABLE 8--Continued

Member in Whose Territories Development Credits Have Been Made	Program or Project	Date of Development Credit Agreement	Original Principal Amount
SUDAN	Roseires Irrigation Project	June 14, 1961	13.0
TUNISIA	Education	September 17, 1962	5.0
UNITED KINGDOM SWAZILAND	Highway Construction	March 14, 1962	2.8
		TOTAL	$347.6

Source: Economic Staff, International Development Association.

TABLE 9.--Per capita gross national product (GNP) at factor cost for countries receiving International Development Association credits through September 30, 1962[a] (expressed in United States currency)

Rank	Country	Per Capita GNP
1	Costa Rica	380
2	Chile	345
3	Colombia	285
4	Nicaragua	210
5	Tunisia	175
6	Honduras	160
7	China	125
8	Paraguay	105
9	Jordan	90
10	Korea	80
11	Sudan	75
12	Swaziland	70
13	India	70
14	Pakistan	65

[a]Estimates are for the period 1958-1960 and are made on an adjusted exchange rate basis.

Source: Based on estimates made by the Economic Staff, International Development Association.

The countries that have received IDA credits have per capita incomes below $300 per year with the exception of Costa Rica and Chile. And some persons would argue that it was a mistake to loan IDA money to Costa Rica and Chile. Undernearth this debate, there are two sharply conflicting opinions. One view emphasizes that IDA should help the really poor countries. The other emphasizes the problems of certain countries--higher income countries--which are close to the take-off and which will soon be able to finance their own development. There are several countries in this latter category--Mexico is an example--which have relatively high per capita incomes but which are having difficulties in the intermediate stage of development. A question could be raised about Yugoslavia, also. It might not be eligible based on per capita income, but, based on performance, it is promising. Yugoslavia has had a rapid increase in exports over the past decade. The marginal savings rate has been high. It ought by 1970--if it can keep its momentum--to be able to end its deficit on current account. But, in order to maintain momentum, Yugoslavia will need a very large net capital inflow--on the order of $300 million per annum. The proposals to channel IDA money to countries like these envision charging a nominal rate of interest. For, if capital is provided on conventional terms, these countries will wind up with an enormous external debt. By the same token, they will also have an enormously increased capacity to pay that debt. As of this date, no IDA funds have gone to countries like Yugoslavia and Mexico.

At the 1961 Annual Meetings, the Governor for Spain presented the problem of a certain group of countries.

> If IDA continues to follow the road upon which it has started, it may well happen that a very important area will remain unprovided for: that served by loans, liberal but not interest-free, normally to finance public utility projects, whose cost could be between three and four per cent at most. There are many countries that, while not underdeveloped, are not world leaders either, and for them the kind of loan mentioned would be advantageous.[1]

At the 1962 Meeting of the Board of Governors, the African nations raised questions concerning the allocation of IDA's resources. The Governor from Nigeria pointed out that all of Africa had received only 6 per cent of IDA funds. Some further observations on the allocation of resources will be made in Chapter XI.

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[1]IDA Board of Governors Press Release No. 6, September 19, 1961, pp. 2-3.

CHAPTER IX

PROJECT APPRAISAL

Basic Policies in Appraising Projects

As Alec Cairncross has pointed out, "There is a tendency in the Bank to erect project appraisal into a mystique."[1] And there is certainly a policy of keeping project appraisals made by the International Development Association a deep secret. The author attempted to examine some of the appraisals which the Association has made, however, this was not permitted. As a consequence, this particular aspect of the International Development Association must remain shrouded in mystery. The Association is not without its reasons in keeping such information confidential. Many of the country evaluations contain information submitted by the applying country in confidence. In all the appraisals, an attempt is made to report all relevant information accurately and candidly. There are, consequently, matters in these reports that might be highly embarrassing to member governments if they were published. And, since it is known that these reports will not circulate outside the staff, they are not prepared in complete detail or with ultimate refinement.

With this warning of the inadequacy of the author's information, an attempt will be made to sketch the procedure in project appraisal.

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[1]Cairncross, p. 18.

There is considerable criticism of the Association's policy of limiting its finance to specific projects, no matter how broadly the term project is defined. "An unkind critic would say that the whole idea of financing economic development project by project smacks of paternalism and a pedagogical outlook."[1]

However, this project approach

> is in large part a reaction from the disastrous experience of the 1920's, when international loans were made at high rates of interest for broad, ill-defined purposes, and followed by wholesale defaults. More productive use of resources transferred . . . would be obtained if funds were tied to the financing of specific power plants, railroad improvements, and other undertakings. This would permit more accurate appraisal of amounts needed, . . . arrangements for management, and economic and social benefits of the proposed undertakings.
>
> The articles of agreement of the International Bank consequently limit loans to specific projects except in unusual circumstances.[2]

The Articles of Agreement of the International Development Association carry the same limitation. "Financing provided by the Association . . . except in special circumstances, shall be for specific projects."[3]

Professor Cairncross, who served for a time as head of the Bank's Economic Development Institute, has outlined the philosophy underlying the project approach. The staff

> insists that the loans cannot be treated as isolated transactions and that the projects which they finance must be examined in relation to the rest of the development effort of the borrower. It constantly emphasizes the value of a development programme into which the major projects are fitted. It aims also at identifying the economic and financial policies most conducive to development and the strategic factors upon which governments should be encouraged

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[1] Ibid., p. 17.

[2] Asher, p. 67.

[3] Articles of Agreement of the International Development Association, p. 10.

> to operate. . . . There are passages in its Annual Reports that recur to the same general themes: the limited value of additional finance if other, institutional factors are not propitious; the importance of good management both in the planning of individual projects and in the conduct of a nation's affairs; the need to encourage initiative, enterprise and the will to develop, and to avoid policies which, through weakness, vacillation or impatience, prevent the emergence of attitudes and institutions favourable to development.[1]

Criticism of the Association's policy of providing funds for specific projects has been increasing. Some of the arguments presented in favor of soft loans in Chapter IV can also be used in favor of non-project assistance, i.e., the problems of debt-servicing may get progressively worse as long as aid is earmarked for specific projects. For the provision of such resources does not help finance existing debt and may in fact create demands for more foreign exchange to meet the "local currency expenditures" brought about by the project. In the long run it is hoped that such projects will contribute to the country's ability to service debt, but the short-run effect may not be so beneficial. The provision for a 10-year grace period before repayment begins on IDA loans is an attempt to solve this problem.

The particular types of projects which have generally been approved have followed a general pattern. The reason for selecting certain types of activities in which to invest IDA funds is given in the following paragraph.

> A dearth of basic services was (and still is) the major physical obstacle to increasing production and raising living standards in the less developed countries. Lack of these services put severe limits on productivity, on income, and on the willingness to invest. The lack of dependable and economical transportation restricted the size of markets for both industrial and agricultural production, and kept regions with promising natural resources

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[1]Cairncross, p. 6.

> beyond the reach of development. Deficiencies of electric power supply conspicuously handicapped industrial growth.[1]

For information on the criteria used in evaluating the bulk of IDA projects--transportation, power, and irrigation--we can turn to publications and speeches of the staff. M. Leonard Rist, who was formerly Chief of the Economic Staff of the Bank, discussed these techniques in a speech which he delivered in Liberia on December 13, 1961.[2] He explained that he was going to confine himself to a discussion of the appraisal techniques used by the World Bank. "However," he said, "I believe that most of these techniques are applicable in virtually all development financing; certainly we have found they need very little modification to act as a satisfactory guide for putting the 'soft loan' resources of the International Development Association to work."[3]

In the same month in which the International Development Association was established, the World Bank issued a handbook which contained the procedures followed in evaluating a project.[4] There are three main questions that are asked. First, are the goods or services to be produced by the project needed by the economy for consumption or export? Secondly, is the project properly designed and planned? Third, is the proposed method of financing appropriate?

In order to evaluate the project from an economic point of view

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[1]International Bank for Reconstruction and Development, "A Note on the World Bank," in Black, The Diplomacy of Economic Development, p. 63.

[2]Leonard Rist, "The Economic Use of International Resources in Financing Development Projects" (Washington: IBRD, 1961). (Mimeographed.)

[3]Ibid., p. 1

[4]International Bank for Reconstruction and Development, Some Techniques of Development Lending (Washington: IBRD, September, 1960).

it must be determined if the project is able to earn a reasonable return on the capital which must be invested. If there are similar projects in the economy, then this project should earn not less than the return from comparable enterprises. However, many IDA projects are of a public utility or monopoly character and no comparable enterprises can be found. In cases where no comparisons can be made directly some pricing formulae must be developed to approximate competitive conditions.

In addition to the direct returns, there are many indirect returns from dams, roads, etc. Some of these factors which must be considered are as follows: Would the project put idle men and resources to work? Would the project be a stimulus to other economic activities? What impact would it have on the country's balance of payments--would it produce import substitutes or exportable items? Or might the project cause increased demands for imports of raw materials, replacement parts, etc?

Another important question is whether the project depends upon protection from competition. If it depends upon high protective tariffs for its success, it needs to be looked at very closely. Or if it is to be protected from competition through public utility type regulation, the regulatory agency must be studied in order to evaluate its attitudes and competence.

Project assessment starts with the availability of natural resources and the capacity of the country to exploit its resources. This includes a judgment of governmental efficiency and of private producers' ability. Any project proposed for financing is considered in relation to the country's overall development program. This consideration may reveal that other projects have a higher priority than the one proposed. Priorities are difficult to establish and the guidelines are vague, however, profitability alone cannot be a sufficient test of a project's contribution to economic development.[1]

Profitability would be the simplest criterion to apply. Investment would be made in those projects which yielded the greatest return over cost. This would be easy to explain to businessmen and governments and it would have great appeal to the rich Western nations, where this criterion was used almost exclusively in their developmental stage. It would be universally applicable and, thus, eliminate the problem of justifying investment decisions to the less developed countries.

However, its simplicity and appeal hide the fact that it is, in fact, a totally wrong criterion to apply. For if pure profitability were the basis for investment decisions, many of the very poorest countries would never get a cent of IDA's funds. It is likely that investments in the industrial nations of the world would yield a higher profit than investment in some parts of Africa and Asia. And surely it was not the purpose of the International Development Association to invest in the United States of America.

What, then, can be used as a basis for allocating funds? Dr. Paul N. Rosenstein-Rodan has suggested that aid should be allocated where it will have the maximum catalytic effect in mobilizing additional development efforts. His primary criterion is to maximize additional

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[1]International Bank for Reconstruction and Development, The World Bank, IFC and IDA Policies and Operations (Washington: IBRD, 1962), pp. 31-35.

effort.[1] This criterion seems to be used by IDA.

Two types of foreign exchange expenditures are incurred in the construction of an IDA financed project. One is the direct cost of imported goods and services used on the project. The second is the indirect foreign exchange expenditure resulting from the fact that local expenditure on labor or equipment usually leads to increased demand for imported consumer goods and raw materials. Loans for this second type of expenditure are referred to as loans to meet "local currency expenditure" even though, strictly speaking, they are loans in foreign exchange.[2] IDA does not ordinarily make loans for "local currency expenditures", although this policy has been criticized by several countries and economists.

Policy Toward State-Owned Enterprise

IDA feels that wherever possible, governments should reserve their scarce resources for those projects which private capital would not find attractive. A policy of this sort, it is felt, will be likely to act as an inducement to investment by privately owned companies. Loans for state-owned enterprises may be approved in cases where private capital is not available and if the government's participation is compatible with efficient operation and will not have a deterrent effect upon the expansion of private enterprise. As a matter of historical record,

Governments seeking to develop their own oil deposits have never

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[1]Paul N. Rosenstein-Rodan, "International Aid for Underdeveloped Countries," The Review of Economics and Statistics, XLIII (May 1961), 107.

[2]Fifth Annual Report of the International Bank for Reconstruction and Development (Washington: IBRD, 1950), p. 10.

> obtained a loan from the Bank for this purpose. In most of the countries to which it has lent the Bank has taken a position hostile to public ownership of manufacturing industry, arguing that nationalization is calculated to slow down economic development and is not the most fruitful use of capital borrowed from abroad.[1]

In his speech to the Board of Governors in September, 1961, Under Secretary of State George W. Ball, of the United States, made a statement of support for Bank policy in regard to the relationship of private enterprise and government.

> We know very little about the anatomy of economic and social growth. An abundance of preconception masquerades as principles; an abundance of theory substitutes for experience. Yet the lessons implicit in the history of industrialized societies are largely irrelevant. For we are dealing with disparate cultures, with violent emotional impulses, and with explosive political pressures.
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> . . . .
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> The Bank, for example, has not been bound by any doctrinaire commitment to the principle that the market place must be the sole arbiter of investment. Many less developed countries possess neither the institutional structure nor a sufficient entrepreneurial tradition to make this possible. . . . And this obviously implies a considerable measure of planning at the national level in which the state must necessarily take the lead.
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> . . . .
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> Every modern society--however advanced or primitive--takes for granted a measure of governmental control over the economy. The critical issue of our times is not "government control" but uncontrolled government. Where the people of any nation lack the power to choose their rulers, can criticize them only at personal peril and have no effective means of influencing their behaviour, these people can easily be reduced to slavery, and there is no guarantee that any degree of economic development will actually benefit anyone except the rulers themselves.[2]

Even though the United States of America approved of the policy toward state-owned enterprises, the Governor for Yugoslavia most emphatically did not. Speaking before the Board of Governors at the Vienna

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[1]Cairncross, p. 27.

[2]IDA Board of Governors Press Release No. 13, September 19, 1961, pp. 2-6.

meeting, Nikola Mincev expressed himself as follows:

> In the past years many of us have strongly believed that industrial development is of the utmost importance for the economic development of the underdeveloped countries. . . . However, the contribution of the Bank has in this respect been very modest (less than 8 per cent of the total of loans granted by the Bank was for industry as such).
>
> To my mind, there is a gap in the international financing of industry and it is our wish to see the Bank fill this gap in a more active way. In so doing, the Bank should not discriminate between private and public industry.[1]

IDA has been opposed to loaning funds to state-owned enterprises except in infrastructure type projects. But, the Yugoslavs argue that IDA is speaking in the classical sense of infrastructure--of such projects as highways, ports, and canals--which were state-owned projects in the development of Western Europe and the United States. The Yugoslavs believe that the infrastructure must be much broader in the development of the underdeveloped countries today. They think it should include such things as steel mills, thermal power plants, etc. The state is taking a much more active role in the economic development of the underdeveloped countries than it did in the nineteenth century. The Yugoslavs think it has to. They argue that the underdeveloped countries do not have time to wait for private capital to do the job. The United States and Western Europe had time to wait. But, even in the United States all big power dams have been built by the state. And in Western Europe the railways and communications networks are state-owned.

The Yugoslavs are able to see that the capital of IDA was provided by the countries of Western Europe and North America and that

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[1]IDA Board of Governors Press Release No. 30, September 19, 1961, p. 3.

these countries are not anxious to provide funds for industries in the developing countries that might compete with them. But, there are certain industries that have served as the means of securing foreign exchange and of financing economic development--the textile industry, for instance, has moved from the developed countries to the under-developed countries--throughout history. Of course, it is understandable that the United States and Western Europe would be reluctant to assist this pattern in its course. Although, in principle, it can be seen to be a beneficient thing; the textile factory owners and workers are not enthusiastic about seeing their companies and jobs eliminated. The Yugoslav Government posits that, for this reason, bilateral aid will not be forthcoming to assist any such process. The argument is made that IDA and the International Bank should, therefore, provide such funds.

IDA's opposition to state-owned industry has been based on grounds of efficiency of operation. But, the Yugoslavs maintain that Yugoslav industries are quite competently run. They have secured loans from the Bank as lately as 1963 for other than industrial-type projects. The Bank knows the industries are efficient--but the Yugoslavs believe that the reason they have not received Bank loans for industry is the Bank's fear of setting a precedent that would have to be honored on a much broader scale in the other developing countries.

Projects in the Field of Education

The types of projects approved by IDA have been very similar to those approved by the Bank. This was only natural since the Bank was set up to handle these particular aspects of economic development.

However, IDA was established partly to finance a broader range of activities than the Bank had done. Such an intention is spelled out in the report of the Executive Directors accompanying the Articles of Agreement.

> The Association is authorized to finance any project which is of high developmental priority, that is, which will make an important contribution to the development of the area or areas concerned, whether or not the project is revenue-producing or directly productive. Thus projects such as water supply, sanitation, pilot housing and the like are eligible for financing, although it is expected that a major part of the Association's financing is likely to be for projects of the type financed by the Bank.[1]

In an effort to carry out this mandate, the Association has moved into the field of education. IDA has concluded that secondary education is the field most in need of assistance. There is great pressure on governments to expand primary education as fast as possible until it becomes universal. And at the other end of the scale, most countries regard the establishment of a university as a sign of their independence and a symbol of great prestige value. Consequently, these two areas have received great emphasis and secondary education has been neglected.

> And this has had unfortunate results, since the secondary schools have to perform three essential tasks; first, to provide teachers for the primary schools; second, to prepare cnadidates for higher education who can man top level positions; and thirdly, to produce recruits for middle level posts in administration, industry, commerce and agriculture. . . . It is these considerations that have led the staff to conclude that much of the aid to be provided by IDA should properly go to the secondary level.[2]

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[1] Report of the Executive Directors of the International Bank for Reconstruction and Development on the Articles of Agreement of the International Development Association, p. 7.

[2] Hugh B. Ripman, "Statement on Educational Projects and Problems,"(Washington: International Development Association, 1962), p. 5. (Mimeographed.)

In the field of education there is a lack of research and a lack of planners. This means that some countries which make requests for IDA funds for education do not have good educational plans and do not have the necessary statistical material on which to base such plans.[1]

The following criteria have been adopted for use in appraising educational projects: (a) Any government wishing to borrow must decide for itself that education has a high priority in its general development plan and be willing to devote its own resources to this purpose. (b) IDA would not normally consider an educational project unless it were an integral part of a plan for the whole educational system which was, in turn, related to the overall economic development program. (c) Projects to be financed should have a high priority within the educational development plan. (d) IDA would prefer to finance the most crucial gaps in the system rather than the normal year-to-year growth in the system. (e) IDA would not normally finance any part of the current costs of an educational system. (f) IDA would have a bias toward projects which would have a speedy effect on national productivity. (g) IDA would require some estimate of cost-benefit ratios. (h) IDA would want to be satisfied that the administration of the system was efficient. These criteria are ideals and the staff fully realizes that all projects are not going to meet all these criteria.[2]

In addition to finance, the staff hopes to provide help to countries in planning their educational investments. It also hopes to help them improve their educational statistics. Finally, IDA will help

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[1] Ibid., p. 8.

[2] Ibid., pp. 9-10.

by underlining the importance of sound administration and will help get the best value out of the large amounts of money spent on school construction.[1]

Problems in Project Appraisal

Mr. John C. de Wilde has presented some of the problems involved in evaluating projects. Although economic analysis of projects has improved as a result of experience, there are still serious difficulties confronting the staff. The most important problem is the divergence between market prices and real costs or benefits to the economy. The staff has attempted to use "shadow" or "accounting" prices to overcome the limitations of market prices. The staff takes cognizance of the fact that the opportunity cost of labor may be considerably below the prevailing wage in many underdeveloped countries. Again, the interest rate is often artificially controlled and in these cases it is recognized that the opportunity cost of capital is considerably higher than this rate. IDA is still baffled by the problem of pricing inputs and outputs. In an attempt to devise a yardstick to be used in evaluating projects, the staff has worked toward measuring the cost of capital. It was hoped that some minimum rate of return could be established by which individual projects could be judged.

> Recently we had a paper on the cost of capital prepared. The paper considered various methods of determining this cost. It examined, for example, the interest rate structure of a number of the less developed countries to see whether one could find a rate which might be considered as approximating a "free market" or equilibrium rate and which would be devoid of any compensation for risk and entrepreneurial initiative and for future loss in the value of money. It also dealt with various formulae for the calculation of

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[1] *Ibid.*, p. 10.

shadow rates of interest, particularly that developed by R. M. Solow and applied to India by S. Chakravarty. The first of these approaches might be regarded as the least sophisticated and in effect depended on the correctness of one's "hunch" that one interest rate was better than another. The Solow formula was more sophisticated, but its use in practice was also found open to serious objections. For one thing, it requires national accounts data which are frequently not available such as statistics on the proportion of profit and property income saved, proportion of wage income saved and the proportion of profit and property income to total national income. Secondly, it assumes static relationships in the economy, such as production functions that are linear and homogeneous, not changing over time, constancy of savings coefficients, etc. Thirdly, the national accounts data used in the formula should really themselves be calculated at shadow prices. The last comment typifies, perhaps, the dilemma that we face when we try to replace market prices; in principle, we are then confronted with the need to devise a completely new price structure.[1]

Another important problem in project appraisal is estimating the time path of costs and benefits. It is difficult to determine just how demand for goods is likely to develop. In some cases the rapidity with which capacity becomes utilized and the benefits accrue depends on institutional factors e.g. how fast will farmers adopt new techniques as a result of irrigation? de Wilde says that, in so far as possible, the staff insists that a revenue-producing project produce revenues considerably in excess of expenditures. In cases of government-owned operations, this sometimes causes upward shifts in pricing. But, this is thought to be necessary in order to increase public savings. "With the progressively larger role played by public enterprise, it is important . . . that 'corporate savings' in the public sector should gradually play the same role in financing public investment as this same type of savings in the private sector already does in financing private investment."[2]

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[1] de Wilde, pp. 13-14.

[2] Ibid., pp. 15-16.

Notwithstanding the fact that project appraisal is a complicated and problem-ridden operation, the Association had approved some 29 projects by September 30, 1962 as presented in Table 8 (see Chapter VIII). Eleven of the projects had been in the field of transportation, including 7 highway construction projects, 3 projects for harbor dredging and improvement of ports, and 1 railway development project. Irrigation projects accounted for 8 of the development credits. Four credits were for ground water development and municipal water supply projects. Two credits went to finance projects to increase power supplies. One of India's credits was for flood protection and drainage. The Association made $42 million available to India to be used by the Indian Post and Telegraphs Department for expanding and improving telephone and telegraph services. The China Development Corporation received a $5 million credit from the Association to assist the establishment, modernization and expansion of private industrial enterprises on Formosa. And, in its first such operation, the Association made $5 million available to Tunisia for secondary and technical school construction. Several of these projects involved funds made available by the Association along with a conventional loan for the same project by the Bank.

Criticisms of Project Appraisal Techniques

There has been criticism of IDA policy on project appraisal. The Governor from Viet-Nam made an impassioned plea for more liberal standards at the 1962 meeting of the Board of Governors. He said, "The Association is determinedly adopting the same policies as the Bank . . . aid given to specific projects, high revenue-producing, unquestionable solvency and absolute security. What can be the use of 'concessionary terms' if the necessary conditions to benefit from the assistance of the Association are absent in most underdeveloped countries?"[1] He went on to describe the particular conditions existing in countries with large communist segments. "Creditworthiness . . . depends to a large extent on the prevailing situation of security. But insecurity . . . is a characteristic of underdeveloped countries. Subversion and instability are rather the consequence of underdevelopment."[2]

The Government of Senegal has been critical of the scale of the projects which IDA has financed. The Governor from that country explained that "rural development . . . calls for widespread or scattered efforts such as the stimulation of activities in the rural sector, small-scale water supply schemes, the reforestation of certain regions and the allocation of agricultural equipment and fertilizer to farmers' cooperatives."[3]

Some of the recently independent countries of Africa have expressed their resentment toward some of the more rigid policies followed by the management. Particularly singled out has been the requirement for detailed statistical data (which is not available in many of these countries). There are countries in Africa which do not have a clear idea of total population and they certainly can't provide figures on marginal savings rates and incremental capital output ratios. Some

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[1]IDA Board of Governors Press Release No. 23, September 18, 1962, p. 2.

[2]*Ibid.*

[3]IDA Board of Governors Press Release No. 72, September 20, 1962, p. 4.

of these countries have a problem in raising the matching funds for local expenses. A third criticism is that IDA has required that a project should have a certain minimum value before financing is available.[1] There are signs that the management is aware of these complaints and is trying to work out some solution so that the very small countries and very poor countries might be able to benefit from membership.

The Government of Tanganyika has echoed the criticism made by the Government of Sierra Leone. These two countries are among the poorest in the world and have a combined population of less than 10 million. Neither country had been able to qualify for IDA funds by the end of September, 1962. They speak for many of the countries of Africa when they criticize these particular policies of the Association. The Governor from Tanganyika raised a further point in 1962.

> We were advised by a Bank survey mission to concentrate on those projects which would bring a quick return, which in nearly every case involves a preponderance of local expenditure; yet we find when we seek aid that it is all too frequently tied to external costs only, and the implication is that we should abandon our carefully considered priorities in favor of larger, more grandiose, but less valuable schemes which do not touch our real needs but suit the established rules of the game.[2]

The management of IDA would not agree that this is the implication in this situation. They, no doubt, would say that the situation calls for a great deal of local effort, savings, and investment; after which, outside aid may be called for.

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[1]These three criticisms were made by Governor A. M. Margai of Sierra Leone at the meeting of the International Monetary Fund in September, 1962. See IMF Board of Governors Press Release No. 62, September 19, 1962, p. 2.

[2]IMF Board of Governors Press Release No. 68, September 19, 1962, p. 2.

The Honorable Chief Festus S. Okotie-Eboh, the IDA Governor from Nigeria, joined the critics of IDA policy. He was especially critical of the slowness of the deliberations. He pointed out that the worsening of the terms of trade of the African nations had posed serious problems for those countries. And, he said, "those of us who have to go cap-in-hand, pleading for more aid, do not enjoy this thankless task for we are not professional beggars. . . . If we could earn more foreign exchange from our legitimate trade we could depend far less on foreign aid."[1] However, he was not optimistic as to the possibilities of increased foreign earnings. Therefore, he said, Africa must have more of the kind of loans IDA is making and these loans should be disbursed with less time-consuming delays. The Governor pointed out that economics "is not an exact science. Economists often disagree among themselves and this is a most potent source of delay and frustration to those who want to get on with the job."[2] To overcome this problem, he suggested that more reliance be placed on the opinions of the man on the spot. This might mean that some mistakes would be made, but, "it is better to attempt 100 projects and see 99 succeed than to attempt only 10 even if all 10 were to succeed."[3] The Bank publicizes the fact that it has never yet had a default on a loan.

One of the hypotheses which underlies this study is that the International Development Association has been able to devise universally applicable criteria for evaluating projects. Experts disagree

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[1]IDA Board of Governors Press Release No. 36, September 18, 1962, p. 2.

[2]*Ibid.*, p. 3.

[3]*Ibid.*

on whether such criteria are possible. Millikan and Rostow present four considerations in evaluating projects which they feel can be used universally.

> A. It must be within the technical and administrative capabilities of the receiving country to carry out its proposed project with reasonable efficiency, over the time period of the loan or grant.
>
> B. Steps must have been taken to insure that the rest of the economy of the receiving country is being developed sufficiently to make the proposed project fully productive in the time period envisaged by the loan.
>
> C. The receiving country must have an over-all national development program designed to make the most effective possible use of its resources; this should include not only a series of interrelated capital projects but also necessary educational and training programs.
>
> D. The receiving country's national development program must be consistent with the requirements of expanding world commerce and the international division of labor.[1]

Perhaps most economists would agree with such broadly stated criteria. However, some economists insist that universally applicable criteria for evaluating projects are not likely to emerge in the foreseeable future. Each project, it is argued, has to be treated in large measure as a special case. We will present our conclusions on this matter in Chapter XIII.

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[1]Max F. Millikan and W. W. Rostow, A Proposal: Key to an Effective Foreign Policy (New York: Harper, 1957), pp. 70-71.

CHAPTER X

SOME PROBLEMS AND ACHIEVEMENTS OF THE INTERNATIONAL DEVELOPMENT ASSOCIATION

The Basic Problem

Mr. Black has expressed the opinion that the major problem that IDA has had to face was the meagerness of its resources. He went on to say that

> There is in sight now a volume of promising applications which, if approved, would absorb a substantial part of the convertible funds initially subscribed for IDA's first five years of operations. India and Pakistan together are already in a position where they could quickly absorb in worthwhile projects all of IDA's capital by themselves.
>
> Some members of IDA cannot yet present concrete proposals for credits because they are not yet able to present adequately prepared and justified projects. But others show every indication of coming forward with very substantial requirements, demonstrating that once a country organizes itself for development it can rapidly build up a burden of debt which may limit, at least temporarily, its ability to borrow abroad on conventional terms. In these circumstances, even on a conservative estimate, IDA's funds are likely to fall far short of the need.[1]

Mr. Black repeated this argument at the 1962 meeting of the Board of Governors and indicated that by mid-1963 most or all of IDA's funds would have been committed.[2] It will be remembered that the Association started its life with total contributions approaching

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[1]IDA Board of Governors Press Release No. 4, September 19, 1961, pp. 6-7.

[2]IDA Board of Governors Press Release No. 3, September 18, 1962, p. 8.

$1 billion. On June 30, 1962, the Association had total subscriptions of $917 million, of which $739 million was in convertible currencies. And, the Articles of Agreement called for review of the adequacy of its resources at such time as it was deemed appropriate and at intervals of approximately five years thereafter. Thus, the impression was created that IDA's first billion dollars was to last for approximately five years. But, was this billion dollars to be committed over five years or disbursed over five years? On this question the Articles are silent.

If it was intended that IDA disburse the whole amount in five years, then commitments would have to take place in the first couple of years, because disbursements follow commitments by a considerable period. There is a necessary lag while projects get underway. However, if the initial amount was intended for commitment over five years--then disbursement would be made over a longer period. The provisions ot the Articles for the subscriptions to be paid in 5 annual installments might lead one to think that this was meant to be committed each year. Some member countries have charged IDA with a breach of faith on this point. They argue that the first $1 billion was for the first five years commitment--not disbursement. The 18 Executive Directors are representatives of bodies politic--although IDA is not political. So, some directors have contributed to this confusion which comes from mixing commitments and disbursements. Some of the wealthy European members have argued along this line, anyway. They are happy to befuddle the issue. At the 1962 annual meeting of the Board of Governors, the Governor from France called for a re-examination of the rate at which loans were being granted.[1]

Whatever the intention of the drafters of the Articles of Agreement and despite the wishes of some member countries, the staff has acted on the assumption that the original funds were intended to be disbursed over the first five years operations. They have proceeded to commit IDA funds at a rate which will leave the Association virtually penniless sometime in 1963. There is some indication that the staff has acted so as to commit the funds as fast as possible (taking account of the criteria that have been established), in order to get some idea of how much IDA-type money could be absorbed by the underdeveloped countries in a year's time. During fiscal year 1963, the rate of commitment approached an annual rate of $500 million. This figure was used by Mr. Black in his appeal to the Governors for replenishment of IDA funds. He estimated that IDA would need $500 million a year for the next five years, and therefore, requested replenishment of IDA resources in the amount of $2.5 billion (see Chapter XII). Of course the Association has no assurance that it will receive this amount. So, it has had to make policy based on a budget of only $1 billion.

Most of the problems which IDA has faced in establishing policies stem from this inadequacy of resources--from the fact that IDA operations are essentially a sub-optimum operation. IDA resources are such a small percentage of the total of all aid that the staff is not able to pick the optimum solution to the allocation problem. Sometimes it is quite obvious what the ideal solution would be if funds were

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[1]IDA Board of Governors Press Release No. 32, September 18, 1962, p. 2.

unlimited. But, they are limited and it is foolish to concentrate too much on the ideal solution--the staff must choose those policies that will work in a realistic situation.

If the Association gets additional funds to allocate at the rate of $500 million a year, this would mean that IDA would be disbursing around $300 million a year for the next several years. The Bank is not expected to increase its rate of lending significantly in the near future. Mr. Black said in 1962,

> Indeed, it may prove difficult to maintain the Bank's operations at their recent level. Many of the Bank's present member countries cannot prudently assume further hard debt without jeopardizing their future, and of about 20 new members expected to join the Bank within the next year or two, few will be in a position to service loans from the Bank.[1]

The Bank loaned $882 million in fiscal year 1962 and disbursed $485 million during that same year. However, repayments amounted to $104 million and interest and commission charges amounted to $163 million. For the future, the staff estimates Bank disbursements to run around $600 million a year with repayments and interest amounting to some $300 million. So, the net addition of funds which will be made by the Bank will be $300 million, also. Thus, the Bank and IDA together will disburse something on the order of $600 million (net) a year, if the assumptions which have been made prove valid.

The Organization for Economic Co-operation and Development estimates that "net official contributions extended bilaterally and multilaterally by all D. A. C. members taken as a whole rose to $6.0 billion in 1961."[2] The D. A. C. is the Development Assistance Committee

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[1]IDA Board of Governors Press Release No. 3, September 18, 1962, p. 9.

[2]Organization for Economic Co-operation and Development, Development Assistance Efforts and Policies in 1961, p. 11.

of the Organization for Economic Co-operation and Development and includes all the Western nations which give foreign aid in significant quantities. Thus, total foreign aid in 1961 (including surplus commodities and defense support funds) was around $6 billion and, in view of past experience, it is unlikely that it will increase by more than 2-4 per cent a year in the future. Thus, total assistance extended by the International Bank and the International Development Association is equal to about 10 per cent of all foreign aid extended now and will be something less than 10 per cent in the future. IDA will have, if the optimistic predictions concerning the size of the replenishment prove realistic, approximately 5 per cent of the total foreign aid going to the underdeveloped countries. And assuming that total soft loans were increased to $2 billion per year, IDA would make only 25 per cent of such loans. How, with such a small portion of total resources could IDA make a significant contribution? What policies would tend to result in the maximum impact?

One solution to the problem of limited resources would be to concentrate on certain countries. But, could this policy be made effective? If IDA concentrated its assistance on certain countries, would other aid-givers acquiesce in this decision--or would they assist these same countries, also? In the distribution of foreign aid, everyone reacts to everyone else. If IDA chooses to finance certain projects, then other aid-givers will not finance them. But if IDA hadn't financed them, would one of the other aid-givers have done so? How can IDA be sure that its funds are making the maximum contribution to economic development vis-à-vis the underdeveloped countries and vis-à-vis the other aid-givers?

This situation is similar to an oligopolistic model. The IDA and the member governments of the Development Assistance Committee are the protagonists in a situation which involves a certain degree of uncertainty about each other's reactions. Of course, the same countries contribute IDA's convertible funds and their own funds bilaterally, after consultation in the Development Assistance Committee. The parties do, thus, have some information about the others' reactions. IDA does not have information on bilateral aid decisions in advance, so, the analogy still holds. If IDA takes a certain action, it will cause the other aid-givers to react in some way. And, IDA must try to predict that reaction in order to have its limited resources have as much impact on economic development as possible.

The problems of drawing up a consistent policy for the allocation of aid are enormous. It is not difficult to conceptualize a sound aid policy in general terms. That is, IDA can seek to maximize efforts directed toward economic development or can choose to maximize economic product, etc. If IDA had control over enough outside resources, this would be a fairly simple task and with \$6 billion of aid, it could allow fairly high margins for error and still come out alright. However, when IDA is allocating one-tenth or one-twentieth that amount, the margin for error cannot be large. And here's the real rub. The technical judgments of the impact of any policy are so extraordinarily crude that they cannot be relied on completely in specific policy cases. It is not known what impact a steel mill or an educational system will have on an economy. Which would add more to economic output? Which should come first? Since there is so little confidence in technical measurements of the impact of any policy chosen, some other checks on policy must be devised. One attempt to devise a consistent policy for IDA was the decision to establish a performance criterion.

Goals for the Performance Criterion

Some of the different goals which might be established for the performance criterion are as follows:

1. The International Development Association should not reward unsound economic policies of the underdeveloped countries. Lack of creditworthiness should not be due to improper management of the economy--from unwise debt, from inflationary policies, etc. This goal was cited in Chapter VIII.

2. Another goal also mentioned earlier was the possibility of using IDA credits as an incentive to the underdeveloped countries in order to promote good performance in the future. Some countries have had really poor administration of their economies in the past. Perhaps an IDA credit could be held out as a lure--to get these countries to improve. This would emphasize future promise rather than past performance. Just how much should future plans be considered? Some countries with poor past performance have well constructed and reasonable plans now in effect. Should IDA help them bring their plans to fruition? This raises an interesting dilemna for IDA. How can one justify ignoring past failures in develoopment? But, if IDA doesn't help with these new plans, this may doom them to failure. Thus, IDA's prediction that the plan was going to fail would become a self-fulfilling prophecy. There are countries that the Bank could not have financed on conventional terms. But, IDA has made it possible for the Bank to have an entré into these countries and thus the Bank staff can work with them

and help them improve the performance of their economies.

3. One purpose that might be served by the establishment of a performance criterion would be to impress upon the Part I countries that IDA was making good use of the funds entrusted to the Association. Fundamentally, IDA is administering part of the foreign aid effort of the rich Western nations. A performance criterion might be useful in convincing these countries that this administration is sound and should be continued.

4. One school of thought would use IDA credits to obtain maximum results, in terms of economic development, from the limited resources available. Performance tests would be used to insure that such maximization took place. This raises the technical problem of measuring the impact of external assistance of various types, and raises another problem, also. Should IDA be interested in getting the most development for its money or should IDA be interested in channeling its funds to those countries which are trying really hard? Some countries are making Herculean efforts with little result. Other countries are having a relatively easy time of it, for environmental and historical reasons, and achieving quite handsome rates of growth--some of the oil-producing countries of the Middle East and South America immediately come to mind. Some people would argue that IDA should place a premium on improvement relative to a country's present position. This would take little account of a country's lack of resources, etc. IDA has chosen, judging from the countries where it has extended credits, to reward effort rather than rates of growth.

As mentioned in Chapter VIII, there is no simple method of measuring good performance. Just how good should domestic effort have to be in order for a country to qualify for IDA credits? Certainly growth and growth-creating policies should be favored, but, what facets of the economy should be considered in assessing these policies? How many non-economic factors should be taken into account in measuring performance?

The establishment of IDA has presented the staff of the Bank with a whole host of problems. How can the staff rationalize its decisions to make IDA loans as opposed to Bank loans? There are difficulties in explaining these decisions to the developing countries and to the donor countries. And, in addition to the two types of money available now, there are proposals for adding a third class of loans, between IDA credits and conventional Bank loans. These proposals will be discussed in Chapter XII.

Relationship of Staff to Executive Directors

There is an entirely different interest in IDA loans, on the part of the Executive Directors, than is shown toward regular Bank loans. IDA money is public money and has been raised through taxes. The money which the International Bank loans is money that has been raised through the relatively painless method of floating loans in the capital markets of the world. Bank money, has, thus, been saved voluntarily and is being loaned to the Bank with the object of earning interest. The Executive Directors representing the richer nations take a purely perfunctory interest in most Bank loans recommended by the staff. Most observers were aware of the fact that Mr. Black and his staff ran the Bank with only nominal direction from the Directors. And the underdeveloped countries' Directors didn't show extreme interest in loans, because there was plenty of Bank money available for any project that could meet the Bank's standards. The Bank could raise whatever money could be loaned for such projects, so the developing countries were not vying with each other for a limited resource.

This has been altered in the case of IDA credits. The donor governments are interested in what's being done with their citizens' tax dollars. The staff's responsibilities to the rich nations are much different in the case of IDA money than with Bank money. The Part I countries' Executive Directors study IDA credits much more thoroughly than Bank loans. And the developing countries have an interest in where IDA money is going. There isn't enough IDA money to go around to all the projects that meet IDA standards. This means that some projects are going to be left out. Every member country is anxious to get its share. This problem will be discussed in considerably more detail, in the case of certain developing countries, in Chapter XI.

What this all boils down to is the allocation problem faced by the International Development Association. This is a problem which the Bank had not had to face. The Bank could raise all the money it could prudently use. The staff had no experience in allocating scarce resources between competing and equally attractive projects. This has been a difficult experience for the staff--one which has thoroughly tested the ability of a banking institution to dispense funds where an orthodox financial return was not the primary consideration.

The Caliber of the Staff

But the International Bank is no ordinary bank. Andrew

Shonfield, who is certainly no blind enthusiast where the World Bank is concerned, has defined the essence of the Bank's character quite well.

> There is a body of influential opinion which believes that the Bank ought to be given the leading role in any enlarged program of economic aid to the underdeveloped countries.
>
> That there should be this feeling is a justified tribute to the shrewdness and energy with which the Bank has conducted its business. . . . The Bank has been able to evoke in many of the underdeveloped countries themselves a feeling that it has genuine sympathy and understanding for their problems. This feeling is more wisespread, it is fair to say, in Asia tnan it is in Latin America. But that the view should exist at all among people who have had requests for loans turned down, as well as accepted, by the Bank is a sufficiently notable circumstance.
>
> This is not just the result of good public relations, though the Bank's characteristically American attention to that side of the business has certainly been a help. More important is the high caliber of the Bank's staff and the general mood in which it conducts its affairs.[1]

Shonfield goes on to admit of the distinct impression that many staff members are not only people of very high ability but they are also the very slightest big odd. The author got the same impression upon coming into contact with the staff for the first time. One person suggested that at an earlier date it had been thought the staff was "faceless", and so could do with a few eccentrics. At any rate, a few eccentrics are there now. The staff is markedly unhurried and easy to interview. It has been suggested that "the 'unhurried' look may be due to a considerable British influence. To an Oxonian, it is not quite proper to show signs of doing any work."[2]

Staff members are not at all the type of people one would expect to find in a bank--even in an international bank. And they have such enthusiasm for economic development! It seems that they have not read

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[1]Shonfield, pp. 116-117.

[2]Personal letter from a member of the staff, IBRD, June 24, 1963.

any of the theories of economic development which demonstrate that such development is practically impossible in the underdeveloped countries of Africa and Asia. If they have read them, they have been left untouched by this message. Almost all development economists agree that economic development is an enormously complicated business where everything depends upon everything else. The underdeveloped countries have been described as having low-level equilibrium traps and vicious circles of poverty, as needing a big push or a minimum effort, as requiring balanced or unbalanced growth depending upon which economist was read. And yet, the staff keeps going about the business of providing money to the underdeveloped countries to build bridges, and highways, and irrigation projects, and schools. They move in a seemingly unsophisticated and simple-minded way to do these things based on a belief that it is good that bridges and highways and schools should be built. And they go at their tasks with such an optimistic attitude that one has the distinct impression that no one on the staff believes in low-level equilibrium traps or vicious circles of poverty.

The International Development Association's Contributions

What has such a group of people been able to accomplish with the billion dollars entrusted to them? A recent report of the Organization for European Economic Co-operation (now the Organization for Economic Co-operation and Development) lists some 165 countries and territories that are considered to be underdeveloped.[1] If the line is drawn at the conventional $500 per capita income (so that countries where per

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[1] The Flow of Financial Resources to Countries in Course of Economic Development 1956-1959 (Paris, 1961).

capita income is below $500 are considered underdeveloped), the staff of IDA includes some 180 countries and territories in the underdeveloped category. Of these, IDA had only advanced money to 14 countries by September 30, 1962 or less than 10 per cent of the underdeveloped countries no matter which total is considered.

Despite the obvious smallness of its contribution, Mr. Black has insisted that "IDA is a major source of development aid, and the principal international instrument for the provision of aid on lenient terms of repayment;"[1] and that "experience had already demonstrated . . . that IDA is capable of meeting a very real and important need."[2]

Perhaps one of IDA's contributions has been that of technique. IDA was the first international soft lending agency. The techniques it has used have been copied by others, as described in a report of the Organization for Economic Co-operation and Development.

> The interesting arrangement first used by the International Development Association which permits private borrowers to repay their governments in local currency at terms appropriate to the project, while permitting the government to repay the lender in dollars at terms appropriate to its external debt servicing capacity, was adopted by the United States in 1961.[3]

The United States foreign aid agency had been making soft loans, most of which provided for repayment in local currency. After IDA developed its pattern, however, the United States program was changed to come close to IDA's arrangements. The patent of IDA lending was also taken over by the Social Progress Trust Fund, administered by the Inter-American Development Bank.

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[1] IDA Board of Governors Press Release No. 3, September 18, 1962, p. 8.

[2] Ibid., p. 9.

[3] Development Assistance . . . in 1961, p. 14.

The Vice President of the Bank, Mr. J. Burke Knapp, when asked if IDA had been a significant force in the development of the underdeveloped countries, replied in the affirmative. His reason for so doing was based on a point discussed earlier, that is, that IDA had made it possible for the Bank staff to bring its technical assistance capabilities into countries where the Bank had not been. He saw this as its major impact.[1]

Of the 14 countries to which IDA made credits available, through September 30, 1962, seven received no assistance from the Bank during the period from January, 1960 to September 30, 1962. In these countries, anyway, there would have been no multilateral funds available if IDA had not been established. The seven countries that received nothing but IDA credits from international sources during this period were Honduras, China, Paraguay, Jordan, Swaziland, Korea, and Tunisia. So, at least in some countries, IDA made the difference between having some multilateral funds available as opposed to having none.

In addition to the countries that received IDA credits in the first two years operations, there were 16 other member countries of the Bank which had previously received Bank loans but haven't received any such loans, for one reason or another, since 1960. They might be considered to be potential recipients of IDA funds. These countries are Mauritania, Iran, Congo (Leopoldville), Rhodesia and Nyasaland, Brazil, Algeria, United Arab Republic, Ecuador, Malaya, Gabon, Lebanon, East Africa, Guatamala, Iraq, French West Africa, and Ruanda-Urundi. Some of these countries would look to IDA as their only hope for outside

[1]Interview, January 22, 1963.

economic assistance without political strings attached and, therefore, as a potentially significant force. The views of some of these nations will be considered in the following chapter.

CHAPTER XI

SOME VIEWS CONCERNING THE EFFECTIVENESS OF THE INTERNATIONAL DEVELOPMENT ASSOCIATION

Three Groups of Underdeveloped Countries

In an effort to assess IDA's significance, representatives of several governments were contacted. In most cases these representatives were the financial (or economic or commercial) ministers of these countries' embassies in Washington, D. C. Representatives were interviewed from countries in Africa, Asia, South America, North America and Europe. An attempt was made to get some representation from each of the major blocs of nations in the world. Some criticisms of IDA have already been presented in earlier chapters. However, the spokesmen for the underdeveloped countries had a good many novel ideas concerning the Association which will be presented.

Upper-Income Underdeveloped Countries

Three representatives of what might be called upper-income underdeveloped countries were interviewed. These three countries are located on three different continents and the views of their representatives are in rather sharp conflict. One of these countries has not even joined the International Development Association. When asked why, the Minister Counselor for Economic Affairs replied that they hadn't joined because they thought it wouldn't be much help to them. They were aware of the intent of IDA to help the poorer of the underdeveloped countries, so they could not see it was to their advantage to put up their prescribed quota (10 per cent of which would have had to be in gold or convertible currency). The fact that they have not joined IDA has not prejudiced their relations with the Bank in any way and they are in the process of negotiating a sizable loan from the Bank. They do not see that they have any obligation to help those underdeveloped countries that are poorer than themselves by contributing their resources to IDA.[1]

The second country in this class had joined IDA but felt wronged that IDA policy had been framed in such a way as to exclude them from eligibility for credits. The Economic Counselor pointed out that his country had numerous quite essential projects involving educating and assimilating a disparate people. These projects cannot be financed through the use of conventional loans. This country is considered to be creditworthy by the Bank and was extended a loan in 1962. It is not, therefore, eligible for an IDA credit for these non-revenue-producing projects. The Economic Counselor also pointed to the very meagre resource base in his country and the quite phenomenal rate of growth that has been accomplished in spite of this shortage of resources. Why, he argued, shouldn't IDA help them get over this crucial decade after which they would surely be economically self-sufficient? The fact that they have been so successful in managing the economy, the fact that they have a relatively high per capita income, the fact that their exports are growing at a rapid rate--all these visible signs of success have been used as the basis for denying them IDA credits. In the eyes of IDA,

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[1]Interview, May 29, 1963.

their worst failure has been the extent of their success.[1]

The third of these upper-income underdeveloped countries has also had a phenomenally successful development program over the past decade. Their per capita income is close to $400 a year, their exports have been rising at more than 10 per cent a year, and they have been given sizable loans from the World Bank to spur their development. They have, thus, not been eligible for IDA credits--but they have joined the Association with enthusiasm, anyway. The Economic Counselor pointed out that his country had felt that they wouldn't be eligible for IDA money when they joined the Association. But, he said "we recognize the obvious need for increased funds for the underdeveloped countries even if we are not eligible for them. All available statistics indicate the desperate plight of many of these countries. Anyone familiar with the problem can see the pressing need for speeding up their development and lessening the gap between the poor and the rich nations."[2]

This support for IDA does not mean that they would have preferred IDA to SUNFED, however. "We would have liked the principle of SUNFED better--there would have been more money available--from countries not included in IDA, i.e., the Soviet bloc countries. This preference for SUNFED is in principle only, however. Realisitically, we see little likelihood of increased funds for United Nations activities in this field and the Soviet bloc has not contributed much to United Nations agencies anyway."[3]

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[1]Interview, May 28, 1963.

[2]Interview, May 28, 1963.

[3]*Ibid.*

Poor and Dissatisfied Countries

A second group of three countries expressed varying degrees of displeasure with IDA. These are all very poor countries that would be instantly eligible for IDA credits on a per capita income basis. None of the three has, however, received IDA funds. The Commercial Minister of the first of these countries was not particularly bitter about the fact that his country had not gotten any money from IDA. He said they would like to receive IDA money. It seemed to him that most IDA money was going to India. His country had friendly relations with the Bank and was hoping for a consortium arrangement similar to the ones established for India and Pakistan. He pointed out the really desperate situation in his country as a result of some bad crop years. He could not understand why IDA hadn't seen fit to make money available to them. They have not had a Bank loan since 1959.[1]

The spokesman for the second country in this group, a country in Sub-Saharan Africa, echoed the comments about IDA money going to India. In fact, he said that "We have the distinct impression that IDA was not set up with the African countries in mind. It was not established to help Africa--but to help India. India is in a peculiar position, caught between the West and the Communists, and it is very large. It would surely be a very great blow to the West if India went to the Communists. That is why the West is so anxious to help India and extend them loans. And yet India is far over-extended as far as conventional debt is concerned. India can't service more hard loans. That is why IDA was

[1]Interview, May 28, 1963.

established--to provide soft loans for India."[1]

This man was not at all optimistic about the replenishment of IDA. "We think it unlikely that IDA will be able to get enough money. Why should the United States give anonymous loans through IDA when she can give bilateral loans and attach strings? And all bilateral loans have strings--despite all this talk about the need for aid without strings. The United States may not require that other countries come here and worship her--but there are political strings. That is why we very much prefer international aid. There are no political strings on IDA money. There are stiff requirements--economic strings--because the aid must be planned and used efficiently. There are delays in negotiations. For these reasons, the Finance Ministers complain that IDA is too tough and too slow. IDA is tough on requirements. But, with the possible exception of the policy that loans will not be made for nationalized industries--IDA has no political strings."[2]

Because Africans feel that IDA will not be replenished very substantially and because they also feel that IDA was not established with Africa in mind, they are trying to establish an African Development Bank. As of now, no money has been raised. "But we have to get organized first before we can start raising money. This is a long-term process. We do not expect to industrialize the whole of Africa overnight. We are not discouraged by not having the African Development Bank financed as yet. It will be financed. We have had encouraging conversations with many

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[1] Interview, May 29, 1963.

[2] Ibid.

of the developed countries. This Bank is much more appealing to us than IDA.

"We have had somewhat encouraging conversations about the African Development Bank with the United States. But, it looks as though the United States may well get out of Africa. This is an understandable attitude--after all the European countries are very rich now--and they were our colonial masters in Africa. They should surely bear much more of the cost of developing Africa than the United States. This is exactly what the Clay Report proposed."[1]

This man echoed an opinion heard in other interviews when he said that "IDA is doing what the International Bank should be doing. This is what the Bank was set up to do--to help countries in the process of economic development. The Bank is very rich now. It could be making soft loans itself. It should be doing so. There have been proposals for lengthening the terms or lowering the interest rate, but the Bank staff is opposed. The staff argues that this would upset the financial community. How much security does the financial community need? The Bank has over $500 million in reserves now and has never had a default on a loan. What more could the bankers ask for?"[2]

For all the reasons given above, the Bank was judged to be completely useless to the developing nations of Africa. "We can't afford to service conventional loans. Our export prospects are not promising. The Bank has nothing to offer us as we have all the hard debt we can honestly expect to repay. IDA is not going to be expanded to anything

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[1] Ibid.

[2] Ibid.

like significant size. It may get a little money--but our information would lead us to think that it will be far less than the $2.5 billion which Black proposed."[1] The country from which this man came received a Bank loan in 1962.

The third country in this poor and dissatisfied group is _sui generis_. The antipathy with which the Economic Attaché viewed IDA knew no bounds. He started his comments by saying that they were quite unimpressed with IDA. This turned out to be a considerable understatement. "We were optimistic at first. We looked forward to assistance from IDA. We joined early. But, it is applying the same standards as those used by the International Bank. A country must be considered to be absolutely secure and stable before it can get IDA money. This is of no help to us. Our future is uncertain."[2]

"There is no international organization to help countries like ours. We have little use for multilateral aid. Bilateral aid seems better to us in our situation."[3]

Then began a by-now familiar argument. "India is getting all the aid from IDA. It seems that every second week I see a press release announcing an IDA credit for India--a dam, a harbor, or an irrigation project. And why is India getting all of IDA's money? There are two reasons. First, there are so many Indians on the staff of the International Bank. When my countrymen apply for jobs there we are told they

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[1] _Ibid._

[2] Interview, May 29, 1963.

[3] _Ibid._

are not qualified. And who decides that they are not qualified? Indians on the present staff."[1]

Secondly, there is the argument that India must be helped so that it can become the showcase or the model for all Asia to follow. "India cannot be such a showcase. Ask anyone in Southeast Asia. They all agree. The United States and the United Kingdome think that the India-China struggle is crucial for the West; and that the West must make India prosperous as an example of the Western system at work. No one in Southeast Asia wants to follow India's example. I will tell you frankly, we admired the Japanese very much. We resented their occupation at the time--but we admired them. We liked the way they went about things--the efficiency with which they had developed their country. This is not true in the case of India. India could not develop in 30 years no matter how much aid was funnelled in. India exists in abysmal poverty today. There is too much to be done there. It won't succeed in becoming economically self-sufficient in the next decade or in the next 5 decades.

"The India-China comparison is meaningless. China can't be stopped. You saw what happened when they started to invade India. India immediately had to call on the United States and the United Kingdom for help. China could conquer India at any time if India had to fight alone. India had a big army--for use against Pakistan. But the army was no good. It can't stand up against the Chinese army.

"India can't serve as a showcase for Asia. We don't need any showcase. We should all develop equally. India is no more crucial to

[1] Ibid.

the West than any other Southeast Asian nation. India could not stand for a minute if all the other countries of Southeast Asia fell to the communists. All the countries are crucial--none more than others. They are all together. They should be treated alike."[1]

It has been thought necessary to repeat this conversation almost in full in order to capture the essence of this disapproval of IDA's policy toward India. This was the most extreme example of this attitude--but the same criticism was expressed in every interview with a representative of an underdeveloped country.

Personnel recruiting policies have also come in for criticism. A complaint is heard from many of the underdeveloped countries that the higher staff levels of the organization contain no representatives from the underdeveloped countries. Interestingly enough, in view of the comments of the Asian just quoted, the Governor of IDA from India expressed this complaint at the 1961 meeting of the Board of Governors.[2]

This is a difficult problem. If the poorer countries send their top planners and economists away to work in an international organization, they are going to have fewer people left at home to run the country. And, although India may not be short of this type of person, most of the developing nations are. Thus, it would make no sense for them to further deplete their already thin ranks. However, one can see the other side, also. They feel that a Nigerian or an Egyptian would be much more sympathetic with their problems than a West German or an

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[1]Ibid.

[2]IDA Board of Governors Press Release No. 16, September 19, 1961, p. 3.

American. They feel that a person who is concerned about what type of motor car to buy next year might show little understanding of people who are concerned about where the next meal is coming from.

One Enthusiastic Recipient of Funds

It was an unfortunate development, but only one country that has received IDA funds was included in the sample of countries that was contacted. Other interviews had been planned, but only one was possible. There is an enormous difference in attitude between those countries who had not received IDA funds and this one country that has. The Economic Counselor of this last embassy was ecstatic in describing the International Development Association.

"My country is very enthusiastic about IDA. Here we have a very capitalistic institution (the International Bank) coming around to a socialist approach--providing money to countries at very low or zero rates of interest for such projects as education. This is not a capitalist undertaking--to provide money at no interest for things like education. This is a socialist endeavor--and we welcome it. It is very interesting and encouraging to see the complete evolution in the thinking of a man like Eugene Black--from a conventional banker's attitude in the classical economic tradition--to a point of view which enthusiastically embraces the International Development Association.

"And this type of thing--the IDA--has posed a very bothersome problem for the communist countries. They have always refused to join the International Bank and the International Monetary Fund because they considered them to be capitalist institutions and, as such, they were out to exploit the underdeveloped countries. But, now IDA is providing money to the underdeveloped countries on better terms than the Russians are doing--for projects like education--and with no political strings attached. How do the Russians explain this? This poses a real problem for the communists and they are showing signs of being worried about it. They are denouncing IDA--but on what basis can they attack it? They can write off the International Bank and bilateral loans from the West as exploitative devices--but how can they explain IDA credits?"[1]

Then the ever-recurring theme of IDA funds for India was broached, however, this time the comments had a little different ring. "One criticism has been made concerning the high percentage of funds going to India. This is due, I think, to the fact that India had the projects ready to present to IDA more than to the political factors involved. Obviously, the political factors had some importance--India is caught between the East and the West and is very large and is in a very critical situation. But, the primary thing was the fact that India had well prepared projects ready to go--India is a very well-run country. These things were basic to the decision to help India.

"The developing countries in Africa are beginning to get projects ready for IDA and will begin to get more money very shortly. There is a great deal of enthusiasm for IDA among the African nations--they support the idea of replenishing IDA very earnestly. If the United Nations had established SUNFED--it would have had the communist bloc countries in it. There is no realistic hope of establishing SUNFED. IDA is the only alternative as far as international aid agencies are concerned. If IDA is not replenished--there will be no genuinely

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[1]Interview, May 28, 1963.

international organization providing soft loans to the developing countries. And that would be very sad, indeed.

"The recognized competence of the IDA staff and the lack of political strings on IDA credits make them very appealing to all the developing countries. Funds coming from the Bank or IDA will be spent wisely on sound projects. They will not be wasted. Everyone knows that. They will not be used for prestige projects and will not be influenced by political considerations. This is one reason why we very much prefer IDA money to bilateral money. IDA money goes for solid economic development and thus our government officials are protected from charges of waste or inefficiency and IDA policies also protect our government from internal political pressures to build junk projects."[1]

When it was pointed out that some underdeveloped countries considered IDA funds to have political strings, in that funds could not be used for nationalized industries, this man brushed it aside. His own country, he said, had chosen to rely on the free market to develop the economy, immediately after independence. They hoped private capital would develop the country in the classical liberal tradition. But, this simply did not work. The people did not have the capital to establish new industries. They didn't have the skills requisite to operate them and they didn't have the necessary entrepreneurial talent. The state, however, could provide these things. The state can raise capital. The state can train workers and managers and can act as the entrepreneur. So, they have undertaken an ambitious development program under state direction--although leaving a considerable segment of the economy to the

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[1] Ibid.

private sector. Yet this decision has not prejudiced IDA against this country. An IDA credit was made available after large-scale planning was initiated. So, this man, at least, would argue that IDA credits are completely free of political strings.

How can this enthusiasm be explained in view of the dissatisfaction expressed by the other underdeveloped countries? First of all we must give considerable weight to the fact that this last country had received an IDA credit. They had materially benefited from the establishment of the Association. Also, this country was more familiar with the policies and criteria used by the staff and was thus able to see some rationality in IDA decisions rather than attributing all decisions to political considerations or the make-up of the staff. Thirdly, this country is relatively well-run and efficiently administered. Some of the representatives who were most critical of IDA neglect of their countries blamed IDA for this, whereas poor administration of their own countries would be the more likely explanation. One country, in particular, is notoriously ill-run and yet the Economic Counselor could not see that this might be the reason IDA had not made credits available to them.

Would it be possible to generalize from the one case of a country that had received IDA money? Would all of the 14 countries so blessed be equally enthusiastic about IDA? If so, this would be a large part of the population of the underdeveloped world, even though not many countries are involved. There are, no doubt, some variations in their views--but it would be safe to say that these countries would share at least some of this enthusiasm for IDA. And even some of this country's enthusiasm would be a considerable amount of enthusiasm.

Some Observations on the Distribution of Funds

India has received $212 million of the $348 million that had been dispensed by IDA through September 30, 1962. This represented about 61 per cent of all IDA funds committed during the first two years. The charge that IDA had been set up to help India had some element of truth in it. Before IDA was really in operation--there was a commitment of $250 million of IDA funds to the India and Pakistan consortia.[1]

Why has India gotten such a large percentage of IDA funds? IDA argues that India has more than 30 per cent of the people in the underdeveloped world (outside the Soviet bloc). India has considerably less than 30 per cent of the gross national product of the underdeveloped world. It is also argued that India has more than 30 per cent of the ability to use capital. Some Part II countries are ineligible for loans because of high per capita incomes. Some Part II countries are financed relatively lavishly by others (particularly some Southeast Asian countries and some of the dependent territories). Some Part II countries in South America have always looked to the United States and its Export-Import Bank rather than to the International Bank for funds. These South American countries now look more to the Inter-American Development Bank than they do to IDA. Some Part II countries are ineligible for loans on the basis of poor performance.

However, India meets all criteria very well. India has a small external earnings sector and acute balance of payments problems. India will need large capital inflows for a long period of time. So, the

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[1]Annual Report of the International Development Association 1961-62, p. 7.

Indian balance of payments will get worse as debt service becomes a greater percentage of export earnings. India also meets the criterion of good performance. She has good plans and good execution of plans. Of course, no plan is perfect and mistakes have been made but a very solid effort to develop is being made. And, they are very poor. The staff estimates India's per capita income at $70 per year on an exchange rate basis. India really represents a classic case for IDA loans. In fact, this has caused some people to wonder if the criteria were established with India in mind.

And, one might also suggest that the International Bank is sponsoring a consortium for India--with the idea that all external sources of capital taken together should meet India's capital requirements. Why should scarce IDA resources be put there if the consortium has agreed to meet the capital requirements? Basically, the same countries supplied the IDA money and the consortium money, so it is really two routes to the same goal. But, doesn't the presence of the consortium have some effect on India's creditworthiness? Some persons would maintain that it is only the presence of the consortium that has allowed India to be considered creditworthy for Bank loans. IDA argues that the members of the Indian consortium are reluctant to make any continuing commitment for India and so the consortium is not so significant as it might appear. IDA also argues that India gets a low per capital inflow of capital from all sources even though the absolute sums are large.

IDA policy toward India is certainly the most criticized aspect of its operations--at least as concerns the other Part II countries. It remains to be seen whether IDA will modify its policy toward India as a result of the widespread condemnation of that policy.

Attitudes of Some Developed Countries

How do the developed countries of the world see the International Development Association? In an attempt to determine their attitudes, interviews were held with representatives of some of these countries.

Belgium was designated a Part I member of IDA and scheduled to contribute $22.7 million in gold or convertible currency. As of today Belgium has not contributed a cent to the Association. Why the reluctance to join? Belgium had been the recipient of loans from the International Bank in an earlier period when reconstruction loans were being made. In fact, the Bank had loaned Belgium a total of $76 million during the period 1949-1957. Why, then, has Belgium been unwilling to share the costs of helping others, now that the Belgian economy is once again prosperous? In order to find the answer to this question, an interview was held with a Belgian representative.

The first reason given was that IDA was established at a time of heavy Belgian expense in the Congo and, in the Belgians' eyes, this expense is still heavy. They are paying the external debt of the Congo that was contracted with Belgian guarantees during the colonial period. They are also paying salary differentials of Belgian nationals serving in the Congo--doctors, engineers, etc.[1]

Secondly, Belgium did not agree with the share assigned to them. The quota used for IDA subscriptions was the quota devised at Bretton Woods for contributions to the International Monetary Fund and the International Bank. This quota took account of such things as exports, imports, currency reserves, etc. These matters are important in

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[1]Interview, May 27, 1963.

apportioning quotas for the International Monetary Fund because the purpose of the Fund is to provide funds in times of temporary crises in a country's balance of payments. However, by the time you come to the International Bank such considerations are already less significant. But, Belgium went along with such quotas in the Bank. It was a once for all thing and only 20 per cent of the $450 million Belgian quota had to be paid in gold or convertible currency. The rest was warranty for possible loans. Anyway that was ancient history. But, by the time IDA came along--this Bretton Woods quota is even less meaningful.[1]

The Belgians argue that a country with a large amount of exports may have little ability to ship capital abroad. Belgium depends on exports for much of its gross national product. But, that does not mean that Belgium is a large capital exporter. The Belgian economy is only one-fifth the size of the French economy, but their Bank quota is more than one-third the French quota. The same would have been true in IDA. Belgium did not want to get a tradition established for using this quota for all questions. They were reluctant to have this quota used for IDA because IDA will require constant replenishment by the Part I countries.[2]

Thirdly, there was some degree of irritation, at the time of the IDA proposal, over the Belgian Congo. "The United Nations was personna non grata in Belgium at the time. This followed the United Nations intervention in the Congo. Thus, it would not have been politically wise to go to the Parliament and ask for an appropriation for a United

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[1] Ibid.

[2] Ibid.

Nations specialized agency. The finance minister must go often enough to the Parliament asking for funds for foreign aid--for the Congo and elsewhere. It would not have helped his case to have asked for funds for IDA membership. However, this was essentially a question of tactics. If we could have reached agreement on a quota for Belgium--we could have waited a while and submitted it to the Parliament later."[1] Most observers agree that the question of the quota was the primary stumbling block in the case of Belgium. And most observers would concede that Belgium's quota is too high. One gets the impression that Belgium is not inflexible on this matter and if some compromise solution could be worked out, Belgium might come into the Association on the second round of contributions. There has been no intimation of criticism of the Association or any lack of conviction that the Association was necessary.

One gets the impression that the United States Government is ambivalent toward the Association. On the one hand, the President of the United States made an unequivocal statement of support for increasing IDA's resources at the 1962 meeting of the Board of Governors. "The work of the International Development Association is particularly important--and this country fully supports the proposal that the Executive Directors develop a program to increase its resources."[2] On the other hand, there is considerable opposition to any increase in foreign aid among influential members of the Congress. Perhaps Senator Monroney

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[1]*Ibid.*

[2]IDA Board of Governors Press Release No. 75, September 20, 1962, p. 1.

described the United States' attitude best when he said, "IDA has been practically unnoticed here."[1]

At least one Part I country is very enthusiastic about IDA. On May 28, 1962, it was announced that the Swedish Parliament had approved a special supplementary contribution of $5.8 million to the resources of the Association. The funds were made available in freely convertible Swedish kronor, not tied to Swedish exports nor restricted to use in any specific country. Sweden's action has been the only such supplementary contribution made to IDA and added to Sweden's original $10.1 million subscription, raises the Swedish contribution to nearly $16 million. Why did the Swedes do this? In an effort to understand this amazing step, an interview was held with a representative of the Swedish Government.

He indicated that there were several reasons for Sweden's supplementary contribution. First, there was and still is considerable internal pressure to get Sweden into the foreign aid business and to increase Swedish contributions for technical assistance. The labor unions have been especially pushing the government in this direction, although the pressure has come from the opposition, also. The Social Democratic Party governs Sweden but both parties favor foreign aid.[2]

Originally, Sweden would have very much preferred SUNFED or an expanded United Nations program to IDA. Sweden was ready to contribute to SUNFED. They had already increased their large (for Sweden) contribution to the United Nations activities in the economic development

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[1]Interview, January 25, 1963.

[2]Interview, May 29, 1963.

field. They would have liked to channel further economic aid through the United Nations because of the strong support for the United Nations in Sweden.[1]

Now, however, Sweden feels differently about IDA. Why? IDA has proven itself capable of administering its funds. It has already assembled a staff which is experienced, capable, and efficient. This is the main point in IDA's favor. Sweden now feels that IDA is the best approach to economic aid to the underdeveloped countries. The Swedes have the impression that IDA has been accepted by the underdeveloped countries, too.[2]

A second reason for Sweden's supplementary contribution to IDA was based on uncertainty as to how best to approach foreign economic assistance. "We were really just looking around to try and see how we should go about increasing our foreign aid. No one seems to really know much about how it is best to do this--I mean whether its best to give them a steel mill right away or educate them or just what. No one really seems to know the answer to this--the people who work in this field all have different opinions. We were considering all sorts of approaches. There are considerable drawbacks to bilateral programs. It is difficult for the underdeveloped countries to accept the money from another government--they are sensitive about it and it does raise problems. We do have some bilaterial programs--primarily school construction--in India, Pakistan, and Ethiopia. We have built schools and we also brought some of their people to Sweden.

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[1] Ibid.

[2] Ibid.

"But a bilateral program costs a lot of money. It is expensive to set up and administer and it's hard to find the right people to get it going. It also represents considerable duplication of staff and administrative costs for every country to have its own foreign aid program. So, IDA seemed the better alternative."[1]

The third reason for choosing IDA was that Sweden liked the idea of a multilateral program based on untied loans and a program where purchases would be based on international competition. Sweden must export to live. The Swedish economy is based on exports and imports. They must compete in the international economy and they want the right to compete for all aid funds. They would like for all foreign aid to be on an untied basis and they felt that their own must be. Sweden has traditionally favored free trade and liberal tariff policies and IDA meets this requirement quite well.[2]

The striking thing about these three reasons was the fact that there was domestic pressure in Sweden to increase foreign assistance. The author pointed out the contrast between the Swedish and the United States situation in this regard. This was quite understandable in the Swedish view. "Foreign aid is a new thing for us. The United States has been at it for 20 years. We may have the same problem in 20 years. The United States Congress and the public is bored with foreign aid. It has been a very long-standing thing. The public wonders when it will end and they are beginning to wonder about the effectiveness of foreign aid--what results have been achieved. The United States, on a realistic

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[1] *Ibid.*

[2] *Ibid.*

basis, has been very generous. People grow tired of being generous."[1]

Thus, Sweden likes IDA and supports it with enthusiasm. The views of most of the other Part I countries will be discussed in Chapter XII. Right now we will look at the comments that have been made by economists who have observed the International Development Association in action.

Comments by Economists

Professor Charles P. Kindleberger, of the Massachusetts Institute of Technology, admits to having been skeptical of IDA at the time of its origin

> Because Senator Monroney's basic idea from which it sprang was based on a fallacy. The Monroney proposal . . . was to make available for international lending the collection of foreign currencies which the United States had acquired in counterpart funds. It was his naive notion that these monies represented resources which somehow had not been put to work. He wanted to put them to work, not realizing that what was needed was not money, which could be printed endlessly, but real resources which were scarce in the countries where the United States had accumulated counterpart funds.[2]

Thus, the local currency aspects of IDA caused concern, not only to the Eisenhower Administration, but to some members of the academic community as well. However, Kindleberger noted that the World Bank had taken Monroney's proposal and changed the financing in order to meet the needs of countries that were approaching a position of inability to qualify for bankable loans.

Such a change in emphasis has caused Professor Kingleberger to

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[1] *Ibid.*

[2] Letter from Professor Charles P. Kindleberger, March 13, 1963.

support the IDA as it is presently constituted. "It seems to me that the International Bank has an effective organization which can be used to handle soft loans as well as hard loans. I think there is plenty of room for IDA as well as DLF and the UN Special Fund. I don't see that it is necessary to make choices between them. The more the merrier."[1]

In the author's letter to Kindleberger, the question of increased United States support for IDA was raised. Here is Kindleberger's reply.

> I think there is an important question whether the U. S. should grant more aid at all until Europe grants more. The decision whether such aid should be channeled through IDA, the UN or bilaterally is a joint decision. It would seem to me to be inappropriate for the U.S. to make a unilateral contribution to IDA.[2]

On the question of IDA's significance, Kindleberger had a positive outlook.

> IDA has been a significant force in the development of underdeveloped countries which are in such bad shape they cannot qualify for World Bank hard loans--such countries as Turkey and increasingly India.[3]

Andrew Shonfield, of The Observer, has presented an argument that the relative size and importance of IDA and the Bank are all wrong. He thinks the tail is wagging the dog so far as these two organizations are concerned.

> The decision about the appropriate relative sizes of IDA and the World Bank implies the belief that the main issue can be dealt with by means of orthodox bank loans; what is left over, as not fully bankable, is treated as a marginal problem only. It is, in fact, the central issue.[4]

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[1] Ibid.

[2] Ibid.

[3] Ibid.

[4] Shonfield, p. 158.

This comment of Shonfield's echoes the view of the African spokesman quoted earlier who said the Bank was of no use to the developing nations of Africa--their need is for IDA-type funds. The decision to establish IDA with only a billion dollars as a subsidiary of the International Bank is an example, to Shonfield, of what's wrong with turning such an operation over to a banking institution.

> Mr. Eugene Black has argued placidly against the critics of IDA's smallness, that the institution will grow as the need for its services and its experience in meeting them develop. The argument is as good an illustration as one could find of the limitations of the banker's approach to this problem. Experience is the last thing that is necessary to establish the need for a massive inflow of capital to the underdeveloped countries, most of which cannot possibly be in the form of ordinary bank loans, over the next ten years or so. Certainly experience would be a help . . . in developing new techniques for lending money on a much larger scale than hitherto, and for purposes which the World Bank has hardly touched. But IDA is not well designed to serve this purpose. The chief missing element in all this is the sense of urgency. What is required now is not the slow accumulation of experience on a series of pilot projects, but a political act of will on the part of the rich countries about the quantity of resources that they are ready to devote to raising the submerged majority of mankind. As IDA has turned out, it has become the means of enabling the rich to evade the essential problem rather than to solve it.[1]

Shonfield is unfair to Eugene Black in his charge that Black argued against the critics of IDA's smallness. There has been no more forceful critic of IDA's smallness than Eugene Black. He has said again and again that IDA was too small--that her resources were inadequate for the task. However, he is guilty of having the opinion (an opinion the author shares) that economic development takes time--that it is not something that can be rushed into with lots of capital and suddenly every country will be producing steel ingots and Nobel Prize winners.

If the Bank's establishment is a typical example, it takes a

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[1] Ibid.

new institution about 3 or 4 years to get established and functioning effectively. It was hoped that by placing IDA in the Bank, this period of organization could be shortened. It would appear, to this observer, that this hope has been realized. IDA was established in September, 1960, and had granted its first credit by May, 1961. This would appear to be rather prompt action as compared to other international agencies. And these credits have gone to sound projects. Any organization could have given a billion dollars away quickly. But everyone knows that projects that are approved by the staff of the World Bank are good projects.

As far as the size of IDA's original fund is concerned, it is hard to see why Shonfield finds fault with Eugene Black on this matter. When Mr. Black was asked to discuss the major problems in establishing IDA, he replied that there was only one problem and that was getting a billion dollars.[1] What else was he supposed to have done? Why is it IDA's fault that its resources are too small? The author has gotten the impression that the IDA staff, from Mr. Black on down, would have liked to have had more money and certainly they are convinced that IDA needs more money now.

Shonfield is right in calling attention to the fact that a sense of urgency is lacking in this whole sphere of economic development. And it may very well be that IDA was a sop to the underdeveloped countries--a sop that was given in order to salve the conscience of the rich Western nations. If it was this--so be it. In the author's opinion, IDA has done the best it could with the limited resources made available to it. And the staff of IDA is trying very hard, at this time,

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[1]Interview, March 13, 1963.

to make the developed countries aware of the need for more funds like IDA's.

Professor Max Millikan, Director of the Center for International Studies of the Massachusetts Institute of Technology, like Professor Kindleberger, had serious reservations about IDA at the time it was established. However, his concern was not over the local currency issue but about the wisdom of pressing for IDA, given the political situation in the United States.

> My fear was that some of the congressional support for IDA was based on an estimate that if such an institution were in existence, the Congress might take this as a good excuse for eliminating or very sharply reducing U.S. development loans on soft terms. My main concern is that an adequate volume of capital should be available to the underdeveloped countries on terms they can afford, whether this comes from multilateral or national sources. If individual countries like the United States are not prepared to make sufficient capital available on non-political terms through their own national instrumentalities, I see no reason to believe they will do so through international organizations.[1]

However, Millikan, like Kindleberger, has found that his earlier apprehensions have given way to support.

> In light of the experience of the last year or so, it now seems to me that my fears were exaggerated. I cannot see much evidence that the existence of IDA has to date led to a reduction of U.S. capital funds which has any more than offset the U.S. contribution to IDA.[2]

It is upon this last point raised by Millikan that much depends. Is IDA money in addition to or a substitute for bilateral aid money? Millikan thinks that United States bilateral aid of a soft loan character has been reduced by the amount of the United States' contribution

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[1]Letter from Professor Max F. Millikan, April 10, 1963.

[2]_Ibid._

to IDA. If he is right in this, then the main argument in IDA's behalf would be that IDA can administer this amount of money better than the United States Government--an argument to which many people would subscribe. The question would be the one discussed in Chapter VI of bilateral as opposed to multilateral aid. If, however, IDA money is in addition to bilateral funds appropriated by the United States Congress and the other parliaments of the Part I countries, then IDA's $1 billion would be a significant increase in total economic assistance.

When Senator Monroney was pushing for IDA, he held out the hope that IDA could be funded out of already appropriated United States aid money--specifically the money of the Development Loan Fund. He also intimated that by using local currency hoards, the United States aid effort could be reduced. This is what Senator Case objected to in Monroney's presentation (see Chapter V). However, these two objectives, transferring Development Loan Fund money to IDA and using local currencies to finance IDA, have come to naught.

It is not easy to ascertain how the Congress would have acted had IDA not been established. Would the Congress have appropriated the $320 million which went to IDA to the Development Loan Fund, if there had been no IDA? No one can say. It would be the author's impression, however, that IDA money does represent an increase over what would have been contributed, in the form of soft loans, without IDA. Even being pessimistic about the matter, Millikan says that IDA has not represented a more than proportionate reduction in United States assistance.

Millikan is pleased with the relationship IDA has with the Bank.

> It is my impression that the present relationship between IDA and the International Bank for Reconstruction and Development is a

> useful and constructive one and I have no suggestions for altering it radically.[1]

On the question of IDA's significance, he feels that "IDA's contribution to the development of the less developed countries has been limited only by the resources available to it."[2] He thinks, further, that those resources should be expanded as rapidly as possible. However, he would advocate such increases only "if the Congress can be persuaded to increase the U. S. contribution to IDA with no more than a compensating reduction in capital made available directly by the U. S."[3]

Millikan is of the opinion that such a shift to IDA could be made "over time gradually, but that a large scale campaign for a radical shift in a short period would be counterproductive."[4]

Barbara Ward Jackson, of The Economist, is another person who supports the International Development Association. However, she would hope that "IDA, as it develops, should become a more independent agency while maintaining links with the International Bank."[5] Lady Jackson thinks more United States aid could profitably be channelled through IDA and that IDA could be a significant force in economic development. She emphasizes the great number of underdeveloped countries that are becoming unable to service debts on commercial lines. To meet the needs of such countries she would urge that IDA be used more extensively.[6]

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[1] Ibid.

[2] Ibid.

[3] Ibid.

[4] Ibid.

[5] Letter from Barbara Ward Jackson, April 13, 1963.

[6] Ibid.

Dr. Robert E. Asher, of the Brookings Institution, finds fault with the terms upon which IDA has loaned money. He thinks that the use of loans repayable in foreign exchange is going to limit the total debt burden of the underdeveloped countries to too low a level. He thinks there is a large need for outright grants which, according to its Articles, IDA cannot make. In view of this limitation, Asher would have preferred that IDA make loans repayable in local currency. "At the same time, it must be recognized that, if the latter is really a loan, it will ultimately have to be repaid in real resources by foregoing goods and services that might otherwise be consumed or invested at home."[1] So far, however, local currency loans have not carried the implication that they would ultimately have to be repaid in real resources and given this history, it would have been hard to get this idea across to the underdeveloped countries. Asher is correct in arguing that local currency loans would have permitted a larger total debt burden than the type of loans IDA is making--but IDA would have sacrificed a number of things, if local currency loans had been made. No one would have expected to repay them in real resources. Local currency loans would have postponed the day when currency convertibility can be achieved world-wide. All the objections can be raised against local currency loans from IDA that were important in causing the United States Government's Development Loan Fund to abandon local currency loans in favor of IDA-type credits.

Dr. Paul N. Rosenstein-Rodan, of the Massachusetts Institute of Technology, is a believer in multilateral aid. However,

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[1]Asher, p. 130.

> if one is not a perfectionist and does not allow the better to be the enemy of the good channeling of all aid funds through an international organization has unfortunately to be abandoned. Congresses are just not willing to vote such funds for international allocation and it wouldn't be worthwhile to sacrifice half or even one-third of the amount of aid for the sake of an international flag. The second best solution is, therefore, to have <u>some</u> international funds and the rest coordinated and administered on the same functional principles.[1]

The rest of these funds are called "bilateral aid in a multilateral setting." This would hopefully provide for more aid funds than could be secured for international distribution and yet would have the benefits of multilateral aid. Such an ideal is not yet approached by such arrangements as the Development Assistance Committee of the Organization for Economic Co-operation and Development, although it would appear to be a step in this direction.

Dr. Rosenstein-Rodan has reservations about IDA's proximity to the Bank.

> It is a more complicated question whether it should have been as intimately linked with the IBRD as it is. The advantages are that IBRD has the best organization and staff on these matters and could therefore provide the service more cheaply and efficiently. The dangers are two: 1) that IBRD has been very slow in developing an over-all program approach and confined itself for a long time to the so-called single project approach. It has, however, been improving during the last two to three years in this respect. 2) There is also the danger that IDA will become a "waste basket" of the IBRD, i.e., that certain marginal projects which would have normally been financed by IBRD will then be passed on to IDA. In this sense not all of the IDA lending would be truly additional.[2]

If IDA financed projects that the Bank would have financed, had there been no IDA, this would, indeed, be a waste of soft loan money. And there is already enough waste of soft money--through bilateral

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[1]Letter from Dr. Paul N. Rosenstein-Rodan, May 8, 1963.

[2]*Ibid.*

programs that make soft loans to countries that are capble of meeting conventional terms. If the Bank were wasting soft money, too, this would be a serious matter. IDA has granted a $2.8 million credit to Swaziland for highway construction. A later announcement of a Bank loan to Swaziland, for the construction of a hydroelectric plant and a thermal plant, presented a picture of Swaziland as a creditworthy country. Two private banks participated in the power loan with the International Bank and the press release announcing the loan carried an account of the rich iron ore resources available.[1] Swaziland's potential exports of wood pulp were touted as being worth $10 million annually. The whole tenor of the report on the Bank loan to Swaziland makes one wonder if an IDA credit to that country were really justified. In denfense of IDA, the per capita income of Swaziland is estimated at $70 per year (on an exchange rate basis). It meets the poverty criterion of IDA quite handsomely. However, Swaziland is still a British dependency and the Bank loan was guaranteed by the United Kingdom. The fact that this country was still able to secure British guarantees for its Bank loans would increase one's doubt as to the appropriateness of an IDA credit. Perhaps it is this type of borderline case to which Dr. Rosenstein-Rodan referred. Certainly IDA should make every effort to see that such fears are not confirmed.

As to the significance of IDA, Dr. Rosenstein-Rodan had the following comment to make.

> There is no doubt that so far IDA could not be a significant force in economic development notably because of very small funds.

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[1]International Bank for Reconstruction and Development Press Release No. 63/14, May 16, 1963.

> Undoubtedly therefore there is a case for an increase in funds available to it, notably from all those very numerous countries which either do not supply enough aid or are particularly deficient in soft loans and grants. In practice this covers all the countries besides the U.S. and France and in between, doing three-quarters of what should be done, is the U.K. The greatest sinner is Germany.[1]

He raises a question which is raised again and again in discussions of soft loans and that is the inappropriateness of the West German response. This question will be discussed at greater length in Chapter XII.

Rosenstein-Rodan sees IDA as a particularly valuable device for countries which have no organization to administer soft loans and grants. He believes that "IDA is a very suitable form for it." As far as the United States contribution is concerned, he thinks there is no logical or moral reason for the United States to increase its contribution to IDA, since it already supplies a great deal of money through the Agency for International Development. An increased United States' contribution might be important "as a gesture and perhaps as a psychological or moral catalyst to induce more of such action by other countries who do not contribute enough in soft loans."[2] Rosenstein-Rodan has fewer reservations concerning the administration of bilateral aid than any of the other economists contacted. Apparently, he makes very little distinction between soft loans administered by the United States Agency for International Development and those made by the International Development Association.

The Director of the Institute of Economic Growth in Delhi, Mr. V. K. R. V. Rao (originator of the proposal for a United Nations

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[1] _Ibid._

[2] _Ibid._

Economic Development Administration discussed in Chapter II), thinks that the

> setting up of the IDA is a great event in the history of economic development, and it is bound to make a significant contribution to the rate of economic growth in the under-developed world....I would look to the IDA, reformed and rejuvenated in the light of the vast requirements of the under-developed world, to be the main instrument for the promotion of economic growth, and the lessening of the differentials in per capita income and levels of living that now make two parts out of this one world of ours.[1]

Rao's plan for reforming and rejuvenating IDA would include adding a great deal more money and doing away with weighted voting (see Chapter XII).

Professor Jan Tinbergen, Director of the Netherlands Economic Institute, "favored the establishment of IDA as long as no broader approach (U. Nations) was possible."[2] This view is representative of the sentiment for SUNFED in the Netherlands. It will be remembered that the Netherlands stood ready to contribute to SUNFED as far back as 1954.

Professor Tinbergen prefers the United Nations as a distributing agency because he thinks that, although cooperation with communist countries has sometimes been difficult if not impossible, we should accept some risk of failure in our development policies. "The world as a whole is in vital need of a way of peaceful coexistence. While the most urgent problem is that of security, an international order will have to bear on economic and social issues as well. These issues may be good issues on which to try out peaceful coexistence."[3]

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[1]Rao, p. 17.

[2]Letter from Professor Jan Tinbergen, (no date).

[3]Jan Tinbergen, Shaping the World Economy (New York: The Twentieth Century Fund, 1962), p. 113.

Since IDA has been established as it has, Professor Tinbergen has "no difficulties with the Bank's administering IDA" and would indeed, favor increasing multilateral aid. He feels that "IDA has been significant already and will become even more significant. I hope considerably more funds will be made available to it."[1]

Until a United Nations approach is possible, the "International Development Association (IDA) seems to be the most appropriate organ, since it is operated by the experienced staff of IBRD. Its policy will have to diverge from the Bank's at several points, however, and it may turn out that an independent organ would be better suited to the task."[2] Tinbergen calls attention to Shonfield's comments about handing IDA over lock, stock and barrel to the head of the World Bank, "to be run by his staff as part of their general business, with no separate offices at all."[3]

Professor Benjamin Higgins, of the University of Texas, would have the United States "spend as much through the IDA as it possibly can without increasing the American share to a figure higher than has lately become customary for technical assistance--about 40 per cent."[4] Higgins is afraid IDA would lose its international character if much more than 40 per cent of its resources came from the United States.

> Large and regular appropriations for a U.N. grant program could not be expected from the U.S. Congress. But it is not impossible

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[1]Letter from Jan Tinbergen, (no date).

[2]Tinbergen, p. 114.

[3]Shonfield, p. 156.

[4]Higgins, p. 181.

> that Congress should in some session increase the United States' contribution to IDA to $800 million, permitting the IDA to have capital funds of $2 billion under the proposed formula. When offering more funds to IDA, the United States should also bring pressure to bear on such countries as Canada, the United Kingdom, West Germany, and Australia to increase their contributions to the IDA program; and should urge France--the second biggest spender of aid--to channel a larger share of its capital assistance through the IDA rather than through bilateral channels.[1]

With Higgins' comments about IDA's expansion as an introduction, we will now turn our attention to the other proposals that have been made for IDA's future.

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[1] *Ibid.*, pp. 181-182.

CHAPTER XII

PROPOSALS FOR THE FUTURE OF THE INTERNATIONAL DEVELOPMENT ASSOCIATION

Eugene Black's Proposal

This study covers the period of IDA's operations up through September, 1962 when the annual meeting of the Board of Governors was held. At that meeting, Mr. Eugene Black proposed a substantial increase in the funds of the Association. Black conveyed as strong a sense of urgency as was possible.

He pointed out that Bank studies had shown "that between 1955 and 1961, a group of 34 countries, accounting for some 70% of the population of the underdeveloped world, more than doubled its total external public debt. Yet, over the same period, the export earnings of the same group increased by little more than 15%."[1] He went on to discuss the limitations of private capital for investment in social overhead projects. He enumerated the problems inherent in bilateral aid. "Aid which is at the mercy of the variable winds of diplomacy offers a poor basis for the rational programing of economic development."[2] He argued that more aid was needed on

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[1]IDA Board of Governors Press Release No. 3, September 18, 1962, p. 6.

[2]*Ibid.*, p. 7.

comparatively easy terms of repayment. He had, he said, "Advanced a number of arguments whose relation to one another may not have seemed very clear. But in fact they are all relevant to a single and urgent issue--the future of the International Development Association."[1] He reminded the audience that IDA faced the imminent full commitment of its initial funds and that if no new funds were provided very soon--IDA would not be able to enter into any new lending commitments after mid-1963.

> This is not a situation that can be ignored and allowed to drift. To do nothing would in itself constitute a decision to bring IDA's operations to a halt.
>
> If IDA continues to operate at its normal pace, it seems probable that it will during the current fiscal year commit something like $500 million. . . . There is no reason, that I can see, to suppose that the demand for worthwhile credits will be any lower in subsequent years. On the contrary, it is my conviction that the demand will continue to increase, and to increase greatly. Experience has already demonstrated, I believe, that IDA is capable of meeting a very real and important need and, in relation to this need, the original capital of IDA was obviously inadequate. But if it is to meet this need--if it is to become a principal instrument for the development of the poorer countries, and not just a minor gesture of good will toward them--it will clearly require a very substantial addition to its resources.[2]

Mr. Black has put the case very well. Should IDA become a principal instument for the development of the poorer countries? Or is it to be only what Shonfield alledges--a minor gesture of good will toward them--salve for the conscience of the rich so that they can go on ignoring the desperate poverty all around them?

Mr. Black reminded the Governors that it was to the IDA, not to the Bank, that most of the newly independent countries would be looking for help. "The future of IDA is therefore the most important

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[1] *Ibid.*, p. 8.

[2] *Ibid.*, pp. 8-9.

issue that I commend to your sympathetic consideration during this week's Meetings."[1]

In Mr. Black's view, IDA was not only the most important item on the international development agenda for 1962, but he pointed out that,

> Over the years, the Governors have made a series of crucial decisions that have shaped the international aid effort, and permitted it to meet the growing and changing needs of the less developed countries. I think particularly of your authorization of the creation of the International Finance Corporation, of the doubling of the authorized capital of the Bank, and of the creation of the International Development Association itself. I believe that your approval of the resolution directing urgent attention to the problem of the enlargement of IDA's resources could well prove to be the most important and fruitful of all these decisions.[2]

The President of the International Development Association was not engaging in mere rhetoric when he uttered those words. He sincerely believed that the IDA should be a potent force. It was, then, a cause for a great deal of pleasure on his part when the Governors approved the following resolution on September 18, 1962.

> Resolved: That the Executive Directors are requested to consider the prospective financial requirements of the International Development Association, and to prepare and submit a report thereon to the Board of Governors of the Association at the earliest date, if possible before December 31, 1962.[3]

This resolution signified the intention of the Part I countries not to bring IDA's operations to a halt. It was proof that those governments believed IDA had made a positive contribution and was worthy of continued support. The richer nations' enthusiasm for

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[1] Ibid., p. 9.

[2] Ibid.

[3] Summary Proceedings of the 1962 Annual Meetings of the Board of Governors (Washington: IBRD, 1962), p. 73.

IDA was not, however, unanimous.

Question of Replenishment Quotas

At the Vienna meetings in 1961 the Governor of IDA for the United Kingdom, Mr. Selwyn Lloyd, while stressing the importance of IDA, called for a taking into account of the relative capacities of member countries in assessing them for additional contributions.[1] His statement illustrated the British view, held throughout the deliberations concerning IDA, that their share was disproportionately large.

Mr. Lloyd's successor, Mr. Reginald Maulding, made the case in more precise terms at the 1962 meeting.

> We readily support the proposal to study the means of supplementing the resources of the Association, and for our part we shall be prepared to play a substantial role in helping to replenish them. At the same time, I must make it clear that in my view the study should also comprise the question of how future subscriptions can best be related to the resources and general economic situation of the countries concerned. Thus far the United States has been the largest and the United Kingdom the second largest contributor to the capital of the Bank and the IDA. In each case the United Kingdom contribution is two-and-a-half times as big as that of the next contributor. . . . We shall wish to go into this question as part of the study of the proposed increase in the resources of the Association.[2]

The Government of the Netherlands has joined the Government of the United Kingdom in protesting the formula for apportioning contributions to IDA. The Governor from the Netherlands, speaking to the 1962 Board meeting, said

My country's response to a call in the coming years for further

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[1]IDA Board of Governors Press Release No. 9, September 19, 1961, p. 5.

[2]IDA Board of Governors Press Release No. 15, September 18, 1962, p. 2.

> financial assistance to IDA will be a sympathetic one. . . . We cannot continue to accept for our part the original distribution formula, based on the capital subscriptions in the Bank. A more equitable criterion, derived from national income comparisons, will have to be applied, and we trust that this time we will not be faced again with the alternative of accepting the unreasonable or abstaining altogether.[1]

This question of quotas has come up as a very serious problem in the discussions that have been held on replenishment of IDA's funds. The staff of IDA has taken a hands-off attitude and decided to let the countries fight it out by themselves in the Development Assistance Committee of the Organization for Economic Co-operation and Development or wherever. Since the discussions on IDA's replenishment have taken place in Paris at the meetings of the Development Assistance Committee, however, the staff of IDA has decided that they do not like that arrangement very well. They would have preferred that the discussions take place among the Executive Directors of IDA. IDA has sent an observer to the Paris meetings on replenishment but has not taken a leadership role in the discussions.

Besides the question of quotas for the Part I countries, there is a question as to whether both Part I and Part II countries should subscribe again. What would the Part II countries subscribe? Should the Part II countries put up part of thier contributions in convertible currency? This view was insisted upon by the United States Government at one time. There have been complaints from some of the underdeveloped countries, however, about the possibility of having to give up more of their scarce foreign exchange reserves in order to replenish IDA.

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[1]IDA Board of Governors Press Release No. 19, September 18, 1962, p. 2.

Some persons would advocate that the Part II countries contribute only their own local currencies on this second round. If they did this, could the Bank use this money? As mentioned earlier, some members of the staff think IDA could make use of local currencies, if they represent real savings. Others think it foolish for these countries to put up currencies that IDA cannot use. But, isn't it important that all members feel that they are making some contribution? Apparently this was felt to be important when IDA was established. Isn't it still important? This is one of IDA's strongest advantages in the eyes of a good many people. It puts the underdeveloped countries in the position of being donors of foreign aid. They are asked to help other countries develop and something important is involved in this. It is not mere show--some of these countries had to make some sacrifice to come up with their convertible currency contribution to IDA. It would seem to be very desirable to continue to require some contributions in foreign exchange.

South Africa, a Part I member of IDA, expressed itself as unwilling to contribute further, at the 1962 meetings. The Governor, Mr. T. E. Donges, explained his country's position as follows:

> We have these large underdeveloped areas, particularly the areas occupied by our Bantu peoples, now evolving towards self-government, which still require considerable amounts of capital for their further development. . . . With our limited resources, it is clear that we cannot afford to incur any very substantial additional obligations in respect of assistance to other less developed countries. While I am in very great sympathy with the objects of IDA and with the proposal before us I feel, therefore, I must make it clear that countries in the special position of South Africa cannot undertake any large new commitments for this cause, however worthy it may be.[1]

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[1] IDA Board of Governors Press Release No. 31, September 18, 1962, pp. 1-2.

Views of West Germany

The Government of West Germany has shown the same reluctance to increase IDA funds that it showed toward the creation of IDA in the first place. Although tempering his reservations with praise of the Association, Ludwig Erhard expressed his country's caution as follows:

> The main subject of this year's Annual Meeting is the proposal made by the Management of IDA to request the Directors to consider the question of additional subscriptions. I agree to this proposal. During its brief existence IDA has done useful work. . . . Whenever extremely attractive credit terms of almost grant-like nature are given, there is a danger that, in view of the increasing possibilities of the developing countries to present well-founded projects, demands will greatly exceed resources of finance. . . . In view of the already very high bilateral assistance of the industrial countries, the question of these countries' capacity to raise such funds must therefore be given special attention.[1]

The Republic of West Germany made official contributions to developing countries totalling $157 million in 1958-59.[2] This was 0.14 per cent of the gross national product of that country as compared to 0.39 per cent of gross national product given by the Western nations *in toto*. German per capita income was $1,014 in 1958 and foreign aid averaged $0.72 per person in that year.[3]

The Government of West Germany, along with the Government of the United Kingdom, is opposed to soft loans. There has been some relaxation in the opposition to such loans on the part of the German

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[1]IDA Board of Governors Press Release No. 7, September 18, 1962, p. 3.

[2]United Nations, Department of Economic and Social Affairs, *International Economic Assistance to the Less Developed Countries* (E/3395/Rev.1,1961) (New York, 1961), p. 25.

[3]*Ibid.*, Table 34, p. 50.

Government--the Kreditanstalt für Wiederaufbau recently made some loans to underdeveloped countries for as little as 3 per cent interest. But West Germany does not like to give money away. Germany has no ex-colonies to feel tender toward and might be expected to be a big contributor to IDA. Almost all observers of the aid effort point to Germany as the country that is not doing its share.

Germany, meanwhile, insists that hard loans are necessary because the discipline that the balance of payments exerts is thought to be essential. But, if soft loans are not granted--and if hard loans have to be made in ever-increasing amounts in order to keep a net inflow of capital--isn't this really the reverse of maintaining discipline? IDA tries to maintain discipline by tying money to programs or projects. If a country gets to a stage of development where a large percentage of outside capital cannot be committed to specific projects, then the need for discipline is thought to be less great.

If discipline is maintained by making only hard loans, what is the cost? If the capital exporting countries do not loan the gross amount necessary to keep a certain high level of net investment coming in, they force the underdeveloped countries into a quite cynical default with all the impact that would have on their ability to raise capital, or, the underdeveloped countries are forced to cut back on imports to the point of cutting back development. This latter alternative may have quite a lasting impact. Once momentum for development is reduced, it may be hard to regain. Growth may be slowed down enough that it will cost the rich countries more in the long run than an uninterrupted flow of capital would have amounted to. Or, the chance for achieving development without violence may be lost forever. The prophetic words of the 1949 International Bank Mission to Cuba are recalled in this connection.

> They (the Cubans) may take advantage of their present opportunity and substitute a growing, dynamic and diversified economy for their present static one, with its single crop dependence. This may be a long and arduous task. It will involve great effort and some sacrifice of tradition and comfort. The Mission believes that failure to choose the dynamic alternatives can bring to Cuba consequences of the utmost seriousness. Control may well pass into subversive but specious hands--as it has done in other countries whose leaders have ignored the trends of the times.[1]

Most of the developed countries accept the pressing need for increased soft loans. The United States Government has argued--against the hard loan advocates--that continuing hard loans is an essentially unworkable policy for lenders because countries will have to go to their legislatures for ever-increasing gross amounts and the legislators won't understand this. Thus, from a psychological standpoint this would be very difficult. The United States Government wants the countries of Western Europe to start making more soft loans so that it can point this out to the Congress and prove that the United States is not alone in this policy and is not carrying a disproportionate share of the cost.

The Germans insist that soft loans are a sloppy way to do

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[1]International Bank for Reconstruction and Development, Report on Cuba (Baltimore: The Johns Hopkins Press, 1951), p. 13.

things. They propose to loan more and more money on hard terms--to maintain a certain net inflow of capital. But, is it right to make a hard loan to a country even if the project generates foreign exchange enough to service the loan on hard terms? The United States view is that this is selfish and unscrupulous. A country pre-empts those projects that are self-liquidating--the creditor takes all the improvement in the balance of payments--and this is felt to be unfair to the borrower and unscrupulous to other lenders. There has been a lively debate in the Paris meetings of the Development Assistance Committee over this very point.

The International Development Association Rejects the Hard Loan Argument

IDA has taken a strong stand in favor of soft loans. Mr. Black has pointed out that of the total flow of public funds going to the underdeveloped countries during 1956-59, more than half went in the form of outright grants. But, he mentioned that the signs indicated that the ratio between conventional and unconventional credit was changing--and from his point of view--changing for the worse. More than nine-tenths of the soft money came from the United States and France--few other countries had extended aid otherwise than on conventional terms.[1] He pointed to the Bank's observation that most countries experienced a rapid increase in foreign debt within a very few years--once development gets underway.[2]

The staff has estimated that external public debt service

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[1]IDA Board of Governors Press Release No. 4, September 19, 1961, p. 9.

[2]*Ibid.*

obligations have been increasing over the period 1955-1961 at an average annual rate of more than 15 per cent per year. Thirty-two low-income countries increased their external public debt between 1955 and 1961 by a factor of almost 2.1. This increase in the total amount of debt was accompanied by a hardening of the average terms. Thus, while total debt more than doubled from 1955 to 1961, it appears that service on this debt increased by a factor of 2.5. The ratio of service on external public debt to exports rose from a little over 3 per cent in 1956 to about 7 per cent in 1962. The total outstanding external public debt of the underdeveloped countries at the end of 1961 is estimated at some $20 billion, or $14 per person. The external public debt service liabilities now appear to be $2.5 billion per year, so that capital inflow has to be more than this amount before any net addition to resources takes place. This annual liability has arisen as a result of capital inflow at the rate of about $4 per person per year in the underdeveloped countries. This outline of what has happened has caused the staff of IDA to conclude that soft loans on the order of $2 billion a year are needed.[1]

Mr. Black has painted a bleak picture of what might happen as a result of this increasing hard debt.

> I do not have to explain to this audience how the machinery of economic development could be overloaded with foreign debt until it sputtered to a halt amid half-built projects and mountains of discarded plans. I expect, indeed, that there are some in this audience who can point to projects in their own countries which are at this very time suspended in mid-air, so to speak, for this very reason. Maybe it is a half-finished highway or a hospital that has been built but not equipped.

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[1]"The Need for an Increased 'Soft Credit' Component in Development Aid" (report prepared by the staff of IDA) (no date) (Mimeographed.)

This kind of disruption kills peoples' hope in orderly economic progress and, if it persists, can lead to serious disillusionment.
. . . .
The safe and sane way to minimize these dangers is to maximize the amount of official capital which is supplied at very long term with only a token interest burden.[1]

Will the external public indebtedness of the underdeveloped countries double again over the next 5 years? Or will the rate of increase go higher? Even if there is a decrease in the rate, IDA is convinced that more soft loan funds are needed.

Role of the United States Government in Replenishment of Funds

Apparently the President of the United States agreed with this prescription. As quoted earlier, in his speech of welcome to the Board of Governors in 1962, President Kennedy said "The work of the International Development Association is particularly important--and this country fully supports the proposal that the Executive Directors develop a program to increase its resources."[2]

Whether the President's enthusiasm is shared by the Congress is problematical. Also, there is a serious question as to the size of the United States' share in any replenishment of IDA's funds. The President of IDA had indicated a need for a 5 year fund of $2½ billion. If the United States maintained its original share, this would mean a contribution of about $750 million. Some indications point to a United States contribution somewhat less than this figure.

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[1]IDA Board of Governors Press Release No. 4, September 19, 1961, p. 10.

[2]IDA Board of Governors Press Release No. 75, September 20, 1962, p. 1.

Perhaps the most limiting factor in any great expansion of IDA is the balance of payments problem of the United States of America. Representative Passman made this something of an issue in the 1962 hearings on IDA's appropriation. There is a question as to how much Congressional support an expansion of resources would have, in view of the continuing balance of payments problem. As Andrew Shonfield has pointed out, "the basic lesson in strategy for the underdeveloped countries is that, if they are to obtain substantially more economic aid, they must take an active interest in protecting the balance of payments of the donor countries."[1] Just how the underdeveloped countries can accomplish this and yet increase multilateral aid is unanswered.

Representative Passman has made quite a sophisticated argument against IDA on balance of payments grounds:

> Mr. Passman. But, these countries which earn dollars or other hard currencies from their exports to the amount needed to deal in world commerce, if through the various aid programs we make dollar credits available to the full extent, or even to a partial extent, of the amount needed to pay for what they would import from the United States, then that would make available the money they earn from exports for them to use for whatever purpose they might see fit.[2]

He continued his argument by stating that in the underdeveloped countries

> Some of those dollars are earmarked to buy something that is produced in America.
>
> If we provide for them credits or gifts, or grants, then they can requisition from America what they would normally

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[1]Shonfield, p. 175.

[2]U. S., Congress, House, Subcommittee of the Committee on Appropriations, Hearings on Foreign Operations Appropriations for 1963, 87th Cong., 2d Sess., 1962, p. 300.

buy with the dollars which they earn from exports.[1]

Mr. John M. Leddy, Assistant Secretary of the Treasury and U. S. Executive Director of the International Development Association, presented information to counter Representative Passman's contention. The following exchange indicates that the Congressman is still not convinced.

> Mr. Leddy. . . . The normal effect of any provision of AID funds or development credits for development purposes in these countries tends in and of itself to increase the total demand for imports into those countries.
>
> Mr. Passman. At least we hoped so.
>
> Mr. Leddy. It has shiftability. It means you have to import more goods to go into the project, it means you have to spend more money internally for labor, et cetera, which then creates a demand for imports. I do not believe that it is correct to say that the effect of lending for development purposes is simply to add to the free dollar resources of these countries.
>
> Mr. Passman. I did not say anything about just lending. I said under the various agencies through which we are disbursing U. S. funds.[2]

This is an extremely important point. If it can be demonstrated that untied aid (all IDA loans must be untied in accordance with the charter) leads recipient nations to spend their earned dollars elsewhere, then this would be a potent argument against expansion of this agency. The United States would be patently foolish to give assistance which would tend to drive customers away.

At the time of the Congressional hearings on United States membership in IDA, in March, 1960, the balance of payments problem was put to Treasury Secretary Anderson. His answer has been discussed in Chapter VII. What he said is still relevant today

> If one looks at the shorter range, while again I would note that we are contributing about 32 percent of the funds to this institution, and the normal practices of the World Bank

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[1] *Ibid.*   [2] *Ibid.*

indicate that about 29 percent of the identifiable purchases under World Bank loans on an international competitive basis are made in the United States, I could not thus be in a position to say that there would not be some temporary addition to our balance-of-payments problem.

But I think that we have got to go about its solution on the basis of establishing a world in which we can become larger exporters, and other people better customers, rather than to go about it in ways which seem to be solutions only for the short run.[1]

In an effort to follow up on Secretary Anderson's statement concerning the percentage of Bank funds spent in the United States, an interview was conducted with an official of the Treasurer's Office in the World Bank. He was asked if there were any figures available on the percentage of IDA's disbursements that had been made in the United States. It was reported that there was no such breakdown available and even if there were, it wouldn't have any meaning. Because, through September 30, 1962, IDA had only disbursed $18.5 million. This would not be at all representative for 2 reasons. First, IDA's Articles of Agreement require that the currencies be drawn down on a pro rata basis. Second, the location of the countries receiving IDA credits would have an influence on the source of purchases made. That is, although purchases are made on the basis of international competition, the underdeveloped countries do have certain trade patterns established. Thus, the smallness of IDA's disbursements to date would be more indicative of what country got the money than of how total IDA resources will be distributed.[2]

So, there are no figures available on the distribution of

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[1]House Subcommittee No.1 of the Committee on Banking and Currency, Hearings on H. R. 11001, 1960, p. 36.

[2]Interview with an official of the Treasurer's Office, IBRD, May 29, 1963.

IDA funds. If it could be believed that the pattern established by Bank lending would hold--that is, that around 29 per cent of IDA funds would be spent in the United States--then there would be little cause for alarm on account of the balance of payments. As long as United States exports are almost equal to the amount of United States funds contributed to IDA, then (except for the import content of the goods exported from the United States--which is quite low), plus and minus items on the balance of payments account are equal.

Another fear has been expressed in the United States Congress--where the doctrines of mercantilism are not dead. Some Congressmen are worried that IDA might make loans to countries whose industries might compete with United States firms.

Representative Alexander of North Carolina was very concerned that IDA might loan funds to a textile firm which would compete with domestic industry.

> Mr. Alexander. Do you have any regulations with reference to loans in regard to industrial development in underdeveloped countries which would pertain to the problem of, say, for instance, textiles, which in this country and throughout the world is right much of a competitive business already? Do you have any rules with reference to what these industrial loans would be made for?
>
> Mr. Leddy. There is no prohibition on the making of any particular type loan under the IDA or the Bank. I should repeat, however, that the Bank and IDA have tended to focus pretty heavily on the field of transportation, power, irrigation. There have been some loans to private industry usually through industrial development banks. The industrial development banks, of course, relend the money to a wide variety of domestic industries, which could include a textile industry but there is no general policy laid down in the international institutions as such which would prohibit any particular type of loan or any particular industry.[1]

Although some of IDA's strongest critics are found in the

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[1]House Subcommittee of the Committee on Appropriations, Hearings, Foreign Operations Appropriations for 1963, 1962, p.317.

United States Congress, some of IDA's strongest supporters are there also. Senator Monroney succeeded in amending the Act for International Development of 1961 (Section 205 of Public Law 87-195, 87th Congress, September 4, 1961) so that the President now has the power to lend up to ten per cent of the funds of the Development Loan Fund to the International Development Association. In fiscal year 1962, this would have amounted to $110 million and would be a substantial boost to IDA's resources. However, there has been no move to implement such a loan. It would have to be a peculiar type of loan since IDA does not charge interest and IDA credits will not be repaid for 50 years. If the Congress meant for the President to loan IDA funds on these same terms, it would be a most helpful arrangement. However, the Association has little hope of securing funds through this avenue at present.

Shonfield was quite enthusiastic about the possibility of transferring such funds to IDA. He argues that

> it would transform the whole character and scale of the international effort. No doubt only a portion of this money would be siphoned off, to IDA initially; but even this gesture might well prompt other countries to look at their own national aid programs more critically, and consider whether it would not pay them--assuming the aim of part of their expenditure, at any rate, is straight economic development, regardless of any particular national interest--to follow suit.[1]

IDA would be most anxious that other countries increase their contribution, also, if the United States made any very sizable contribution to IDA on a unilateral basis. The Bank, by selling its bonds in the financial markets of the world, has tried to steer clear

[1]Shonfield, p. 167.

of domination by the United States. Since IDA funds are governmentally provided, this is harder with IDA. So, it is extremely important that the United States' share not be all out of proportion to every one else's contribution--if United States domination is to be avoided.

Relationship with the United Nations

IDA has entered into an agreement with the United Nations which establishes a liaison committee consisting of the Secretary General of the United Nations, the Managing Director of the United Nations Special Fund, the Executive Director of the United Nations Technical Assistance Board and the President of the International Development Association. There has been a growing amount of cooperation between the Association and the Special Fund--in the field of technical assistance and the drawing up of projects.

There have been several cases recently of the United Nations Special Fund contracting for the services of the Bank staff in making project appraisals. This has led some people to promote the idea of an even closer alliance between IDA and the United Nations. Benjamin Higgins calls for making the United Nations regional commissions subdivisions of IDA. In his plan, all country economic development plans would be approved by IDA headquarters--then discussions would be undertaken with the specialized agencies and the bilateral programs to determine which ones would provide which parts of the outside assistance needed.[1]

Mr. Paul Hoffman, Managing Director of the United Nations Special Fund, has some proposals for IDA's role in the future.

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[1]Higgins, pp. 196-197.

Hoffman thinks that $20 billion more than is now in sight for the underdeveloped countries is needed for the decade of the 1960's. He would like to see at least half of this channeled through the International Development Association. Hoffman came to this conclusion because of his high regard for the staff. "The World Bank has gained universal renown as an efficient and effective and objective international financial institution."[1] He argues that IDA should be considered as an institution that must expand its operations promptly.

The Horowitz Proposals

An interesting and intriguing proposal for future development of IDA came from Mr. David Horowitz, Governor from Israel, at the 1962 meeting of the Board of Governors.[2] Horowitz reasoned that the Bank has plenty of money, but a paucity of projects to finance. On the other hand, IDA has many worthy projects but not much money. Why not merge the two operations? Horowitz would have the Bank borrow money at conventional terms and loan it to IDA countries and IDA projects on IDA terms. The difference between the interest paid by the Bank and the interest charged by IDA would then be made up by the developed countries of the world. Thus, IDA could loan $1 billion a year at no interest and the rich countries would only have to contribute $50 million for the interest payment to the Bank.

If some such plan is not adopted, Horowitz warned, the

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[1]Paul G. Hoffman, One Hundred Countries: One and One Quarter Billion People (Washington: Albert D. and Mary Lasker Foundation, 1960), p. 51.

[2]IDA Board of Governors Press Release No. 20, September 18, 1962.

repayment of interest and principal by the poor countries is soon going to be equal to the total financial assistance extended by the rich nations. In 1958, 32 low-income countries of the world were paying $1,280 million in service payments on private account and $770 million in service payments on public debt.[1] These two flows equalled more than $2 billion in 1958. This compares to total official grants in 1958 of $2.4 billion to all the underdeveloped countries of the world.[2]

IDA gave Horowitz' suggestion serious consideration. It was concluded that the proposal was unrealistic because it would involve getting governments to agree to pick up the tab for interest for several years in advance. As more and more funds were loaned, interest costs would rise appreciably. It was not felt that the developed countries would be willing to accept this responsibility.

Horowitz proposed a second solution to the imbalance he saw between needs and resources. Why shouldn't the funds of IDA be used as a guarantee fund for loans made by the International Bank? Thus the $1 billion of IDA funds would be held intact to make up any defaults on loans made by the Bank. This would allow the Bank to extend its operations into countries and projects where it had not been before.[3] The Association studied this proposal also and again concluded that

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[1] Avramovic and Gulhati, Table III and Appendix Table XXI, p. 19 and p. 73.

[2] Organization for European Economic Co-operation, The Flow of Financial Resources to Countries in Course of Economic Development 1956-1959, Table 1, p. 10.

[3] IDA Board of Governors Press Release No. 20, September 18, 1962, p. 4.

the proposal was unrealistic. It was felt that the donor countries would not approve of putting the $1 billion into a guarantee fund. Secondly, it was felt that any weakening of the Bank's standards would lead to a loss of confidence in the Bank by the financial community and a lessening of responsibility on the part of the under-developed countries.

Horowitz' proposals did stimulate thinking on the alternatives open to IDA. One idea that was put forward as a result of Horowitz' proposals received some lukewarm support from IDA. This proposal would have the developed countries float bonds, in their own countries, at commercial rates of interest and loan these funds to IDA at no interest. This would amount to a subsidy of the amount of the interest. The appeal of this plan lies in the possibility that the parliamentary bodies in the rich countries would be more favorable to borrowing for IDA than to taxing for IDA. Certainly the interest subsidy would be much smaller than an outright appropriation for IDA. And the amount of the subsidy could be controlled by the donor government rather than being a blank check as in the Horowitz plan.

It might be possible to remove the IDA subsidy from annual parliamentary debates if some type of long-run borrowing authority could be given as has been done for the Export-Import Bank in the United States. This relief from the yearly ordeal of the appropriation process is very appealing to some persons who favor increased aid to developing nations. Nothing, however, has come of any of these proposals to date.

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[1]IDA Board of Governors Press Release No. 20, September 18, 1962, p. 4.

Other Proposals

Another proposal for IDA's future came from the Government of Pakistan. This plan was presented at the Board of Governors meeting in September, 1961 by Mr. M. A. Mozaffar, Governor from Pakistan. He pointed out that Pakistan had suffered from declining terms of trade over the past 10 years. Is it inevitable or equitable that the burden of adjustment should always fall on the weaker economies? Is it in the interest of the industrial countries to have the primary producing countries continually whipsawed by the terms of trade? The Government of Pakistan, the Governor stated, is of the opinion that a solution can be found which would be in the interest of all. The principle that should be followed is straightforward. The countries which benefit from fluctuations in terms of trade should contribute some part of their gain to the International Development Association. This would apply to both the primary producers and the industrial nations.[1]

Alan Neale has made a proposal that would increase IDA's resources and help solve the problem of fluctuating terms of trade. He suggests that the rich countries, working through the Organization for Economic Co-operation and Development, agree to impose common flat-rate excise duties on their total intake of certain commodities and to devote the proceeds of such taxation to IDA. He estimates that a 5 per cent levy on all coffee, cocoa, and tea sold in the Western countries would produce $100 million a year.[2]

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[1]IDA Board of Governors Press Release No. 5, September 19, 1961, p. 3.

[2]Neale, pp. 15-16.

Mr. V. K. R. V. Rao makes a dramatic case for expanding and re-structuring the International Development Association.

> Time and compound interest are working against the under-developed world and along with it also the built-in progress in science and technology that is accompanying the rake's progress of compound interest in the developed world, parts of which are already wrestling with the problems arising out of affluence, when surrounding them are vast deserts of poverty, and low levels of living and the dismal tyranny of the economic problem. I have no doubt in my mind that the present situation is fraught with instability and constitutes a much graver menace to the peace of the world than anything that the cold war has produced so far. Oases may exist with impunity in a natural world of deserts, but there can be no security for human oases of affluence in a mass-inhabited world of poverty and low levels of living. . . . I believe the answer is the internationalizing of all aid and the entrusting of this international aid to an organisation like the International Development Association. Only I do not think it can take such a major job in its present form, certainly not as an affiliate of the International Bank, with its peculiar structure of voting rights, and whilst its membership does not include the Soviet Union and Communist China.[1]

Several of the developing countries have suggested that the Bank's reserves be transferred to IDA. The Bank had acquired reserves of over $700 million by the end of 1962. However, this idea has received a very cold reception from the Bank's management. They feel that this would be a serious violation of trust to the Bank's creditors. At the time the financial community put up the funds for Bank bonds, it was understood that the reserve fund would be available in the case of country default. To use this fund for any other purpose would be a serious breach of faith, it is argued. Some of the staff go so far as to say it would be disastrous for the Bank, if such a transfer were made. Mr. Black told the bond markets that IDA was separate from the Bank and every effort has been made to keep it so. To transfer Bank reserves to IDA would destroy the bond market's confidence in the Bank's management, it is felt.

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[1]Rao, p. 19.

It has also been proposed that a new type of loan be introduced--a low interest loan to countries not really in need of IDA-type credits. Some countries, Mexico, Yugoslavia, etc., are able to pay some interest but are not able to meet much further debt service at conventional rates. It has been proposed that the Bank's reserves be used for loans at lower than Bank rates to these particular countries. There have been suggestions that regular IDA funds might be used for other loans than the present 50-year, no-interest rate credits now being extended. Why should all IDA credits be for so long and at no interest? Could some IDA credits be less soft?

There has been some consideration of a division of labor between the Bank and IDA--so that IDA would concentrate exclusively on poor and non-creditworthy countries and the Bank would work with the relatively well-off and still creditworthy nations. There would be no more in-between mixture of Bank and IDA funds as there has been in the past. IDA would only finance projects in countries which could make no claim for conventional loans.

But, this would leave a gap as far as the middle-income countries are concerned. There are a good many such countries at the end or approaching the end of their creditworthiness. It is this group that is the target for the in-between type loans that have been proposed. But, this third type loan raises the whole complex issue of justifying 6 per cent loans to some countries, 3 per cent loans to other countries, and zero per cent loans to still other countries. This would really put the staff in an awkward and unjustifiable position. There are already enough problems deciding between Bank and IDA loans. Another type loan would complicate things even further.

In addition, there is a degree of discrimination involved in low-interest loans, that is, the discrimination between those countries getting interest subsidies and those countries paying the going rate. The countries borrowing from the Bank at conventional rates of interest would be paying for the subsidy given to those countries receiving low-interest loans. This is hard to justify. There is also the possibility that giving low-interest loans might lead to a casual attitude about repayment. This is really a "fuzzy" loan which, of course, has been the target of so much vituperation on the part of the Bank's staff. This author would conclude that, because of all the problems cited, there is no prospect for any intermediate interest rate loans by IDA.

One other possibility that has been discussed is the possibility of lengthening the term of Bank loans. Or, perhaps, the Bank could lengthen the grace period before repayment begins. This would involve some degree of interest risk. Interest rates might rise on the money that would have to be borrowed to complete loans already contracted. In the past, the Bank has loaned on the same terms on which it has borrowed (except for the commission that has been added to go into reserves). If it extended the period of the loan, this would involve borrowing short and loaning long. One possibility would be to put the Bank's reserves to work covering this interest risk. This assumption of interest risk would not involve the outright interest subsidy that would be involved in loans at less than conventional rates of interest.

It would appear that there is a greater likelihood that some alteration might be made in the duration of Bank loans than that any intermediate interest rate loans might be made. If loans of longer duration were made, it would help meet the pressing problems of a good many countries. It would extend the time before repayment began until such a time as, hopefully, their export earnings will be a bit higher.

This brings to mind a whole host of other problems. Will the export earnings of the developing countries grow significantly in the future? IDA expects that export earnings of the underdeveloped countries will grow at something like 4 per cent a year over the next decade. This 4 per cent average growth rate disguises a wide range in the individual countries' prospects, however. Countries like India have experienced real problems in their export sector and some experts do not predict a bright future for Indian exports. However, India's present export sector is so small that it has little weight in the average growth rate of all the underdeveloped countries.

The World Trade Conference, to be held under United Nations auspices in 1964, is expected to go into this whole problem of the export earnings of the underdeveloped countries--not just the problem of stabilization of earnings--but the whole question of exports of primary products. As world income increases, there is going to be a less than proportionate increase in demand for foodstuffs. This is the problem of inelastic demand faced by agriculturalists in the United States for the last several decades. And the outlook for a good many industrial raw materials is not so promising, either. Rubber, in particular, is being threatened by synthetics and cotton has its rivals. Some of the schemes for dealing with these problems have been discussed. Several would channel the funds collected through the

International Development Association. However, there does not seem to be a very likely prospect that any such gimmicks will be worked out. In the end, it will be to the governments of the developed nations that IDA will have to turn for more funds. If they are not forthcoming from that source, they simply will not be forthcoming.

CHAPTER XIII

SUMMARY AND CONCLUSIONS

Summary

Now it is time to summarize what has been said about the International Development Association. We have seen the long and tortuous path the idea took. The United Nations debates were important. Mr. V. K. R. V. Rao's proposal for a United Nations Economic Development Administration started members of the United Nations thinking about the need for another type of finance than that provided by the International Bank for Reconstruction and Development. The Rao idea was criticized by the Bank because it was felt that the Bank and the other specialized agencies of the United Nations could carry out the functions which would have been assigned to Rao's proposed new agency. The Government of the United States opposed Rao's proposal, also, on much the same grounds.

The committee of experts, appointed by the Secretary General of the United Nations, drew significant conclusions concerning the capital needs of the underdeveloped countries. They concluded that these countries needed to increase per capita income at least 2 per cent per year and they estimated that the rich nations could meet the needs for external capital, if they provided as much as 1 per cent of gross product. The Bank argued against setting up a new institution to administer these funds--at least until the Bank had been given a chance to prove itself.

The proposal for the Special United Nations Fund for Economic Development (SUNFED)had an important impact. The outline for SUNFED was drawn up by a committee appointed by the Secretary General. They recommended that the organization depend upon voluntary contributions from governments. It was also recommended that SUNFED be authorized to make loans of indeterminate duration and at concessionary rates of interest. Mr. Raymond Scheyven, of Belgium, was given the task of determining the reactions of member ogvernments to SUNFED. He prepared two reports which indicated that: the underdeveloped countries were very enthusiastic about establishing SUNFED, the major contributors were opposed to establishing SUNFED until such time as substantial progress had been made toward disarmament, the Scandinavian countries and some few other developed countries favored immediate establishment of the organization. As a result of Scheyven's studies, substantial changes were made in the proposed outline of SUNFED.

Despite these changes, however, there continued to be strong opposition to establishing SUNFED. The United States objected to the fact: that the communist nations would have been included, that the United States would have had to provide most of the funds, and that the United Nations was going to administer it. Many people objected to equal voting rights in SUNFED--the underdeveloped countries would have been able to exercise majority control on the basis of each nation having one vote. The International Bank objected to the political administration of SUNFED and to the fact that SUNFED would have made lenient loans--which might have driven the Bank out of business.

However, most observers agree that the pressure for SUNFED was a crucial factor in the establishment of the International Development Association. The threat of creating SUNFED gave the rich nations a reason for wanting to establish an organization which would be more satisfactory to them.

The International Development Association can be traced back to two reports that were made at the request of the President of the United States. The Gordon Gray Report outlined the need for multilateral administration of foreign aid funds to assure the maintenance of high standards while overcoming the charges of imperialistic meddling. Gray's report also presented a strong case for public funds for social overhead projects that were not attractive to private capital. The International Development Advisory Board, chaired by Nelson Rockefeller, prepared a report on foreign economic policy which contained a strong recommendation that an International Development Authority be established. This Authority was to be linked to the International Bank, but would make loans on more lenient terms than the Bank and would finance non-revenue-producing projects. This proposal started influential people thinking about the need for an organization like the International Development Association.

A United States citizen, Mr. Stringfellow Barr, dramatized the case for an International Development Association. He posed the problem of economic development in a terse manner. On the one hand, Barr, and the others, wanted to set up a large, bold, innovative agency that would create a sense of emergency concerning the economic development of Asia, Africa, and Latin America. Barr argued that it could be financed in the same emergency fashion that the industrial nations were financing their defense expenditures. Barr and those of his persuasion pointed to the enormous programs of education, training, plant construction, etc. that went on during the Second World War. They argued that such crash programs could be effective in the underdeveloped countries. The West had the resources, the technology, the capital required--all that was lacking was the will. On the other hand, the International Bank and its supporters wanted to treat economic development as a long-continuing process which should be carefully planned, soundly financed, and competently guided. People of this persuasion point to the consequences of revolutionary economic changes in Germany and Russia. They would hope that the development process in Asia, Africa, and Latin America could proceed along less revolutionary lines. Can development be achieved without the social injustice and political cruelty that have been evident in the past? The Bank believes that, with outside aid, it can. The debate between the proponents of these two views continues to this day. That is essentially the difference between the IDA approach and the SUNFED approach. As of now, the proponents of the IDA approach have carried the day.

There was a third attitude toward economic development that assumed importance in the debate prior to the establishement of IDA. Some officials of the United States Government took the position that economic development should be financed by private capital. If private capital was not adequate, then loans could be made by governments on the same terms on which the governments borrowed the money, i. e., the Export-Import Bank approach. Some officials argued that the Marshall Plan should have been put on a strictly business-like basis, because it was not until after the United States provided Western Europe with

Marshall Plan funds on a grant basis that the underdeveloped countries got the idea that the United States should finance their development on the same terms. Some United States officials wanted to make it clear that the Marshall Plan was a one-time effort and that no more programs of this sort were in prospect. As a result of some changes in personnel in the United States Government, this view was rejected and by the time the Monroney Resolution was presented the United States Government was receptive to some such proposal.

Senator A. S. Mike Monroney must be given much of the credit for finally getting the International Development Association accepted. He had wanted to contribute local currency holdings of the United States to a multilateral institution that would administer soft loans to the underdeveloped countries. And he introduced a resolution in the United States Senate to that effect. There were protracted debates on three aspects of the Monroney proposal.

There was a feeling that soft loans were immoral and that soft loans would distort the distribution of capital. Some persons argued that hard loans were necessary because the discipline of the balance of payments was essential. On the other side of the argument, the staff of the World Bank presented studies which tended to show that some underdeveloped countries' capacity to service conventional debt was already strained. These studies also tended to show that, once development gets underway, external debt mounts very rapidly. Service payments on this debt then became quite burdensome, because many developing countries had not been able to increase export earnings significantly. This left these countries with bleak alternatives. They could continue to pile up debt on conventional terms and hope that someone would bail them out; they could pile up debt and default on it; they could reduce their capital imports and cut back on their economic development programs; or they could resort to the forced savings methods of the communists.

Monroney's proposal to use local currencies stirred up more opposition than any other part of his proposal. He wanted to find some way to use the surplus commodities of the underdeveloped countries. He had seen some underdeveloped countries with excess rice and other such countries with rice shortages. He had seen excess petroleum, minerals, and lumber in some countries while other countries were short of these commodities. Monroney thought that the local currencies the United States had acquired could be used to facilitate trade between developing countries in these surplus commodities. The trading nations of the world objected to this idea for fear that such three-cornered swaps might reduce their exports. The underdeveloped countries that had received agricultural surpluses were reluctant to see their local currencies used to finance unrequited exports. The United States Government argued that the developing countries needed steel, machine tools, etc. which were not available in other developing countries. Monroney got little support for his local currency proposal. IDA is authorized to accept local currencies from other governments, but only if IDA agrees to the terms. The United States Government had not transferred any local currencies to IDA through September 30, 1962. The debate on local currencies has, however, continued.

Monroney's third objective was to put foreign aid on a multilateral basis. He had seen the reluctance of many developing countries to get involved in the Cold War. They did not like to accept bilateral aid from either the United States or the Soviet Union. And yet, they needed capital so desperately that they were taking assistance from both sides--with all the strings that were attached to such assistance. Monroney thought bilateral aid was inefficient because it was based on political rather than economic considerations. He was impressed with the effectiveness of the World Bank, however. It seemed only logical, to him, to transfer some United States aid money to the Bank. The "multilateral aid" aspect of Monroney's proposal brought forth surprisingly little opposition.

Through an extensive publicity campaign, the adriot re-writing of his original resolution, and the personal influence of Eugene Black--Monroney was able to get the Eisenhower Administration to support the establishment of the International Development Association. On July 23, 1958, with bipartisan support, the United States Senate passed the Monroney Resolution.

The United States Government took the lead in establishing IDA. The Board of Governors of the International Bank debated the idea at their 1959 meeting. West Germany and the United Kingdom were not happy about the soft loan idea. The Netherlands and Belgium objected to application of the Bank's quota arrangements to IDA. Some underdeveloped countries, who had their local currencies in the hands of foreign governments, and the trading nations opposed the local currency aspects of IDA. There was negotiation on all these points and the Board of Governors came to unanimous agreement that the Executive Directors of the Bank should draw up Articles of Agreement for IDA.

The drafting of the Articles was remarkably smooth. The United States Government, working with the Bank, had prepared some guidelines which the Board of Governors had considered. These guidelines served as a blueprint for the Executive Directors. There were, however, two problems. The International Bank's quota arrangements were unacceptable to some countries, however, no other basis for agreement could be reached and these quotas were finally adopted. There was also a problem over the type of currency that would be subscribed. It was finally agreed that the developed countries would contribute gold or convertible currency and the underdeveloped countries would contribute 10 per cent of their subscriptions in gold or convertible currency and 90 per cent in their own currency.

There was little opposition to United States membership in IDA. Some members of Congress suggested that membership in IDA would make the balance of payments problem more difficult. Some Congressmen resented World Bank administration of IDA because of pique over a Bank loan to Egypt for the Suez Canal project. There was an intimation that IDA had been made necessary by the excessively high interest rates prevailing in the United States. There was a surprising degree of support for IDA among the business, farm, and labor groups in the United States.

The International Development Association has been stamped with the basic philosophy of development held by Eugene Black. He argued that economic assistance should be used to illuminate the possibilities for change in the underdeveloped countries. He insisted that quality was more important than quantity in economic assistance.

It was decided that IDA would extend development credits (the Articles specifically excluded grants) for 50 years, with a 10 year grace period, at no interest--but with a 3/4 of 1 per cent service charge to cover administrative expenses. Credits are repayable in foreign exchange. It was also decided that much of IDA's money would go into projects like those financed by the Bank--transportation, irrigation, and power. In addition to these projects, IDA has financed projects in the field of education.

It was decided that IDA would apply the same standards to projects as are applied by the Bank. In an attempt to overcome difficulties in servicing external debt, the terms to the borrowing country would be of a concessionary nature, however. This combines an emphasis on the soundness of specific projects with an emphasis on the country's balance of payments position. The country that receives IDA credits for revenue-producing projects "on-lends" the funds for the projects at the prevailing rate of interest, within the country, and is repaid in its own currency.

In order to establish countries' eligibility for IDA credits, three criteria were established. First, a country must be at the end or approaching the end of its international creditworthiness. Secondly, this lack of creditworthiness must not be due to poor performance or mismanagement of the economy in the past. This second criterion was believed necessary, because without it the underdeveloped countries might have been encouraged to exhaust their creditworthiness in order to qualify for IDA's no-interest loans. It is reasonable to expect the underdeveloped countries to manage their economies as wisely as possible, if they expect to qualify for soft loans made available by the richer members of IDA. Third, the recipient countries must be very poor. There has been considerable criticism of these criteria. Some people wonder if they were established with India in mind. It is argued that the performance crierion is too ambiguous. Exception has been taken to some credits IDA has extended because it was felt that the recipient countries' per capita income was too high or that they were not approaching the end of their international creditworthiness.

IDA has taken a dim view of loans to state-owned industrial enterprises. This position has been defended on two grounds. It is argued that, generally, state-owned enterprises are less efficient than those that are privately owned. Secondly, it is argued that loans to state-owned enterprises subsidize such enterprises vis-à-vis their privately-owned domestic competitors and vis-à-vis their international competition. Some persons have taken exception to IDA's arguments on this point, but the policy stands.

IDA has made credits available for specific projects. This was done in order to exert pressure on countries to spend foreign credit for economically justifiable activities. There has been increasing criticism of the project approach, however, because loans for specific projects do not help countries in meeting service payments on past debt. Also, project loans often lead to increased demand for imports of consumer goods and raw materials--which puts added strain on the balance of payments. The 10 year grace period is an attempt to overcome this last problem.

There have been criticisms of IDA's techniques of project appraisal. It has been charged that IDA requires data that are not available in the underdeveloped countries. Some governments feel that typical IDA projects are too large to meet their needs. Quite strong criticism has been made of the time consumed in appraising projects. The International Bank prides itself on never having had a default on a loan. Some critics would urge the Bank and IDA to take a few more risks and get more projects going.

The basic problem of the Association has been the meagerness of its resources. This has meant that sub-optimum solutions have had to be found. IDA has not been able to choose that policy which would do the most for economic development--because IDA funds are so limited. The Bank had been able to get all the funds that could prudently be used from the financial markets. Thus, IDA has been confronted with an allocation problem that the Bank had never faced. There is not enough solid knowledge of how best to achieve economic development and there is not enough ability to predict the outcome of various policies. The performance criterion has been designed to help overcome these difficulties. If a country performed well in the past, this augurs well for the future. And if a country has performed poorly but is inclined to improve, IDA funds may be used as an incentive to make improvements. Perhaps IDA could use the performance criterion to show the rich nations that IDA is administering their foreign aid funds well. Just what goals should be established for the performance criterion? Some persons would advocate channeling IDA funds into those places where the most economic development would result. Others argue that institutional and environmental factors must be considered--that is, that IDA funds should go to those countries which are trying really hard. In practice, this debate seems to have been resolved in favor of providing IDA funds for those countries that have tried really hard in the past and for those countries where IDA funds might be used as an incentive for better performance in the future.

The Executive Directors and staff of the International Bank are the Executive Directors and staff of IDA. However, there has been a different interest in IDA proceedings than in Bank business. It was common knowledge that Eugene Black and his staff ran the Bank. The Executive Directors took a perfunctory interest in the loans the Bank made. This has changed with IDA. The Executive Directors are much more interested in the allocation of IDA's relatively scarce funds. The developed countries want to make sure that their foreign aid is being used wisely. The underdeveloped countries want to make sure that they get their share.

IDA's staff is, perhaps, its main asset. The staff has won the respect of both the developed and the underdeveloped countries, which is no minor accomplishment. The author has the impression that the staff is remarkably competent and unusually optimistic about the future of the underdeveloped countries.

IDA has made an important contribution to the techniques of development lending. IDA has enabled the staff of the Bank to make technical assistance available to a number of developing countries. IDA has effectively highlighted the need for a greater soft credit component in development financing. IDA has entered a field of investment, education, which could have enormous consequences.

IDA has not, however, pleased everyone. There are a number of relatively high per capita income countries that resent the fact that IDA is not making funds available to them. There are some poor nations that have not received IDA credits and feel that IDA is administered with political considerations in mind or with favoritism based on the composition of the staff. One economist has expressed fears that IDA will become a "wastebasket" for projects that the Bank could have financed--a clear waste of soft loan money. One economist has argued that IDA has not represented an increase in soft loan money, and is only substituting multilateral for bilateral administration of funds. Some economists would have preferred SUNFED to IDA. Others would have preferred that IDA make loans repayable in local currency. Some countries are critical of the quotas that have been assigned in IDA. There have also been complaints about the requirement that the underdeveloped countries put up part of their subscription in convertible currency and about the system of weighted voting which prevails.

IDA was warmly endorsed by the Swedish Parliament on May 28, 1962, when a supplemental appropriation from the Swedish Government to IDA was announced. The President of the United States has spoken of IDA with approval. It remains to be seen whether the Congress shares the President's enthusiasm, but it must be remembered that it was a member of the United States Congress who got IDA underway. The Governments of West Germany and the United Kingdom have been no more enthusiastic about IDA's replenishment than they were over the establishment of IDA in the first place. They are reluctant to forego the normal return on hard loans, and they are concerned about the budgetary charges which are incurred in providing funds for soft loans. The other developed nations are reluctant to provide soft loan funds and thereby forego a claim on the underdeveloped countries' resources so long as West Germany and the United Kingdom stick to their hard loan policies.

The staff of IDA has presented evidence that the external public debt for 32 underdeveloped countries more than doubled between the end of 1955 and the end of 1961. The service on this debt increased by a factor of 2.5 from 1956 to 1962; as a percentage of export earnings, the service on this debt rose from 3 per cent to 7 per cent over this same period. The total external public debt of the underdeveloped countries was estimated at $20 billion at the end of 1961 and the total debt service was $2.25 billion in that year. Will external public debt double again in the next five years? IDA is convinced that, whatever happens in the next five years, there is clearly a demonstrable need for more funds on a soft loan basis. The United States Government has agreed with IDA's analysis and is trying to get the other industrial nations to increase their soft loans.

Eugene Black proposed that this increased soft loan component in foreign aid be channeled through the International Development Association. Speaking at the 1962 meeting of the Board of Governors, Black indicated that the funds originally entrusted to IDA would be committed by mid-1963. Based on fiscal year 1963, Black estimated IDA's minimum needs at $500 million a year and suggested that IDA be replenished on that basis for a 5 year period. The Board of Governors agreed to have the Executive Directors study replenishment of IDA funds, but no action has yet been taken on definite commitments. The quota problem and the local currency problem have both been interjected into the replenishment discussions.

In addition to Black's proposal, there have been several other suggestions made for IDA's future. There have been proposals that the relative sizes of IDA and the Bank be reversed. There have been suggestions that closer ties with the United Nations should be established. Some persons have suggested that IDA be give the reserve funds of the Bank. It has been proposed that IDA serve as a guarantee fund for Bank loans, and that the developed nations provide the difference in interest between the Bank's interest costs and IDA's service charges. There have been various proposals to extend the duration of Bank loans or to set up an intermediate category of loans--between Bank loans and IDA credits. Several persons have suggested various stabilization and equalization schemes for world commodity prices--which would channel the funds through IDA. The author concluded that it was not likely that such gimmicks would be implemented and that it was to the developed nations that IDA would have to look for funds.

It will be very interesting to see the results of the replenishment discussions. Enough has been made public already, however, to indicate that the International Development Association is going to continue. Enough has been learned of the operations of the Association that it can also be said that IDA will continue to promote economic development by financing sound projects, in very poor countries, in countries that are also near the end of their rope so far as obtaining outside assistance is concerned, and yet in countries that hold out promise for future economic advance.

Conclusions

What light does the experience of the International Development Association shed on the hypothesis that universally applicable criteria can be developed for evaluating development projects? Certainly it has been demonstrated that the Association, employing techniques devised by the Bank, does have a set of general criteria for evaluating projects. It was seen that the Association has general standards for evaluating the direct return on revenue-producing projects. There are some techniques for measuring return on such projects as schools. The Association has some guidelines for evaluating indirect returns from projects, also. The Association has standards for judging the management of public utility-type operations and for measuring the efficiency of state-owned industrial enterprises.

There are, however, enormous problems in evaluating projects. Many problems stem from a lack of basic data in the underdeveloped countries. IDA has developed certain techniques for overcoming these problems. However, the fact that the author did not have access to specific project appraisals--to study the reasons given for selecting one project over another or for rejecting some projects altogether--makes any definite conclusion difficult. If the data had been available, it might have been possible to establish the author's hypothesis. Therefore, we must conclude that the hypothesis was not proven conclusively and that we must wait for more definite proof until such time as additional data are made available.

What of the second hypothesis? Have the first two-years operations indicated that IDA is a significant new approach to foreign aid? Throughout this study, criteria for evaluating IDA have been developed. It has been seen that IDA's funds amount to something like 5 per cent of total foreign assistance going to the underdeveloped countries. If IDA is replenished on the scale outlined by Eugene Black it will have \$500 million per year. If total foreign aid and soft loans continue to increase as they have in the past, IDA will have something like 5 per cent of total foreign assistance and something less than 25 per cent of all soft loans. Could IDA be considered significant, then, on this basis? Perhaps, but there is certainly no <u>prima facie</u> case for such a conclusion. There has been a question raised as to whether even these limited funds represent any real increase in foreign aid. Have bilateral soft loan programs been reduced by the amount of IDA's resources? It is difficult to answer this question but, it is the author's impression that soft loans on a bilateral basis have not been reduced as a result of the establishment of IDA.

We saw that IDA had 52 Part II members by the time the annual meetings ended in 1962. These countries had some 75 per cent of the population of the less developed countries (outside the Soviet bloc). Fourteen of these countries had received IDA credits by September 30, 1962. The population of these recipient countries totalled some 620 million or close to half the population of the non-Soviet bloc underdeveloped countries. So, IDA has touched the lives--albeit somewhat indirectly--of half the people living on the fringe of modern life.

IDA has been able to influence the direction of some capital going to the developing nations so that, at least, there has been a marginal influence on the direction that economic development is taking. The countries that have received IDA credits have had to provide local funds for part of the projects' total cost, so IDA's influence has been larger than the mere size of credits would indicate. And IDA has set the pattern on terms that has been adopted by the United States Agency for International Development and the Inter-American Development Bank's Social Project Trust Fund. Some countries have been helped that would not have qualified for Bank loans and thus the Bank's staff has been able to exert some influence on these countries and lend some technical assistance that would not otherwise have been possible. IDA has effectively highlighted the need for an increased soft credit component in development aid. Continuing pressure has been placed on the developed countries to recognize this need and to do something about it. IDA has also pressured the underdeveloped countries to use the soft loans they have received wisely. One would not think of the International Development Association as a revolutionary institution. Yet it is trying to promote a revolution in the underdeveloped world--in the way they look on public administration, tax collection, highway construction, education--in the entire approach to economic development.

Before this study was undertaken the author had been exposed to a substantial amount of criticism of IDA. Some persons had questioned the ability of a bank to administer funds not intended to earn interest. The author had also heard some persons express the opinion that IDA was completely controlled by the United States Government. On the basis of the findings presented in this study, it appears that the staff has acquitted itself of the charge of "thinking too much like bankers" and certainly the staff tries very hard to function free of outside influence.

The conclusions reached as to IDA's significance would, to some extent, depend on what was expected of the International Development Association. If bold and glamorous innovations were expected--we would be disappointed. If, however, we view economic aid as a long-continuing effort to see that the hungry are fed, the naked clothed, and the homeless sheltered--then IDA was an imaginative step in this direction. This latter view of the role of economic aid is one the author shares. It would, thus, seem that the second hypothesis has been proved. The International Development Association has been a significant new approach in this long-continuing effort.

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