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DEVELOPMENT - General

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Development - General - Correspondence - Volume 1

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AUG 31 2011

WILLIAMS GIBBS
STRICTLY PRIVATE AND
CONFIDENTIAL

September 21, 1948

My dear Alastair:

My letter to you to-day about The Lebanon, leads to my writing to you, on a purely private and confidential basis, about an idea of mine which you may think worth your consideration.

The International Bank is receiving, and is likely to go on receiving, applications for financial assistance from those of our Member States who fall into the category of "under-developped" countries - e.g. Latin-America, The Middle East, India and the Far East.

Very few of them have any ideas at all about how to proceed with a properly integrated and co-ordinated programme of economic development. They all want steel-mills of course; most of them are in foreign exchange difficulties, and it would be a pity if they incurred further foreign indebtedness to service loans, of which the proceeds were to be spent on projects which were not the most suitable to their needs.

We think that a very useful service could be done to these countries if there were some organisations in existence which were competent to advise them about the economic development policy that they ought to pursue, on the priority of the various fields of development within the general development plan, and on the priority of specific projects within each particular field.

For example, we have the case of Iran, who has been tentatively talking to us about a loan of \$25 million to finance the foreign exchange costs of their grandiose Seven-Year Plan. I may say that we have no intention of lending to Iran on anything like that scale, but we have told the Iranians that we are willing to give sympathetic consideration to individual projects which fit suitably into the general pattern of Iranian economic development. We have advised them that, as a first step, they should try and secure the services of some organisation who would help them with their planning on the lines I have mentioned in the previous paragraph. We have suggested to them the names of two organisations which we think might possibly fill their needs, namely (1) Overseas Consultants Incorporated, and (2) The International Basic Economy Corporation. Both of these are American organisations. I do not know if you will ever have heard of either of them. Overseas Consultants is

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c/o Sir Alexander Gibb & Partners
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Colonel Alastair Gibb
September 21, 1948

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a consortium of American engineering and management firms of national reputation, which was formed at the request of the United States Government some years ago to undertake an economic survey of Japan. It consists of eleven American firms, among them is Madigan-Hyland, whose senior partner (Jack Madigan) acts as Consulting Engineer for the Bank.

International Basic Economy Corporation is one of Nelson Rockefeller's creations. They operate mainly in Latin-America, and Nelson Rockefeller has told me that on account of the oil complication they would not be willing to undertake work in the Middle East. I know less about this organisation than about the other, but indeed I know very little about either.

It does occur to me, however, that, as the Bank is an international institution, we might go farther afield than the United States for the availability of services to these under-developed countries, of the kind I have mentioned. It would, indeed, be interesting if some consortium of British consultants could be formed who would be open to take on work of this kind. Or, indeed, is there any reason why a Western European International Consortium should not be formed? My ideas on the subject are all very embryonic, and if you think I am aiming at the moon, then please say so.

The ideal organisation, of course, would be something that could undertake to provide not only technical advice on the economic and engineering aspects of particular projects, but also advice in the financial field, for example, in regard to how the local currency as well as the foreign exchange costs of development projects could best be financed.

Perhaps when you have had time to think all this over, you will drop me a note and let me have your views.

Yours ever,

W.A.B. Iliff

Development

CROSS REFERENCE SHEET

COMMUNICATION:

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DATED:

February 9, 1948

TO:

COMMITTEE ON DEVELOPMENT POLICY

FROM:

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SUMMARY:

"THE DEBT DEFAULT PROBLEM IN UNDERDEVELOPED COUNTRIES"

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Development

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT
WASHINGTON 25, D. C.

June 29, 1948

ADVISORY COUNCIL NOTE NO. 2

THE MOST SUITABLE FIELDS FOR DEVELOPMENT LOANS
BY THE BANK

The widely differing conditions and needs among the Bank's underdeveloped member countries make it impossible to lay down universally applicable policies for the financing of projects in the development field. All that can be done is to indicate some general considerations which must be taken into account in arriving at sound conclusions in any particular case, recognizing that the applicability and relative weight of these considerations will vary substantially from one country to another.

The purpose of economic development is to promote an increase in production, and consequently in real income per capita, in economically underdeveloped areas; this depends basically upon the introduction of capital goods and improved production techniques. The application of capital may take place in any of the various aspects of the economy - in agriculture, mining, public utilities, light or heavy manufacturing industry, etc. The most desirable pattern of development in any particular country depends upon its location, climate, resources, labor force and other economic characteristics. And the specific role of the Bank in promoting development must be determined in each case by those characteristics, in the light of the following considerations:

a) The Bank's loans, by the terms of its Articles of Agreement are confined to projects for which financing through private or other channels is not available on reasonable terms.

b) The Articles of Agreement also provide that Bank loans, except in special circumstances, shall be for the purpose of "specific projects". Specific project loans are considered to include any loan the proceeds of which are available for use only for defined productive purposes; such loans include, but are not confined to, the construction or modernization of specific productive facilities.

c) Because the Bank's resources are very limited in relation to the over-all development needs of its member countries, it must finance not merely isolated projects which, on examination, appear to be soundly conceived and to give promise of repayment, but must rather emphasize those strategic projects which will eliminate bottlenecks in production or will generate increases in production of related goods or in related areas. This means that specific projects submitted to the Bank for financing must be examined not only on their own merits but also in relation to each other and to the world economy.

d) The Bank, as an international financial agency, is particularly interested in projects which will contribute to achieving a balance in world trade.

e) The Bank's Articles provide that "the more useful and urgent projects, large and small alike", shall be dealt with first; the Bank must satisfy this requirement either by financing such projects itself or by helping to promote conditions necessary for their financing from other sources.

In most countries sound and balanced development involves the investment of capital and the improvement of efficiency in three broad fields of production: primary production (in general, agriculture and pastoral occupations), secondary production (mining and manufacturing, including the processing of primary materials), and tertiary production (non-commodity

output, such as transportation and power). It may be useful to discuss these three categories in turn; the discussion below, however, is not intended as an exhaustive analysis of all types of developmental projects which may be appropriate for Bank financing.

1. Agriculture. The worldwide shortage of food, and of certain agricultural raw materials, makes agricultural development at this time a matter of special significance. The food shortage is especially acute in many of the underdeveloped countries. Their productivity in agriculture, as in other fields, is generally quite low, and the possibilities for increased production of foodstuffs through the application of modern agricultural techniques are substantial. Such increased production might be achieved in various ways, depending on specific conditions: a) by expanding arable land through irrigation or reclamation; b) by increasing the supply of agricultural manpower in labor-short areas through immigration or resettlement programs; c) by increasing yields through greater use of fertilizers, pesticides, etc., or through the employment of improved seeds and livestock; d) by improving the efficiency of cultivation through the provision of more modern tools and equipment; e) by using better food processing methods to reduce waste and spoilage; and f) by facilitating the distribution of food products.

Large scale irrigation and reclamation projects may produce very large returns in the form of increased agricultural output and indirect benefits to the whole National economy; but because they generally require a heavy initial outlay which must be financed over a long term, and involve a large measure of government intervention, they are likely to be unattractive to private initiative and capital. Moreover, although in most cases local currency expenditures account for the major part of the financing

required, it is frequently necessary for underdeveloped countries to obtain foreign assistance in undertaking such projects, because of the inadequacy of their capital resources and the pressure of domestic inflationary forces. It is believed, therefore, that Bank financing may be especially necessary and suitable in this field.

Migration programs designed to increase agricultural manpower in underdeveloped countries involve many of the same considerations; extensive government participation and a heavy initial outlay are required and the direct returns are likely to be long delayed and uncertain. The financing of migration programs is discussed further in part 4 below.

The importation of fertilizers, pesticides, agricultural machinery, and similar producers' goods generally involves a smaller initial outlay and provides a more immediate return than the two categories of agricultural development first mentioned. In the long run, therefore, a better prospect exists that such imports can be financed through commercial channels. But at present they are impeded by temporary domestic economic difficulties and balance of payments problems in many underdeveloped countries where the expansion of agricultural output is most necessary. In view of the importance of increasing world food production, and the relatively quick rise in output which can be obtained, under proper conditions, from the use of fertilizers, farm machinery, etc., the Bank must be prepared to meet these needs so far as is possible.

In some countries it may be more efficient in the long run to develop local production of fertilizers, pesticides, agricultural tools, etc., rather than to continue to import those products. Projects for this purpose, and for the improved processing of food products, involve the development of secondary (manufacturing) industry. Some of the considerations relating

to this phase of economic development are suggested in part 2 of this memorandum.

The Bank's policy with respect to financing specific agricultural development projects must be worked out in close collaboration with the Food and Agriculture Organization of the United Nations. The Bank and FAO are agreed that such collaboration can best take the form of informal consultation, at the working level, between the staff's of the two organizations, with a view to determining in as comprehensive a form as possible which projects promise the greatest benefits for the investment required.

2. Mining and Manufacturing. The exploitation of mineral resources of underdeveloped countries, for export purposes, has generally been undertaken at a fairly early stage in the development process. Investment in these fields has been attractive to private capital, and despite the increasingly restrictive policies of many underdeveloped countries with regard to minerals development, it is likely that private financing will continue to be forthcoming in substantial amounts. The need for mineral products is growing, not only in highly industrialized countries but also to supply the expanding industries of the developing countries themselves, while at the same time important present sources of supply are being exhausted or seriously depleted; thus there is a continuous incentive to develop new supplies. Moreover, foreign exchange transfer problems, which are an important deterrent to investment in other fields, are minimized by the fact that a large share of the mining output of most underdeveloped countries is usually exported. Generally, therefore, Bank financing for minerals development, although entirely appropriate where private financing is not forthcoming, is likely to be less necessary than in other fields.

The development of appropriate manufacturing and processing industries is usually an essential aspect of any sound over-all program. But because conditions vary so much from country to country it is difficult to generalize as to the particular types of industrial projects that are most important or urgent for well-balanced development. It is necessary, in the case of any projected industrial undertaking, to weigh its economic soundness in a broad sense of the term - including comparative costs, domestic and foreign market prospects, its potential contribution to the over-all national development, and its general suitability to the resources and needs of the country concerned.

An especially important consideration is the relative weight or priority to be given to different branches of industry, and in general to light as against heavy industries. In many cases, especially where there is an excess rural population lacking industrial skills, and where resources peculiarly adapted to heavy industry are not available, major emphasis should be placed at first on the development of light consumer goods industries. Such industries require a relatively small investment of capital per worker employed, and usually contribute more immediately than heavy industries to raising general living standards. They can often build upon traditional craft skills in the introduction of mechanized techniques. The short-run result of this type of industrialization, therefore, tends to be a relatively quick increase in the output of simple consumer goods, which helps to stimulate further development by increasing the health and efficiency of the population and by providing them with incentives for further production effort.

In many cases the development of heavy manufacturing industries may have to be delayed until after progress has been made in building up

the simpler and more immediately productive light industries. This principle is, of course, subject to many individual exceptions, especially where the world demand situation and the existence of the requisite natural resources make it advisable to establish promptly some particular heavy industry. Since, however, the capital necessary for investment in essential public utilities and other facilities which are not directly remunerative may often amount to as much as two-thirds of total capital requirements, it is usually important to allot the remaining third to enterprises which will employ a maximum number of workers and produce the greatest increase in the standard of living. This argues, in the case of most underdeveloped countries, against a diversion of too much additional capital from light to heavy industries.

The fact that the light consumer goods industries should be given a prominent place in most development plans does not mean, of course, that they are necessarily peculiarly appropriate for Bank financing. To the contrary, the development of consumer goods industries usually does not involve any very large single investment, and such industries tend to produce fairly quick returns. Investment opportunities in this field are likely, therefore, to be attractive to private capital. Accordingly, it is believed that the Bank's policy in respect to the development of consumer goods industries should be designed to encourage maximum investment by private capital. This general policy should not preclude the Bank's financing meritorious consumer industry projects in special circumstances where adequate private capital is not available. Such financing by the Bank may sometimes be required to provide an initial impetus to development before private capital will be attracted.

Private capital is rather less likely to be available in adequate amounts to finance heavy industrial projects, in view of the larger initial investment required, the longer delay in obtaining financial returns, and the greater degree of government initiative and control exercised by most underdeveloped countries in relation to heavy industries. Moreover, because the investment required is so large and the returns are frequently so long delayed, development of heavy industries is likely to aggravate inflationary pressures in the underdeveloped countries unless substantial foreign financial assistance can be obtained. For these reasons the Bank may be an appropriate channel for the financing of heavy industries, where such industries are needed, are economically justified, and are unable to secure private financing. In this field especially, however, consideration should be given, insofar as it may be possible, to anti-cyclical timing of the heavy investments involved, in order to reduce the cost of equipment to the underdeveloped countries and to help stabilize the demand for capital goods exports from the more highly industrialized countries.

3. Public capital projects. The financing of projects in the field of "public capital" - i.e. public utilities in the broad sense, including transportation and communication facilities, port developments, power generation and distribution facilities, water and sewage systems, etc. - is particularly appropriate for the Bank in several respects:

(a) The lack of necessary transportation, power and other facilities in underdeveloped areas constitutes a major obstacle to their development along any lines; conversely the provision of such facilities, by opening the way for investment of capital in other more directly productive fields, is a powerful stimulus to development.

(b) Public utilities form the skeleton of an economy, largely determining its general shape. By assisting in the development of such projects along sound, coordinated lines, the Bank can help to assure a balanced development of the entire area in question.

(c) Because of their monopolistic character and strategic importance in relation to the whole economy, public capital projects are inevitably subject to close planning and regulation, and often to complete ownership and control, by the government. Governmental sponsorship and financing in this field has tended more and more to replace private initiative and investment.

(d) Private interests are often unwilling to finance public capital projects because of the large investment usually required and because the financial returns are likely to be smaller or longer delayed than those from more immediately productive enterprises. The direct return which can be obtained from users of highways or ports, for example, may be quite small or even non-existent; their economic validity derives from the indirect benefits which accrue from them to the economy as a whole. An adequate return on other types of public capital investments (e.g. railways and power projects) may be long delayed pending the growth of a sufficient volume of demand, or may as a matter of public policy be kept at a low rate to maximize the indirect benefits of the project. Finally, returns from such investments are normally entirely in local currency and thus may involve especially difficult transfer problems.

(e) The heavy initial investment and the length of time before returns are obtained also constitute serious obstacles to government financing of public capital enterprises in most under-developed countries. Not only are the foreign exchange requirements for any large public utility

project likely to be quite considerable in relation to the country's resources, but the necessary local currency costs may often seriously aggravate inflationary pressures within the country.

The Bank cannot, of course, finance all public capital requirements of underdeveloped countries. As has been noted, it is estimated that these requirements (if housing and similar facilities are included) may amount to two-thirds or more of the total capital needs of many such countries; most of this total must certainly be obtained from local resources. Nevertheless, it is believed that in most underdeveloped countries the Bank has perhaps its most significant opportunity to contribute to rounded and coordinated development by financing those public capital projects which are most directly and urgently needed for expanded production and more efficient distribution of essential goods.*

4. Specific programs to supplement ERP. Because of the importance of the European Recovery Program, not only to Europe but to other areas of the world as well, the Bank has been examining the possibility of encouraging and helping to finance programs which would not only increase productivity in underdeveloped non-European areas but would also contribute directly to the success of ERP and the restoration of a balance in Europe's economic transactions with the rest of the world. There are two fields in particular in which action of this sort may be possible: (a) the development of sources of supply in non-dollar areas for products now imported by Europe from dollar sources, and (b) migration and resettlement programs.

* Many of the same considerations which make public capital projects especially suitable for Bank financing apply equally to projects for increasing labor productivity through such means as technical training and health programs.

It is clearly of prime importance for European recovery and for the restoration of economic equilibrium in the world to achieve a better balance in the trade of Western Europe with dollar areas, principally the Western Hemisphere. Reduction of the normal flow of supplies from Eastern Europe and the Far East has forced the countries participating in the ERP into an unduly heavy reliance on Western Hemisphere supplies. One method of helping to remedy this situation would be to promote expanded production of essential materials in non-dollar areas for export to the ERP countries. Some efforts to this end have already been initiated.

Several advantages have been cited for projects of this sort: that they would mitigate over-all shortages of foodstuffs and other essential materials, and thus help to ease the general supply situation; that they would, in addition, be an important supplement to the ERP, and would contribute substantially to its success by lessening European dependence on dollar aid; that they would also help to raise productivity and living standards in underdeveloped areas; and finally, that in the long run, if properly devised, they would promote a balanced growth of international trade by fostering a continuing and reciprocally advantageous exchange of goods between Europe and other areas.

Because all these purposes are of interest to the Bank, careful consideration must be given to any promising schemes of this nature. Care must be taken, however, to avoid over-emphasizing transitory factors in international trade. It is hoped that the dollar shortage, which now dominates the world economic picture, may be brought within manageable limits by the end of ERP, and that the economic pattern of international trade will then be determined by more normal economic considerations.

Certainly the Bank should not finance any major development programs, however immediately promising in relation to Europe's short-run dollar problem, unless it is convinced that such programs will make a permanent contribution to the expansion and stabilization of international trade; they should not be undertaken merely as an emergency reconstruction measure to supplement ERP, although the latter aspect may properly give added validity and urgency to projects which in any event are intrinsically sound.

One other consideration should be noted in this connection. The Bank should avoid giving undue emphasis to the development of economies which are auxiliary to those of European countries, in comparison to other underdeveloped economies, solely because of their relationship to Europe. Nor should the production of raw materials for Europe be over-emphasized in the development of these areas, at the expense of a balanced expansion of production in all suitable lines and the development of a broadly-based self-supporting economy.

Action to encourage migration presents very difficult problems, political and psychological as well as economic. The over-all advantages of the great movement of population from Europe to the Western Hemisphere and other areas during the last century - advantages to the country of emigration, to the receiving country, and to the migrants themselves - have been convincingly demonstrated both in theory and by experience. At present, however, the migration process has become considerably more difficult. The new "frontiers" that still exist are generally harder to open. The shortage of shipping hampers any large-scale overseas movement and exchange restrictions present an obstacle to the removal of migrants' possessions, the payment of transportation costs, and the transfer

of remittances. The scarcity of housing and consumer goods, and the inflated prices prevailing, complicate the adjustment of immigrants in their new country. And in many cases trade unions, remembering the unemployment of the 1930s, have opposed extensive immigration.

Nevertheless, for many underdeveloped and underpopulated countries, notably in Latin America and Africa, immigration offers the most immediate hope for acquiring additional manpower to develop their resources, and especially for obtaining a variety of skills and experience. And for some overpopulated countries, such as Italy, emigration is an economic necessity to relieve unemployment, to reduce the volume of food and other imports required, and to obtain foreign exchange through the medium of remittances.

Because of the complex political and economic questions involved, over-all arrangements must generally be worked out directly between the countries involved (or by interested governments with the International Refugee Organization), covering the selection of migrants, the allocation and payment of transportation and other costs, and the conditions governing resettlement, employment, remittances, etc. It is believed, however, that the Bank, because of its broad concern with the economic problems of both overpopulated and labor-short areas, should consider how it can best facilitate these arrangements and to what extent it may be able to provide the funds necessary for their success.

The costs of migration from Europe to underdeveloped countries, for which some international financial assistance may be necessary, include the following:

(a) Transportation - The cost of initial transportation to the port of embarkation is relatively slight, and in most cases would constitute

no serious burden on the country of origin. Overseas transportation, however, is much more expensive and may involve considerable foreign exchange.

(b) Subsistence, training, and other expenses during the period of readjustment - For some time after their arrival in the new country the immigrants will not be fully productive, and will either have to support themselves from their own savings (which will involve a transfer problem) or be supported by the country of immigration (which will cause a temporary drain on local supplies and accentuate inflationary pressures).

(c) Initial remittances - It may sometimes be necessary to provide for remittances to support dependents remaining in the country of origin even in the period before the immigrants become fully productive. Any such remittances would accentuate short-run balance of payments difficulties in the country of immigration, and some provision may be needed to meet this problem.

(d) Productive capital - To ensure success of any migration program it will be necessary to make available some capital goods to enable the immigrants to produce effectively. Such goods may include agricultural tools and machinery, livestock, industrial equipment, etc.

(e) Public improvements - Migration programs which involve a large-scale movement of immigrants into an underdeveloped country may create a need for additional permanent improvements, such as housing, health and sanitation services, and so on. These improvements will involve expenditures both in foreign exchange, for raw materials and equipment, and in local currency. Some external help may be required even for the latter portion if domestic savings are insufficient.

The first three items noted above might involve short-term financing; for the last two medium or long-term credits might be appropriate.

Participation in the organization and financing of migration and resettlement programs would involve substantial operational problems for the Bank, and arrangements would probably have to be worked out individually to meet the needs of each separate country. However, the long-term economic benefits which would accrue, both to overpopulated countries in Europe and to labor-short underdeveloped countries, make it important that the Bank continue actively to explore the possibilities of assisting in such programs.

Development

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT
WASHINGTON 25, D. C.

June 29, 1948

ADVISORY COUNCIL NOTE NO. 3

EXTENT TO WHICH THE BANK SHOULD TAKE AN ACTIVE
ROLE IN ASSISTING ITS UNDERDEVELOPED MEMBER
COUNTRIES TO SOLVE THEIR DEVELOPMENT PROBLEMS

Effective action by the Bank in the field of development has been hampered by the lack, in many underdeveloped countries, of clearly defined development objectives or adequate plans for their attainment. Many of the projects submitted to the Bank have been isolated enterprises, unrelated to any program for the balanced, coordinated development of the various phases of the applicant country's economy. Investigation has shown some of them to be inappropriate for the country in its present stage of development, or to be less urgent than other undertakings which are not yet planned, or to require supplementary investments, which have not been taken into account, in order to obtain the anticipated benefits. Although the lack of an adequate over-all program will not necessarily prevent either substantial useful development or Bank financing of meritorious projects, it is nonetheless likely to result in insufficient, spotty and sometimes wasteful investment, often determined by the special interests of particular economic or political groups rather than by the real needs of the country or the most efficient use of its resources.

Development in many countries is also hampered by financial instability, resulting from unsound fiscal and monetary policies and inadequate machinery for taxation, mobilization of capital, exchange controls, etc. In such cases, the Bank can have no assurance that any loan

it may make will be productive, or that there will be reasonable prospects for its repayment, unless effective steps are taken by the country concerned to remedy these conditions.

It thus appears that the extent of the contribution which the Bank may be able to make to the development of its member countries will depend, to a large extent, upon their own action in formulating an appropriate over-all development program and in working out the economic and financial measures necessary for its accomplishment. Many of the underdeveloped countries, however, are lacking in the technical and administrative resources necessary for these purposes; indeed, in the absence of outside technical assistance, the very countries most in need of financial aid from the Bank will often be the ones most seriously handicapped in obtaining such aid. It would seem, therefore, that the Bank, if it is to realize its full potential in the development field, must take an active interest in assuring that the requisite technical help is made available to those of its underdeveloped member countries who need and want such help. Any other policy would limit the Bank's role merely to passing upon the merits of individual loan applications as they are received; under existing circumstances, this would mean that the Bank would be forced either to reject a very large proportion of the applications which come to it or to take decisions on the basis of inadequate information and analysis.

The Bank clearly cannot, by itself, provide all, or even a major share, of the external technical assistance that is required by its underdeveloped members. Such assistance will have to be sought largely from independent consultants and private enterprise; in appropriate cases, too, assistance may be secured through inter-governmental

arrangements or from other international organizations, such as the United Nations, the International Monetary Fund and the Food and Agriculture Organization of the United Nations. The Bank can, however, play a constructive role by helping its member countries to secure technical assistance from these other sources and by consulting with its members from time to time concerning the general pattern of their development programs and concerning the economic and financial policies necessary for the success of such programs. The Bank would appear to be in a particularly good position to be of help in these connections, not only because it has no selfish interest to serve and thus is recognized to be objective in its approach, but also because, as one of the principal sources of international financing, its advice is apt to be persuasive.

Some underdeveloped countries have already turned to the Bank for technical assistance, and it may be anticipated that the number of requests for such assistance will increase in the future. However, the need for a coordinated development program, and for technical help in formulating such a program, is not always recognized; and frequently a good deal of time and effort is expended unnecessarily in making plans for individual projects which will not fit into a balanced program. Accordingly, the Bank has emphasized that any member desiring a loan should consult informally with the Bank before submitting a detailed loan application for the financing of specific projects, in order to permit the Bank to get a general picture of the basic needs and assumptions which underlie the applicant's plans.

In offering to furnish advice to its underdeveloped member countries the Bank must, of course, avoid any gratuitous interference in the internal affairs of those countries, or the assumption of financial or other commitments which it cannot fulfill, or too deep involvement in

the details of a particular program. The extent and nature of the assistance which the Bank can and should offer will vary widely from country to country, depending upon the differing conditions in each case; an empirical approach seems clearly necessary. Nevertheless, there appear to be certain general principle which may be used as guideposts.

1. Insofar as possible, in the light of its other responsibilities, it would seem that the Bank should be prepared to undertake, if asked to do so, a broad investigation of economic conditions in any underdeveloped member country. This should provide the basis for general conclusions as to the development needs and possibilities in that country, the principal obstacles to development, and the internal measures required to overcome those obstacles. Such a survey would not go into the details of specific development projects but would be confined to over-all economic conditions and policies.

2. It also seems appropriate that the Bank should encourage its member countries to establish suitable machinery, where it does not now exist, to undertake or coordinate comprehensive surveys of development possibilities within the country, to establish priorities for development projects to be undertaken under governmental auspices or with governmental aid, to work out appropriate sources and methods of financing, including both domestic and foreign capital, to propose measures to encourage private investment in constructive enterprises, to review the nation's economic and financial policies and propose revisions needed to promote development, and so on. Where necessary and desirable, it would appear that the Bank (acting to the extent possible in cooperation with the Fund) should be willing to advise with the government of the country concerned on the ways and means by which

such machinery might best be established.

3. It would also seem that, upon request, the Bank should be prepared to assist member governments in mapping out the general contours of a constructive program of economic development, including necessary improvements in the country's financial structure as well as additions to its productive capacity, and providing for measures to encourage private investment as well as for government-financed projects. The Bank should not, of course, attempt to impose a particular conception of development on any country. Any development program, if it is to have the necessary popular and governmental support, must emerge from the thinking of the responsible leaders of the country itself. The proper role for the Bank would appear to be to provide impartial counsel and, if possible, to stimulate and crystallize local thinking and action, official and non-official.

4. The Bank itself is in no position, and could not, without creating an unduly large and unwieldy staff, put itself in a position to provide extensive aid in working out the details of the development programs of its various underdeveloped members. Moreover, it would seem unwise for the Bank to get involved too deeply in the detailed planning of any particular country, or in the measures taken to implement those plans, for the Bank might thereby be put in the position of assuming at least moral commitments inconsistent with its international interests and obligations. It seems clear, however, that the Bank should be ready to recommend, upon request from any member country, qualified independent experts in the fields of agriculture, engineering, finance, taxation, etc., who could provide the assistance required by the local government

in working out the details of its program; and in certain special cases it might be appropriate for the Bank to consider a loan to finance the external cost of such assistance.

5. After the general outlines of a development program have been formulated, it would seem proper for the Bank to offer to consult periodically with the government regarding the progress made and the problems encountered in carrying out the program, and the alterations that may be required to meet changed conditions.

The granting of loans by the Bank need not, and normally should not, await the formulation by the borrowing country of an over-all development program or the adoption by it of all the economic, financial and administrative measures which may appear necessary for the success of the program. To the contrary, financial assistance from the Bank may form part of an integral plan for the long-range development of the borrower, and in most cases it should be possible for the Bank to select particular meritorious projects for financing concurrently with the initiation by the borrower of the other steps involved in such a long-range plan. Furthermore, as the general shape of the borrower's development program emerges, the Bank should have constantly in mind the selection of additional projects, public or private, which appear especially suitable for Bank loans.

The Bank cannot hope to overcome, through its own efforts, the deficiencies in technical background, administrative efficiency and political and social organization which exist in many underdeveloped countries. Nor can it assure that those countries will themselves adopt the policies required to remedy these deficiencies. But by taking a positive approach,

along the lines indicated in this paper, to the problems of those of its underdeveloped members who need and want the Bank's advice, the Bank may be able to help them substantially to accelerate the pace of their economic advance.

March 1, 1948

Local Currency Loans for Development Purposes

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The general heading "Local currency loans" may be misleading, as it covers two kinds of financial transactions:

- (1) Loans of foreign currency to finance expenditure in local currency.
- (2) Loans in local currency only to be used exclusively for internal purposes.

Though the second group of loans is perhaps not quite as uninteresting as it appears, the first one is, of course, by far the more important. It was traditional in times of freely convertible currencies, but has now largely been replaced by a new type of loan, to be used outside the borrowing country, for the purchase of specified items, mainly of raw materials and capital equipment. In addition, loans are discussed for the purchase of capital equipment only. This development seems, at first, fully justified by the shortage of hard currencies, and the resulting necessity to husband carefully scarce foreign resources for their most obviously productive use. After further study, however, the underlying policy may well appear insufficiently realistic to allow for a successful solution of development problems.

When a country starts a development program, the claims on its existing national resources rise. The resulting inflationary pressures are described in another paper. To appreciate fully their extent, it might be useful to remember that normally two-thirds of the total capital to be created must necessarily come from internal labor and materials. This covers mainly such items as buildings and earthworks, but even some simple equipment may be with advantage produced locally from existing facilities. In the process, skilled local manpower receives new occupations, while unskilled population of active age, formerly in open or disguised unemployment, is offered work. Resources are thus diverted from the

consumption goods output^{1/} at the very time when new incomes are distributed.

To keep in check inflationary pressures, if foreign loans are entirely earmarked for raw materials and equipment, taxation and borrowing will remain as the only means at the disposal of the government, and both are likely to be inadequate. High rates of direct taxation are technically difficult to achieve in an underdeveloped country. If, however, they are successfully enforced, they will reduce incentive to work when it would be most necessary. On the other hand, borrowing on the domestic market may often prove to be impossible. But even in the cases where savings are available in some volume, their redistribution, largely in the form of salaries, will not relieve the pressure on consumption goods. If it is assumed, however, that inflation in a development program is inevitable (which may be true to some extent), then the rise in prices will lower real incomes and reduce claim on consumption goods. But, in underdeveloped countries, real incomes of the bulk of the population are already at or below subsistence level. Any attempt to cut real wages still further would hardly be compatible with the preservation of political stability.

Indeed, in a democratic environment, consumption cannot be much reduced from existing low levels, and the additional work required for investment must, to some extent, be rewarded by additional tangible goods. In the first stages of development, at least, these additional rewards can only come from abroad. Even merely to maintain the former standards of consumption, increased foreign exchange resources would be necessary, as some of the exports, that used to pay for consumption goods could no longer be maintained, while some of the domestic supplies, as a result of the shift towards equipment, would disappear.

^{1/} Or from the necessary increase in output of consumption goods.

Foreign loans, earmarked entirely for purchases of "producers' goods" are clearly insufficient in bridging the gap between claims and resources in the early development period. Only very ambitious borrowers and very confident lenders could, it seems, overlook this fact.

The effects of a loan in the traditional sense, freely convertible usable anywhere and for any purpose are quite different. Domestic savings, in the recipient country, are supplemented by the countervalue of the foreign exchange borrowed. Part of the money earned in development work may enable its holder to purchase abroad. The incomes distributed are thus real incomes, not nominal receipts to be later annihilated by shortages, taxation, and/or inflation. No excessive drain is put on growing capital markets by government borrowing. "Non-essential" consumer goods will, no doubt, be imported along with equipment, but they cannot, it seems be really considered non-essential if they provide the only tangible incentive to work in a politically stable environment. In conclusion, it seems that some proportion of the loan (say 20%) could advantageously be allowed for purchases of consumption goods.

Apart from their general anti-inflationary effects, foreign loans spent in local currency appear useful in many specific instances. Stabilization loans are one case in point. Loans for promoting immigration, solving at the same time the internal problem of investments in housing, and the external problem of remittances may also usefully take this form. In any case, end use supervision of such a loan will offer a view of the over-all import programme of the country, and not only a detailed but limited supervision of expenditure in foreign exchange, up to the amount of the loan.

Loans of foreign currency to finance local currency expenditure are a combination of currency loans, and free foreign exchange loans. They appear thus as a flexible means to solve development problems of many countries, the proportion

to be spent on equipment being fixed at different levels, according to the domestic situation in the country concerned.

Loans in Local Currency Only

It certainly seems odd for a government to be in need of foreign help to obtain its own currency. This, however, may be the case in underdeveloped countries where available savings are small, and where governmental ability to enforce a difficult fiscal policy is questionable. Two procedures can be envisaged for IBRD loans.

- a) Loans from the members' 18% subscription in its own currency.
- b) Loans issued internally by the governments concerned with an IBRD guarantee.

In the first case the influx of money released from hitherto idle IBRD balances will, of course, have quantitatively the same inflationary effect as a creation of new money. In the second case, on the contrary, genuine savings, where they exist may be tapped. The main advantages, if any, of both types of loan seem to be psychological and political. They may free a politically weak government from the necessity to wage a fight for increased taxation resources. They may psychologically help to avoid the effects of open inflation, or of unsuccessful borrowing. Further, from the point of view of the domestic investor, the fact that the Bank will share his interest, following and to some extent influencing the financial policies of his Government, should not prove indifferent, and should allow for reduced interest rates.

What about adverse psychological effects? e.g. govt is not strong enough to raise its own funds; ∴ currency must be weak.

A DRAFT NOTE

ON

THE FUNCTIONS OF GOVERNMENT IN NATIONAL DEVELOPMENT POLICY

(Prepared by the Secretariat)

This Draft Note is strictly provisional and does not express the views either of the Secretariat or of any organ of the U.N. It is also subject to further review and amendment in the Department of Economic Affairs. It is presented to the Sub-Commission merely as a Draft Working Paper.

SUMMARY AND ISSUES RAISED

(1) The attached Paper is in the nature of a Background Paper for the Sub-Commission on Economic Development. Its purpose is to throw up specific points for discussion which may clarify the place of government policies in economic development and lead to recommendations on the subject. The paper does not represent either the considered view of the U.N. Secretariat nor does it even claim to be a statement of policy on the subject. All it attempts to do is to put before the Sub-Commission a tentative formulation of some of the main issues as they appear to the Secretariat at present.

(2) It will be noted that this Paper has been made as general as possible. Each individual country has its specific problems, and even among those which are common to all or many, emphasis varies considerably from country to country. This paper attempts a synthetic study; no individual country is specifically discussed. In view of the great diversity of conditions in different countries, the discussion of development problems as affecting individual countries or groups of countries must be taken up after the general ground has been covered.

(3) The main issues which arise from the discussion in the Paper are summarised below:-

I. Ignorance of resources - natural and others is stressed as a retarding factor in development. The issue is raised as to: What is the proper place of government policy in making known and analysing the developmental prospects of the various types of resources, and what are the possibilities of international cooperation in this field? (Para. 3).

II The view is expressed that the patient laying of foundations from the very beginning is just as important as the launching of spectacular plans and projects. Is there danger that the less spectacular aspects of development policy be neglected? (Para. 4).

III. How can a development country be knit together into a closely integrated national exchange economy? The development of transport communications by governments could play an essential part in this process. Governmental policy in the field of power provision is also instrumental in creating a climate and determining the lines of economic development. The issues raised and how much of the resources and attention of national governments should go into these fields, and which is the most suitable combination of types of transport and power facilities? (Para. 5)

IV. Deficiencies of capital and know-how are among the main bottle-necks in industrial development. Several lines of policy are open to governments in breaking them. The issues arising are: In what proportions should the required capital be provided from domestic and foreign sources? What are the relative advantages of government and private borrowing? What forms of organisation of technical advice are suitable for development countries? (Para. 6.)

V. The idea of "balance" in development has many aspects - diversification, industrialisation, establishment of key industries. Issues raised include: Which are the "key" industries which development countries need? Should it

be a general rule for development countries to avoid monoculture? To what extent is the exhaustion of natural resources defensible? How far is a country justified in subduing other considerations to the pursuit of a system which offers a broad front to economic progress? What is the role of government in resolving these issues? (Para. 7).

VI In the final resort, success or failure of development policies hinges on the productivity of the new branches of production and projects. What can governments do to safeguard and improve productivity? What standards of measurement are appropriate? Which is the right stage of technique at which development countries should come in? (Para. 8).

VII Economic development is apt to create peculiar balance of payments difficulties and the set of possible government measures to cope with them is described. This raises the issues of: What is the right commercial policy for a development country? What is the position of development countries under the I.T.O. Charter? Which is a typical sequence of balance of payments situations through which a country passes in the course of economic development? (Para. 9).

VIII. Development will create a potentially inflationary condition. Various alternative remedies are considered. This raises the issue of what constitutes a proper monetary and fiscal policy for a development country? (Para. 10).

IX. A desire for economic independence is universal among development countries. The sources of this desire are analysed. Issues raised are: In such desire necessarily harmful to international trade? What can be done by international measures to make economic interdependence appear less risky in the eyes of development countries? (Para. 11).

X. Governmental development programmes vary in scope, methods of preparation, degree of detail, relationship of means and ends, and "status" of the published targets. Various cross-classifications of development programmes are attempted - Issues arising: Is there any possibility of international standardisation of forms and methods of publication of development programmes? Is there any general technical advice which could be given on the methods of preparation of such development programmes? (Para. 12).

XI. How far the state should itself be the executive organ in the execution of the development projects is partly a question of principle and political philosophy. Various arguments, specially applicable to development countries are further considered which affect the choice of state versus private enterprise. Issues raised are: Can state operation of plants in development countries prevent the growth of private power positions? What are the alternative pricing policies for state-operated plants, and what are their economic effects on development? (Para. 13).

LIST OF CONTENTS

- Survey and intelligence. (Para. 3)
- The laying of foundations for economic development. (Para. 4)
- The creation of an economic climate suitable for development. (Para. 5)
- The breaking down of bottlenecks and specific impediments to economic development. (Para. 6)
- The provision of economic balance. (Para. 7)
- Improvements in productivity. (Para. 8)
- Protection of Balance of Payments (Para. 9)
- Internal Monetary framework for the orderly progress of development. (Para. 10)
- Reduction of economic dependence. (Para. 11)
- The publication, under government auspices, of a development programme consisting of an inter-related set of target figures. (Para. 12)
- Execution by the government itself of a more or less comprehensive and more or less co-ordinated system of measures for the development of their national economy. (Para. 13)

FUNCTIONS OF GOVERNMENT IN NATIONAL DEVELOPMENT POLICY

1. The present situation may be described as a state of acute awareness on the part of undeveloped countries focussed in their national governments, of their under-privileged position and an urgent desire at least to attempt development programmes under government auspices. This state is made up of the ingredients of improved knowledge of other countries' conditions, improved knowledge of their own condition, a sharpened social conscience, experiences of wars and depressions, the groping towards new forms of international co-operation, the abandonment or weakening of laissez-faire philosophies, the spread of rationalist and activist attitudes, and finally new developments in economic thought. In this paper, however, we shall not try to trace the growth of this awareness but shall assume that awareness of backwardness has become focussed in a national government with an activist desire for improvement.

2. What then are the lines of policy open to such a government? The various measures which could be taken and are in fact taken are of infinite variety. They can however, be grouped into classes or categories of measures as follows:

- a. Survey and intelligence.
- b. The laying of foundations for economic development.
- c. The creation of an economic climate suitable for development.
- d. The breaking down of bottlenecks and specific impediments to economic development.
- e. The provision of economic balance.
- f. Improvements in productivity.
- g. Protection of balance of payments.
- h. The creation of a monetary framework for the orderly progress of development.
- i. Reduction of economic dependence.
- j. The publication, under government auspices, of a development programme consisting of an inter-related set of target figures.
- k. Execution by the government itself of a more or less comprehensive and more or less co-ordinated system of measures for the development of their national economy.

There are other ways of classifying government policy in the field of development. All that is claimed for this classification is that it may provide a convenient list of headings for a brief separate analysis of the different types of government measures.

3. Survey and Intelligence: It is inherent in the condition of undeveloped countries that there should be a considerable element of ignorance of the available resources. Such lack of knowledge can be traced to two sources: (a) lack of a suitable organization for collecting and collating information, and (b) conditions which make the collection of information specially difficult. Under (a) we may note that the organization of current economic statistics, is a very late development and one which has presented in the past and is still presenting considerable organizational difficulties even in the advanced industrial countries. It is, therefore, neither surprising nor discreditable that there should be serious gaps in the available information on the resources of development countries. It also stands to reason that the undeveloped countries have generally a less tight system of state administration and that the collection of economic intelligence in all countries has usually been - at least at its start - a by-product of state administration.

Under (b), among the conditions which make the collection of information specially difficult we may notice: a lack of literacy among the population in many development countries which makes form filling more difficult or impossible, a population which is often widely scattered over a sparsely populated large area, lack of development of transport system which make some regions difficult of access even for the purpose of collecting information, the cost of large-scale census inquiries etc. All these difficulties apply more specifically to the collection of information regarding the human and capital resources - such as data on occupational grouping of population, equipment used on farms, available skills etc. - and less so to the collection of information regarding natural resources - such as mineral resources, water resources etc. All the same, in many development countries there is very scant evidence even regarding natural resources.

In this field, we may note the presence of a vicious circle at work. Lack of previous development has made it seem unnecessary to survey and prospect the available natural and technical resources, and the absence of knowledge of availability of natural resources in turn has tended to retard development. The improvement of knowledge in this respect is, therefore, much more than mere stock-taking - essential though this is as a basis for sound economic plans; surveying of resources may in itself be an active element in a development programme in so far as it helps to break one of the vicious circles preventing development. Knowledge of resources will suggest ways of developing them. Among the resources in development countries, natural resources evidently play a much larger part relative to human and capital resources - specially to the latter - than in advanced countries. There are no general grounds for assuming that development countries are less richly endowed - in proportion to area - with natural resources than the more advanced countries. It is true of course, that many of the industrially advanced countries are so because of important natural resources, specially of coal. As against that, however, we must set the fact that the natural resources of the industrial countries have for some time past been subject to much more extensive exploitation.

4. Laying the foundations: Economic development is not something which proceeds in vacuo but it has to rest on certain foundations without which it will be, at best, an unstable structure. Many of the measures of government policy which come under this heading are also valuable in themselves (apart from economic development) and a normal function of modern government, but at the same time they are also an essential part of any government programme of economic development. Indeed, since some of these measures seem so much

a part of the normal business of government there may be a danger that governments intent on accelerating economic development may neglect this class of measures since its close relation to economic development may not be immediately obvious. Among those measures the most important are the improvement of education standards and the spread of literacy, the improvement of health services, the breaking down or softening of social or religious customs antagonistic to technological development, the establishment of internal safety, law and order.

Modern agriculture no less than modern industry or services require the availability of alert labor with a basic understanding of machinery. It may sometimes be possible to provide such a labor force by processes of specific training on a scale sufficient for the earlier stages of a development programme. In the long run, however, the only workable method is to have a current supply of the type of intelligent labor required available naturally as it were, as a normal product of the educational system of the country. Even more important is educational progress in respect of the supply of technicians and engineers required. Even where initial development can be started with the help of foreign technicians, a supply of national technicians is usually an essential condition for taking up and carrying on the original impetus. Even where the specific training of professional people, specially technicians, may be done at foreign universities or institutions, the supply of suitable candidates for such foreign training may still raise problems of educational improvement within the country itself. At the very highest level of scientific research and discovery we may assume that in general development countries - except perhaps for the unprogrammed "flash of genius" - will more depend on free access to progress in the more advanced countries than on developing their own facilities. To this last statement there is, however, an important exception in that the adaptation of techniques developed in the more advanced countries to the peculiar climatic, labor transport and capital conditions obtaining in development countries will usually be neglected in those advanced countries, and may be a useful field for governmental activity by development countries in the field of higher education and research (and also, we may note in passing, a useful field for international action).

The improvement of health services is also essential for the raising of productivity and development of industries in many countries. There is a well-known vicious circle at work. Low health is due to the absence of proper nutrition which in turn may be due to the absence of agricultural machinery which in turn may be due to low productivity of labor preventing the accumulation of capital which in turn may be due to poor health. The breaking of such vicious circles by the development of health services may in the end be a more productive contribution towards industrial development than the direct promotion of specific projects. The improvement of nutritional knowledge, including the suppression of narcotics is another essential requirement for industrial development in a number of development countries.

The devising and maintaining of a proper legal system is also of great importance for the economic development of a country. To mention a few important examples, systems of land tenure and inheritance laws have an important bearing on agricultural developments, property rights in sub-soils and mineral deposits determine the amount of surveying and prospecting for natural resources going on. The maintenance of lawful and orderly conditions is an essential pre-condition for the influx of foreign capital, and by reducing the risk of investment and keeping the rate of interest low it also

has a direct bearing on the rate of industrial development. Well-ordered labour relations also bear directly on productivity.

In all these respects, government has (and always had, even under laissez-faire philosophies) an essential part to play in a field where there are no other agencies at work. We may repeat that the fulfillment of their essential duties in laying the foundations of economic developments may be a more useful service than the formulation of specific development projects. The danger is that the patient laying of foundations may be neglected as being less spectacular than the formulation of plans and the launching of projects.

5. The next group of measures were listed under the heading of creating an economic climate suitable for development. As the classical economists explained (stating a truth which is still very important to development countries), productivity depends on division of labour, and division of labour in turn depends on the existence and size of an exchange market. Many development countries lack the primary requirement of an integrated exchange market covering their whole rational territory or at least important regions of it and knit together by transport and communication services. We may distinguish three separate features to explain the absence of a sufficiently large exchange market; the discussion of development problems has often been confused by not distinguishing them clearly.

(a) Since many development countries are primarily agricultural a high proportion of the national output by-passes the exchange market and is home-consumed on farms. This is a natural phenomenon which applies to agriculture in the industrialized countries as well. It is, however, arguable that the absence of market facilities leads to an excessive development of subsistence farming and that in some cases developments in the direction of cash farming would increase agricultural productivity. The absence of cash farming is also sometimes related to the lack of development of an agricultural credit system, or to high rates of interest charged for agricultural credits.

(b) The monetary system may be so ill developed or so strongly distrusted that whatever exchange takes place is largely on a barter basis. Barter exchange is demonstrably inefficient and tends to limit the total volume of exchange transactions taking place. Hence the development of a trustworthy and universally accepted monetary medium is a further essential step towards the creation of a sufficiently large exchange market.

(c) Lack of transport and communications prevents economic transactions between the different parts of the country or region, and more particularly between towns and countryside. The main remedy for this deficiency clearly is the improvement of transport and communications which in some countries may probably be defined as a primary requirement for further economic development.

If the creation of a unified national exchange market represents an essential part of the economic climate of development it will be seen from the preceeding analysis that it requires much more than just the improvement of transport facilities. The latter is, however, an integral part of development, and the government role in the development of transport may be characterized as follows:

- a Capital expenditure per person employed in transport services tends to be specially heavy, higher even than in manufacturing industry. Thus transport development tends to absorb a heavy proportion of developmental capital expenditure, specially in the early stages.

- b. Transport development under governmental auspices has an advantage over uncontrolled private development in that it can avoid wasteful competition, and create a co-ordinated system of air, rail, road and water communications.
- c. Developmental transport improvement can be creative and anticipatory and not of a strictly commercial nature. Commercial transport improvement caters for an already existing demand; creative transport improvement is one which is not only based on a future anticipated higher level of demand but which by the transport development itself creates a demand for these services, as a result of new economic transactions taking place. This is essentially a governmental task since to private enterprise anything going beyond commercial transport improvement is extremely risky although some advanced countries provide examples of private creative transport development.

Apart from the creation of exchange markets, the other ingredient of a suitable economic climate for economic development is the provision of power. Just as the classical economists stressed the exchange market as the starting point of development, so they will know that economic development did, in fact, start in countries with a favourable power basis. At the time this mainly meant the possession of coal resources. Now, however, the provision of power is no longer tied to domestic coal resources. Not only have some countries managed to achieve high degrees of economic development entirely on imported coal - Sweden and Switzerland are useful examples - but also oil and water have become prominent as important sources of power. The development of water resources in particular holds important prospects for development countries as a source of power. The provision of power facilities - especially of hydro-electric power - shares with transport the characteristic of high capital intensity. A large initial capital investment is required, and this, together with the unpredictability of demand, the possibility of "creative investment", and the key nature of these installations in economic life all combine to make this a likely field for governmental activities.

The provision of power shares with the provision of transport facilities the feature that its beneficial effects are widely diffused throughout the whole economic and social structure, and not confined to purely industrial development. The provision of electricity on farms makes possible the introduction of farm machinery and raises the whole level of rural life, electricity, through the introduction of wireless sets, is an important part of educational progress, it makes possible an improvement in health standards etc. There is also of course, a mutual relationship between the provision of transport and power. The development of power resources open up new transport facilities and vice-versa. These two measures have the dual advantage that their effects are diffused, and also that they are non-specific, i.e. they do not commit the developing country to any specific type of project or line of development. This last is a great advantage specially in the early stages of development.

Development of water power displays a further special feature in that it is often best undertaken not as an isolated measure but as part of a multi-purpose scheme which also includes improvements in irrigation, navigation, flood control and other subsidiary purposes. To illustrate the close inter-relation between the different aspects of development it may be mentioned that in some cases - specially in the Middle East - the development of irrigation has created serious new health problems.

6. The next group of developmental measures may be defined as the breaking down of bottlenecks. The specific bottlenecks holding up development - as distinct from general obstacles - are varied between the different countries but there are some which are of almost universal application. Among such we may mention a lack of capital, and a lack of technical knowledge. In both these field, governments have opportunities for assistance.

The provision of capital may take place either from abroad or domestically through a reduction in home consumption. Where the second method is chosen, the government of a development country will have to provide for the requisite reduction of home consumption by methods of fiscal policy combined with wage and for profits controls, prohibitions on luxury expenditure etc. This, however, is the more negative aspect. In general, it will also be incumbent on the government to see that the resources thus diverted from consumption are actually invested in capital goods. This involves, first of all a full employment policy to make sure that the resources set free are not wasted in unemployment; but secondly, in the conditions obtaining in development countries, it also often involves the actual provision by the government of facilities for the domestic production or importation of capital goods. Here again, measures of normal fiscal policy may be sufficient to tilt the balance from consumption goods industries to capital goods industries, but in other cases the government will have to provide the physical facilities directly.

In many other cases, the capital will have to be provided from abroad, partly because home consumption is so low that it cannot be further restricted, partly because the technical know-how required for the production of capital goods does not exist inside the country, and partly because the scale of requirement may be too small to serve as the basis for an efficient home industry. In such cases the role of government consists in the following measures, concurrently or alternatively: (a) to achieve an export surplus or in other ways acquire sufficient foreign exchange to import the capital goods required, (b) to limit other less essential requirements of foreign exchange in order to import capital goods, (c) to negotiate and arrange for foreign credits, either with international bodies or foreign governments or corporations, (d) to facilitate contact between private national borrowers and lending agencies abroad, (e) to create conditions of domestic stability making it attractive for foreign investors to lend. The main measures which the government could take to attract foreign capital could again be subdivided into creation of general security of foreign capital, specific guarantees for capital borrowed and direct borrowing by governmental agencies.

The advantages of government borrowing as distinct from private borrowing are: (a) Certain agencies, specially lending governments, are precluded, either constitutionally or practically, from making loans to borrowing agencies other than governments or government controlled institutions.

(b) Government borrowing takes place in larger blocks than private loans. Governments therefore, have access to sources of large-scale financing which might not be accessible to a multiplicity of smaller firms in development countries. Government functions in this field may best be defined as achieving the economies of pooling in borrowing; these economies may be important.

(c) Government debts are backed by the additional security of the country's revenue and general economic prospects. Thus, they often carry a lower rate of interest than private debts.

(d) There is also the additional factor that government-controlled and financed development is less risky if it proceeds as a balanced development scheme where each part tends to support the other. Isolated private projects are more liable to failure and, therefore, more expensive to finance.

(e) Governments may be able to obtain better terms by introducing political factors into the loan negotiations. Other countries may be specially interested in raw material supplies or for other reasons - political or economic - want to promote the economic prosperity of the developing country. In such cases a government may be able to obtain loans at better than strictly economic terms.

These factors taken together represent a powerful set of reasons why governments in development countries have tended to play an active part in the provision of foreign capital for their countries. An additional reason is seen in the fact that foreign capital movements are an important factor in countries' balances of payments - in development countries more so than in more advanced countries - and for this reason governments, specially if they maintain exchange restrictions in any form, inevitably have to take an interest in foreign borrowing.

The second major bottleneck in economic development, apart from the deficiency of capital, may be seen in a deficiency of knowledge and initiative, both entrepreneurial and technical. In both these fields government policy has been active. In the entrepreneurial field the government can either stimulate or else replace private initiative. Stimulation of private initiative may take the form of taxation privileges (including tariff privileges), the rendering of free or cheap services to enterprise by government agencies (such as preferential transport rates, or free prospecting and surveying by government departments, cheap power, market surveys, etc.), government loans or credits, government guarantees against losses etc. A survey of actual measures of stimulation in development countries would reveal a great variety of different measures. A government can replace private enterprise (which may or may not exist) by direct government enterprise through civil servants in government departments, by the creation of special entrepreneurial government agencies, by co-operation in mixed corporations, etc. Here again we find an almost infinite number of varieties; their detailed enumeration would be beyond the scope of a general paper.

In the technical field, the government can arrange for foreign technical advice, for the admission of foreign technical missions, for the immigration of technicians and skilled workers; it can create a technical staff within the civil service which in turn can either be directly employed in government enterprise or else can be loaned or their advice be made available to private enterprise. The government can promote the dissemination of technical knowledge partly as part of its general educational programme, partly by specific measures, such as model farms, a patent information service for business men etc.

7. The next government function in development policy has been defined as the provision of balance in development. This idea of balance has tended to become somewhat vague in discussion for lack of a close definition; but it is important enough in actual policy to merit closer consideration. The promotion of balance in development has come to mean a number of things;

(a) In many development countries there is a feeling that excessive reliance on agriculture and primary production should be "balanced" by the development of manufacturing industries and services. From this point of view, agricultural progress is held to hold out less useful prospects than industrialization. The fear of excessive reliance on agriculture and primary production in turn contains a number of ingredients: lower productivity of agriculture, absence of economies of scale, importance of industry for security and defense, the advantages of an urban civilization, the instability of agricultural prices, the exhaustion of agricultural and mineral resources - all these and others are inextricably mixed with the idea of balance in development.

(b) Balanced development may mean the avoidance of mono-culture, i.e. excessive dependence on one single product. Such excessive dependence especially in exports is evidently very risky, especially where the single product represents an exhaustible natural resource. The social instability of mono-cultural development countries is sometimes mitigated by the prevalence of subsistence farming. From the point of view of the development country, however, this is getting the worst of both worlds: a large sector of subsistence farming at a low level without an exchange market on the one hand, and mono-cultural exploitation of an exhaustible resource for export purposes on the other. A diversified exchange economy seems naturally, under these conditions, preferable to the governments of development countries. It should be stressed, however, that where the export of an exhaustible natural resource leads to an export surplus which is used for the import of capital goods for the permanent development of the country the "depletion" is somewhat deceptive and more technical than economic in nature. Mono-cultural exploitation of exhaustible resources can be the right policy for development countries. It all depends on the utilization of the proceeds from the exports. By the time the resource is exhausted it may also be technically obsolete, and the development country which has exported its natural resources and invested the proceeds in machinery and other permanent assets may be able to get the best of both worlds. On the whole, we must recognize the desire for diversification as a justifiable and reasonable trend in development policies.

(c) Balance may mean the establishment and development of certain key industries which tend to exert a kind of radiation through-out the economic structure and which tend to open up a widely developed system. A good example of such a key industry are the steel and basic engineering trades. Countries increasingly feel that without such key industries the economic structure is lop-sided. The desire to establish such key industries is universal. The means employed are largely in the field of commercial policy, i.e. the granting of protective tariffs or the non-profit operation of such industries under government auspices.

The desire on the part of development countries for "balance" cannot be properly understood unless we realize the specific advantages of such a course for development countries. A desire for diversification - specially regional diversification - is indeed also noticeable among some of the older industrial countries. The reasons for such a desire, mainly the avoidance of undue risks and undue extremes of depression, apply to all countries alike. But on top of this development countries have specific reasons to attach importance to diversity. A country with a diversified structure offers as it were a larger surface to technological progress; it is less likely to be by-passed. Also, each new occupation and in particular each new industry provides a new "growing point" for technical progress and the spread of new skills and improvements, in a way in which a mere extension of existing industries or occupations would not. Since accessibility to technological progress and the spreading of skill are

among the two key problems of development countries, stress on balance and diversification is fully understandable. It is not as is often thought, a case of confused thinking but it lies at the very core of the problem of economic development.

There is no other agency in the field which could consider it as its job to promote balance and diversification; this automatically devolves on the governments of the development countries.

8. Next among the categories of government measures is protection and maintenance of productivity. This is a vital part of any development policy. Industries and also agriculture in development countries struggle with specific difficulties not felt to the same degree by the more advanced countries. The stimulating atmosphere of automatic progress and extensive education is lacking, the scale of production is often small, the health and vigor of the worker often inferior, access to external facilities difficult, experience and standards of comparison lacking, competition often reduced by protective tariffs and other restrictions, etc. For all these reasons, the price of development is eternal vigilance. It is much less possible than in the more advanced countries to let productivity look after itself. Development of unproductive industries would be a hot-house growth which could only be maintained to the disadvantage of the developing country itself and the world community as a whole.

The role of custodians of productivity naturally falls to governments where there is no other candidate. In discharge of this role governments have taken a variety of measures: they send missions abroad or encourage visits by their technicians to study new methods abroad; they try to improve the accounting and performance measurements standards at home; they run model farms to demonstrate new technical methods; they tend to encourage the improvement in capital equipment by granting fiscal and commercial advantages; they select the location of new plants so as to lead to maximum efficiency in a national pattern; they taper off or reduce tariff protection so as to encourage efficiency as the scale of production grows; some of them in their development targets prescribe rates of output which in relation to available labor and equipment can only be achieved by improved productivity.

On the other hand, it seems safe to say that there is a danger of a tendency to neglect this particular aspect of government policy. Productivity is a difficult thing to measure; international comparisons of productivity are even more difficult to undertake with any degree of precision; deficiencies in productivity can always be covered up or excused on the grounds of the youthfulness of the industry; it will always be more spectacular to devote one's energies to the construction of entirely new plants and projects than to the improvement of the productivity of existing ones.

Special problems arise in development countries in attempts to raise productivity by the introduction of new machinery. On the one hand, there is a well founded desire in development countries to offset the other manifold advantages of the more advanced countries by at least avoiding the old and antiquated equipment characteristic of some of them, and of some plants in all of them. On the other hand, the very latest stage of technology may well be of a somewhat untried experimental character, and whereas an advanced industrial country can afford to take experimental risks with new techniques, a development country cannot. In the normal case, for a poor country each new development or improvement of an existing one is a unique and precious thing and no risks can be taken with it. Thus the governments of development countries must

steer a middle course calling for a considerable degree of skill in recommending and introducing techniques of production which permit their country to reap all possible advantages from its youth as an industrial producer, and yet at the same time avoid excessive risks.

It may also often pay a development country to utilize second hand machinery cheaply acquired from industrialized countries. There are economic arguments for believing that economic progress in industrialized countries results in large scale premature scrapping of machinery and equipment which is still perfectly serviceable and capable of yielding good returns specially when acquired at scrap value. A firm in an industrial country frequently cannot afford to operate such machinery since it cannot afford to fall behind in the technological race compared with its competitors. In a development country such considerations often do not apply. There seems no reason why second-hand machinery which has been discarded in industrial countries should not be usefully employed to the benefit of development countries.

9. The protection of balances of payments of development countries also raises specific problems of governmental policy. In the course of industrial development the balance of payments will tend to become unfavourable, and only part of the gap may be covered by current new credits. Economic development in its early stages imposes a strain on the balance of payments in the following ways:

(a) Development tends to reduce exports of food and agricultural products by raising average levels of consumption, and also by increasing the urban population and diminishing the agricultural population.

(b) Development reduces the export of primary materials since a higher proportion will be retained for domestic use. This is an especially important factor since many development programmes are specifically based on the utilisation of domestic raw materials.

(c) Intense development within the country, with a high proportion of output consisting of capital goods rather than immediately consumable goods, tends to raise price levels inside the country, and thus to hamper exports. A disequilibrium arising in this way would certainly be classified as a "fundamental disequilibrium" in the sense of the International Monetary Fund Agreement which would qualify a member country to depreciate its currency, but the depreciation of currency will not always be a remedy for balance of payments difficulties.

(d) Industrial development carries with it a demand for increased imports of raw materials.

(e) The improved standards of living and a higher level of industrial wages - compared with agricultural levels - carries with it an increased demand for imported consumption goods, especially of a semi-luxury kind.

(f) The new developments at early stages will often be of a heavily capital intensive nature requiring large amounts both of domestic labour and of imported machinery without immediate return. This applies specially to transport and power.

(g) Since economic development will often depend on a constant flow of foreign credits the developing country - which will typically be a debtor country - may also have to resume or increase payments on previous debts which had been partially or wholly in abeyance.

From all these various directions, the balance of payments will be under considerable strain. The output of the newly developing industries will not usually be directly exportable, and even where general development of such services as transport, power, etc. may gradually be expected to lead to the development of exporting industries, this will usually be a long range process.

Governmental measures in protection of the balance of payments may take the following forms:

- (a) The development programme may be so adjusted as to give priority to industries replacing previously imported goods. The danger of such measures is that they may unbalance and twist the development programme, that they may lead to the development of low-productivity industries, and that they may tend to restrict the total volume of world trade.
- (b) Priority within the development programme may be given to industries producing immediately exportable goods. The previous objection against (a) would also apply in this case, except that there is no restrictive effect on world trade. There is also the danger that concern with immediate balance of payments difficulties will interfere with the patient laying of foundations and development of a suitable economic climate which in the long run may be a more rewarding approach to development.
- (c) Strict domestic price control may be introduced and domestic consumption reduced by heavy taxation or by rationing in an attempt to cope with balance of payments difficulties. This will impose a heavy burden on the administrative machinery at a moment when it is already heavily taxed by a development programme, in under-developed countries where in many cases the administrative machinery is weak to begin with, and in an economic structure where measures of control, taxation, and rationing are extremely difficult to administer.
- (d) Currency may be depreciated. As has been mentioned before, this will normally be permitted under IMF rules but it may not be sufficient to restore the balance of payments. Also it may undermine confidence in the monetary field within the developing country and thus do more harm than good. Currency depreciation will also increase the real debt burden on the development country.
- (e) The government may attempt to improve the terms of trade, i.e. obtain better prices for its exports and obtain its imports at lower prices. Since development countries are primarily exporters of primary products exposed to keen international competition, their main hope of obtaining better prices for their exports will normally lie in the promotion of international commodity agreements such as are provided for in the ITO Charter. The main method of obtaining imports at low prices would be by the pooling of import orders and by the placing of long-term bulk contracts.
- (f) The government may try to increase the total quantity of exports or to diminish the total quantity of imports by measures of commercial policy such as tariffs, import quotas, etc. Such measures, of a non-discriminatory character, have been permitted to countries in balance of payments difficulties by the ITO Draft Charter. It is specially note worthy that under the ITO Draft Charter development countries may discriminate, in imposing import restrictions, among commodities according to the degree of essentiality; thus they may reduce the import of luxury goods without at the same time having to cut down on machinery. The ITO Draft Charter also would prevent the Organization from

calling in question the development policies which have given rise to the balance of payments difficulties. Each country would remain free to carry through its own autonomous development policy. In cases of currencies declared "scarce" under the IMF Charter, development countries would also be permitted to alleviate their balance of payments position by switching imports to other countries.

(g) The government may try to cover the gap in the balance of payments by securing additional credits. Since the balance of payments difficulty of the development country will usually be of a chronic nature, resort to the IMF will not usually be appropriate. The main agencies for development countries would seem to be the International Bank, direct loans from other governments, loans from banks in other countries, the floating of securities in capital markets abroad, and finally direct credits from manufacturers abroad. The interests of development countries in general may be defined by saying that whatever credits are obtained should be as freely spendable anywhere and on anything as possible; but that if any tied loans can be obtained over and above the freely spendable amount this evidently would clearly add to the import potential of the development country.

10. The next group of tasks by governments in development countries has been defined as the prevention of inflation. The domestic effect of economic development is a tendency toward the development of an inflationary condition. The propensity to save is very low in most of these development countries because of their low standard of living unless their propensity to save is increased by a very unequal distribution of income and high private profits. This, however, would go against the social philosophy and intentions of many development countries, and in any case there seems to be something contradictory about reducing international inequalities in standards of living at the expense of creating or accentuating internal inequalities within the development countries. The resulting internal inequalities could of course be curbed by heavy taxation. In this case the high propensity to save is really achieved by fiscal methods but many development countries lack the fiscal system required for heavy taxation of higher incomes. If internal inequalities are allowed to develop without effective taxation there is a risk of a heavy demand for imported luxury goods. In that case not only would internal inequalities have failed to increase the propensity to save, but they would have created balance of payments problems in the bargain. To permit the accumulation of large profits out of the inflationary position arising in connection with economic development would also run the risk of an export of accumulated capital to the often safer and more agreeable conditions of more advanced countries - again raising awkward balance of payments problems. In other development countries high incomes might lead to hoarding of currency and gold. In this case the inflationary pressure is neutralized but there is a danger of a paralyzing effect on further development if profits are hoarded in gold instead of being invested or deposited in banks; hoarded currency and gold will also hang like a Sword of Damocles over the development country threatening its economic stability.

An inflationary position may also be awkward in creating a shortage of industrial consumption goods which in turn will make the agricultural population reluctant to sell and deliver food in the open market. In this case economic development may end in a food shortage and the suspension of the ordinary system of monetary exchange.

Effective methods of rationing and allocation may be the best methods of producing the savings required but in the conditions of many development countries this may be beyond the capacity of the administrative machinery. The main choice in that case seems to be between heavy taxation - which may take the indirect form of high prices being charged for the state-owned or controlled output of newly developed industries - or controlled inflation as a method of enforcing the requisite savings.

11. The next item listed among our main categories of development measures related to the reduction of economic dependence. This desire is universal among development countries. In it, for purposes of discussion and analysis it may be useful to distinguish the following:

(a) Many development countries are in the process of emerging from a state of colonial or semi-colonial dependence. Their whole policies are acutely influenced by this experience of dependence, and their development programmes are colored by this.

(b) Many development countries have had past experience of wide-spread foreign ownership of their most important economic assets, and of the outflux of profits and interest payments which is characteristic of the position of a debtor country.

(c) The two world wars have brought home to development countries the dangers and risks of dependence on imports for vital commodities. It is one of the threats to international specialization that its benefits in the form of increased productivity of labour all round are diffused and difficult to measure, whereas its drawbacks in times of emergency are obvious and dramatic. Thus development countries tend to read the history of the last war as an argument in favour of diminished economic dependence, even though from a different point of view it could also be read as a triumph of international division of labour over more self-sufficient economic systems.

(d) The great depression of the early 1930's diminished the importing capacity of the more advanced countries very sharply. Moreover, it turned the terms of trade very heavily against most development countries. Also, low-priced exports from the industrialized countries, often below full average cost, tended to nip in the bud the incipient development of industries in development countries; at the same time advanced countries tended to resort to stimulation of their own agricultural and other primary producers. It was thus in many ways that the depression tended to rub in the dangers of economic inter-dependence for development countries and their governments.

(e) Development countries often feel that they are in an inferior bargaining position. The machinery and other manufactured goods which they require can usually only be obtained from a few major sources of supply; on the other hand, the agricultural and primary products which they export - and also the simpler manufactured products, if any - can often be obtained from many other sources, and they are liable to competition from substitutes (natural or synthetic). Profit margins on specialized capital goods are often higher because of imperfections of competitions, and there is also greater danger of monopolistic control of output and prices of those articles which development countries require as imports. Possibly the provisions in the coming ITO Charter providing for commodity control agreements for primary products and the prevention of restricted business practices in others will go some way to meet the problems of development countries in this respect.

(f) Development countries feel that dependence on foreign trade - which means for them specialization on primary products and simple manufactures - removes them from an important sphere of dynamic technical progress. Another way of putting this would be to say that development countries feel that international specialization based on present comparative costs relatively to more advanced countries is not a desirable economic course for them to steer because it neglects the possibility (or as many development countries think the certainty) of dynamic changes in the comparative cost position once a more self-contained balanced economic structure has been created.

(g) Foreign trade is naturally less subject to internal planning control than domestic production. For this reason there is an almost inevitable tendency, as attempts at planned development spread, to shift emphasis from foreign trade, which is more unpredictable, to domestic production. From the point of view of the development country, the fact that domestic production is easier to control than foreign trade may seem a genuine argument in favour of less dependence.

Thus the desire for less dependence has many sources and many aspects. It is worth pointing out that this desire is not necessarily disruptive to international trade. On the contrary it may contain the elements of a sounder and more permanent international division of labour. Development countries, on the whole, like to feel somewhat less dependent on foreign trade; but this is not the same thing as saying that they want to diminish the amount of foreign trade which they actually carry on. You can still want to have as much as possible of a good thing while at the same time guarding against the possibility of having to do without it. It is a problem for international policy to reconcile these two trends.

12. Next we have listed the publication, under government auspices, of development programmes consisting of an inter-related set of target figures. This stage in development policy is reached by most but not all development countries. Usually such a programme when published is referred to as a "plan".

Neither in the preparation of such a plan nor its method of publication, nor in its scope do we find anything like international uniformity. A plan may be prepared by the various government departments, or else the fundamental data required may be gathered from private sources or private professional organizations, or else a separate planning commission or a public corporation charged with drawing up a development plan may collect the necessary data. The data required and collected may be very detailed and analyzed with the help of up-to-date statistical techniques. At the other extreme, the drawing up of a plan may take place entirely on the basis of guess work, intuition or qualitative information. It is worth noting that the consistency of a plan can be no greater than the consistency of the individual data from which the plan has been prepared. Thus if the original data are unevenly prepared or defined for the different sectors of a plan, the resulting plan itself is likely to be uneven as between its different parts.

Methods of publication may vary from detailed economic descriptions containing something like a grand conspectus of national resources and prospects to informal statements scattered over many different administrative circulars or publications. Statements in parliaments, law decrees, or the publication of statistical tables without descriptive text are other vehicles of publication.

As for scope, this may vary from figures for individual plants or branches of industry to ones containing all the internal production, trade and foreign trade, fiscal and general financial policy, prices and balances of payments. In general development plans tend to be confined to internal production. On most of the other factors, especially on prices, assumptions are made but these are not an integral part of the plan. Foreign trade is usually thought of as too unpredictable and too far removed from the control of the planning authority to be included, but assumptions regarding the course of foreign trade are often implied in internal plans, though not always consciously.

The status of these figures once drawn up also varies widely between countries. The targets at which they aim run the whole gamut from what may be frankly described as wishful thinking - aims demonstrably impossible to attain in the period stated - to targets which represent the optimum possible in the event in that frictionless sequence which simply does not happen in economic life (and even less so in the precarious conditions of development countries) to what may be accomplished with a reasonable degree of efficiency and a reasonable amount of good luck, to what may be regarded as a realistic forecast of the probable course of events down to a sort of series of minimum targets any deficiency below which would spell a serious economic outlook. Any economic development plan will find its place somewhere along this scale of a development plan barometer. It is to be noted that the publication of almost impossibly ambitious development targets is not necessarily a bad thing. Governments may feel that such targets act as a spur so that even if the targets are not reached actual performance is higher than it otherwise would have been. And after all it is performance which matters, not the fulfillment of target figures. As against that, the non-fulfillment of target figures will be a blow to the prestige of governments although it is open to government to side-step or soften this blow by using non-fulfillment as an occasion for public exhortation, or - less desirably - to cover up non-fulfillment of targets. Another method of getting the benefit of targets without loss of prestige is to keep the plans flexible, i.e. to raise the targets high to begin with but to reduce them if fulfillment seems impossibly difficult. It will be seen that the relationship between development targets and performance is one of great complexity which calls for the application of diplomatic psychology.

Similarly the status of target figures varies regarding the closeness of their relationship to actual performance. Targets may be published as a sort of "shopping list" by the government to other agencies - mainly private enterprise and farmers - leaving the onus of fulfillment and the selection of means towards fulfillment very largely to their devices and ingenuity. Next in the list come targets which have a purely statistical significance, i.e. they serve as comparative standards against which actual performance can be measured. Such plans or targets serve a similar function as standard costing and standard budgeting techniques in private enterprise. Other targets may be of the nature of a mandatory duty of government departments, organizations and even of private individuals concerned in the execution of the plans. In such cases a deficiency from the target figures may be viewed as a serious offense unless a valid excuse is present. Evidently the real economic significance of target figures depends very highly on where they stand in this scale.

Finally, we may draw a distinction - although this is related to the one discussed in the previous section - between economic development plans which (a) confine themselves to stating the goals to be obtained, and (b) plans which at the same time try to provide for the means by which the goals are to be

obtained. The second type of plan would indicate such things as the provision of labour for the different types of projects and different fields of the development programme, the allocation of state resources for different projects, the responsibility of different government departments in the various fields, the amounts and types of foreign machinery to be made available for different projects, the new plants to be constructed for implementing production programmes, etc. Plans under (a) without indication of means of fulfillment tend to be somewhat "in the air" (unless of course the means for their fulfillment is separately determined in administrative discussions, circulars or separate documents; in such cases the development plan itself ought to be studied in conjunction with those other documents or such other information as is available on means of fulfillment).

Development plans will also be sub-divided into those which indicate the goals to be obtained - with or without indication of the means of attainment - and plans which also indicate the stages by which the goals are to be attained, either in point of time or in point of priority of execution. Again, as in the previous case, the prescription of stages of execution may be either contained in the same document or pronouncement as the original development plan, or else it may be contained in separate documents or administrative instructions issued separately from the plan.

13. We have now reached the last item in our list of government measures: the execution by the government itself of a more or less comprehensive and more or less co-ordinated system of measures for the development of the national economy. The degree in which governments themselves are the main executive agencies - in addition to the measures discussed - will of course depend very closely on the prevailing political philosophy. Some countries make it a matter of principle that the state should displace private enterprise, and this evidently applies to the development programme as well, other countries make it a matter of principle that the state should not compete with private enterprise, and their development programmes tend to reflect this general view. Quite apart, however, from these questions of principle - which it would not be useful to discuss within the framework of this paper - they are a number of more specific reasons why governments often do not confine themselves to the range of measures in the field of development previously discussed - wide as those are but why they should also become executive agencies for development projects. Some have already been mentioned incidentally in the course of the discussion: here we can confine ourselves to consider the following;

- (a) Under government operation, the factor of private profits is eliminated. This is important for development countries because the rate of profits, in view of capital scarcity and greater risks, is often high or excessive in relation to more advanced countries. The scarce supply of domestic enterprise is also probably a factor in the high rates of profits. There is also the point that high private profits in a development country, superimposed upon generally low standards of living, produce a high degree of economic inequality, and they are also liable to embarrass the balance of payments position by creating a demand for luxury imports. Moreover, in many development countries the fiscal system may not be sufficiently well developed to curb private profits by methods of taxation. In view of all this, state operation may often seem the easier way out, as a matter of expediency and not of principle.

- (b) Government produced output may be sold at a profit. In such a case, the excess in price charged for government output over cost of production is in the nature of indirect taxation in hidden form. Since in many development countries the possibilities of imposing and collecting direct taxation are often poor, since this may apply even to openly imposed indirect taxation, government operation combined with sale of government output at a profit may be adopted as the easiest way, in the circumstances, of solving the budgetary problem.
- (c) Alternatively, pricing policy in the sale of government output may be based on sales below cost price, i.e. at a loss. In this case, government operation partakes of the nature of subsidies. Such a policy may serve partly economic purposes, specially where capital goods are sold below cost in order to stimulate economic development, and partly social purposes specially where consumption goods are sold below cost to low income groups. In either case, government operation of plants may be said to serve the purpose of stimulating selected branches of the economic system according to the general development programme. On the other hand, government operation at a loss intensifies the inflationary pressure to which a country in rapid process of development is liable to be subject.
- (d) Apart from general operation at a loss, state operation can apply the weapon of price discrimination, charging different prices to different types of consumers and customers, and thereby discouraging development in some fields while intensifying it in others. Thus state operation of plants may be adopted in development countries because of the possibility which it opens of regulating the rate of development in the different branches of the national economy by discriminatory price policies.
- (e) Finally, state operation in development countries may serve the specific purpose of preventing the building up of private power positions dominating the economic system. It must be realized that in a development country where the number of large-scale plants and the total volume of capital employed are both small, command over economic resources gives a very much more prominent position in economic life (possibly also indirectly in political life) than in an advanced country. Also, in a development country the number of plants and the number of branches of industry is likely to be so small that effective competition as a curb on economic power is not operative.

Many development countries are groping for new forms of organization, somewhere in between full state operation and private enterprise. The public corporation, with varying degrees and types of state participation is a wide-spread solution for this problem, specially in Latin America. The analysis of the relationship between the State and private initiative within development countries is an important study, but it would require a separate paper to do.

Bank op

IMPLEMENTATION OF LOCAL CURRENCY LOANS TO
ECONOMICALLY UNDER-DEVELOPED COUNTRIES

1. Definition

It seems that the only "local currency loans" which could be considered by the International Bank are the project loans in local currency secured by foreign exchange. This results from the following:

a. Direct loans in local currency:

These loans are either (1) made on the basis of the 18% participation to the IBRD, or (2) made out of local funds raised by the IBRD in the local markets. In the first case, a loan would be no more than the creation of so much paper money and furthermore, the 18% participation would usually represent a trifling amount compared with the local currency requirements of a development program. The second form of financing could only mean that local capital can only be acquired if a US\$ guarantee is given. There would be a premium on defaults.

b. Loans in local currency secured by foreign exchange:

1) Loans unrelated to projects.

These loans could be utilized, for instance, by a Government to cover a budgetary deficit or by a private company to cover the service of an outstanding debt. It is doubtful that such a loan could be undertaken by the Bank under the Articles of Agreement.

2) Loans in local currency related to a project which may or may not be partially financed directly in foreign exchange for expenditures to be made on equipment.

The theory of such a loan is that foreign exchange provides an adequate backing for the local currency issued against it, insofar as its sale to the public will promote imports of consumers goods equal in value to the emission of new currency. After the completion of the project,

and thus after the period of in-flow of foreign exchange, it is expected that the value of the goods produced by the newly created project will be equal or superior to the value of the new currency in circulation. Inflation will thus be averted.

2. Implementation of project loans in local currency secured by foreign exchange.

It is evident that if (1) the total cost of the new projects is carefully calculated, (2) the value of the total future production per year is clearly determined, and (3) the timing of the process is carefully studied and followed, there can be no inflation, if the amount of local currency issued against the total value of the project is absorbed exactly by the total value of the new production. To achieve this perfect match, however, the lender would have to assume a considerable amount of control over the overall economic policy of the borrower.

If, for instance, the additional imports financed by the foreign exchange loaned are not of an essential nature (i.e. which can be consumed by the workers on the new construction project) the equilibrium will be shifted with a consequent immediate increase in certain internal prices.

If the Central Bank reacts traditionally to the induced pressures for higher wages or stable profits, a secondary inflation will start.

In order to avoid these effects, a strict control must be set on imports, the disposition of imports and central Banking policies. This example is only one of the many which could be imagined.

The same necessity for complicated supervision would appear if the Bank attempted to follow the end use of the funds lent to the country.

The above suggests that the supervision and control of local currency loans secured by foreign exchange is extremely difficult if it is to be effective. It may involve far-reaching measures of internal control.

An additional point to be considered (and this can be applied also to normal foreign currency loans on specific projects) is the "locus standi" of

the Bank's right to control a nation's economy, for to all practical purposes, it is such a control which is implied.

In practice this will be reduced to a matter of quantities and proportions and any control will in effect depend entirely on the size of the loans the Bank will be able to make and their impact on the nation's economy. It would be really a case of "wishful thinking" to believe that the Bank can exert a control on the economic and financial policies, present and future, of a country with a foreign trade volume of about US\$ 600 million by means of a loan of US\$ 20 million.

3. Conclusion

We have seen above that the prerequisites of success in a project loan in local currency secured by foreign exchange are stringent security provisions of economic, financial, technical and administrative character which will be studied in another paper. As it seems that the Bank will be unable to obtain all the security provisions which would be desirable, the question is to know whether a project loan in local currency is less attractive to the investors in the Bank than a project loan in foreign exchange. The answer seems to be that as long as a specific project is involved, the investors will be satisfied as they will feel that the Bank can follow the proceeds and deposits of the funds in a traditionally satisfactory manner.

March 23, 1948

NOTE

The necessity for complete supervision of a nation's economy, in the case of a direct foreign exchange project loan is as great as in the case of local currency loan secured by foreign exchange.

This will be easily demonstrated if it is noted that when for instance hydroelectric power projects are undertaken, the local construction expenditures involved amount usually to $1\frac{1}{2}$ times the value of the equipment needed.

If local currency is issued to meet the construction costs, or if local capital is displaced, the situation created can be thus more dangerous, from an economic standpoint than the one created by a project loan in local currency secured by foreign exchange.

In the foreign exchange field, it may be that the additional exchange made available to the country by the financing of a project will be utilized on non-essential imports. In such case, the project loan in foreign exchange, although carried successfully to completion, could impair the economic situation of the country, insofar as the expenditure could have been financed out of normal foreign exchange receipts.

Without a strict control on the disposition of the foreign exchange available to the country, after the granting of a loan, the IBRD will never be certain that it will have achieved its aim, i.e. the improvement of the conditions in the borrower country.

It is, therefore, doubtful that a distinction should be made between project loans in foreign exchange and project loans in local currency secured in foreign exchange.

J. Torfs
3/23/48

Development Policy Committee

February 25, 1948
(Revised)

Papers to be Drafted by Committee on Development Policy

<u>Title</u>	<u>Department</u>	<u>Status</u>
1. The Bank's Policy in Under-developed Countries	Loan	Preliminary draft discussed by Committee February 25, 1948. To be revised.
2. Capital Formation in Latin America	Research	Draft completed and circulated to Committee.
3. The Moral and Political Problems of International Participation in the Development of Backward Countries	Research	Draft to be ready February 27.
4. Should the Bank Finance only Foreign Exchange Expenditure or Local Currency Expenditure also?	Research	Draft to be ready February 26.
5. What Financial Assistance Has Been Given to Latin America in Recent Years?	Research	
6. Comparison of Prewar and Present Economic Conditions in Latin America	Loan-Research	
7. Economic Development in Latin America in the Last Ten Years	Loan-Research	
8. Barriers to Private Investment in Latin America	Research	

February 24, 1948

COMMITTEE ON DEVELOPMENT POLICY

Note by the Chairman

It is proposed that the original agenda of the Committee be considerably abridged, but that the following papers should nevertheless be completed as soon as is practicable:

- 1) The moral and political problems of international participation in the development of backward countries.
- 2) Survey of economic problems of Development Countries.
- 3) Should the Bank finance only foreign exchange expenditure or local currency expenditure also?

After discussion and revision by the Committee, these papers, together with the papers on The Bank's Policy in Underdeveloped Countries and Capital Formation in Latin America, might form an ensemble which could usefully be discussed by the Bank at a higher level.

A meeting of the Committee will be held in Room 414, in the Loan Department at 2:30 PM on Wednesday, February 25.

AGENDA

- a) The Bank's Policy in Underdeveloped Countries
- b) Capital Formation in Latin America
- c) Consider the above proposal, and in the event of its adoption by the Committee, set final dates for the completion of drafts of the three papers still outstanding.
- d) Consider whether the Committee shall undertake any additional work on an ad hoc basis — particularly in regard

to Latin American problems.

Members of the Committee are requested to notify the Secretary, Mr. Skillings, not later than 5:30 PM today (Tuesday) if the proposed time of the next meeting is inconvenient so that another time may be fixed to meet the general convenience.

OFFICE MEMORANDUM

TO: W.A.B. Cliff
 FROM: J. M. Penton
 SUBJECT: Development Committee

DATE: 2/16/48

A.

The major contribution to the work of the Committee on Development Policy to date has come from the Loan Department. A perusal of the papers suggests strongly that they are too long, contain too many generalities, and overlap one another. I shall therefore endeavor to have them rewritten in such a way as to gear their contents more closely to the activities of the Bank. The aim will be to amalgamate them, so far as possible, to form a short section of a final report.

The sections, when ready, could be discussed by the Policy Committee when it has finished discussing Latin America. They could then be rewritten in final shape to take account of the ideas of the Policy Committee.

B.

When the latter discusses Development Committee papers, I should be grateful if an additional representative of the Loan Department could be present to assist in the final editing of the sections.

J.M.P.

Mr. Penton

I agree as regards A, & shall arrange as you suggest re B.

W.A.B.

16/2/48.

Miss Austin

FILE COPY

February 13, 1948

PAPERS DRAFTED BY COMMITTEE ON DEVELOPMENT POLICY
THROUGH FEBRUARY 13, 1948

<u>Agenda No.</u>	<u>Title</u>
II-B-2	"The Debt Default Problem in Under-developed Countries"
II-B	"How can the Bank Secure Active Cooperation of Private Investors, both Local and Foreign, in Development Projects?"
II-C	"Activities of Other Inter-governmental Organizations Interested in Economic Development"
III-B, -C, -D	{ "The Position of the IBRD in the Formulation and Implementation of Development Programs" (Also Supplementary Agenda 2)
	{ "The IBRD's Relationship to Governments Undertaking Development"
Supplementary 2	"Policy for the Bank and Latin America"
Supplementary 3	"The Effect of Marshall Plan on Latin American Development"
Supplementary 4 and 7	"Capital Formation in Latin American Countries"

OFFICE MEMORANDUM

TO: Henry W. Riley

FROM: R. F. Skillings, Secretary *RFS*
Development Policy Committee

SUBJECT: Agenda for Meeting, Wednesday, February 11, 1948

DATE: February 11, 1948

There will be a meeting of the Committee on Development Policy today, at 3:00 PM, in Mr. Penton's office (Room 414).

The following papers will be discussed at this meeting:

<u>Agenda No.</u>	<u>Title</u>
II-D-2	"The Debt Default Problem in Under-developed Countries"
II-E	"How can the Bank Secure Active Cooperation of Private Investors, both Local and Foreign, in Development Projects?"
II-G	"Activities of Other Inter-governmental Organizations Interested in Economic Development"
III-B, -C, -D	("The Position of the IBRD in the Formulation and Implementation of Development Programs" (Also Supplementary Agenda 2)) ("The IBRD's Relationship to Governments Undertaking Development")
Supplementary 3	"The Effect of Marshall Plan on Latin American Development"

I am attaching rough drafts of three of these papers for your use. Unfortunately, the copies of the drafts of the others have been exhausted, but more will be available when second drafts are made.

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30-11

Development Loans and Inflation

The dangers of inflation created by a development loan are very similar to those which in agricultural and raw material exporting countries have emerged from high export values and restricted import volumes in recent years.

If the development loan is "free", and expendable in any manner desired by the borrowing Government, the parallel may be very close. To the extent that loan proceeds are transferred into domestic currency and used to finance enhanced Government developmental expenditures, the inflationary effects in the short-run are identical in aggregate result with the effect of increased export values of equal size. Both create new money incomes and enlarge the monetary circulation pro rata, inducing a movement towards "full employment". Both become inflationary when this monetary increase can no longer be matched by increase of available consumer goods, the most quickly variable supply of which is in both cases imports, for which, up to a point, foreign exchange is available, in the one case from exports, in the other from the original development loan.

But, at the present time, there is an overall shortage of available imports, the only country of immediate supply being the United States; which has led to wide-spread "dollar shortages". Hence inflation, due to high war and post-war export incomes coupled with physical import shortages, has emerged in many food and raw material supplying countries.

This is a pattern which may well re-emerge from international developmental lending. It is unlikely that any great proportion of such official

lending will be "free", available directly for domestic development expenditures. The greater part, it is expected, will be linked to specific development projects, and granted to enable the borrower to finance foreign purchase of necessary capital equipment. Loans of this nature do not directly permit greater consumer good imports; physical import shortages (mentioned above) are replaced by financial restriction. Yet the development programme, of which the loan is a part, will increase domestic money incomes and monetary circulation in advance of the increased flow of domestically produced consumer goods resulting from successful development. During the development period, that is, money incomes are increased without pro rata increase in flow of consumer goods, whether from imports or from domestic production. Clearly, therefore, during that period danger of inflation is real.

Just how serious that danger becomes will depend upon the exact manner in which the development programme is administered and financed. Two aspects may be distinguished; the shorter-period, concerned with the handling of the development loan itself, and the longer-period, in which consequences flowing from the loan merge into the effect of the whole development programme.

Consideration of the short-period centres upon the manner in which domestic financial transactions on account of import of developmental capital equipment (originally purchased from loan proceeds) are handled. One possibility is that such capital equipment remains throughout in Government ownership, so that no subsequent domestic financial transactions occur, and hence no short-period inflationary dangers arise. Another possibility, at the other end of the inflationary scale, is that such imported capital equipment is resold by Government to private operators, the proceeds when received by Government being used for current official expenditure. Here the effect is wholly inflationary, to the extent of the capital value of the equipment sold, and is closely parallel to the effect of an equivalent increase of

export proceeds with no increase of available consumer good imports.

Direct inflationary pressure from this cause would disappear if the proceeds of sale of imported capital equipment were "sterilised" by Government, that is, withheld entirely from further domestic circulation. It is suggested that such receipts should be paid into a "Development Capital Account, Foreign Section", and not disbursed in any form domestically, either as current expenditure or expenditure upon domestic capital account. So held, it constitutes a fund of local currency, available for the domestic fiscal burden of foreign debt service and redemption, minimising current domestic budgetary costs on this account. Final service and redemption depends, of course, upon international balance of payment conditions rather than upon domestic budgetary considerations; nevertheless, proper treatment in Government accounts would later minimise consequential budgetary disturbances such as have in the past led to inflation in many countries.^{1/}

Even granted successful sterilisation of proceeds of sale of imported capital equipment, however, matters are probably not at an end even in the short period. They would be only if purchasers of capital equipment were able to finance purchase wholly from genuine domestic savings, whether their own or through issue of stock. It is more probable that some part at least of necessary funds would be obtained by advances from banks, representing a new addition to monetary circulation. Suggested "sterilisation" would prevent this increase becoming cumulative, but the once-over consequences

^{1/} The argument may be encountered that a local currency fund so originated should properly be available for development purposes in supplement of domestic savings, by analogy with UNRRA practice in some countries with relief supplies. The essential point here, however, is that the foreign exchange corresponding to the fund has already been spent in acquisition of imported capital equipment, and is in consequence no longer available to sustain domestic consumption during development.

remain. In the non-government banking sector, advances have increased, while commercial bank cash reserves have decreased, since the cheques drawn against those advances were cleared against commercial bank holdings with the Central Bank. The commercial banking position is thus less liquid, at a time when the public's genuine monetary requirements are probably increasing, in part under necessity of at some time repaying the original advances, in the main for finance of increased financial and commercial transactions consequential upon the progress of development.

Thus complete "sterilisation" of original capital proceeds may in fact be too drastic, unless accompanied by an official banking policy designed to permit growth of domestic monetary circulation in step with growth of volume of domestic financial transactions.

This merges into the longer-term problem, that of avoiding inflation during a period of economic development. Such a development period necessarily involves domestic expenditures, which may be considerable in aggregate, in formation of domestic capital equipment. An example would be local wage disbursements on account of construction of a dam. Such expenditures increase immediately spendable domestic money incomes, but there is no immediately increased flow of consumer goods, since development takes time, and imports of consumer goods not increasable (international development loans being taken up in the form of imported capital equipment). Thus economic development involves a lag between increase of money incomes and increase of available consumer goods, during which special inflationary dangers exist.

Normally, recipients do not spend the whole of income, but save some part. If the part so saved is for the developing country as a whole, equal to domestic development expenditure, income expended in consumer goods (income not saved) would remain equal to consumer goods available, and no

inflation emerge in the transition period. Voluntary domestic savings, that is, would equal domestic capital formation. But by definition under-developed countries are poor countries, and the rate of capital formation desirable for their economic development is most probably in excess of voluntary domestic saving. Hence, if the programme is to go through, domestic savings must be "forced", either by fiscal policy (increasing current taxes to cover expenditure on capital account), or by inflation (reducing the real value of money incomes), or by a combination of the two.

If one policy be used alone, ^{to}the exclusion of the other, development itself may break down, particularly if the gap between necessary saving and voluntary saving be wide. Penal taxation rates may kill private initiative and incentives. Runaway inflation would destroy the basis of orderly economic action. Some combination of the two may be the most workable compromise, keeping both taxation increase and inflation within limits.

But there may, in fact, be no acceptable or practicable limits unless the original development programme called for a rate of domestic capital formation not too greatly in excess of domestic voluntary saving; or, if that saving be very low, some portion of international development loans be made "free", in support of domestic saving, and imported consumer goods are available.

THE POSITION OF THE IBRD IN THE FORMULATION AND
IMPLEMENTATION OF DEVELOPMENT PROGRAMS

Purposes of
the IBRD

- In accordance with Article 1 of the Articles of Agreement, the basic purposes of the IBRD with respect to Development countries are;
1. to encourage the development of productive facilities and resources in less-developed countries;
 2. to promote private foreign investment, provided that such money is not available and cannot be obtained by Member Governments on reasonable terms;
 3. to raise the standard of living and conditions of labor in Member Governments by raising production and by promoting long-range balanced growth of international trade;
 4. to arrange that loans are made so that the most useful and urgent projects will be dealt with first; and
 5. to conduct operations with due regard to the effect of international investment on business conditions in the territories of Members.

Interpreting the Bank's Articles with specific reference to underdeveloped countries, it might be stated that the Bank has two primary responsibilities: (1) assisting to create an environment of fiscal and economic stability within the member governments so that private capital can operate to increase productivity, and (2) lending its own funds which will supplement such capital.

Basic
Objectives
of IBRD

The IBRD, in accordance with its policy, must raise the funds it lends from the investment markets in the world. In itself, it is not the creator of money. It is merely an instrument through which its members can tap the investment markets. Because of this limitation upon the Bank's ability to obtain funds, it must be recognized that the Bank cannot finance all of the development requirements of all

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nations. The Bank cannot even finance all of the development requirements of any one nation at any time. The Bank should spearhead an attack of capital. However, the Bank will not achieve the purpose for which it was established unless private capital will follow to supplement and fulfill the capital needs of the Member Governments over an extended period of time. Such private capital must be both local and foreign. Therefore, in all lending operations, the Bank must keep in mind not only that the projects financed are sound and productive, but that the creation of fiscal and economic stability within the Member Governments should be a primary, basic and immediate objective in order to secure its own loans, permit it to continue to raise money in the investment markets, and create an environment into which private capital will feel free to come.

The Bank should not, initially, stimulate loan requests.

The burden of requesting financing from the IBRD rests upon the Member Governments. At least in its initial stages, the Bank cannot advise Members as to specific development programs. After the Bank's credit becomes established and after the Bank's personnel become more experienced, it may be possible to encourage the Bank's Members to request loans and even indicate the type of loans in which the Bank is interested. However, at the moment, it is suggested that the Bank undertake no positive action, except that it should be of assistance to Members by suggesting independent consultants who might assist them with their development programs, provided that the Members request such assistance.

Procedure of Members in Applying for loans.

All Member Governments should be notified by the President of the IBRD that if they desire a loan, they should indicate such desire to the Bank through the Washington Embassies, Executive Directors, or by letter from the Ministries of Finance or Central Banks.

Action of
IBRD upon
notification
of a Member's
desire for a
loan.

An indication that a loan is desired should be the signal for the Loan and Research Departments of the Bank to bring up-to-date major studies, statistical series and commodity and finished material studies affecting the country involved. Also, the Loan Department should ascertain, informally the nature of the loan contemplated.

Bank missions
to Member
countries.

As soon as possible after the initial loan inquiry, the Bank should send a mission to the country to confer with the leaders of the Government. This mission should be headed by a representative of the Loan Department and should have the following responsibilities:

1. to explain the functions and procedure of the Bank. Officials of the Government should have a complete understanding of the Bank's limitations, ability and powers.
2. to piece-out the Bank's existing background information and present such supplementary requirements or data as may be necessary.
3. to develop a "modus operandi" for negotiations from this point onward. It should be the purpose of the mission to create the beginning of a continuous relationship with the country. The mission should explain the Bank's procedure and should arrange for representatives of the country to come to the Bank for discussions as soon as the background information and project details are complete.

Requirements
needed by Bank
before con-
sideration of
a formal
loan appli-
cation.

Before a loan application is transmitted to Washington, the Member Government should be notified that the following information is desired:

1. A diagnosis of the principal fiscal and economic problems facing the country. Such diagnosis should deal with such fiscal matters as the budget, foreign exchange position, Government debt, flow of currency, and basic economic problems.
2. A program designed to remedy these problems. If such a program

cannot be created due to lack of technical skill, the Bank should stand ready to assist the country in obtaining necessary experts. These experts should be private individuals who can be engaged by the Government. The Bank should not undertake to draft separate programs of fiscal reform. It should merely indicate desirable objectives, such as a stable budget, sound exchange rates, a settlement of the external debt (see special paper on debt default), etc.

Development
Program

3. An overall integrated development program, in order to determine what the development requirements of the country may be and which projects are considered by the Government to be the most useful and urgent. If a single project is requested by a Government, such project should be honored only in the first loan and even then only if it is particularly useful and urgent. For the consideration of additional loans, a development program should be established. Such program should include an analysis of the country's development possibilities. For example, the development of the major resources should be evaluated in terms of comparative costs and potential markets. Any specific projects which the Government has ready for financing should be listed in order of priority and should include a detailed description of the projects, the costs in both foreign and local exchange, the availability of local capital, the nature of the administrative organizations designed to undertake the project, the plans for the distribution of the finished products, and the impact which the project would have upon the economy. If such a program cannot be undertaken by the Government due to lack of technical personnel, the Bank should assist by suggesting independent experts, if so requested.

4. The Government should also furnish a financial program showing the financial resources available to the Government for financing development within the country while still retaining a sound and stable fiscal system. In this respect, the Government should show the amount of money available for development in the budget, the sources of obtaining additional money, if borrowing is contemplated, and the estimated amount of local private capital that might be obtained to assist in financing the projects requested.

Initial negotiations with Member Governments upon receipt of background and project information.

Upon receipt and investigation of the fiscal and economic information, the Bank should determine whether a loan of any kind can be made to the Member Governments. If conditions exist which would prevent an immediate loan, the Member should be so informed. If a loan can be made, providing projects are found worthy, the Bank should inform the Member as to security and representations that will be required. Agreement with the country should be reached on all of these points, together with a program of fiscal reform, if necessary.

If the Bank and the Member Government are in accord as to the security and representations, and other basic considerations of a loan, and if the Bank has approved a loan to such country, subject to the availability of good projects, the various developmental projects should be reviewed.

Types of loans which IBRD should finance.

Projects to be financed should be those which have the greatest cumulative impact upon the economy of the country, and which will tend to most effectively reduce the existing fiscal and economic problems. The projects which appear to be the best from this point of view, should then be analyzed as to their cost and the financial drain upon the available local resources of the country. Moreover, such projects should also be analyzed from the point of view of world or area needs.

In choosing projects which will be financed, every effort should be made to obtain local private capital, in order to relieve the strain upon the Government budget and in order to provide financially-interested management, as well as to stimulate local capital development. Before any project is approved, it is essential that the Bank satisfy itself that the project is not only useful, urgent and productive, but that it is well engineered, markets for the products are available and management is available and able to execute the plans. This may involve the necessity of obtaining foreign engineers, technicians and managers. It may even involve the necessity of obtaining foreign financial participation and, in certain instances, on a basis which will be satisfactory both to the Member Government and to the participating foreign interest. The IBRD should visit, if possible, all projects and should obtain its own engineering advice wherever it appears to be required.

The IBRD should finance projects designed to industrialize under-developed countries whenever such projects met the requirements stated above.

**Frequency
of loans.**

In all of its loan activities, the Bank should not be interested in merely one large loan. It should work to establish a relationship whereby the lending functions of the Bank can be extended over a long period of time. Small loans for specific projects should be made from time to time as the Government develops fiscal stability, as it becomes evident that such loans can be absorbed without a too great a strain upon the nation's economy, as the projects themselves come to fruition, and as the Bank's own resources are able to provide the money. Development of a sound nature can only occur over an extended period. Project loans are also indirectly balance of payments loans;

thus it is important that continuous flow of capital be injected into the Member Governments during their developmental phase. Attention is also invited to the fact that if a country realizes that additional loans may be made from year to year, it will provide the strongest possible incentive to repay these loans previously made and to continue the process of achieving fiscal and economic stability.

Loans
should be
made to a
single
agency
wherever
possible.

In any loan made by the Bank to a Member Government, it is important that an agency be created or appointed which will be the actual recipient of the loan and which, in turn, will relend the money for the various projects agreed upon. This agency should act as a portfolio manager for the IBRD. As loans are made by this agency, adequate security should be deposited with such agency and provisions for periodic reporting on the loans should be made. This will place the basic burden of "policing" the loan clearly upon a local agency of IBRD--thus eliminating the charge of threatening a member's sovereignty. It will also provide a vehicle through which the IBRD can act over an extended period.

Continuous
contacts
should be
maintained
with Member
Governments

It is of particular importance that representatives of IBRD maintain a continuous contact with Member Governments. Representatives of the Bank should visit countries requesting loans or to whom loans have been made frequently. Through this contact, it should be possible for the Bank to police its loans, assist its Members in achieving fiscal stability and assuring that the project loans are being made for well-defined purposes.

G.H. Clee

The IBRD's Relationship to Governments Undertaking DevelopmentI. The Need for Action -

Questions which would be comic if they were not indicative of the most abysmal ignorance regarding the Bank have been put by important public men abroad to visiting officials of the Bank. Many governments and officials are actively considering ways and means of launching development schemes in their countries, but it is clear that they frequently lack technical advice as to how to set about it. When schemes are first mooted, for instance, they are often on a dangerously grandiose scale and could not possibly be absorbed by the country except over a prolonged period of time. Very little attention is paid to priorities and programs are insufficiently studied and frequently changed at short notice. Ministers and officials in these countries often realize that the International Bank should be able to help them but they have only the vaguest idea of how they should go about obtaining its aid. These facts clearly demonstrate the need for the Bank to take the initiative and acquaint the world with its aims, how it intends to work towards these aims, and in general, the economic and financial factors which underlie its work in the field of development.

What is most required to enhance the prestige of the Bank is that governments and others should be brought to look upon it not only as a potential source of funds, but also as a source of specialized economic and financial advice.

On the other side, an attempt should be made to cause investors to regard the Bank as a trustworthy source of information about conditions in countries to which investment is being directed, so that in time the Bank may have a chance to act as a regulator of the flow of investment to certain countries. In this way, the volume of investment might be kept at a level appropriate to the needs of any particular country or area - thus avoiding

the disastrous consequences which are apt to flow from unsound and misplaced loans.

II. Fields of Action -

There are, broadly speaking, four main headings under which the Bank might take the initiative:

- A. The Bank's Structure and Organization - A factual understanding of how the Bank is set up is the most rudimentary starting point for the Bank's work. Men holding important public positions in some of the member countries have visited the Bank and asked for information of this nature. In some cases they have been glad to receive simple publicity pamphlets such as "What the International Bank Means to You." This shows that an effort should be made to spread information more widely as to how the Bank functions.
- B. Limitations on the Bank's Potential Action - It is as important that member countries understand what the Bank cannot do as that they know what it can do. A great deal of future disillusionment can be avoided if too brilliant and alluring a picture of the Bank's possibilities is not now painted.
- C. The Type of Program which should be submitted to the Bank - There appears to be a widespread impression that the less advanced countries only need to obtain a grant of U. S. dollars to be able to realize in a few years their dreams of economic prosperity. This is untrue, not only in relation to the activities of the Bank whose resources can never be adequate to deal with more than a fraction of the world's potential development, but also because of the physical, economic, and social barriers to unreasonably rapid development. Furthermore there will arise in almost every case the problem of attaching the correct priority to the various projects from the point

of view of obtaining a maximum contribution to the productivity and foreign exchange resources of the country in return for the capital outlay. A thorough examination should be made by the countries themselves of every means whereby they can help themselves and thus avoid assuming an unnecessarily large debt burden. Consideration of these factors should take place preferably before these countries turn to the Bank with a request for finance, but in any case, the attention of their governments should be directed to this side of the matter by the Bank at a very early stage, so that awareness of the above mentioned factors can be reflected in the programs.

- D. Internal Reform and Policy - A sound groundwork of economic, fiscal and social reform is often required before a development scheme can be launched. This may entail the preparation of legislation. Related questions such as local investment to cover the part of the program not financed with foreign exchange, and the availability in the country of trained technicians may also need consideration. The necessity for examination of such matters might appropriately be made clear in material or discussions which the Bank sponsors in order to provide a fuller understanding of the economic framework in which it operates.

III. Methods

- A. General Educational Campaigns - The most obvious means of spreading information on the Bank and its activities would be an educational campaign directed not only in general terms to the more or less well-informed business and banking circles in member countries, but also aimed in an appropriate manner more directly at Ministers, civil servants, central bankers, and other prominent people. The technique has already been developed to some extent. A variety of published material can be used.

Some sort of question and answer pamphlet about what the Bank is setting out to do, such as is at present under consideration by the Public Relations Department, would be of value. It has further been suggested that material should be prepared giving a detailed description of how the Bank studies a loan application, emphasizing the care with which all phases of the applicant's economy are examined. This would bring home to governments and officials the importance of their turning to the Bank for advice at the inception of their planning. It would also help to persuade them to produce the required information more readily when making a loan application and to consider more realistically the size and priorities of their plans in relation to the capacity of their countries to carry them out, as well as to the possibilities of obtaining the necessary internal finance. The question and answer pamphlet and the description of the Bank's treatment of loan applications would be useful, also, for wider circulation not only in the potential borrowing countries, but also in financial and investment circles in the U.S.A. and elsewhere. All material of this sort for circulation should be translated into several languages.

- B. Other International Organizations - As far as possible, the Bank should cooperate with other international organizations in the promotion of economic development. The aims of all the international agencies working in the development field are excellent but it appears unlikely that most of them will often be of use to the Bank in connection with its own problems. Nevertheless it is clearly necessary for the Bank to remain in close contact with some of the U.N. specialized agencies if only to prevent misunderstanding on interpretation of its aims. A perusal of the recent report of the U.N. Sub-commission on Development seems to confirm this view.

C. Missions and Personal Contacts - By far the most effective means of acquainting leading figures in underdeveloped countries with the Bank's development policies is through personal contact by members of the staff of the Bank traveling abroad. It must be recognized, however, that this means is limited by the size of the Bank's staff and by the large number of countries wishing to undertake development, as well as the number and diversity of the problems confronting them. The Bank may never have a large enough staff of experts to permit them to spend lengthy annual periods in a large number of countries and cover the whole ground. It is however important that member countries in Latin America, for instance, should not feel cut off from the Bank. This would partly be obviated by having members of the staff who would permanently be located as the Bank's representatives in an area. Their presence could be supplemented by periodical visits of the staff in Washington. In the long run it will in any case probably be found desirable for one member of the staff to remain in fairly constant contact with a particular country's representatives from the inception of the preliminary conversations right up to the conclusion of the loan negotiations and thereafter, as necessity may arise, in order to maintain that confidence which in practice is not always accorded to a succession of strangers.

The question of security for the Bank's loans will be dealt with in another paper, but it is obvious that this is a matter of peculiar delicacy when dealing with sovereign governments. Even where a loan is made to a private corporation, it will still have to be repaid in foreign exchange, dealings in which have by now in the majority of cases been placed under strict governmental control. Repayment is in any case guaranteed by the member government concerned. This means that in some cases the Bank's best hope of obtaining repayment will lie in a tactful

supervision of the borrowing country's policy through almost daily contacts with officials and ministers on the spot. This would enable the Bank to receive notice of any impending crisis likely to impair the country's capacity to service the loan as far ahead as possible so as to permit of corrective action being taken in time to avoid default.

- D. Research Department Studies - The Research Department of the Bank might be of the greatest help if it were able to make thorough economic and financial studies. Such studies should not only be of world-wide trends concerning industries, commodities, population, etc., but also of the importance of those trends in relation to the problems and potentialities of different areas and of the individual countries which compose those areas. Publication of such works when completed by the Research Department would do a great deal to increase the Bank's stature in the eyes of governmental and educational bodies all over the world and would serve to make it clear that there is an advisory side to the Bank's functions, which is as important in many respects as its lending operations.
- E. Directors and Alternate Directors - Another useful way of spreading information about the Bank's role is to utilize as much as possible the Bank's Directors. Many of them are appointed to represent several governments besides that of their own country, and it is possible that they are not able to devote an equal amount of attention to each. They are, nevertheless, in frequent direct contact with the governments which they represent, and from time to time they should pay visits to these countries. One of their most useful functions is to explain the Bank's policies to their governments, and to this end they should be provided with material suited to the Bank's purpose, including the educational publications described above.

F. Cooperation of Major Stockholding Governments - The Bank is a cooperative institution whose members have an interest in using its facilities to obtain finance and also in contributing to its general success. The cooperation of its major stockholding governments might, therefore, be enlisted in the spreading of information about the Bank through their embassies and legations in the underdeveloped countries. Commercial and Financial Attaches occupy ideal positions from which to do this, and every effort should be made to ensure that they are kept informed by their governments of the Bank's policies and activities, and that they receive instructions to pass the information on to those with whom they come into contact. In this way they will help to stimulate interest in the Bank. Furthermore, members of the Bank's staff, when traveling abroad, should make a point of meeting the diplomatic staff, as well as the financial and economic representatives of the United States, United Kingdom, French, and other governments in order to awaken their interest in the Bank. Through the agency of governments, embassies might also be provided with a suitable supply of the Bank's publicity material.

Embassies could also be of great assistance to the Bank in helping to keep governments on the right lines once a development plan has actually been begun. Governments are frequently unstable, and, when they fall, their successors do not always carry on along generally agreed lines. There may be a risk, therefore, that action which has been undertaken at the instigation of the Bank may be discontinued suddenly or else that a disruptive change of plan may take place for political reasons. Concerted pressure on the part of the principal embassies as well as representatives of the Bank might help to prevent such a course of events. It is, in any case, a delicate question to decide just how

far the Bank should go in keeping a watchful eye on a country's economy once a loan has been given, and the cooperation of embassy staffs could greatly ease the difficulties.

COMMITTEE ON DEVELOPMENT POLICY

February 9, 1948

Official File Copy

At the meeting which took place on Friday, February 6, it was agreed that the following additional papers should be prepared for early discussion:

- | | |
|---|----------------------------------|
| 1. Trend of recent economic development in Latin America. How has it been financed? | Messrs. Basch, Clee and Urquidi. |
| 2. Policy for the Bank in Latin America. | Mr. Urquidi |
| 3. Effect of Marshall Plan on Latin American development. | Mr. Rosenstein-Rodan |
| 4. Private capital lending. | Messrs. Basch and Urquidi |
| 5. Should the Bank make local currency loans? | Mr. Rosenstein-Rodan |
| 6. Summary of conditions necessary to prevent loans from being inflationary. | Mr. Rosenstein-Rodan |
| 7. Mobilization of domestic savings. | Messrs. Basch and Clee |
| 8. What security should the Bank require for its loans? | Mr. Clee |

As soon as papers are completed they should be sent to the Secretary for distribution to the other members of the Committee. It is hoped that the Committee may meet on Wednesday next (February 11) to discuss the first group of papers.

R. F. Skillings,
Secretary

c.c: Messrs. Penton
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HOW CAN THE BANK SECURE ACTIVE COOPERATION OF PRIVATE INVESTORS,
BOTH LOCAL AND FOREIGN, IN DEVELOPMENT PROJECTS?

1. Introduction

The Bank has been intended as an agency that, through its own activities, would encourage and promote private foreign investment in member countries, the use of its own funds being conceived principally as a supplement to private investment when private capital is not available on reasonable terms. It therefore seems pertinent that the Bank should be more active in promoting private foreign investment, especially in view of the practical problem in the immediate future posed by the limited capital funds of the Bank itself and the uncertainty regarding future borrowing.

Before attempting to answer any specific questions it might be useful to set out an important aspect of the problem faced by foreign private investors generally. Specific obstacles to private investments are dealt with later.

A first step is to ask who are the private investors of today. Private capital may be provided (a) out of earnings and reserves of existing enterprises with investments abroad, or (b) enterprises as yet without substantial interests in other countries. (c) It may consist also of individual savings borrowed directly from the capital market by either of the types of enterprise just mentioned, or subscribed as additional stock to the latter. (d) The capital may be provided by "new" investors, presumably the so-called venture capital. (e) Finally, one may think too of the substantial supplies of capital funds reaching the market

indirectly, via different institutions; whether they are available for subscription to capital stock of new private enterprises in development countries, or whether they can only be used via International Bank bond issues or other fixed yield investments is a question to be determined.

But, broadly speaking, one thinks of two kinds of private investors (wherever they get the funds from): one is the already established enterprise and the other is the newly-created risk-taking enterprise or venture. Both these kinds of investors have three potential fields of investment (again speaking broadly): raw material and foodstuffs production, public utilities, and manufacturing and services.

The main problem facing private capital in the raw materials and foodstuffs field is that "world markets" no longer exist for such products in the 19th century sense of the term. It is no longer possible, by and large, to go into the development of oil, minerals, cereals, fibers, fruits, or other foods hoping to compete freely in world markets. Today it seems to be necessary to ensure some sort of carefully prepared tie-up with the consumer of the products, whether foreign or national, if any foreign investment is to be made at all in the development of natural resources. In spite of the present attempts at liberalizing international trade and creating conditions of wider competition, the prospect seems to be that, either for monetary or for general policy reasons, new investments to produce natural resources would require some previous agreement as to the market for the products. This leads, in many cases, to the consumers themselves making the investment or participating in it, for example, steel mill interests investing

in the development of iron ore deposits. In other cases it may mean that a field of activity is already more or less monopolized or subject to market arrangements so that independent producers may not enter into it with any prospect of success unless they became absorbed by the larger enterprise. This could conceivably occur in the development of certain minerals, petroleum, etc. If private, independent venture capital is thus excluded and the additional investments in a development country must be carried out substantially by the already existing companies, there is no assurance that the latter's policy will be one of expansion unless they can obtain for the future very favorable conditions from the borrowing countries. Their attitude toward new investment is very much colored by their past experience, when (a) they were accustomed to obtain extraordinary concessions and more or less behaved as they thought fit in return for a small royalty payment or a grudgingly-paid tax, and (b) they started fighting a losing battle against nationalistic economic policies, which have ranged all the way from regulations about proportions of foreign employees to nationalization of the sub-soil and even of the investments themselves.

But even where the linking of the proposed investments to the consuming markets is not an important consideration, there is the additional problem that in most cases it would be necessary to link the development of raw materials to national economic policies. The latter are not always very consistent. There may be no actual development program, but there is bound to be at least a "national economic consciousness" involving at least a feeling that in any foreign investments in primary product development there is nearly always a danger that the foreign capital might behave in ways

detrimental to the country. At best such foreign capital would have to conform to a new type of concession or franchise, to regulations concerning ownership of resources, or concerning participation with local capital, regulations concerning labor, stipulations as to meeting the needs of the domestic market, tax provisions, etc. which might easily be discouraging.

All this is not intended to mean that no private foreign investment at all is possible in those fields. But certainly there is a general problem of fairly great importance, and it will be a difficult one to solve since it will not depend exclusively on what the borrowing country may do to attract the foreign capital, but also on the policies of the already established foreign enterprises.

Regarding the field of public utilities, where the market is nearly always local, the deterrent to private foreign investments would seem to be mainly the possibility of transferring earnings out of the country and the fear of having earnings limited by legislation, coupled with the fear of eventual nationalization. It is not an easy field to enter, the sums of capital required may be unduly large and the periods of construction long; the returns on the investment are, furthermore, not likely to be as large as in other fields. Furthermore, some of the equipment required seems likely to become scarce during the next four years at least.

Investment of private capital in manufacturing industries and in services offers a more open field. It can take the form both of the setting up of subsidiaries by established companies or of new individual enterprises. The latter have the advantage that the owners of the capital provided frequently become residents of the borrowing country. But even subsidiary manufacturing concerns, it is true to say, have given relatively little cause of complaint or friction

with the national governments. Most of them comply readily with the laws of the countries, do not demand special privileges, usually pay high wages and, if anything, are concerned mostly with securing fair treatment in general and assurance of transferring earnings out of the country in particular. The problems for this field of investment seem to be that such type of investment is largely a matter of whether raw materials, power and transportation facilities are locally available, whether the domestic market is wide enough to make the enterprise economical and whether legal and other arrangements, including participation with local capital where required, can be fairly easily made. The experience of the last decade or so would seem to indicate that there are, broadly speaking, two attitudes among potential investors in manufacturing: those who, in addition to complying with the laws and policies of the countries in which they invest, also take pride in contributing something to the development of the country, and those who consider the proposition merely as something in which to invest money and get a return, regardless of anything else. The latter are the type who have shied away and who are vocal in complaining in advance of unfair treatment, exclusively onerous conditions and so forth. Whether they can be persuaded to change their attitude remains to be seen.

To complete the general picture it should be mentioned that a problem affecting all fields of investment is the fear of discrimination against foreign capital, a subject dealt with separately later on. Similarly, uncertainty regarding the return on investments affects every field. It should be possible for the Bank to help to create conditions which would guarantee a better economic outlook in general.

2. Should the Bank Encourage and Assist a Development Program by Financing a Portion of It and the Rest Being Provided by Private Lending?

The answer to this question depends first, on what is meant by "program," secondly, on what kind of private lending is envisaged, and thirdly, on what type of country one is thinking of.

To take the last point first, it may be possible to distinguish three broad types of development countries:

- a. Predominantly primary producing countries, small in population and resources, with a very low standard of living, generally very undeveloped and even culturally backward,
- b. Countries that, while still relying largely on the production of primary products, have reached a moderate stage of development including transportation, textile, metallurgical, chemical, and other industries, processing of raw materials, etc., but still with a low average standard of living and,
- c. Countries which, although still classified as development countries and producers of primary products, have a highly productive agriculture, a considerable amount of industry, an abundance of local savings and, in general, a higher average standard of living.

The reason for classifying countries in this manner is that the types of economic programs in each one are likely to be quite different. The first group is likely to have no program at all, even to the extent that there may be no national policy, and no idea of how to go about developing the country. The second is likely to have some sort of a national economic policy but a very uncoordinated program insofar as a program exists at all; at best

it may be an actual consciousness of the need for carrying out some of the basic development work such as road-building, improving port facilities and waterways, generating power and so on, but with little idea of what the task may require in terms of real and financial resources and of its significance in terms of alternative means of action. It is only the third group of countries which probably has anything that can be called a satisfactory development program in the sense that the responsible social groups and the government know what can be achieved and how.

This poses a serious problem for the Bank. If the less-developed countries do not even have a satisfactory program, how far should the Bank go, let alone in financing a portion of it, but actually in assisting them to formulate a program? This is a subject which is to be dealt with in a separate paper but it may be said here that if no program exists and the Bank, directly or indirectly, does nothing about it, the Bank would not have much influence in encouraging private foreign capital.

The problem is perhaps even more complicated by the fact that some of the countries we have in mind, especially the small, very undeveloped countries, seem to be typically countries where development has to be undertaken very substantially by the Government rather than by private capital or, at any rate, under Government sponsorship. Two interesting examples of this are Guatemala and the Philippines, where a tendency toward Government enterprise or sponsorship seems to be very strong. If, however, it is felt that the Bank should not wait until a development program be formulated, with or without its help, the possibility of financing

individual projects of basic necessity, as distinct from a "program", might be explored further.

In the second and third groups of countries, where the difficulty of the existence of a development program is at least partly overcome, the Bank could undertake to finance parts of the program in order to encourage private lending to finance the rest of it insofar as the program has room for private capital. But what sort of private lending do we mean? Do we contemplate the investment of risk capital, or additional investments by existing enterprises, or the purchase of bond issues? In view of what has been said about the general outlook for different fields of investment, it hardly seems very likely that private lending of the risk-capital type or even of the established-enterprise type could go into anything but manufacturing and service industries. Investment in bond issues, on the other hand, might be possible if there were adequate guarantees given, perhaps by the Bank itself. If the prospects of private capital going in are not very hopeful, and if a development program as such aims at only the basic needs, it would appear that the proportion that the Bank might have to finance would be relatively large.

This ties up with the thought that the Bank's action is to serve as an encouragement to private capital investment and to private lending in the sense of a sort of insurance that basic development will lead to conditions favorable for private capital activities, it would then seem that the Bank would have to participate quite largely in determining the type of development program to be adopted including its qualitative aspects, such as a certain degree

of direction or control over the kinds of capital formation. To put it in other words, it is only if the Bank steps in in a big way that it can have much appreciable effect in encouraging private capital investment.

Given this background, the Bank's action on a number of specific points might help to promote private investments. Such action could include (these points are capable of further elaboration):

- (a) To create the proper atmosphere for the borrowing country among private investors,
- (b) To promote, encourage and even finance the study of investment possibilities and projects in the borrowing country,
- (c) To "sell" the program and the specific projects to potential investors,
- (d) To aid in removing any unreasonable obstacles to foreign investments, and
- (e) To provide appropriate guarantees where necessary.

There are a number of other complications relating to the precise type of project particularly appropriate for the Bank. Public utilities have been mentioned as a possible appropriate kind of project, assuming that this would cover power, railways, tramways, airlines and transportation in general, port developments, gas, telephones, municipal water-works and drainage, irrigation schemes, etc. The question arises: would it be sufficient from the point of view of private capital that such

kinds of projects be undertaken, or would private capital be better satisfied if the Bank undertook additionally or alternatively to help finance some of the other bottlenecks of economic development which may include the production of agricultural machinery, petroleum development and refining, road-building, colonization schemes, food supply projects, and so on? From the standpoint of the Bank, some would have the disadvantage of not requiring very heavy foreign exchange outlays (the possibility of financing part of the local currency expenditure is to be discussed in another paper). Another problem is created by the fact that the probable yield on some public utilities is too low to cover the interest on the Bank's loans. There are also problems connected with the fact that some public utilities require at least a participation of foreign private capital in view of the requisite technical knowledge which usually accompanies it. And there are questions of management of public utilities in which there may be very little local experience. It may well be possible to work out arrangements for having private capital participate technically but not financially, or of bringing together local private capital into the schemes with foreign private capital. The question arises, too, as to whether borrowing countries have banking or other institutions capable of channeling the flow of local savings.

3. Should the Bank undertake to guarantee private foreign capital investments in development projects?

(This point open for discussion)

4. What have been the most important obstacles to private foreign investment in various countries? Can these obstacles be removed through international agreement or otherwise?

Obstacles to private foreign investment may be economic or non-economic in nature. By economic is meant the conditions regarding raw materials, market, transportation, labor supply, etc. that make possible and profitable a new investment. Those facing the investor in an undeveloped country are no different in nature from those facing him in a developed country.

A distinction seems to arise, however, with regard to non-economic obstacles. An enumeration of the chief of these follows:

a. Lack of equality in access to law and fear of arbitrary behavior by the administrative authorities. The elimination of this obstacle is reasonable, although it is to be doubted whether investors' protests are likely to be successful should they be directed against existing constitutional provisions in the borrowing country.

b. Double taxation. Means are being studied to prevent it.

c. Fear of discriminatory taxation. While it appears to exist in some countries, it is sometimes merely the result of the fact that some specific activity that is taxed more than others is monopolized by foreign capital.

d. Compulsory reinvestment of profits.

e. Compulsory participation with local capital. A variant of this is compulsory 51% majority of local capital.

f. Rigid provisions regarding percentages of local and

foreign employees, technicians, directors, etc.

g. Fear of nationalization.

h. Restrictions on ownership of land, mineral deposits, etc.

i. Restrictions on the transfer of profits.

Apart from the pressure brought to bear on certain countries by foreign Governments or by business groups, which has no doubt resulted in the reduction or elimination of some of these obstacles, there has been no concerted attack on the obstacles. However, some countries are known to accord foreign capital satisfactory treatment, and others have gone a long way to eliminate any suspicion of discriminatory practices.

Judging by the efforts of the last year or two, the attempt to remove these obstacles by international agreement has not met with much success. Such international agreement has taken the form of a proposed "investment code". The League of Nations published a report by a special joint committee which met in 1945. This report, although it does not suggest an outline of an investment code, does nevertheless survey the problem and make recommendations as to ideals to be achieved, behavior to be observed by foreign investors, minimum conditions to be offered by borrowing countries and relations between capital-exporting and capital-importing countries.

Subsequently the Economic and Social Council of the U.N. suggested that a study of an investment code be taken up by its Subcommission on Economic Development. The first meeting of the latter was held in December, 1947, but that subject was dropped from the agenda, although reference was made to it with special emphasis on the protection of the capital-receiving countries.

Meanwhile, the I.T.O. Preparatory Committee at the London conference in November, 1946, proposed a technique of consultation under which the ITO could attempt to seek redress for the investors in cases in which the latter considered that a particular national policy was injurious to them.

This line of approach was considered to be weak, however, and it was abandoned.

The next stage was the Geneva Conference of 1947 to draft the I.T.O. charter. The United States delegation tried to obtain a more definitive statement on the rights of investors, namely that there should be equal treatment, except when announced publicly to the contrary, provided there were most favored treatment and just compensation in cases of nationalization. A further suggestion was made that the Government of the investee country should file, in each case, a statement with the I.T.O. setting forth conditions, requirements or restrictions of the country, applicable to the opportunity for making investments and to the treatment of existing and future investments. It was still felt, also, that the I.T.O. should take the initiative in the matter of an investment code. A complementary aspect was that the conference envisaged the creation of a Committee on Economic Development and Investment.

The United States proposals at Geneva were initially well received but later objected to and were watered down by the United States delegation itself. Some of the objections were technical, and others were of a political nature. The wording adopted at Geneva was introduced again at Havana where the United States delegation has reduced the proposed provisions to providing mere consultation. There seems no prospect of getting a text which would give investors generally enforceable rights.

The conclusion seems to be that, given the apparently conflicting interests between the developed and the undeveloped countries, it is not possible to obtain agreement to an effective

investment code setting forth general obligations as to the treatment of foreign capital. It is notable that even a country like Australia, which is said not to have discriminated against foreign capital, is reluctant to undertake general international commitments. This would seem to indicate that the general investment code procedure has been, up to now, weighted heavily on the side of the investor countries in its demands upon the borrowing countries. Unless the whole approach is brought down to a level nearer the interests of the capital-importing countries, no definite commitment seems obtainable.

A specific proposal has been made by a close observer of the subject over the last two years, namely, that of filing "investment agreements" with some international organization, be it the I.T.O. or the IBRD. An outline of this proposal is given below for purposes of discussion.

It may well be, however, that the first and most important thing to do, at any rate from the point of view of this Bank, is to make a careful survey among investors (both individuals and corporations), as well as in business and financial circles of the United States, to ascertain what precisely are the obstacles which at present (as distinct from 5 or 10 years ago) are holding back foreign investment in undeveloped countries, or in particular areas or particular countries. The so-called obstacles to private foreign investments seem to have been taken a good deal for granted. Potential investors are often apt to generalize on the basis of one particular experience or as a result of having approached investment in a particular country starting out on the wrong foot. There would appear to be a considerable amount of mis-information and misunderstanding among potential in-

vestors, for example, as to taxation, participation with local capital, 51% rule, etc. It would be very advisable for the Bank, therefore, to poll opinion among the investor public.

Whether or not such a poll were to reveal results differing substantially from what is now taken for granted, it should, at any rate, indicate the lines along which the Bank could act among the lenders and investors themselves. The need is keenly felt for some organization to persuade the sometimes recalcitrant investors to change their attitude by pointing out to them the cases in which their fears are unjustified and helping them realize the constructive forces at work in borrowing countries.

It would seem that any success in that direction would help a great deal towards eventual adoption of an investment code or some intermediate transitional scheme such as that of "investment agreement filing".

This system envisages "foreign investment agreements" to which the Government of a borrowing or investee country is a party or in which it has an interest. The agreement would lay down the conditions, restrictions and general regulations to which the particular investment is subjected, and the Government could file it with an international organization such as the I.T.O. or possibly the IBRD.

Some disadvantages are recognized such as:

- a. It could not apply to past investments, nor to cases where the Government is not a party,
- b. It would permit Governments to discriminate,
- c. It would lead to pressure by investors on their own Government to bring pressure in turn on the Government in

the investee country to enter into an agreement with the investors.

On the other hand, such a system would have advantages:

- a. That, in return for the contractual system of conditions, restrictions, etc., binding the Government and the investor, the Government would have a quid pro quo in the form of a definite and tangible investment,
- b. That the case could be heard by an independent arbiter.

As regards having the system handled by the I.T.O., there is this in its favor:

- a. The I.T.O., in view of its other functions, is better adapted than other Agencies,
- b. It would be an aid to the I.T.O.'s economic development activities,
- c. In the I.T.O. there is likely to be only one vote per member, and
- d. There are less conflicting interests in the I.T.O.

Among the disadvantages in having the I.T.O. handling it are:

- a. The large number of other functions of the organization which may be more important or urgent, and
- b. A delay in setting the I.T.O. up.

A possible suggestion would then be that the Bank participate actively in the matter. The Bank (or the Fund) might call a conference on the subject of the treatment of foreign capital and the possibility of filing investment agreements. Three main questions would have to be answered first:

- a. Could, and should the Bank take over the filing function,
- b. Would there be a conflict of interests between arbitration on this matter and the loan functions of the Bank, and
- c. Would sanctions be necessary?

In conclusion, the proposal for filing investment agreements is not specifically recommended in this paper, either in general or for the Bank, but it is hoped that the Committee will discuss it and that any other alternative methods of achieving similar results will be brought up and outlined for consideration by the Committee.

February 5, 1948

Committee on Development Policy

Summary of Mr. Luxford's Memo on Enforcement of "Foreign Investment Agreements".

Mr. Luxford proposes "investment agreements" (to which a Government is a party) as part of measures to safeguard foreign investments from unreasonable Governmental action.

He makes a brief review of recent developments in connection with the subject of a foreign investment code:

1. The Economic and Social Council of the UN instructed its Subcommission on Economic Development, in February 1947, to study the need for an international investment code. Mr. Luxford concludes that, especially since the emphasis in the Subcommission has subsequently been on protecting the country receiving the investments, the prospect of an effective investment code is very remote in this line of approach.

2. The I.T.O. Preparatory Committee, at the London Conference of November 1946, proposed a technique for consultation for cases in which the investor believed he had been injured. The possibility of I.T.O. sanctions was envisaged. However, the chances of this approach are also weak.

3. The next stage was the Geneva Conference of 1947 to draft the I.T.O. charter. The United States delegation tried to obtain a more definitive statement on the rights of investors, namely that there should be equal treatment, except when announced publicly to the contrary, provided there were most favored treatment, and just compensation in cases of nationalization. A further suggestion was made that the Government of the investee country should file, in each case, a statement with the I.T.O. setting forth conditions, requirements or restrictions of the country, applicable to the opportunity for making investments and to the treatment of existing and future investments. It was still felt, also, that the I.T.O. should take the initiative in the matter of an investment code. A complementary aspect was that the conference envisaged the creation of a Committee on Economic Development and Investment.

The United States proposals at Geneva were initially well received but later objected to and were watered down by the United States delegation itself. Some of the objections were technical, and others were of a political nature. The wording adopted at Geneva was introduced again at Havana where the United States delegation has reduced the proposed revisions to providing mere consultation. There seems no prospect of getting a text which would give investors generally enforceable rights.

Mr. Luxford believes that the general ^{obligations} ~~applications~~ procedure is not feasible. The reluctance to undertake a general international commitment comes even from a country like Australia, which has not discriminated against foreign capital. Instead of that, Mr. Luxford proposes a system whereby any member of the I.T.O. may file with the latter "any foreign investment agreement to which it is a party or in which it has an interest", thereby permitting any complaints to be heard by the I.T.O..

There are some disadvantages to this proposal which he, himself, recognizes:

- a. It could not apply to past investments, nor to cases where the Government is not a party,
- b. It would permit Governments to discriminate,
- c. It would lead to pressure by investors on their own Government to bring pressure in turn on the Government in the investee country to enter into an agreement with the investors.

On the other hand, such a system would have advantages:

- a. That, in return for the contractual system of conditions, restrictions, etc., binding the Government and the investor, the Government would have a quid pro quo in the form of a definite and tangible investment,
- b. That the case could be heard by an independent arbiter,
- c. That the I.T.O. is to be empowered in any case to employ sanctions,
- d. That there would be flexibility in interpretation.

It ^{is} ~~was~~ recommended then that a beginning be made with this filing procedure on a voluntary basis and that its scope be enlarged later. Both the Bank and the Fund could help to get members to give a broader application to the procedure in time, especially if the Bank were to enter the guarantee field; and in some cases in connection with debt settlement programs. The procedure is essentially to be understood as a stimulus to investment.

As regards having the system handled by the I.T.O., there is this in its favor:

- a. The I.T.O., in view of its other functions, is better adapted than other Agencies,
- b. It would be an aid to the I.T.O.'s economic development activities,
- c. In the I.T.O. there is likely to be only one vote per member, and
- d. There are less conflicting interests in the I.T.O.

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A possible suggestion would then be that the Bank participate actively in the matter. The Bank (or the Fund) might call a conference on the subject of the treatment of foreign capital and the possibility of filing investment agreements. Three main questions will have to be answered first:

- a. Could, and should the Bank take over the filing function,
- b. Would there be a conflict of interests between arbitration on this matter and the loan functions of the Bank, and
- c. Would sanctions be necessary?

vLU:js

Victor L. Urquidí

February 5, 1948

John M. Penton

Development Policy Committee

Mr. Garner is anxious that the Development Committee should press on urgently with its work with a view to the formulation of the Bank's policy towards Latin America. Latin American problems require more urgent attention than those of other development areas of the world, and our objective should be ultimately to provide Mr. McCloy with the basis of a statement which he could take with him to the Conference at Bogota.

This will necessitate the calling of a meeting of the Development Committee early next week and a review of the agenda in order to see what papers can be produced, if only in rough form, speedily and in such a form as to stimulate thought on Latin America. Before convening the full Development Committee, however, I should like to have a talk with the Loan Department's Development Committee, and, consequently, I hope that it will be possible to arrange a meeting tomorrow (Friday). I would suggest 11:00 AM, but if this time is unsuitable to anyone, perhaps he would get in touch with Miss Pahl with a view to fixing another time for the meeting which would be convenient to all concerned.

cc: Messrs. Clee
Skillings
Consolo

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

January 30, 1948

Mr. Demuth:

Mr. Rist requested that I
send to you, on his behalf, two
copies of the attached memoran-
dum on "Industrialisation and
Economic Development".



Harold Larsen,
Economic Policy
Studies Staff,
Research Department.

Attachments 2

Industrialisation and Economic Development

"Industrialisation" may mean either the economic development of "backward" countries, or a proportionate growth within a country (itself at any stage of economic evolution) of industrial factory production, as contrasted, for example, with agricultural production. Industry may be classified as either primary, (broadly speaking, agricultural and pastoral) secondary (factory output of manufactured commodities) and tertiary (non-commodity output such as transport, electric power distribution, and direct personal services). Using this classification, "industrialisation" in the broad sense embraces both increased efficiency of primary production and simultaneous emergence probably of secondary and certainly of tertiary industry. In its narrower sense, it may mean only a proportionate growth of secondary industry.

That is, in its wider meaning of economic development, "industrialisation" does not necessarily and in every case involve any great growth of secondary or factory industry. It denotes a change in the methods and perhaps range of production, potentially embracing the whole scale of productive activity, a change brought about by introduction of more modern techniques using increasing capital equipment and able to draw more fully on native natural resources. "Industrialisation" in this sense is thus equivalent to capitalisation, production becoming more "mechanised" and less manual. Historically, the result of such capitalisation has been considerable increase of output and national income. And in certain conditions

"industrialisation" may have this result without any emergence of heavy industry proper, without the appearance of new Pittsburghs or Birminghams in "backward" countries. Essential capitalisation may, that is, be principally in the field of power distribution, transport and communication (tertiary industry or "public utilities"), and in agriculture.

The economic development of New Zealand illustrates the process, and suggests the circumstances under which it may usefully be stimulated to the neglect in official programmes of industrial factory production, namely, conditions of under population and the existence of good export markets for agricultural products.

Without export markets for agricultural products, the output of which would be increased by capitalisation of agriculture, that output can neither be disposed of profitably nor permit (through international trade) increased consumption by the local population of manufactured products. "Industrialisation" in the narrower sense becomes necessary to provide a growing range of consumption goods corresponding to increased national income.

At the same time, increased output in the industrial sector, both factory and public utility, generates new incomes for producers concerned, enabling them to take up increased or improved farm products, such as foods. In this sense, growth of domestic industry can provide some substitute for agricultural exports, enabling and finally necessitating improved agricultural methods. Rural and industrial consumer demand thus becomes mutually and cumulatively stimulating, suggesting a promising line of economic development for "backward" countries lacking export markets.

Under conditions of "over-population" it may be vitally necessary

in the capitalisation of agriculture to move people off the land into other and useful employment. Where a high proportion of population is supported on land under conditions of rural poverty, much of this potential labour-power is, properly speaking, unemployed; that is, it is making no contribution at all to national output. Any degree of mechanisation of agriculture, even so slight as the introduction of modern plows or improved live-stock, will, under these conditions, necessitate a reduction of rural population to permit increase of agricultural output. Such reduction in turn involves the provision of alternative occupations for those displaced. Some may be absorbed into transport construction and services and the like, but it is to be expected, in these conditions, that growth of domestic factory industry would be desirable and justified. Part of such growth might, of course, be represented by capitalised "factory" methods of processing food products.

It should be noticed that, in addition to the whole problem of appropriate directions of capital investment, this occupational transfer of population in heavily populated "backward" countries raises extremely difficult problems of personnel education and technical training. Farm workers, knowing only traditional rural methods cannot be turned in any short period into skilled factory workers, and if their training, and more particularly that of their children, be inadequate or neglected, industrial plant provided by international investment programmes may be of little real utility to anyone. The physical existence of a factory does not guarantee output. This in turn suggests that in "backward" countries of high rural population, such industry as is stimulated in the earlier stages of economic development should be simple, requiring the minimum of specialised industrial skills.

Such industries are most likely, at first, to be those producing simple consumption goods, and to be "light" industries, employing small amounts of specialised capital equipment per worker. It may be possible to build upon traditional craft skills in introducing some mechanised techniques, and so avoid the dilemma of an over-wide "technical gap" in labour abilities. Should the development programme include distribution of electric power, additional capital investment for the mechanisation of such light consumption good industries would not necessarily be heavy, and may well be within the reach of local initiative. And the immediate short-run result, being a relatively quick increase in simple consumption goods, may itself cumulatively stimulate development, both by increasing the health and efficiency of the consuming population, and by providing them with cash incentives for further effort as producers. Moreover, once the services of reasonably adequate public utilities were available, in the form of transport facilities, power distribution, and the like, the scale of useful capital investment in such light consumption-good industries would be relatively continuous, that is, would involve no very large single investment to make increase of output possible. In economic development, the heavy "all or nothing" investment is more probably necessary in establishment of adequate public utility services.

It is, however, the heavy factory industries, requiring similar large "all or nothing" investment, that representatives of "backward" areas usually claim as essentially necessary for even their early economic development. For the reasons already outlined, it is doubtful if this claim is economically sound. Such heavy industries, normally utilising a very high

proportion of capital equipment to value of output, represent a diversion of capital investment (always in any one period a finite maximum amount) from directions more likely to result in an over-all economic development in the early stages, such as provision of transport facilities and power, which provide the basic capitalisation of an integrated regional or national economy. They would demand of both management and labour technical know-how and skill of a depth and range unlikely to be available. And, since the product of heavy industry is not usually finished consumption goods, its development provides little demonstration to the bulk of the population of the direct advantages to them of further economic development.

In the early stages of development, the proper source of heavy industrial output, itself largely of the nature of capital equipment, useful not for direct consumption but for further production, is the advanced industrial countries, which are geared to its economical production. Indeed, it is partly for the reason that efficient capital equipment is only, or best, available overseas, and partly because export earnings of foreign exchange are usually insufficient to finance its current acquisition in the quantities required for development purposes, that international investment is called for to make a reasonable rate of economic development possible during the relevant future.

It is clear, nevertheless, that in highly populated "backward" countries "industrialisation" in the sense of economic development may well involve an appropriate rate of growth of both factory and public utility industries, but the rising national income which results from such development does not originate in factory industry as such; it stems from the more efficient use of labour in all activities which become adequately

capitalised, that is, "mechanised". It is the problem of "surplus" rural population, and perhaps of inadequate export markets, which necessitates some growth of "industrialisation" in the narrower sense.

If economic considerations are to prevail, therefore, a case must be made in each case taken separately for the establishment of factory industries as part of economic development. The "backward" countries whether over- or under-populated are "backward" essentially because they do not yet use modern methods of transport and power, modern types of capital equipment and technical methods, not only or even importantly because they lack factory industry. Their desire for the early establishment of such industry in full panoply probably arises partly from mistaken interpretation of the economic strength of advanced countries, and principally from intrusion of considerations of political and national prestige. Yet Britain, for example, derived little power or prestige from the possession of idle cotton capacity in Lancashire in the 1930's.

OFFICE MEMORANDUM

TO: R. H. Demuth

FROM: Victor L. Urquidi *jm*

SUBJECT: Committee on Development Policy:
Technical Training and Education

DATE: January 27, 1948

In addition to the Resolution of the UNESCO creating an International Institute of the Hylean Amazon, I find a number of other Resolutions passed at the recent Mexico City conference which have a bearing on economic development, especially with regard to technical training and education. I am listing these in the attached memo. The main purpose of this note, however, is to suggest that it might be useful for the work of the Development Committee to have fuller information on technical and vocational training problems of under-developed countries from:

- a. The Unesco, Division of Education, and
- b. The International Labor Office.

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attach.

cc: Messrs. Penton
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Resolutions of the 1947 UNESCO conference relevant to the
work of the Development Committee, especially
to technical training and education

"1.1.1. The Director-General is instructed, following the contacts already made with the Economic and Social Council of the United Nations and the Economic Commission in Europe and the Far East, to approach the appropriate organs of the United Nations and the Specialised Agencies in order to ensure that in the development of reconstruction plans, proper attention shall be paid to the needs of reconstruction in the educational, scientific and cultural fields.

"1.6. Meeting Technical Needs. In order to promote the implementation of the recommendations made in the first report of the Commission on Technical Needs (2C/8), the Director-General is instructed:

.....
"1.6.4. To obtain the advice of a group of financial experts on the feasibility and methods of creating an international loan for cultural reconstruction, and of making arrangements whereby countries in need of foreign currency for cultural reconstruction might receive the currency they need and in return provide facilities in their own currencies for professional and cultural visits to their own countries; to present a report, if possible to the first session of the Executive Board in 1948, and to take such further steps as may be authorised by the Executive Board.

"2.1. Exchange of Persons.

"2.1.1. Unesco will in 1948 continue a programme for the Exchange of Persons.

"2.1.2. The Director-General is instructed:

"2.1.2.1. To request the co-operation of Member States in the preparation of reports on the activities of governmental and non-governmental organisations affecting the international movement of persons. These reports should include data on the number, character, availability and sponsorship of fellowships and other types of assistance --

currently offered or proposed for study, research, teaching, training and observation abroad together with information on fellowship awards, fields and countries of study.

"2.1.2.2. To collect, compile, analyse and publish this and other relevant material and determine the effectiveness of existing programmes for the interchange of persons in terms of Unesco's general objectives.

"2.1.2.3. To disseminate the results of this work to Member and Non-Member States and to those private agencies and individuals which may be interested in such information.

"2.1.2.4. To stimulate the establishment of additional governmental and private fellowships and travel grants, suggesting to donors appropriate conditions and standards of award.

"2.1.2.5. To administer in collaboration with national commissions or appropriate bodies in the Member States the fellowships already authorised out of Unesco's 1947 funds, and in addition ten new fellowships (or the equivalent expenditure for travel grants) to be awarded in exceptional cases where Unesco's purposes are clearly involved and where no other funds are available; and also to collaborate, when requested by donors, in the administration of those fellowships already offered or which may be offered by governments, voluntary organizations or individuals.

"2.1.2.6.1. To study in collaboration with the relevant organs of the UN, the barriers which impede the interchange of persons between and among nations, thereby impeding the free flow of ideas between peoples. Special attention should be given to barriers due to the shortage or lack of transport facilities, the difficulties of currency exchange, and the restrictive laws and regulations of Member States.

"2.1.2.6.2. To take such measures as are appropriate and practicable to remove these barriers.

"2.1.2.7. To study the possibility of encouraging the interchange of persons through bilateral or multilateral conventions among Member States.

"2.1.2.8. To recommend to the Member States concerned appropriate steps for the co-ordination of the movement of young persons between countries in certain parts of the world, where such co-ordination is needed.

"2.1.2.9. To observe the following conditions in carrying out the Programme of Interchange of Persons:

"2.1.2.9.1. That the Director-General's efforts be specially concerned with mature persons, such as research workers, technicians, teachers, professors, artists, government officers, experts, leaders in adult education and industrial and agricultural workers.

"2.1.2.9.2. That, in the administration of fellowships, the Director-General maintain the closest collaboration with the Economic and Social Council, the World Health Organization, other specialised Agencies of the United Nations and Member States to ensure that overlapping is avoided and conformity of operations and finance is developed.

"2.1.2.9.3. That, in encouraging the establishment of fellowships and travel grants, as well as in the recruitment of fellows, the Director-General give special attention to the needs of the war-devastated countries.

"3.4. Fundamental Education. The Director-General is instructed:

"3.4.1. To encourage Member States to fulfil the obligations of establishing a minimum Fundamental Education for all their people, in conformity with the spirit of Article I, paragraph 2 (b) of Unesco's Constitution; among these obligations would be the establishment, within the shortest possible time, of universal free and compulsory primary education and the essential minimum education for adults.

"3.4.11. Pilot Projects. To co-operate with Member States in establishing or assisting, with adequate staff, "Pilot Projects" in Fundamental Education.

"3.4.11.1. To continue to develop the Pilot Projects approved in 1947 in China and East Africa, and to develop, within the East African Pilot Project, as a comparative experiment with the Nyasaland enterprise, Unesco's participation in the Tanganyika agricultural development scheme under the British Overseas Food Corporation.

"3.4.11.2.1. Subject to the subsequent provisions of this resolution, to explore all appropriate means to assist the financing of the "Pilot Project" in Haiti, to which Unesco is committed.

"3.4.12. Associated Projects. With the co-operation of Member States, to link up as Associated Projects, within Unesco's network, important enterprises in Fundamental Education in all parts of the world. In an Associated Project the responsible authorities will appoint their own liaison officer with Unesco, send to Unesco general and technical reports on its progress and receive in return relevant documents and material distributed by Unesco. Personal contact will be established with as many as possible of the Associated Projects by occasional visits of a Unesco travelling Expert Consultant or of other members of Unesco's staff or Panel of Experts.

"3.15. Science in General Education. The Director-General is instructed to invite Member States to submit to Unesco general statements on the role of science in general education in their communities.

"3.17. Vocational Guidance and Technical Education. The Director-General is instructed:

"3.17.1. To collaborate with the International Labour Office in its study and development of vocational guidance.

"3.17.2. To recommend to all States that they orient technical education at all stages toward the achievement of the objectives of Unesco.

"3.17.3. To give priority in the programme of technical education to the needs of those countries which, possessing natural resources, lack the means to utilise them.

"5.6. Social Implications of Science. The Director-General is instructed:

"5.6.1. To prepare, in co-operation with appropriate international organisations, a summary report on work for the popularisation of science being carried on by existing national organisations; and to circulate this report to all Member States in order to encourage the establishment of organisations for popularising science in those countries not possessing such organisations.

"5.6.5. To bring to the attention of the Secretary-General of the United Nations the importance of a wide understanding of the social implications of scientific developments.

"5.6.6. To promote basic research on the social implications of science as shown in recent and earlier history, by seeking to obtain funds for at least three fellowships for representatives of diverse nations within the general programme approved for fellowships.

"6.1. Field Science Co-operation Offices. The Director-General is instructed:

"6.1.1. To maintain Field Science Co-operation Offices in the Middle East, the Far East, and Latin America and to establish an Office in South Asia in 1948, as undertakings of the highest priority within the Natural Sciences programme. In this connection the Director-General shall give due regard to the following considerations:

"6.1.2. The effort and budget of the Latin American Field Science Co-operation Office in 1948 shall be concentrated on specific liaison tasks and shall be closely co-ordinated with the Hylean Amazon project.

"6.2. Latin American Conference. The Director-General is instructed to convene a Panel of Experts in Latin America to advise Unesco as to the best way in which the development of science in Latin America may be assisted in the future; provided that the governments and other Specialized Agencies of the United Nations concerned are prepared to pay the expenses of the meeting and that Unesco's only expenditure shall be for the attendance of its own representative and, if necessary, that of an exceptional expert not nominated by his government.

"6.3. Hylean Amazon Institute. The Director-General is instructed to take steps to bring into being in 1948 an International Institute of the Hylean Amazon. To that end he shall:

"6.3.1. Forthwith call a meeting of the Council, consisting of representatives of the nations and international organisations named in the report of the meeting of the Commission at Belem in 1947, together with representatives of any other country or international organisation that may express itself as interested.

"6.3.2. Use his best efforts to assure that the Executive Committee and the Survey Staff proposed in the report of the Belem Commission are set into motion as soon thereafter as possible.

"6.3.3. In carrying out the above instructions, 6.3.1. and 6.3.2., observe the following conditions:

"6.3.3.1. Unesco's role in the setting up of the Institute is to initiate and to stimulate. Without any financial commitment beyond 1948, Unesco shall in 1948 make available the sums necessary for the meeting contemplated in 6.3.1. and shall provide the temporary survey staff contemplated in 6.3.2., and shall make available the services of the Field Science Co-operation Office in Latin America, as provided in 6.1.2. above.

"6.3.3.2. Consult with interested governments and organisations concerning the future financing and administration of the Institute and present his recommendations to the Executive Board prior to the Third Session of the General Conference.

"6.6. Co-operation with Non-governmental Organisations. The Director-General is instructed:

"6.6.1. To further international scientific co-operation by means of grants-in-aid and other similar forms of assistance to international scientific and technological organisations, unions and societies.

"6.6.2. To assist in the international organisation of scientists engaged in the applied field of engineering, agriculture and medicine, provided that in the latter fields the necessary close co-operation with the Food and Agriculture Organisation and the World Health Organisation respectively be maintained.

"6.6.3. To provide to scientific bodies within nations appropriate financial and other aid for carrying out scientific work of international significance along the lines of Unesco's aims, after consultation with the relevant Government or National Commission or co-operating body, with the International Council of Scientific Unions and with the appropriate specialised union, subject to regulations adopted by the General Conference.

"6.9. Protection of Nature. The Director-General is instructed:

"6.9.1. To accept the invitation of the Economic and Social Council of the United Nations to participate in the preparations for, and the deliberations of, the forthcoming Scientific Conference on the Conservation and Utilisation of Natural Resources."

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INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

January 27, 1948

*Development
Committee
file*

Mr. Demuth, Rm. 1023

Attached is your study on Item II-G of the agenda which I have had copied and circulated to the Committee in preparation for discussion at an early meeting. I have also had circulated recently the following papers of interest to the Committee:

- (1) Two documents from FAO on agricultural development and on the need for concerted action to increase world food supplies.
- (2) An analysis by the Research Department of the Bank of the Report of the United States Railway Mission to Mexico, 1942-46.
- (3) The report to Mr. McCloy by Mr. Illanes after his recent trip in Latin America.
- (4) A statement by Mr. Martin of the Exim-bank before the Inter-American Economic and Social Council.

RFS
R. F. Skillings
Secretary, Committee on
Development Policy

Prepared by: ~~Staff Office~~ Committee on Development Policy
~~Enrique Lopez-Herrero~~

January 20, 1948

Item II - G of Agenda

Activities of Other Inter-Governmental Organizations Interested in Economic Development

1. The United Nations and its Subsidiary Organs

The United Nations is charged with responsibility, under Article 55 of its Charter, ^{to} ~~with~~ ^a ~~promoting~~ "higher standards of living, full employment, and conditions of economic and social progress and development." Chapter X of the Charter establishes the Economic and Social Council, giving it specific powers to set up commissions in the economic field, and "such other commissions as may be required for the performance of its functions."

A. Economic and Social Council

From the beginning of its activities the Economic and Social Council has stressed economic development. At its first meeting in London in January 1946, the Council adopted a resolution establishing an Economic and Employment Commission charged to advise the Council, among other things, on problems of economic development, including particularly those relating to less-developed areas. Further, the Commission was directed at that time to establish a Sub-Commission on Economic Development to advise the Commission "on the long-term development of production and consumption throughout the World", with particular emphasis on the "methods of increasing production, productivity and levels of consumption in the less-developed regions of the World", and "the effects of industrialization and technological change on world economic conditions."

During the Third Session of the Economic and Social Council held in December 1946, the Council decided to modify the terms of reference of the Economic and Employment Commission regarding the Sub-Commission on Economic Development, requesting it to instruct such Sub-Commission "to study and advise on the principles and problems of long term economic development with particular

attention to the inadequately developed parts of the World."

The Fourth Session of the Economic and Social Council, held in March 1947, considered at length various aspects of economic development. At this Session, while considering the instructions of the Economic and Employment Commission to its Sub-Commission on Economic Development, the Council requested the Commission to investigate and report the most appropriate form of international action for facilitating the better utilization of world resources in order to promote adequate economic development in under-developed areas. Likewise the Council expressed the view that it would be appropriate for the International Trade Organization to assume the functions relating to economic development set forth in its draft charter.

During the course of the Fourth Session of the Council, it established an Economic Commission for Europe, with headquarters in Geneva, and an Economic Commission for Asia and the Far East, with headquarters in Shanghai. The terms of reference of each Commission stress economic development by directing it to "make or sponsor investigations and studies of development." The activities of those Commissions will be discussed later in this Report.

The concept of regional economic commissions to carry out the responsibilities of the Economic and Social Council seems likely to spread. An ad hoc committee appointed by the Council has already recommended the establishment of an Economic Commission for Latin America, and this recommendation will be considered by the Council at its forthcoming session in February. At that session, too, the Council will consider the establishment of an Economic Commission for the Middle East.

B. Economic and Employment Commission

The Economic and Employment Commission held its first session in January 1947. At that session the Commission considered the following items on its agenda related^{ing} to economic development:

- a) Consideration of its possible activities in the ~~Field~~ of ~~Economic Development~~, and the relation of those activities to the activities of the Specialized Agencies and of the various Commissions and Sub-Commissions established by ECOSOC.
- b) Consideration of ~~Surveys~~ of the ~~Economic Development~~ of ~~Less-Developed Areas~~.
- c) Consideration of ~~Effective Ways and Means~~ for ~~Furnishing Technical Advice~~ to Member Governments.
- d) Consideration of a ~~Proposal~~ to ~~Establish an International Code~~ ~~Relating to Foreign Investments~~.

On the above questions the Commission arrived at the following conclusions:

The Commission concluded that "responsibility for the actual carrying out of development activities rests with the governments and peoples of the countries or areas concerned, who may seek assistance from whatever source they deem expedient." The Commission stated that "the initiative for the preparation of concrete plans and programmes for the economic development of any country or area, is in all cases the exclusive prerogative of the governments or peoples of the country or area concerned."

On the matter of technical assistance the Commission concluded "that countries desiring technical assistance should themselves perform as much of the work as possible in advance, including the preparation of preliminary studies in such detail as is possible."

The Commission agreed to instruct its Sub-Commission on Economic Development to make a study, in cooperation with the other Commissions of the United Nations and the Specialized Agencies concerned, of the need for an international code relating to foreign investment, and of the need for and methods of international incorporation of private business firms conducting business operations on an

international or a world scale.

C. Sub-Commission on Economic Development

The Sub-Commission on Economic Development met for the first time in November 1947.

The terms of reference of the Sub-Commission on Economic Development were, among others, "to study and advise the Commission on the principles and problems of long-term economic development, with particular attention to the inadequately developed parts of the world, having the objectives of (1) promoting the fullest and most effective utilization of natural resources, labor and capital; (2) raising the level of consumption; and (3) studying the effects of industrialization and changes of a technological order upon the world economic situation."

The Sub-Commission adopted the following list of topics for discussion:

1. Principles and problems of development.
2. International action in the field of development.
 - a. Finance and investment.
 - b. Foreign exchange, balance of payments and terms of trade.
 - c. Capital goods and export prices.
 - d. Technical assistance.
 - e. Technical education.
 - f. Role of United Nations agencies in promoting international action in the field of development.
3. Short period problems.
4. Future work and research projects.

Considerable time was devoted to the problem of formulating precisely the concept of development, the conditions which had retarded development in the past, and the constituents of a sound policy of economic development in the future. The Sub-Commission stated that while the pace of development in each country would be conditioned by several factors, such as the availability of raw materials etc., the entire pattern had to be thought of largely in terms of industrialization. This brought about a long discussion among the members

of the Sub-Commission since several advocated the principle of diversification in production, both industrial and non-industrial, as the basic pattern for effective economic development. The members of the Sub-Commission were also at odds on the question of private investment as a means to promote economic development; most members of the Sub-Commission thought that emphasis should be placed on the dangers of private investment on the economy of less developed countries, while others were of the opinion that it was important to stress the need for private capital for development.

The Sub-Commission agreed to postpone until a future date the preparation of the study on an Investment Code, and on the international incorporation of private business firms, operating on an international scale.

The conclusions reached by the Sub-Commission on these and other matters related to economic development are found in the report of the First Session, which has been circulated within the Bank.

D. Regional Commissions.

The terms of reference of the various regional commissions thus far created by the Economic and Social Council stress development in less developed areas; each regional commission has been authorized to "make or sponsor such investigations and studies of economic and technological problems and development as the Commission deems appropriate."

The Economic Commission for Europe has held three sessions. Due to the special circumstances now prevalent in Europe, it has been forced to devote all its time to problems of reconstruction of war devastated areas and to the restoration to normalcy of the multitude of services which have remained idle since the termination of the War.

The Economic Commission for Asia and the Far East has met twice and has considered, in an exploratory manner, the problems related to development in that area of the World. Thus far, only recommendations of a general character

have been adopted. The most important ones, adopted at the recent meeting of the Commission in Baguio, Philippines, may be summarized as follows:

a. The Executive Secretary of the Commission was authorized to enter into immediate negotiations with F.A.O. and to request F.A.O. to formulate a food production program for 1948-49 for the countries within the scope of the Commission.

b. The Executive Secretary was directed to prepare at the earliest possible time a report on existing plans for promoting industry and development in each ~~Nation~~ Nation of the region. To this end, he was instructed to set up a working party of experts which would formulate definite proposals on development for the Commission.

c. The Secretariat was requested to publish a comprehensive annual survey on economic conditions and problems of the area.

It should be noted that the Sub-Commission on Economic Development recommended that the Economic Commission for Asia and the Far East and other regional economic commissions make a study of the magnitude and variety of the short-term requirements of underdeveloped countries, and that the governments of ~~said~~ ^{such} countries should consult with one another and with others on their immediate requirements and on the extent to which they could be met by mutual economic agreements.

E. International Monetary Fund

The activities of the International Monetary Fund in connection with the maintenance of stable exchange rates, the regulation of exchange control practices by members and the promotion of conditions suitable for multilateral trading^e, although not specifically directed towards development or confined to less-developed areas, do nonetheless constitute a material contribution to development. In particular, less-developed countries have been given technical assistance by Fund missions in connection with their currency, banking and other monetary

problems, the solution of which is a prerequisite to sound development. The right of access to the Fund's resources by any member of the Fund, if necessary to meet a temporary disequilibrium in that member's balance of payments, is, of course, an asset of importance to underdeveloped as to more fully developed countries alike.

F. International Trade Organization

The draft Charter of I.T.O. agreed upon in Geneva and now under discussion at Havana, has many features which directly affect the field of economic development. The Charter begins with a statement of the purposes and objectives to which members of the I.T.O. will pledge themselves. The most important of these basic principles, so far as development is concerned, may be paraphrased as follows: first, member countries of I.T.O. pledge themselves individually and collectively to promote national and international action for maintaining a balanced and expanding world economy; and second, two conditions are set forth as necessary to achieve this objective: there must be industrial and general economic development, particularly in countries which are relatively undeveloped; and there must be a flow of capital between countries for productive investment.

Economic development, and the attitude of I.T.O. towards its encouragement in the so-called underdeveloped countries, has proven to be one of the most controversial aspects of the draft Charter. Many countries have regarded Chapter III, which deals with this subject, as a key to the effectiveness of the Charter as a whole. The general point at issue at Geneva was this: what protective measures can be used, to what extent, and with what degree of consultation with I.T.O., to promote economic development in an "underdeveloped" country? A compromise had to be reached between, on the one hand, the promotion of economic development of undeveloped countries by the use of protective devices such as quantitative restrictions and, on the other hand, the reduction or elimination of barriers to world trade which is a fundamental objective of

the proposed Charter.

Faced with this basic problem, the draft Charter offers a compromise. Chapter III recognizes that protective measures such as quantitative restrictions "may be required to promote the establishment, development, or reconstruction of particular industries or particular branches of agriculture, and that in appropriate circumstances the grant of such assistance in the form of protective measures may be justified" provided prior approval is obtained by the enacting member government from I.T.O.

At the I.T.O. Conference now in session in Havana, the Mexican delegation presented an amendment to the proposed charter, suggesting the establishment of a Committee for Economic Development within the framework of I.T.O. The idea for such a committee had been originally proposed at the Preparatory Committee in London, but a decision on the matter was not reached at that time and the proposal was not incorporated in the draft charter in Geneva. ~~Under the terms of the Mexican proposal, "when any request for economic assistance submitted by a Member of the I.T.O. to the International Bank for Reconstruction and Development or any other inter-governmental organization has been rejected, or if no decision has been given within a reasonable period of time, the Committee for Economic Development shall, upon the request of the Member and subject to previous consideration and approval, support the request."~~ Present indications are that ~~The Mexican proposal is not likely to be adopted.~~ *still under consideration.*

G. Food and Agriculture Organization

The F.A.O. has as its principal functions the collection and distribution of information concerning agriculture, nutrition and rural industries, the furnishing of technical assistance on these matters upon request of member governments, and, in the case of a limited number of commodities, the formulation of allocation recommendations (a function until recently performed by the International Emergency Food Council).

Three missions have been sent to member governments (Greece, Poland and Siam) to work out proposals for the rehabilitation and development of agriculture, forestry and rural industries. Missions are now being organized to assist Hungary in planning increased agricultural production and to help Venezuela expand the production of oil-bearing seeds.

Technical advice has been given to member governments on many different aspects of their food and agriculture problems. For instance, advice has been given to Near East countries on irrigation and irrigation-drainage problems, and to Peru on the establishment of refrigerators and storage facilities for the catch of the bonito fishermen.

With the establishment of the new World Food Council, F.A.O. hopes to be able to assist member countries to develop specific small projects which will increase food production. For instance, it is planned to pin-point some small projects in connection with rice production, such as small pest control stations, experimental fields and water projects.

H. United Nations Educational, Scientific and Cultural Organization

In spite of the brevity of its active existence, UNESCO has already begun operations at most of the points of its broad front of international education, science and culture. Although most of the activities of UNESCO are not of an economic character, many of them do have a bearing on economic development.

Of special significance in this connection are the "Fundamental Education" projects of UNESCO by which it is hoped to combat ignorance and illiteracy, particularly in underdeveloped areas and among underprivileged groups. These projects are intended to include, in addition to a basic curricula for fundamental education, education in the principles of economic development, health, citizenship and international understanding. Pilot projects have been started in Haiti, China and in British East Africa.

Together with the government of Brazil, UNESCO called a meeting of an

international Scientific Commission which met in August, 1947 in Belem, Brazil. This Commission consisted of the representatives of ten countries, and it discussed the possible establishment of an Institute of Hylean Research for the scientific exploration of the Hylean Amazon, a vast area stretching from the Andes to the Atlantic, and ranging over Brazil, the Guianas, and parts of Venezuela, Colombia, Ecuador and Peru. This region, the largest drainage basin in the world, possesses natural resources which have been virtually unexplored to date.

The General Conference of UNESCO held in Mexico City in November last, approved the following resolution in relation to the Institute of Hylean Research:

"The Director-General is instructed to take steps to bring into being in 1948 an International Institute of the Hylean Amazon. To that end he shall:

Forthwith call a meeting of the Council, consisting of representatives of the nations and international organizations named in the report of the meeting of the Commission at Belem in 1947, together with representatives of any other country or international organization that may express itself as interested.

Use his best efforts to assure that the Executive Committee and the Survey Staff proposed in the report of the Belem Commission are set into motion as soon thereafter as possible.

In carrying out the above instructions, observe the following conditions:

Unesco's role in the setting up of the Institute is to initiate and to stimulate. Without any financial commitment beyond 1948, Unesco shall in 1948 make available the sums necessary for the meeting contemplated, shall provide the temporary survey staff and shall make available the services of the Field Science Co-operation Office in Latin America.

Consult with interested governments and organizations concerning the future financing and administration of the Institute and present his recommendations to the Executive Board prior to the Third Session of the General Conference."

2. Interamerican Economic and Social Council

The Interamerican Economic and Social Council was created by a resolution adopted at the Conference of American Republics held at Chapultepec, Mexico, in the Spring of 1944. It superseded the Interamerican Economic Advisory Board which functioned in Washington throughout the war period.

The Interamerican Economic and Social Council has thus far been quite

inactive. However, the Interamerican Conference for the Maintenance of Peace and Security of the Continent, held in Rio de Janeiro in August 1947, instructed the Council "to prepare a draft of a basic agreement on inter-American economic cooperation" in order that the text be presented to the Ninth Interamerican Conference which shall take place in Bogota. A special commission of the Council has prepared such a draft, which is still to be approved by the Council itself.

The proposed basic agreement contains the following clauses of interest to the Bank:

"The American Republics reaffirm the objectives of the International Bank for Reconstruction and Development and agree to harmonize their efforts so that the Bank may be an instrument ever more effective for the realization of those aims, especially those related to the promotion of their mutual economic development. They declare likewise that they will continue, when appropriate, extending credits between themselves, on short and long terms, by means of governmental institutions for the economic development and increase of international trade, in order to supplement the flow of private investments.

"The American Republics recognize that the lack of national savings, or the ineffective use of same, has led to inflationary practices which in the final instance, may endanger the stability of their rates of exchange and the orderly development of their economies.

"Therefore the American Republics agree to promote the development of local capital markets to provide, from non-inflationary sources, the national funds necessary to cover investment expenses in national currency. While local capital markets are not sufficiently developed, the American Republics agree that, in strictly justified cases, they will cooperate among themselves to the end that investments referred to in Article 2 of this Point include expenses in national currency.

"The American Republics declare that the investment of private capital and the introduction of advanced technical experts of other countries is an important factor in their general economic development, and consequent social progress. They likewise declare that such capital and technical experts should be made available under reasonable terms and conditions to countries needing them, and should be utilized for appropriate productive ends, emphasizing especially that investments should increase the national income and not simply displace national capital funds. Therefore, they pledge themselves to give ample facilities and appropriate reciprocal encouragement towards the free flow, investment and reinvestment of capital and for the normal transfer of capital and profits. Also, they obligate themselves to give equitable and non-discriminatory treatment to foreign capital, except when such practice may be contrary to the public interest.

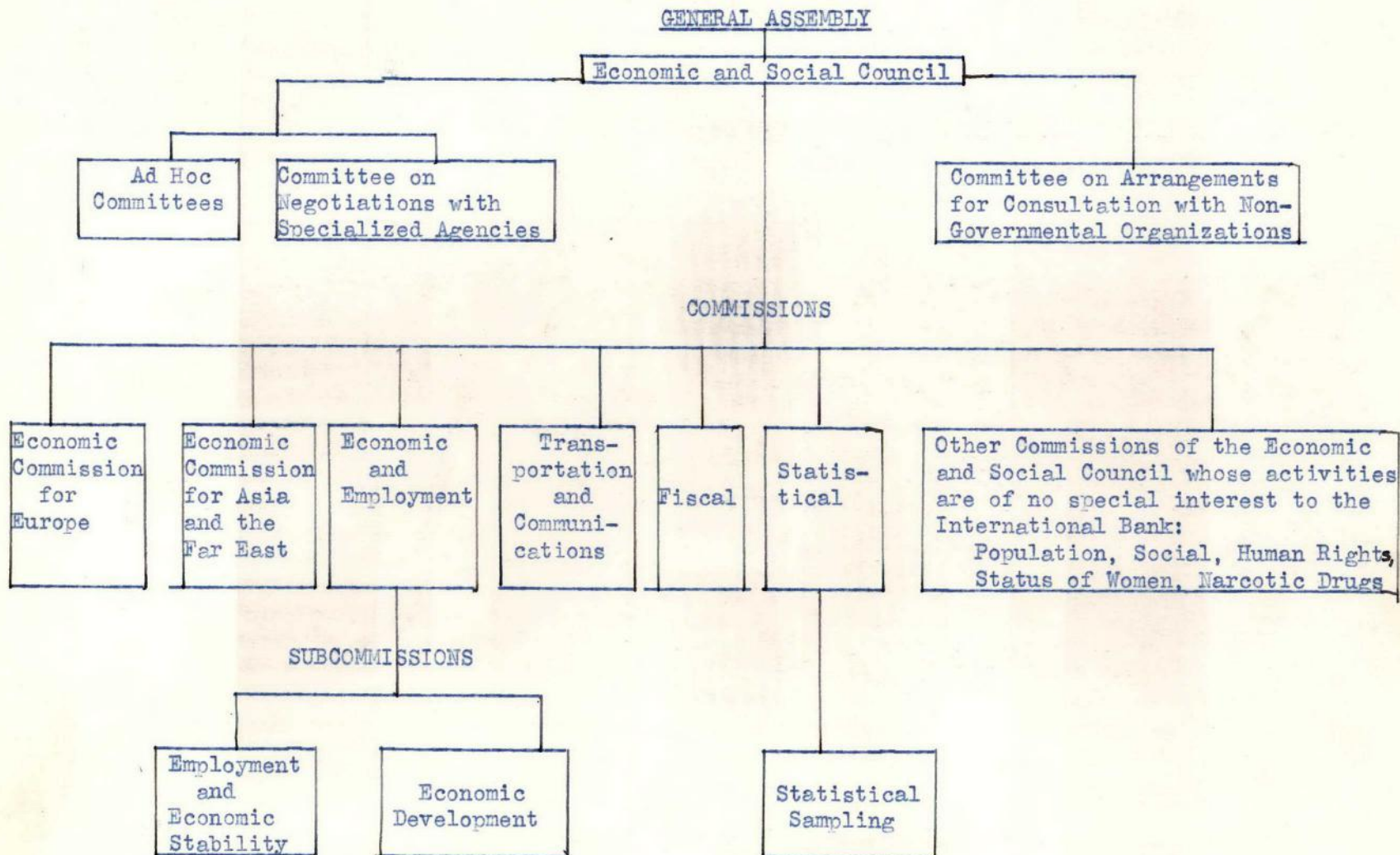
"The American Republics declare that foreign investments should be made not only for the legitimate use of the investors, but also to further the sound economic

development of the receiving country, protecting thereby the welfare of the persons dependent on them. Just, equitable and non-discriminatory treatment shall be accorded, with regard to employment and conditions of employment, to all the personnel, whether national or foreign, of such enterprises. The aforementioned measures will create an atmosphere of public opinion which will facilitate the equitable and non-discriminatory treatment for those investments."

In view of the probable creation by the Economic and Social Council of an Economic Commission for Latin America, the future of the Interamerican Economic and Social Council is uncertain. This matter will probably be considered at the Ninth Interamerican Conference to convene in Bogota on March 30.

For the convenience of the committee a chart showing the Economic and Social Council of the United Nations and its Commissions and Sub-Commissions, and a chart showing the Specialized Agencies, are attached hereto.

CHART OF THE ECONOMIC AND SOCIAL COUNCIL OF THE UNITED NATIONS



14

SPECIALIZED AGENCIES (OTHER THAN THE
BANK AND THE FUND)

ILO	FAO	UNESCO	ICAO	WHO	IRO	ITO
International Labor Organization	Food and Agriculture Organization Of the United Nations	United Nations Educational Scientific and Cultural Organization	International Civil Aviation Organization	World Health Organization	International Refugee Organization	Internat- ional Trade Organi- zation
Constitution approved April 11, 1919. On May 30, 1946 Agree- ment entered into bringing ILO into re- lationship with U.N.	Organization established at Conference in Quebec, Oct. 1945	Organized at meeting held in London Nov. 1945	Created by Conference held in Chicago, Nov.-Dec. 1944	Organization created at Conference held in New York June-July 1946.	Created by Resolutions of the General Assembly and ECOSOC in December 1946.	Prepara- tory Committee to create organi- zation first met in London in 1946 & GENEVA 1947 At present CONFERENCE meeting in HAWANA

Mr. V. L. Urquidi, Acting Chairman, C'tee on
Development Policy
D. Crena de Iongh, Treasurer

January 12, 1948

With reference to the Revised Agenda for Committee on Development Policy, dated December 31, 1947, which you sent me with your memorandum of January 6, I thought it might be a good thing if a representative of the Treasurer's Department were included in the Committee mentioned under Section III - Bank Technique.

DC/mct

cc Mr. Riley ✓

FILE REFERENCE	
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COPY 2	
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January 2, 1948

COMMITTEE ON DEVELOPMENT POLICY

As a result of the meeting of the Committee on Development Policy held December 30, further revisions in the Agenda were agreed upon to accord with the suggestions made by the wider committee. The Agenda is circulated herewith together with a tentative list of dates for the completion of the first draft of some of the papers.

During Mr. Penton's absence, Mr. Urquidi will act as Chairman of the Committee.

Attachments

CC: Messrs. Penton
Basch
Clee
Consolo
Demuth
Rosenstein-Rodan
Urquidi

<u>Item Number</u>	<u>Completion Date</u>
Preliminary Study and I-A	January 15
I-B (Middle East)	January 15
I-B (South America)	January 31
II-C	Beginning of February
II-E	January 15
II-G	January 15
III-B and -C	January 31

December 31, 1947

Revised Agenda for Committee on Development Policy

Rosenstein-Rodan

Preliminary Study: The moral and political problems of international participation in the development of backward countries.

I. What should be done?

A. Survey of economic problems of Development Countries. Purpose of development programs.

B. A brief survey of each underdeveloped area setting forth in general terms such basic factors as:

1. Population, population trends, labor supply and education.
2. Migration.
3. Climate, natural resources.
4. Principal economic activities.
5. Principal exports and imports.
6. Efficiency of political and administrative organization.
7. Internal financial conditions.
8. Extent and history of recent development.
9. Summary of principal obstacles to development.

Basch/Consolo

C. Income, standard of living and investment in different areas, with some quantitative estimates of what development could be done --

1. Eastern and Southeastern Europe

Postpone

2. Middle East
3. The Far East
4. Latin America
5. Colonial Territories

Research

D. Surplus population problems in relation to development programs.

Urguidi

E. The problem of promoting adequate technical training in Development Countries having regard to the activities of other organizations, public and private, in this field.

F. Integration -

Basch

1. Effect of reconstruction and development programs on trade relations between developed and underdeveloped countries.

Skillings

2. Integration of regional development programs.

II. How it can be done.

Research

A. An estimate of how much international investment can be expected on the optimum assumption for the next decade. What proportion of it might be handled by the International Bank?

Loan and Research

B. Analysis of the formation of savings in different areas. What could the Bank do to stimulate the formation of internal savings?

Research (preliminary paper)

C. What kind of loans should the Bank make to contribute to the capital formation of underdeveloped countries? Possible inflationary effects?

(Should the Bank finance only foreign exchange
(expenditure or local currency expenditure also?
(

Research

(D. (1) What is the present foreign funded debt
(burden of Development Countries?
(

Clee

((2) What can be done to facilitate the settle-
(ment of defaulted debt?
(

(E. How can the Bank secure active cooperation of
(private investors, both local and foreign, in
(development projects?
(

Urquidi and
Special Committee

1. Should the Bank encourage and assist a development program by financing a portion of it, the rest being provided by private lending? If so, is there any type of project particularly appropriate for the Bank, for example public utilities? What procedures should the Bank follow to promote the interest of private enterprise, local and foreign, in undertaking development financing?
2. Should the Bank undertake to guarantee private foreign capital investments in development projects?
3. What have been the most important obstacles to private foreign investment in various countries? Can these obstacles be removed through international agreement or otherwise?

Postpone

(F. Possibility of obtaining financial and other
(assistance from countries other than the U.S.
(What steps, if any, can the Bank take to assist
(in the readjustment of economic and financial
(relations between Europe and Development
(Countries?

Demuth

(G. The work of other international agencies in the
(field of development and the Bank's relations
(with these agencies.

Postpone

(H. Proportions and priorities to be attributed to
(different areas or purposes -

(1. General

(2. Bank

III. Bank Technique.

Loan

(A. What applications, formal and informal, for
(development loans has the Bank received and
(what is the mechanism for handling such applic-
(ations?

Penton and
Special Committee

(B. What is the Bank's position in connection with
(assistance by it or other agencies to underde-
(veloped countries in (a) formulation of practical
(development programs, (b) the construction and
(management of development projects, and (c)
(internal economic and financial conditions?
(What initiative should the Bank take in moulding
(its members' development policies along econ-
(omic lines? To what extent should the Bank

(send missions to underdeveloped countries in
(order (1) to publicize the purposes of the
(Bank and (2) to gather information for the
(Bank's use?
(

- (C. By what methods should the Bank seek to pub-
(licize achievements in the field of develop-
(ment with a view to restoring the confidence
(of private investment and thus encourage the
(resumption of private international lending?
(
- (D. What should be the Bank's method of consider-
(ing loan applications from underdeveloped
(countries?
(
- (E. What methods of lending are most appropriate
(for the Bank to use with underdeveloped
(countries?
(

Clee

Loan - Legal

Develop. Com
December 30, 1947

Notes on Meeting of Staff Loan Committee on December 29, 1947

Present: Messrs. Garner, McLain, Hoar, Penton, Rosenstein-Rodan, Clee, Basch, Consolo, Demuth and Urquidi.

The purpose of the meeting was to discuss with the Staff Loan Committee the progress report of December 18 on the Agenda of December 16.

A discussion ensued regarding the procedure of the Committee. Mr. Garner felt there were two broad categories of questions: (1) factual studies and (2) policy problems. He felt that many of these were clearly of a kind which could be dealt with in brief outlines in papers which would bring out the points for discussion, rather than in long papers. He agreed with the present procedure of the Committee of having a number of papers drafted in a short period of time to serve as a basis for discussion.

Mr. Garner stated that the end results of the Committee's work should be answers to the following questions:

- a. What kind of loans should the Bank make to Development Countries,
- b. How much money should be loaned to them,
- c. How should the loans be made and
- d. What supplementary activities should the Bank engage in.

The answers to point (a) imply that a study should be made of what are the development problems which can be solved through Bank and other loans.

It was agreed also to consider the possibility of drawing on the experience of outside experts and economists for the study of problems of certain areas, but not before a certain amount of preliminary work had been done in the Bank.

Mr. Garner added that he would also like the Committee to discuss and work out specific ideas with regard to Latin America in preparation for Mr. McCloy's proposed trip to that part of the world. It was agreed that the Committee discuss this matter at its next meeting and report to Mr. Garner.

With respect to work by other Agencies, it was stated that the Committee would soon be able to read and discuss the report of the United Nations Subcommittee on Economic Development. Mr. Demuth agreed to prepare a draft of a proposed statement by the Bank to the United Nations in that report.

It was agreed that the study of specific suggestions for a Latin American loan policy should not lead to the exclusion of the survey of the economic features and problems of the Middle East which had been agreed upon at a previous meeting as a model of the kind of work corresponding to point I-B of the Agenda.

It was agreed that at a forthcoming meeting of the Committee, consideration would be given to whether a separate paper should be written on the use

and development of local savings and means whereby the Bank could encourage such use, or the subject could be included in one of the points of the Agenda.

The Agenda was reviewed by the Staff Loan Committee. A summary of specific comments and additions brought out by the meeting follows (numbers of paragraphs correspond to those in Agenda):

I-A Clarification of what is meant by "Development Program". There appears to be a distinction between uncoordinated economic problems on the one hand and "Five-Year Plans" on the other. What is a practical development program? What is the Bank's position with regard to a "Plan"?

I-B Clarification of the content of item 1. (Population Trends) to take account of migration, qualitative differences, labor force, etc. Also addition of item 9. to deal with obstacles to economic development.

I-E This subject should include learning what different Agencies are doing in the matter of technical training as well as reference to local training for skilled work, health and educational training, and management. How strong a position should the Bank take with regard to management and adequate training in relation to projects financed by the Bank and others and in respect of legislation on the percentage of Nationals and Foreigners allowed in certain enterprises. This last point should be related to II-D-3.

I-F Include immigration and colonization problems.

II-B Clarification is required as to whether this point covers the question of the development of local savings and the local capital market, as well as the extent to which the Bank should take a position on the control of capital formation and the proper orientation of investment. Also can the Bank influence the distribution of income?

II-D-1. This item should cover points such as the combination of Bank loans with local capital through banks, investment companies, and groups of local capitalists, and also with foreign equity capital. In addition, consideration of what types of projects are best from the point of view of the problem of management and from a standpoint of credit worthiness. How can the Bank promote the interest of both local and foreign enterprise?

II-D-2. Clarification of this item to understand that by guarantees is meant, not a guarantee of bond issues, but of other types of investment: what would the procedures be? What are the problems involved? What should the Bank guarantee?

II-D-3. Inclusion under this item of other methods of removing obstacles to private foreign investment in addition to international agreement.

II-E This item should cover both financial and other assistance.

III-B Should include consideration of whether missions should be sent

to countries before loan applications are received or only after. There was also the suggestion that there should be consideration of the methods of lending to Governments, Development Corporations, private companies, etc., of the extent to which control should be exercised over the borrowing entities, and of the methods of obtaining required guarantees.

Dev. Committee.

29 December 1947

copies for attention of Development Com.

NOTE ON FOOD, AGRICULTURE AND PEACEFUL DEVELOPMENT

1/21/48

The Organization believes that after the present acute stage of the world food crisis has passed, a sub-acute stage will persist for a number of years. The reasons for this belief are set out in the attached memorandum. FAO, therefore, following the recommendation of the Preparatory Commission on World Food Proposals and that of the Third Session of the FAO Conference, is drawing to the attention of the Economic and Social Council the urgent need for cooperation between all Governments and all United Nations Agencies to increase food production.

The purpose of this note is to suggest that the urgent need to increase world food production provides an opportunity for the concrete demonstration of the effectiveness of international action. The type of developmental activities discussed could also become a starting lever for the general development of the underdeveloped countries which may not be able to be undertaken on a large scale until European factories can again play their part in the supply of capital goods.

In the present state of the world, increased agricultural production is an immediate first essential. In the Middle East, the Far East and Latin America much can be achieved at relatively little capital cost. Progress in these regions will help to improve the world food situation and would not only dovetail with, but indeed should be an essential forerunner to industrial development which in many countries must depend upon better fed populations.

How far have the nations collaborating as the United Nations placed themselves in a position to assist the underdeveloped countries? They have equipped themselves (1) to provide for the exchange of information, for advice, and for some degree of technical aid on food and agriculture through FAO, on labor relations through ILO, on education through UNESCO, on industrialization, transport,

etc., through ITO when it is established; (2) to provide through the International Bank for loans to Governments for specific projects of reconstruction and development which can be regarded as relatively good banking risks.

The United Nations thus either have or are in process of providing for what might be termed the first state, i.e., international advice, and for a last stage, namely, financially sound investment propositions. It is however doubtful whether the advisory functions can be effective or the specific projects properly developed and put forward on a sound banking basis unless an intermediate stage is developed.

This intermediate stage can take its most useful form at the present time through many relatively small scale projects for agricultural development. The need for this can be well illustrated from the standpoint of FAO.

At the request of the government of one of the underdeveloped countries FAO sends an expert mission to assist that country in the survey of its problems. The mission makes a report to the government and to FAO regarding the action which should be taken in order to increase the efficiency of agricultural production and distribution and thus to raise the level of nutrition and better the conditions of the rural population. Such reports will in most cases involve proposals for action in regard to irrigation and drainage, soil conservation, reforestation, improvements in marketing facilities, transport, and a number of other subjects. The mission will recommend that technical experts be engaged for several years to assist the local authorities, that citizens of the country in question should receive special training at suitable centers outside the country. It will further recommend that improved implements, fertilizers, and seed be obtained and probably that a start should be made in the local production of some of these requisites.

The external funds required would for the next three to four years be of modest dimensions. They would be needed in order to enable a country to meet the

cost of payments for the specific development projects which could not readily be met from the country's own command of foreign exchange. They might be described as "initial agricultural development loans."

The government receiving a developmental loan would be asked to provide all internal expenditures from internal sources and to agree to secure the necessary technical assistance through internationally approved channels. The technicians so engaged would undertake not only the initial surveys but would insure that both production and distribution were conducted with maximum efficiency. In such ways the age-long obstacles to progress can be broken down and a start made towards the increase of production capacities upon which all else will depend.

It will be clear from the foregoing that what is in contemplation is the expenditure of relatively small sums in a number of underdeveloped countries on projects which would have an immediate beneficial effect. In addition, the monies could be used for the necessary detailed surveys for longer-term projects for later submission to the International Bank.

It is suggested that in many of the small underdeveloped countries an annual loan expenditure of a few million dollars spread over five years could, under proper supervision and applied to the most useful purposes, have a really significant effect in starting a beneficial trend of development. Even in large countries modest sums could also be made to have significant results.

FAO is directed by its Constitution to provide its member nations with advice and in this phase of international affairs could properly act as "an impartial international expert" advising a Government regarding the needs of its country and the Bank regarding the technical means of meeting such needs.

The whole general purpose of the development loans would be to act as a starting lever in a determined and persistent drive to increase the productive capacity of the underdeveloped countries. The success of such action would tend

to make the recipient countries places where private capital could later find outlets for investment with a minimum of risk.

Circulated by:
J. M. Penton, Chairman

December 18, 1947

Committee on Development Policy

Progress Report

The Committee on Development Policy has adopted a plan of work which is set out on the attached sheet.

This program is admittedly ambitious and much of the work will necessitate a thorough and somewhat lengthy study of the problems. It was felt, however, that as time went on and as the havoc of war was repaired in Europe, the Bank would devote an increasing proportion of its resources to the development of less advanced countries. Moreover, during the course of the discussions it has become clear that, for reasons which are discussed below, the Bank's policy, which it is the Committee's task to elaborate in connection with underdeveloped areas, will be largely applicable to the whole range of the Bank's relations with potential borrowers, whether these are classed as "development countries" or not.

The Bank is already receiving loan applications from various Middle Eastern and Latin American countries so that it is necessary to tackle some questions included in the Agenda immediately in order to provide the Loan Department with guidance in connection with their day-to-day negotiations. Examples of this type of problem are: what kind of loans the Bank should make to contribute to the capital formation of underdeveloped countries; the proper course to be followed by the Bank when providing its members with advice on economic questions, and the desirability of bringing about discussions with would-be borrowers at an early stage before the presentation of a loan application, so as to ensure that when the application is made, it is in a form which the Bank can consider.

It was also thought necessary to define at an early date the Bank's policy with regard to its relations with other international agencies working in the development field, and there are several other points to which priority will be accorded.

Examples of items which the Committee may need further time to study are, broadly speaking, a survey of underdeveloped areas such as is suggested in I-B on the Agenda, quantitative estimates of what can be achieved in the different areas, problems relating to surplus population in underdeveloped countries, and research into the potential availability of private investment funds over the next decade. These questions will require to be dealt with by economists, of which the number on the staff of the Bank is limited. Consequently, some of these items must be regarded for the time being as more in the nature of long-term projects rather than papers which the Committee can undertake to produce within a definite and fairly short period of time.

It has been decided to allocate the responsibility for providing the drafts of the various papers for discussion by the Committee to its individual members. It was realized, however, that on many of these questions it would be necessary to draw more widely on the accumulated knowledge of the Bank, and for this reason, it was decided that the individuals responsible for the provision of the papers should, if they thought it desirable, form sub-committees with a wider membership among the Bank's staff, in order to assist them in drafting the papers. In this way it is hoped that the collective experience and manpower resources of the Bank will be used to the maximum without compromising the principle that the members of the Committee are responsible for ensuring that the various parts of the Committee's work are completed.

Some difficulty was experienced by the Committee, not only in defining the elements of the problem which has been rather loosely classified as "development", but also in deciding which areas of the world should be properly classed as "development areas". For instance, the resources of Western Europe will undoubtedly be still further developed in the future, but most members of the Committee were of the opinion that Western Europe should be excluded from the areas of the world

under review by the Committee since it was hoped that the problems of that area would be dealt with under the Marshall Plan. Southeastern Europe, the Middle East, Asia and Africa, all seem areas, however, to which the word "development" can reasonably be applied, and in many of these areas, particularly the Middle East, similar problems are found in all or most of the component countries. It seemed clear, however, that there would emerge from the discussions of the Committee a broad line of policy which the Bank should pursue in its dealings with Development Countries, and that, if it was decided to exclude only Western Europe and the countries of the North American Continent from consideration by the Committee, this policy would apply to an increasing proportion of the Bank's work. Moreover, as has already been stated, in many cases it would be found that the policies evolved for the so-called "development areas" would not be exclusive and might, in varying degrees and according to circumstances, be applied to the Bank's relations with more advanced countries as well.

attachment

Distribution:

Mr. Garner
Mr. Hoar
Mr. Hill
Mr. Rist
Mr. McLain
Mr. Crena de Iongh

Members of the Committee

December 16, 1947

Agenda for Committee on Development Policy

Rosenstein-Rodan

Preliminary Study: The moral and political problems of international participation in the development of backward countries.

I. What should be done?

A. Survey of economic problems of Development Countries. Purpose of development programs.

B. A brief survey of each underdeveloped area setting forth in general terms such basic factors as:

1. Population trends. *and characteristics, climate; health; demography.*
2. Resources.
3. Income, standard of living and investment.
4. Principal economic activities.
5. Principal exports and imports.
6. Extent and history of recent development.
7. Efficiency of political and administrative organization.
8. Internal financial conditions.

C. Some quantitative estimates of what could be done in different areas -

1. Eastern and Southeastern Europe
2. Middle East
3. The Far East
4. Latin America
5. Colonial Territories

D. Surplus population problems in relation to development programs.

Basch/Consolo

Postpone

Research

What is a practical development programme?

Limitations now operating

9. obstacles to further development

-2-

Urquidi

(E. The problem of promoting adequate technical train-
(ing in Development Countries.
(

F. Integration -

Basch

(1. Effect of reconstruction and development
(programs on trade relations between devel-
(oped and underdeveloped countries.
(

Skillings

(2. Integration of regional development pro-
(grams.
(

3. *Migration of labour*

II. How it can be done.

Research

(A. An estimate of how much international investment
(can be expected on the optimum assumption for the
(next decade. What proportion of it might be handled
(by the International Bank?
(

Research (prelim-
inary paper)

(B. What kind of loans should the Bank make to contrib-
(ute to the capital formation of underdeveloped coun-
(tries? Possible inflationary effects? Should the
(Bank finance only foreign exchange expenditure or
(local currency expenditure also?
(

Research

(C. (1) What is the present debt burden of Development
(Countries?
(

Clee

((2) What can be done to facilitate the settlement
(of defaulted debt?
(

Urquidi and
Special Committee

(D. How can the Bank secure active cooperation of pri-
(vate investors in development projects?
(

(1. Could the Bank encourage and assist a devel-
(opment program by financing a portion of it,
(the rest being provided by private lending?
(

Urquidi and
Special Committee

*Should Bank
finance end
where history
has shown
necessary flexibility
unlikely to be found
under public
control?*

If so, is there any type of project particularly appropriate for the Bank, for example public utilities? What procedures should the Bank follow to promote the interest of private enterprise in undertaking development financing?

2. Should the Bank undertake to guarantee private foreign capital investments in development projects?

*If so, what technique
should Bk use?*

3. What have been the most important obstacles to private foreign investment in various countries? Can these obstacles be removed through international agreement?

or by other methods

Postpone

*Need
loans*

E. Possibility of obtaining assistance from countries other than the U. S. // What steps, if any, can the Bank take to assist in the readjustment of economic and financial relations between Europe and Development Countries?

Demuth

F. The work of other international agencies in the field of development and the Bank's relations with these agencies.

Postpone

G. Proportions and priorities to be attributed to different areas or purposes -

1. General

2. Bank

III. Bank Technique.

Loan

A. What applications, formal and informal, for

development loans has the Bank received and what is the mechanism for handling such applications?

- B. What is the Bank's position in connection with assistance by it or other agencies to underdeveloped countries in (a) formulation of development programs, (b) the construction and operation of development projects, and (c) internal economic and financial conditions? What initiative should the Bank take in moulding its members' development policies along economic lines? To what extent should the Bank send missions to underdeveloped countries in order (1) to publicize the purposes of the Bank and (2) to gather information for the Bank's use?
- C. By what methods should the Bank seek to publicize achievements in the field of development with a view to restoring the confidence of private investment and thus encourage the resumption of private international lending?

Penton and
Special Committee

Methods of lending

- 1 To Govts
- 2 To Govt agencies
- 3 To private corps.
- 4 Participations with other
Capital
- 5 Sum of Govt glcs

etc.

December 16, 1947

Committee on Development Policy

At the Committee's meeting today it was decided to adopt the Agenda and the allocation of work already submitted, with a few minor modifications.

It was agreed that there should be a further meeting of the Committee on December 30, at 2:30 P.M., in Room 410, at which the progress of the preliminary work done on the various items of the Agenda would be reviewed with a view to setting tentative dates for the completion of the various parts of the Committee's program.

Distribution

J. M. Penton, Chairman
A. Basch
V. Checchi
F. Consolo
R. H. Demuth
M. Madigan
P. Rosenstein-Rodan
V. L. Urquidí

December 16, 1947

Agenda for Committee on Development Policy

Rosenstein-Rodan

(Preliminary Study: The moral and political problems of inter-
(national participation in the development
(of backward countries.
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(I. What should be done?
(

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(in different areas -
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(4. Latin America
(5. Colonial Territories

Postpone

Research

(D. Surplus population problems in relation to develop-
(ment programs.

Urquidi

(E. The problem of promoting adequate technical train-
(ing in Development Countries.
(

F. Integration -

Basch

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Urquidi and
Special Committee

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(vate investors in development projects?
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Urquidi and
Special Committee

If so, is there any type of project particularly appropriate for the Bank, for example public utilities? What procedures should the Bank follow to promote the interest of private enterprise in undertaking development financing?

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Postpone

E. Possibility of obtaining assistance from countries other than the U. S. What steps, if any, can the Bank take to assist in the readjustment of economic and financial relations between Europe and Development Countries?

Demuth

F. The work of other international agencies in the field of development and the Bank's relations with these agencies.

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- (B. What is the Bank's position in connection with
(assistance by it or other agencies to underdevel-
(oped countries in (a) formulation of development pro-
(grams, (b) the construction and operation of devel-
(opment projects, and (c) internal economic and fin-
(ancial conditions? What initiative should the Bank
(take in moulding its members' development policies
(along economic lines? To what extent should the
(Bank send missions to underdeveloped countries in
(order (1) to publicize the purposes of the Bank and
((2) to gather information for the Bank's use?
(
- (C. By what methods should the Bank seek to publicize
(achievements in the field of development with a
(view to restoring the confidence of private invest-
(ment and thus encourage the resumption of private
(international lending?
(

Penton and
Special Committee

December 15, 1947

Committee on Development Policy

At a meeting of the Sub-Committee to continue study of the Agenda, which took place on Friday, December 15, the division of work on the Agenda was discussed, and a redraft of Section I-D made. The Sub-Committee's recommendations are set out in a revised Agenda, hereto attached.

It was felt by the Sub-Committee that, in general, primary responsibility for each item on the Agenda should be given to one person. The person in charge should, however, be able to enlist the assistance of anyone in the Bank who might contribute to the examination of the problem at hand. In two cases (II-D and III-B and -C) it was felt that the person in charge should set up a special committee to study the problem.

Allocation of a few topics was postponed, - it being felt that they were not of immediate urgency, or could not be evaluated until other studies had been made.

The next meeting of the full Committee will be on Tuesday, December 16, at 2:30 P.M., in Room 410.

attachment

Distribution:

J. M. Penton, Chairman ✓
A. Basch
V. Checchi
F. Consolo
R. H. Demuth
M. Madigan
P. Rosenstein-Rodan
V. L. Urquidi

Develop. Com

DEC 18 1947

OFFICE MEMORANDUM

TO: Drew Dudley

FROM: John M. Penton

SUBJECT:

DATE: 12/15/47

The Committee on Development Policy appointed by Mr. Garner is undertaking a study of the Bank's role in increasing the productive capacity of underdeveloped countries.

One of the chief questions which arises is that of the Bank's participation in giving expert economic and/or technical advice to its members in such fields as the formation of development programs, the moulding of internal economic and financial policies in order to achieve the best conditions for development, the construction and operation of development projects, and the maintenance of overall policies throughout the life of loans which will create the most favorable environment for the loans's success.

The degree of initiative which the Bank might use, either in making known its aims and purposes, or in participating in any one of the above activities should be considered. The scope of Bank missions in the field is also an important factor, as yet undecided.

It is also desirable to discuss the extent to which the Bank can publicize any achievements it may have in the development field, with a view to restoring the confidence of private investment, thus encouraging the resumption of private international lending.

It is proposed to hold a discussion on this subject in your office on Wednesday, December 17, at 2:30 P.M.

*J.M.P.**meeting was held*

Stan Sep 7 - Mrs. leorn

OFFICE MEMORANDUM

TO: F. D. Stephens
FROM: John M. Penton
SUBJECT:

DATE: 12/15/47

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It is proposed to hold a discussion on this subject in Mr. Drew Dudley's office, Room 1111, on Wednesday, December 17, at 2:30 P.M., and I should be glad if you could attend.

J.M.P.

December 11, 1947

AGENDA FOR COMMITTEE ON DEVELOPMENT POLICY

PREFACE - The moral and political problems of international participation in the development of backward countries.

I. What should be done?

- A. Survey of economic problems of Development Countries. Purpose of development programs.
- B. A brief survey of each underdeveloped area setting forth in general terms such basic factors as:
 - 1. Population trends.
 - 2. Resources.
 - 3. Income, standard of living and investment.
 - 4. Principal economic activities.
 - 5. Principal exports and imports.
 - 6. Extent and history of recent development programs.
 - 7. Efficiency of political and administrative organization.
 - 8. Internal financial conditions.
- C. Some quantitative estimates of what could be done in different areas -
 - 1. Eastern and Southeastern Europe
 - 2. Middle East
 - 3. The Far East
 - 4. Latin America
 - 5. Colonial Territories
- D. Surplus population problems in relation to development programs.
- E. The problem of promoting adequate technical training in Development Countries.

F. Integration -

1. Effect of development programs on trade relations between developed and underdeveloped programs.
2. Integration of regional development programs.

II. How it can be done.

- A. An estimate of how much international investment can be expected on the optimum assumption for the next decade. What proportion of it might be handled by the International Bank?
- B. An analysis of nature and composition of development loans (and possible inflationary effects).
- C. Should the Bank finance only foreign exchange expenditure or local currency expenditure also?
- D. What is the present debt burden of Development Countries? What can be done to facilitate the settlement of defaulted debt?
- E. What are the present obstacles to private lending and what steps could be taken to remove them and speed up the flow of private capital?
- F. Possibility of obtaining assistance from countries other than the U. S. What steps, if any, can the Bank take to assist in the re-adjustment of economic and financial relations between Europe and Development Countries?
- G. The work of other international agencies in the field of development and the Bank's relations with these agencies.
- H. Proportions and priorities to be attributed to different areas or purposes -
 1. General
 2. Bank

III. Bank Technique.

- A. What application, formal and informal, for development loans has the Bank received and what is the mechanism for handling such applications?
- B. What steps should the Bank take to inform countries of its purposes and aid them in the formulation of their development policy? How can the Bank influence general financial and economic policy in countries in which it is interested?
- C. By what methods should the Bank seek to publicize its aims and achievements in the field of development with a view to restoring the confidence of private investment and thus encourage the resumption of private international lending?
- D. General policy papers.

Distribution

J. M. Penton, Chairman
A. Basch
V. Checchi
F. Consolo
R. H. Demuth
M. Madigan
P. Rosenstein-Rodan
V. L. Urquidi

ROUTING SLIP

Date 12-12-47

T0-	Name	Room No.
1	Mr. Hoar	407
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FOR-		
Action		Initialing
Approval		Preparing Reply
Comment		Previous Papers
Filing		Noting and Returning
Full Report		Recommendation
Information		Signature

REMARKS

Revised version of previous note
dated November 6, 1947, JT/213/amh.

FROM- J. Torfs

CONSIDERATIONS ON THE DEVELOPMENT OF
ECONOMICALLY UNDERDEVELOPED COUNTRIES (a)

The following is the synthesis of the opinions and observations of the writer, formed after several years of personal studies in economically backward countries and in Washington.

These opinions and observations have been discussed with and often suggested by members of the staff of the IBRD, the IMF, the Eximbank, State Department, and officials of Belgium, Belgian Congo, Gold Coast, and Latin American Governments.

They form a logical pattern and lead to conclusions which at best are tentative in nature, for the demonstration of each point would, if handled on a strictly scientific basis, absorb the efforts of a staff of skilled economists for at least a year.

Tentative as they are, however, it is hoped that the conclusions can serve as basis for further discussion with the Bank and provide a general pattern for an IBRD policy towards development countries, which policy appears to be only in an embryonic stage at this time.

CONCLUSIONS

1. Latin America, Africa, the Middle East are areas where development is needed to bring about the efficient utilization of their resources for the sake of their inhabitants and for the sake of the world at large.
2. Development should be in the nature of projects of modest size which are designed to increase directly national production or efficiency.
3. Eligibility for development financing requires that countries desiring such financing have taken or be willing to take the steps necessary to a demonstration of financial and political stability and to an increase in the skills and efficiency of their population.
4. Other than US dollar currency or currencies should be the financing media, where feasible, and project(s) machinery and equipment should be obtained from other than US suppliers.
5. In the short-run, and this is to say until the end of Marshall financing, the development countries should receive only a small

(a) The countries under consideration are mostly self-governing Latin American, African or Near Eastern countries, although many remarks apply as well to Colonial Africa. The economically underdeveloped countries will henceforth be referred to as E. U. countries.

amount of financial help. However, they should receive a great amount of technical help, and both should be conducive to the establishment of sound economic practices and to the creation of the solid framework of small industries, local capital, and skills on the basis of which further large scale development will be able to take place.

6. In the long-run, an International Development Corporation could act as project(s) manager until local management can be arranged and local technicians trained to take over the project(s). The IDC would be staffed by experienced economists, businessmen, and technicians recruited on a world basis. It would (a) procure the material necessary and induce non-US suppliers to plan their production along the needs of the development countries and (b) be financed by capital subscribed by development areas Governments, by their nationals, by the IERD, IMF, and private investors.

1. The General Problem of Development

- (A) Is the development of L. U. countries necessary?
- (B) In what realm of economic activity should development be undertaken?
 - 1.a. Agriculture
 - 1.b. Animal husbandry
 - 1.c. Forestry and forest industries
 - 1.d. Fisheries
 - 2. Metallic and mineral resources
 - 3. Industry
 - 4. Distribution
 - 5. Education
- (C) What should be the size of development?
- (D) Through whom should development be undertaken?

II. The Financing of Development

- (A) Difficulties inherent to private financing
- (B) Difficulties inherent to dollars investment
- (C) Restrictions placed on certain kind of loans

III. Development within the Framework of a World Policy

- (A) Short-run
- (B) Long-run

IV. Prerequisites to Development

I. The General Problem of Development

In order to arrive at coherent conclusions, we deem it necessary to start from the very beginning and to investigate at first the very premises of our reasoning. Our first question is thus:

(A) Is the development of E. U. countries necessary?

The answer is affirmative for two reasons:

1. For the sake of the inhabitants of the countries under consideration development is necessary, for the standard of living of these people is generally extremely low.^(a) Many of these countries enjoy a democratic set-up; nevertheless, there are wide differences in the income of their inhabitants. Usually, a dominant group of rich landowners and industrialists and their families, mostly educated abroad, rule the country directly or indirectly. Practically all capital is concentrated in their hands. Their oligarchic group does not represent more than one-twentieth of the population. About ninety-five percent of the population is constituted of badly-educated farmers or workers enjoying little hygiene, usually undernourished, and unable to make the best of the little knowledge they have, because they are submitted to a social framework (like the system of the big Hacienda) which makes it impossible.

Theoretical measures have been taken to improve the lot of this proletariat. In Chile, for instance, the social legislation is one of the most progressive of the entire world. However, no amount of legislation will feed the workers.

At the root of this problem is an inadequate production, resulting from a lack of per capita efficiency, and this in turn is the result of a lack of education or scientific training. This in great part can only be corrected through years of education and a total revision of psychological attitudes toward life and work. However, this is a slow process which will not do in many cases, for the problem of low standards of living is urgent. Although it has existed for a considerable number of years, without creating considerable disruption and chaos, it is taken at present as a political platform by communistic agitators who threaten to make the situation worse. Immediate measures are necessary.

2. For the sake of the world at large and especially for the sake of Europe, development in E. U. countries is necessary, because the world is short of practically every possible kind of goods.

It would be unrealistic, however, to predicate a policy of development on the proposition that everything should be produced because the world lacks everything. The world unfortunately is not yet in a position to purchase twice or three times the amount of goods currently produced, and this

(a) They have no access to a quantity of calories, vitamins, proteins, clothing, and housing sufficient to enable them to have US or European life expectancy.

is due to the extremely low per capita efficiency of large masses such as the Asiatic peoples. Most of the Chinese and Hindus are improperly fed and clothed; however, the product of their own labor has such a low economic significance that its value in exchange is practically nil. The clothing and feeding of most Chinese and Hindus could only be justified on the basis of charity, and the world cannot afford this at the present moment.

A large region of the world exists, however, where the inhabitants have potential ability to pay in goods for the goods they receive. This part of the world is Europe - short of most foodstuffs and raw materials for its industry. A higher production in E. U. areas could and should be attained through development, thus, were it for the sake of the Europeans alone.

On the two bases above, the intensification of production is necessary, and development by definition is the technique conducive to such intensification.

(B) In what realm of economic activity should development be undertaken?

1.a. Agriculture The development of agriculture in most of the equatorial and subtropical parts of the world is difficult, for it brings about the phenomenon of laterisation which is no less than the sterilization of soils. In order to avoid laterisation it is necessary to select carefully proper soils and to introduce systems of erosion control. This implies reforestation, the planting of nitrogenous plants, the building of dams and levees, etc.^(a) It is, therefore, a long-range proposition which must be studied very carefully.

Even where the terrains do not laterize, they are usually extremely poor except in such areas as Argentina or Uruguay.^(b) The expectation of high yields per acre on large scale development can, therefore, easily be disappointed.

Social difficulties hinder the development of agriculture even more. Where the land is in the hands of big landowners who practically dominate large masses of quasi serfs, there is little incentive for efficiency: The master of the property has a large income sufficient for him and for his family even when the methods of cultivation are completely out of date. The workers on the other hand are accustomed to such low incomes that they have absolutely no incentive to try to obtain better yields. Many countries like Mexico have attempted to break down the system through the redistribution of land to farmers. Unfortunately, they have gone far in the other direction and have split up property so much that exploitation on an industrial scale becomes difficult. In order to depart from both inefficient systems, a

(a) The problem has been successfully tackled in Kiva (Central Africa) and in Northern and Central Peru.

(b) Regions of the highlands of Brazil f.i. are almost exhausted.

real revolution is necessary. This either takes time or involves bloodshed, and the latter method creates an atmosphere which is little conducive to developmental endeavors.

It should be noted here that the agricultural system in E. U. countries is one of the reasons for the small "capital formation".^(a) The quasi serfs or the very small farmers do not save. The big landowners do save, but as they do not trust the local political and financial setup, they convert their savings balances into foreign currencies and keep them in the United States or in Western Europe.

1.b. Animal husbandry offers little more than agriculture in the way of possibilities of rapid development. The control of diseases, which is absolutely essential as proven by the current hoof and mouth disease epidemic in Mexico, is a costly proposition, and the scientific up-keep and marketing of cattle has not yet been introduced very far in Latin America or in Africa.

1.c. Forestry and forest industries are better prospects for immediate yield. However, they imply the introduction of scientific methods of reforestation, the standardization of products, and the existence of considerable know-how.

All of this, however, can be acquired in a few years. The progress in the exploitation of Parana Pine in Brazil is in this respect very encouraging.

1.d. Fisheries seem to have even better prospects than forestry. The only factors needed to develop this activity in E. U. countries are local and foreign capital, for where fish are abundant, the question of skill and know-how is practically negligible. The considerable growth of Chilean, Peruvian, and Mexican fish industries prove both points clearly.

2. The more intensive exploitation of metallic and mineral resources raises a completely different kind of problem.

Very large investments must be made in mining and petroleum exploitations before they can yield any sizeable profit. This capital is not available in the economically underdeveloped countries because of the small amount of real savings; therefore, the exploitation of mining and petroleum must be left to foreign capital. Most backward countries are reluctant to let more foreign capital enter into these fields,^(b) since the profits, reserves, and the dividends of the foreign corporations are usually transferred abroad as soon as they are created. In Chile, for instance, about 25 percent of the gross sales value of copper leaves the country. In the case of small mining and petroleum enterprises, the share of foreign exchange

(a) The little amount of real "savings" (or voluntary refrain from consuming) is the single most important factor which prevents a fast growth of E. U. countries.

(b) Brazil and Chile practically exclude foreign investments in petroleum fields.

which remains in the hands of foreign interests is much larger. In order to obtain a larger "cut" in the fruits of exploitation of their own natural resources, many Latin American countries utilize methods of taxation that are extremely discouraging to foreign capital, or insist on sharing the partnership, or in introducing their own technicians and administrators in foreign enterprises. This results very often in a sterilization of the enterprises or in a reduction in efficiency.

In mining and petroleum as in the case of agriculture, little capital is formed for local use. Most of the savings are made by foreigners which transfer them abroad.

3. Industry The myth of industrialization at all costs has pervaded large developmental regions like Latin America or the Middle East. In certain cases when the condition of the soil is so bad as to make agricultural endeavors non-productive, a limited industrialization is justified. However, the creation of large industries requires considerable amounts of capital, know-how, and skills. Most of them are often lacking in L. A. countries. Industrial endeavors in the direction of self-sufficiency, such as the manufacture of jet-propelled pursuit planes in Argentina, are completely unjustifiable. The creation of a steel mill in Brazil, which is neither close to the iron ore deposits nor the coal deposits, might not have any beneficial effect.

However, a local steel mill in Chile at the proximity of coal fields, situated at the proximity of iron ore deposits, and close to a large market should not be dismissed as inefficient on the basis of cost calculation alone. It might very well be efficient in terms of labor costs, and the monetary costs may alter the picture, because of non-industrial factors such as inflationary situation or over-valued currency. But in general large industries in backward regions are expensive, their products cannot compete with foreign goods, and they do not help solve the world problems at all insofar as they expand lines of production which are practically the only ones left to areas such as Western Europe and where no shortage is foreseeable in the future.

Small industries can have a considerably better chance of success. Small textiles mills when cotton is available, small tool factories, manufactures of canned foodstuffs, beer, or copper appliances can be justified and productive; and, furthermore, they can constitute a strong basis for capital formation.

4. Distribution Where no market facilities exist or where they are extremely elementary, the organization of an efficient distribution system is sometimes much more helpful than the development of production itself. Cooperatives, warehouses, quick-freezing plants, canning plants, and packing manufactures can be organized on the basis of local capital, but require foreign technical knowledge. This is a line where much could be done at little expenditure.

New railroads involve large investments, and extremely careful consideration. In E. U. countries, as everywhere, the building of new railroads is a risky business at best, and even lines of old standing experience great difficulties. However, the creation of new lines in backward countries should not be always predicated on the basis of existing traffic. New lines open up new regions, and the demand for traffic follows the supply. It is unfortunate that the old free enterprise spirit which presided at the opening of most lines in the US and many in Africa, Asia, and Latin America seems to be replaced by the fear of risk which characterise present day Western European or US big investors, for large profits and immense economic improvements could accompany the creation of lines between Chile, Bolivia, Brazil, or across Africa. Owing to the present mentality, however, only the improvement of existing lines and the opening of "sure-fire" sections of railroads can be considered. This could, however, have beneficial effects.

The building of highways on the other hand seems to be the favorite manner of wasting money in many E. U. countries. It remains to be demonstrated that road transport is cheaper than the rail, and that the building of highways parallel to railroad lines presents any economic advantage whatsoever.

5. Education The analysis of the four points above indicates that the development of practically all lines of economic endeavors is possible and desirable in backward countries, except in the domain of heavy and medium-heavy industry. But it is just as important to note that in practically no instance is that development possible without technical knowledge, know-how, and social reforms. This leads to the suggestion that, as the acquisition of more knowledge must come before the utilization of this knowledge, the first step which should be made in development should be along the lines of education. It may be that the most beneficial action which could be taken in favor of E. U. countries is the creation and financing of schools, laboratories, universities, and the dispatch of technicians, scientists, etc. on the spot.^(a)

(C) What should be the size of development?

Under North American psychological influence, the leaders of some backward countries seem often to have come to the conclusion that the one way to undertake development is to spend a considerable amount of money in magnificent and often completely useless public works which at best could be justified if they had a contra-cyclical effect. The building of huge dams, enormous airfields, four-lane super highways, and gigantic bridges will not solve any standard of living or production problem at all, but will raise considerable questions of repayment.

(a) The launching of small scale "agricultural" enterprises such as those created and projected by the F.A.O. small industries engineers could have the doubly beneficial effect of adding to the productivity of nations and to the skill and knowledge of their people on a self-financing basis.

As revealed by the analysis of Latin American or Middle Eastern budgets, the ability of the Governments to finance developmental expenditures is extremely small. As revealed by the study of the accumulation of savings, the ability of private people to finance such expenditures is just as moderate. However, the foreign and local borrowing already engaged in for such purposes has created a serious problem of transfer. In most cases it is extremely difficult to see how any of the E. U. countries will be able to reimburse what they owe to their creditors out of increased production. However, when all is said and considered, this is the only way for any country to redeem its indebtedness in the long-run.

New investments should, therefore, be as small as possible and give as large a productive yield as possible. The multitudinous unproductive public works undertaken or planned by Governments of economically underdeveloped countries should be avoided, for even if all undertakings financed with foreign capital are sound and productive, they will not have any beneficial effect at all if the Government and the people of the borrowing countries stop their own productive expenditures and dedicate everything to non-productive investments.

The above suggests not only the need for a considerable modification in the attitude of Latin American Governments or Governments of E.U. countries, but, too, the need of a change in the mentality of the technicians hired by them to help in their economic troubles, but who in fact accelerate the trouble by introducing the grandiose US scale. Certain countries, such as Venezuela, are well aware of that fact and try to secure the advice and opinion of people who will teach them to build at low cost and to find inexpensive solutions to large production problems. It is not necessary to have double super highways (to towns) if the traffic is small. It is not necessary to build a 60,000 k.w. dam if the predictable demand for the next 10 years does not exceed 12,000 k.w. It is not necessary to build a complicated dispatching system and a two-way railroad line where single track, low-speed, no ballast line can do the job.

In short, development should avoid the spectacular and turn towards the useful.

(D) Through whom should development be undertaken?

Where development is placed under the direct control and management of the Government or under a parastatal institution, risks are great that political considerations will influence the selection of projects and that the local Government will, in order to raise the local capital necessary for its undertakings, create such a pressure on private savings and private capital formation that private endeavors will be practically stopped. This seems to have occurred in Mexico during the execution of the 1941-46 plan. On the other hand, it would be unrealistic to expect that private interest will be attracted only to those projects which produce more commodities for the good of the nation and the good of the entire world. The tendency would be rather to seek quick profits through the construction of buildings, purchase of real estate, and operation of soft or hard drinks factories.

Furthermore, the quantity of capital which private people in E. U. countries are able to mobilize is small, and this makes them poor partners to an international effort in the direction of the expansion of production.

Most of the time the only private capital able and willing to participate in positive and practical development is the foreign capital, but, unfortunately, with a few exceptions, the psychological effect of an expansion of foreign-owned enterprises in backward countries is bad for reasons expressed above.

II. The Financing of Development

Various difficulties seem to surround the problem of the financing of development expenditures with foreign capital.

(A) Difficulties inherent to private financing

The long history of defaults, expropriation, and abusive taxation in many E. U. countries and the difficulties which the large and sound foreign interests encounter in their dealings with Governments and private people alike in the last 15 years have changed considerably the nature of the new capital penetrating in these countries. At present, the institutional investor or the large firm is reluctant to engage in new investment activities, and often the Governments of economically underdeveloped countries are loathe to welcome investment from a politically powerful source. Therefore, only small firms penetrate in E. U. countries, firms which have only the intention of making a large profit and which will leave little, if any, equity in the country when they will have brought their activity to a close.^(a) In order to reestablish confidence in that kind of investment which will be productive for both foreign interest and the countries concerned, many prerequisites have to be filled.

Amongst others, default situations must be cleared in one way or another. It is important to stress here that the paying ability of backward countries is small and that debt settlements which involve too heavy a burden will not be successful.

It will be necessary also to establish a record of sound investment in backward countries. This could be done by institutions such as the Exim-bank or the International Bank which have the power to obtain from borrowing countries the execution of certain essential reforms, without which any new enterprise would be doomed to failure.

If the above were realized, it would be necessary furthermore to establish a set of rules governing the transfer to the creditors countries of these profits which result from their investment in E. U. countries.

Latin American, Middle Eastern, Asiatic, and African countries can barely afford normal growth on the basis of the benefits derived from foreign trade. It is, therefore, even more difficult for them simultaneously to take care of their own growth and to give large profits to foreigners. To expect a complete freedom in the disposition of profits is thus unrealistic. However, the rules governing exchange control, the maximum profits which can be made by the foreign companies, the maximum taxes to which a foreign company

(a) This finds another manifestation in the net annual yields from foreign investments in Latin America - from pre-war averages of 2½ to 4% for non-US and US investments respectively, they jumped to 4 to 9% in 1946.

can be submitted should be set once and for all and possibly with the approval of a supreme body such as the United Nations. These rules should only be revised through negotiations with all parties.

(B) Difficulties inherent to dollars investment

1. Latin America suffers at present from a considerable dollar shortage. Its yearly indebtedness to the US amounts to approximately \$2 billion,^(a) while its favorable balance with Europe is about of the same size. The world as a whole suffers from a shortage of dollars ranging presently from 8 to 10 billion yearly.

In the short-run, the World's and Latin America's \$ shortages may be reduced or even eliminated through Marshall Plan loans or grants in aid. During this period, large US\$ loans to Latin America should be avoided: It can be surmised that the dollars which will be available to E. U. countries without any IBRD loans will of themselves create a heavy inflationary pressure on the USA, so heavy as to justify export controls. There is no need of increasing that pressure.

In the long-run (after 1950/52 f.i.), the basic disequilibrium in balances between the US and the rest of the world would not present any difficulty if the US would be willing to invest abroad several billion US\$ a year for many years to come and would be willing after 25 to 30 years to lower its tariffs, reduce its production, and accept repayment of its loans in goods.

Many indications exist that for political and psychological reasons the US will not adopt such measures in the long-run. Even though they were ready to invest billions abroad every year, it is doubtful that they are ready to organize after a period of years a national reduction of hours of labor or be submitted to widespread unemployment. And, nevertheless, these measures are necessary if the repayment of the loans is to come.^(b) Therefore, unless the US is ready to make gifts to the world for a long period, no definite improvement in the US\$ shortage is logically possible. Europe will thus have to take its share in financing E. U. countries as soon as possible.

(C) Restrictions placed on certain kind of loans

There has been and there is a considerable reluctance on the part of the Eximbank and the International Bank to finance local expenditures in

(a)	Balance of trade deficit with US:	1.7 billion US\$ a year.
	Capital payments to US:	0.23 " " " "
	Balance of trade with world - US: (Assumed)	2.3 " " " "
	Capital payments to World - US:	0.25 " " " "
(b)	The prewar "creditor" nations of Europe have obviously enjoyed for years a standard of living which was not justified by local production alone. They were in fact benefiting of investments made in the pre-World War I "imperialistic" period.	

development countries. Furthermore, the balance of payment loans have been rejected as non-productive. This reluctance may be explained for psychological reasons, (a) but when it comes to hard economic facts, the effect and implication of any of these forms of loan are exactly the same as those of the loans for development. The success of the endeavors of a country will be determined by the totality of its policy, and not by the fact that it is tied to extremely stringent rules for a very small part of its national economy.

A balance of payments loan could enable a country to enjoy a considerable industrial and agricultural development, if industrial machines and agricultural implements constitute a large part of the country's imports. On the other hand, a straight development loan would be completely ineffective if the country spends the rest of its money on non-essentials and dedicates its local capital or foreign exchange surplus to the execution of political public works or to the up-keep of a large army.

Two factors, therefore, should only be considered in the making of a foreign exchange loan, and they are:

1. Is the overall policy of the country directed toward more production or toward more useless expenditures?
2. Will the production of the country increase sufficiently to enable it to service a loan of the size considered?

(a) Investors in IBRD bonds might prefer to see "productive loans."

III. Development Within the Framework of a World Policy

(A) As described above, development countries will not suffer from a shortage of dollars or a shortage of any other currency in the short-run, i.e., until the Marshall financing is completed. During the "Marshall Period", development countries will in fact assume the position of creditors as they did during the World War. They could take care of their own development requirements if this did not mean an undue pressure on US and European equipment exports. It is, therefore, suggested that they utilize the few years of short-run financial help to put their house in order and plan for the large-scale development that will only be possible after 1951-52. In order to achieve that effect, they will have to avoid mistakes of the 1940-46 period during which they utilized their foreign exchange balance as a basis for an uncalled-for monetary expansion and then for the purchase of luxury items as soon as goods became available. In the drafting of such laws and regulations which will make sounder policies possible, the help of organizations such as the International Bank and the International Monetary Fund would be valuable.

Simultaneously with the improvement of their financial and economic situation, development countries could engage in a form of limited development endeavors. The system they wanted to inaugurate in 1945-46 was one of large-scale developmental growth. In most cases, however, the E. U. countries failed to demonstrate that their administrative setup and the local availability of "know-how" and local capital were sufficient to warrant the success of the new creations. In the "Marshall Period," the E. U. countries could start again at the beginning and inaugurate skeleton organizations which would provide them by 1951-52 with a healthy framework upon which development can start on a large scale. Some form of financial and technical help may be required for the creation of this skeleton. It would be advisable that small dollar loans be made, earmarked for very small projects of great strategic value which could be and should be equipped with European material.

This condition seems to be essential, since further short-run expansion on the basis of American material would create an inflationary pressure in the States and at the same time close a little further the development markets for European goods. Marshall Europe cannot survive if it cannot import raw materials and export manufactured products. But then comes the problem of availability of material. Assuming even that Europe is ready to deliver goods on credit to Latin America, the ability of Europe to supply enough material in a short period of time needs to be demonstrated. It is believed that this ability is much greater than usually assumed. This might be illustrated by the fact that the yearly exports of Belgium will amount to nearly US\$1.8 billion a year in 1947 while the exports of the US will only reach about US\$14 billion. The difficulty is that most Latin American countries want to receive equipment too fast and that no effort is made to find sources of supply in Europe. Furthermore, European producers sell without consideration for the productive yield of their sales. They ignore the fact that 10,000 tons of rails sent to India or used in European yards will have a much smaller productive effect than the same weight of steel utilized in agricultural or mining sections of Venezuela or Peru.

(B) In the long-run it must be assumed that the industrial potential of Europe will be partially restored. In this case Europe will be in a position to finance through the International Bank or otherwise the development in E. U. countries which again are likely to be in a situation of balance of payments deficit. Furthermore, US dollar financing if available will be then sustained by US exports, and this will not disturb the internal price structure of the US. But, the availability of capital and funds will not by itself imply the existence of a situation conducive to harmonious development: the internal soundness of the countries to be developed is necessary, and a workable organization for development must exist. It is hoped that the first goal will have been achieved through the collaboration of the countries and international institutions during the "Marshall Period," but then the procurement and organization of the problem still will remain to be solved.

We have seen that for various reasons the existing institutions in charge of development are extremely sensitive to non-economic factors to which they should be immune. Furthermore, the procurement of material and skill has been adulterated by the dominant position of the US during the war and by the relative inadequacy of European sales organization in development countries.

Therefore, there appears the necessity of the creation of an international board, which would be a clearing house for a part of the goods and commodities produced all over the world. It should be provided with a list of all the projects and plans of backward countries, study them from the point of view of production efficiency, and finance the operation of the transfer of these goods with IBRD or private funds, or on the basis of commodity exchange.

On the management side, such organization should set up independent development corporations with the financial participation of local governments, private nationals, foreign interests, and international funds. These would be staffed with or utilize international experts and would sell their creations after their successful operation to local interests. The sum total of the Board and of the instrumentalities created by it would in fact be an International Development Corporation.

IV. Prerequisites to Development

The above suggests that no loan can be successful if a set of rules is not adopted by the country in which development should take place.

It would, of course, be futile to set stringent laws as prerequisites to a loan. However, the following should be considered:

1. The country should make the best of the opportunities offered by the Marshall period, undertake a skeleton framework for large scale development to come, and be ready to participate to an International Development Corporation.
2. The country should clear its default situation.
3. The country should establish a set of clear rules governing foreign investment.
4. Since much of the capital of nationals of E. U. countries is invested abroad and since local capital is almost always lacking, the nationals should be obliged either to repatriate their holdings or to invest them in an institution dealing with international investment, for the purpose of being used in E. U. countries.
5. The country should eliminate from its budget non-productive items except the minimum required for the smooth administration of the country and the minimum required to meet its international obligations. Similarly, credit restrictions should be imposed on all non-productive endeavors.
6. The Governments of the countries should at least arrive at the point where the whole of their ordinary expenditures are covered by ordinary receipts. They should only borrow from the public or from their central bank for the execution of productive and long-range development projects.
7. A strict exchange control should avoid flight of capital and prohibit unnecessary imports. If such controls cannot be imposed for psychological reasons, devaluation is the only alternative.

December 8, 1947

COMMITTEE ON DEVELOPMENT POLICY

At the first meeting of the Committee, Friday, December 5, it was decided that each member would submit a list of specific topics on the problems of Development Countries, the problems of lending to Development Countries, and the problems relating to the Bank's participation in such lending. These lists will be submitted to the Secretary in Room 401 not later than Tuesday afternoon, December 9.

It is intended that the subjects suggested be the basis for special papers which the Committee will sponsor in order to enable it to prepare a final report. The lists which are submitted will be assembled by the Chairman into a tentative program of work to be discussed at the next meeting.

Dr. Rosenstein-Rodan will prepare an initial survey of the economic problems of backward countries.

Mr. Clee will circulate a paper describing his Division's method of procedure in following up a loan application from a Development Country.

The next meeting of the Committee will be held on Thursday, December 11, at 4:00 P.M., in Room 410.

R. F. Skillings
Secretary

cc: J. M. Penton, Chairman
A. Basch
V. Checchi
F. Consolo
R. H. Demuth
W. Hill
A.S.G. Hoar
M. Madigan
P. Rosenstein-Rodan
V. L. Urquidí

Develop. Comm.

Mr. A. S. G. Hoar

5th December, 1947

C. C. Hamilton

DEVELOPMENT COMMITTEE

Your note of the 1st December in reply to mine of the same date.

1. I am not convinced. Perhaps the point will be clear if I move it from the departmental to the inter-departmental plane and consider the principle in relation to someone else, e.g., the Loan Director.

2. The first duty and function of the Loan Director is defined in the Administrative Manual as the development of loan policy. If, every time a major aspect of loan policy has to be developed, the matter is taken out of his hands and put into those of an inter-departmental committee, his function becomes in effect to develop minor (but not major) aspects of loan policy. His objections could not be met by pointing out to him that the Vice President had nominated "appropriately experienced personnel" to sit on the committee, that his department was represented, and that he was, therefore, not left in the cold. The fact is that it is his function to do this job.

3. The point of principle I am making is that

- (a) inter-departmental committees should not be set up to perform duties already assigned to a department, and
- (b) departmental committees should not be set up to perform duties already assigned to a division or office.

4. In both cases, of course, an advisory committee would often be desirable and sometimes necessary, but it should be advisory only.

(This point has already been established as regards the Staff Loan Committee.)

December 3, 1947

COMMITTEE ON DEVELOPMENT POLICY

The first meeting of the Committee will be held in
Room No. 410 on Friday, December 5, at 4:30 p.m.

Agenda

1. Constitution of the Committee
2. Program and methods of work
3. Any other business

R.F.S.
R. F. Skillings
Secretary

cc: Messrs. J. M. Penton, Chairman
V. L. Urquidi
G. H. Clee
F. Consolo
R. H. Demuth
P. Rosenstein-Rodan
A. Basch
W. Hill
A. S. G. Hoar
M. Madigan

OFFICE MEMORANDUM

Mr. J. M. Penton

TO: Chairman of Development Committee

DATE: 2 December 1947

JT/225/amh

FROM: J. Torfs

SUBJECT:

At the occasion of a meeting held by the Working Party on Development of the Loan Department, the conclusion was reached that in certain circumstances the Bank should supervise very closely the execution of small pilot programs.

This would occur mainly in very small countries which obviously are unable to plan and to carry out successfully development programs of their own and which would not object to some form of foreign intervention.

I pointed out that an organization already existed which could assure the Bank of experienced international control of a development program and which could provide correct planning and management. This organization is the Agricultural Industrial Division of the Food and Agricultural Organization of the FAO. Its leader, Mr. Harry Clement, and his team of specialized engineers demonstrated what could be done successfully in Central American countries and in China.

Letters from Mr. Clement, biographical data on his team, and descriptive graphic records of the achievements of this organization are annexed herewith.

Mr. Clement recently confirmed that he was ready to describe his program at your best convenience.

He mentioned a new line of endeavor which had been entered into by his team:

In very primitive countries, slaughter houses waste considerable amounts of animal glands, the content of which could be marketed easily at a large profit.

Several countries have approached his organization in order to install locally such material which would be needed for the process.

Develop. Com

Mr. A. S. G. Hoar

1st December, 1947

C. C. Hamilton

DEVELOPMENT COMMITTEE

You will remember that when it was proposed to set up a departmental committee to study development problems with a view to working out some broad lines of policy on development loans, I drew your attention to the fact that assistance to the Loan Directorate in the development of loan policy was an important part of the duties of my office. I expressed my doubts as to whether a departmental committee should be set up to assume duties already assigned to an office, just as I had previously expressed doubts as to whether an inter-departmental committee should ever be set up to assume the duties already assigned to a department. You then explained to me that Davies' position as Secretary to the committee was not intended to be a "secretarial" one, but rather that of a "rapporteur", and that he would be expected to make a substantial contribution to the findings of the committee and do most of its drafting. This seemed to ensure, to some extent, that a responsibility already assigned to my office was not entirely handed over to a committee.

This departmental committee has now been dissolved and has been superseded by an inter-departmental committee to which all the members of the earlier committee have been appointed except Davies; moreover, another member of the staff of the Loan Department has been added to the new committee, while my office is not represented on it.

I am sure that this was an oversight which you will wish to remedy, and I have only set the facts down in writing because the principle involved is one which I wish to put on the record.

CCH mcw

November 28, 1947

Ex
MEMORANDUM FOR: MR. HOAR
MR. HILL
MR. RIST
MR. DEMUTH

Ind
Mr. Penton
May we speak, please!
Ex 28/x1

Confirming discussions, I hereby appoint the following interdepartmental Committee on Development Policy. Inasmuch as development of various types of loan policies is the primary function of the Loan Department they should provide the chairman. The Committee shall be as follows:

J.M.
~~A. L.~~ Penton, Chairman
V. L. Urquidi
G. H. Clee
F. Consolo
R. H. Demuth
P. Rosenstein-Rodan
A. Basch

I think it will be useful if you will request Madigan to sit in when appropriate.

I believe it would be most suitable if this committee acts in the first instance as a programming group to outline the basic problems which should be considered in the formulation of the development policy and recommendations as to how such a policy might be worked out. I think this should include drawing up lists of other organizations and individuals who have done or are doing substantial work in this field as well as information regarding the best sources of material. This should lead to recommendations as to how we should proceed with the study of the various aspects of the problem.

I think that the committee should also develop a list of the important subjects into which the problem divides itself and perhaps develop certain preliminary recommendations regarding them.

I hope that most of the members could give this committee a high priority so that they would have a preliminary paper ready within a week or ten days. At that time I think it would be useful to submit this to the Staff Loan Committee for discussion.

R. L. Garner
R. L. Garner

TENTATIVE AGENDA FOR DEVELOPMENT PROBLEMS COMMITTEE

1. Nature of the problems confronting underdeveloped countries:
 - (a) Are these problems common to all or only to some?
 - (b) Classification of underdeveloped countries
 - (c) Types of problems
 - (i) Economic
 - (ii) Financial
 - (iii) Administrative
 - (iv) Political
 - (v) Social.
2. The International Bank's role in the solution of problems
 - (a) Separate projects versus integrated development programs
 - (b) Financial assistance only versus financial, technical, and economic assistance.
3. International policies for development.
 - (a) Role of IMF.
 - (b) Effect of Marshall Plan
 - (c) United Nations Economic and Social Council, with particular reference to Subcommittee on Economic Development.
 - (d) Inter-American proposals.
 - (e) Middle-Eastern proposals.
 - (f) Other regional proposals.
4. Policy for the International Bank.
 - (a) Short-term policy, defined to include up to the time of Europe's rehabilitation.
 - (b) Long-term policy.

Mr. Victor L. Urquidí

November 26, 1947

A. S. G. Hoar

Development Problems Committee

We should now aim at systematizing our thinking on development problems. To this end I wish to set up a Development Problems Committee, of which I should like you to act as Chairman, and of which the other Loan Department members will be Messrs. Consolo, Davies, Madigan, Torfs and Welk. Mr. Davies will also act as Secretary.

I have already told Mr. Rist that we should value the participation of a representative of the Research Department on this Committee. Please ascertain who this representative is to be, and invite him to attend your meetings.

The Committee should take as its terms of reference the following:

- (1) To examine and compare the development problems of different areas;
- (2) To consider the different possible solutions of these problems and the Bank's possible role therein;
- (3) To make tentative recommendations as to the Bank's short-term and long-term policy respectively;
- (4) To indicate the lines on which further study should proceed.

Attachment

CHD:dh

Develop Com

PROCEEDINGS OF DEVELOPMENT PROBLEMS COMMITTEE

A meeting of the above Committee was held on the 24th of November. Those present were the Messrs. Urquidí (Chairman), Davies (Secretary), Consolo, and Torfs.

The Committee discussed the problems raised by development programs in the different branches of production viz., agriculture, forestry, fisheries, minerals, and industry, with special reference to

- (a) The degree of technical assistance, supervision and experiment which might be needed in countries in different degrees of development;
- (b) The extent to which the Bank should encourage the development of these different branches of production in view of the desirability of promoting balanced economies.

Mr. R. L. Garner, Vice President

25th November 1947

A.S.G. Hoar, Assistant Loan Director

DEVELOPMENT PROBLEMS COMMITTEE

You may be interested to know that the membership of the Loan Department Committee to consider development problems is as follows:

Messrs. Urquidi (Chairman)
Davies (Secretary)
Consolo
Torfs
Madigan

The Research Department have been invited to appoint a representative to participate in its deliberations.

ASGH/ts

Mr. Rist

25th November 1947

A.S.G. Hoar

Development Problems Committee

You may be interested to know that the membership of the Loan Department Committee to consider development problems is as follows:

Messrs. Urquidi (Chairman)
Davies (Secretary)
Consolo
Torfs
Madigan

As I mentioned during our conversation last week, we should be very pleased if you would care to appoint a representative to participate in the Committee's deliberations.

The Committee is now ready to get down to brass tacks and I have asked Urquidi to advise you of the date of a meeting within the next few days.

ASGH/ts

Develop. Com

Mr. John J. McCloy

24th November 1947

A.S.G. Hoar

Memorandum by Mr. Rist on Development Policy

I received a copy of Mr. Rist's memorandum on development policy of Latin America. I am now engaged in studying it and will give you some comments as soon as possible.

You will be glad to know that for some time the country divisions in the Loan Department have been giving close consideration to the subject of development. They have, in fact, already arrived at some estimates of development possibilities in Mexico, Chile, Bolivia and El Salvador and have reached certain tentative conclusions as to desirable policies and methods of operation.

In consequence of this, we have thought it opportune to set up a committee composed of representatives of the Asia-Africa Division, the two Latin American Divisions and Mr. Madigan, to review the problem and to develop a basic policy relative to development loans. The Research Department has also been asked to send a representative to participate in this committee's deliberations.

It is hoped that this committee will shortly be able to produce substantial contributions for consideration.

wider

GC/ASGH/ts

cc: Mr. Clee, Mr. Arquidi, Mr. Garner.

Ex OFFICE MEMORANDUM

TO: A. S. G. Hoar
FROM: Victor L. Urquidi *VM*
SUBJECT: Development Committee

DATE: November 20, 1947

The first meeting of this Committee was held yesterday. Present were: Messrs. Madigan, Consolo, Torfs and myself. The attached preliminary agenda was considered and accepted in principle. There was a discussion of the scope of the Committee's work. It was agreed that meetings would be held at frequent intervals and that a program of work for the Committee should be mapped out in such a way that the Committee might conclude its preliminary activities in a reasonably short period of time.

The Committee considered the advisability of establishing a broad classification of development countries according to their relative level of economic advancement in order to bring out the main differences in the type of problems confronting them.

Consideration was given also to whether Turkey and the non-self-governing territories should come under the scope of the Committee.

VLU:js
encls.

cc: Messrs. Hill
Consolo
Torfs
Madigan
Davies

Tentative Agenda for Development Committee

1. Nature of the problems confronting underdeveloped countries.
2. Are these problems common to all or only to some? Classification of underdeveloped countries. List of countries.
3. General nature of solutions.
 - a. Economic
 - b. Financial
 - c. Administrative
 - d. Political
 - e. Social
4. Scope of International Bank's role.
 - a. Separate projects versus integral development programs.
 - (1) Intervention in plans only.
 - (2) Intervention in general economic activity.
 - b. Financial assistance only versus financial, technical, and economic assistance.
 - c. Basic conditions.
 - (1) Status of external debt.
 - (2) Specific obstacles to foreign private capital investment.
5. International policies for development.
 - a. Role of IMF.
 - b. Effect of Marshall Plan.
 - c. United Nations Economic and Social Council, with particular reference to Subcommission on Economic Development.
 - d. Inter-American proposals.
 - e. Middle-Eastern proposals.
 - f. Other regional proposals.
6. Policy for the International Bank.
 - a. Short-term policy, defined to include up to the time of Europe's rehabilitation.
 - b. Long-term policy.

*Development Prob
com*

Mr. R. L. Garner, Vice President

18th November, 1947

A. S. G. Hear, Assistant Loan Director

DEVELOPMENT PROBLEMS COMMITTEE

We have set up in the Department a committee to consider development problems, composed of:

Messrs. Urquidi (Chairman)
Davies (Secretary)
Consolo
Torfs
Madigan.

The committee will hold its first meeting tomorrow and we hope that its discussions will result in a report which may form the basis for discussions of the Bank's policy with regard to loans for development purposes.

ASGH CCH mcw

ROUTING SLIP

Date _____

TO-		Name	Room No.
1	<i>Mr. Davies</i>		<i>404</i>
2			
3			
4			

FOR-			
	Action		Initialing
	Approval		Preparing Reply
	Comment		Previous Papers
	Filing		Noting and Returning
	Full Report		Recommendation
	Information		Signature

R. AKS

*I spoke to Urquide. He
will postpone the mtg to 19 Nov*
GH

FROM-

Urquide

LS. - Develop Com

OFFICE MEMORANDUM

TO: Mr. C. H. Davies

DATE: November 17, 1947

FROM: Victor L. Urquidi *VM*

SUBJECT: Development Committee

We are planning a meeting of the Development Committee for tomorrow at 3:30 P.M. to consider the attached agenda.

FILE COPY

Mr. Madigan

November 17, 1947

Victor L. Urquidi

Development Committee

A Departmental Development Committee was set up last week to consider development problems with a view to working out certain principles for action by the Bank. It is composed of Mr. Consolo, Mr. Torfs, Mr. Davies, yourself and the undersigned. We are planning to have a preliminary meeting tomorrow afternoon at 3:30 P.M. to consider the attached agenda.

VLU:gvs

FILE COPY

1. Nature of the problems confronting underdeveloped countries.
2. Are these problems common to all or only to some? Classification of underdeveloped countries. List of countries.
3. General nature of solutions.
 - a. Economic
 - b. Financial
 - c. Administrative
 - d. Political
 - e. Social
4. Scope of International Bank's role.
 - a. Separate projects versus integral development programs.
 - (1) Intervention in plans only.
 - (2) Intervention in general economic activity.
 - b. Financial assistance only versus financial, technical, and economic assistance.
 - c. Basic conditions.
 - (1) Status of external debt.
 - (2) Specific obstacles to foreign private capital investment.
5. International policies for development.
 - a. Role of IMF.
 - b. Effect of Marshall Plan.
 - c. United Nations Economic and Social Council, with particular reference to Subcommission on Economic Development.
 - d. Inter-American proposals.
 - e. Middle-Eastern proposals.
 - f. Other regional proposals.
6. Policy for the International Bank.
 - a. Short-term policy, defined to include up to the time of Europe's rehabilitation.
 - b. Long-term policy.

ROUTING SLIP

Date _____

TO-

Name

Room No.

1 Mr. A. S. G. Hoar

2

3

4

FOR-

Action

Initialing

Approval

Preparing Reply

Comment

Previous Papers

Filing

Noting and Returning

Full Report

Recommendation

Information

Signature

RE: IS

The original of this draft note has been sent the Development Committee as a contribution for further discussion.

J. Torfs

FROM-

CONSIDERATIONS ON THE DEVELOPMENT OF
ECONOMICALLY UNDERDEVELOPED COUNTRIES (a)

The following is the synthesis of the opinions and observations of the writer, formed after several years of personal studies in economically backward countries and in Washington.

These opinions and observations have been discussed with and often suggested by members of the staff of the IRRD, the INC, the Eximbank, State Department, and officials of Belgium, Belgian Congo, Gold Coast, and Latin American Governments.

They form a logical pattern and lead to conclusions which at best are tentative in nature, for the demonstration of each point would, if handled on a strictly scientific basis, absorb the efforts of a staff of skilled economists for at least a year.

Tentative as they are, however, it is hoped that the conclusions can serve as basis for further discussion with the Bank and provide a general pattern for an IRRD policy towards development countries, which policy appears to be only in an embryonic stage at this time.

CONCLUSIONS

- ✓ 1. Latin America, Africa, the Middle East are areas where development is needed to bring about the efficient utilization of their resources for the sake of their inhabitants and for the sake of the world at large.
- ✓ 2. Development should be in the nature of projects of modest size which are designed to increase directly national production or efficiency.
- ✓ 3. Eligibility for development financing requires that countries desiring such financing have taken or be willing to take the steps necessary to a demonstration of financial and political stability and to an increase in the skills and efficiency of their population.
- ✓ 4. Other than US dollar currency or currencies should be the financing media, where feasible, and project(s) machinery and equipment should be obtained from other than US suppliers.
- ✓ 5. In the short-run, and this is to say until the end of Marshall financing, the development countries should receive only a small

(a) The countries under consideration are mostly self-governing Latin American, African or Near Eastern countries, although many remarks apply as well to Colonial Africa. The economically underdeveloped countries will henceforth be referred to as E. U. countries.

amount of financial help. However, they should receive a great amount of technical help, and both should be conducive to the establishment of sound economic practices and to the creation of the solid framework of small industries, local capital, and skills on the basis of which further large scale development will be able to take place.

6. In the long-run, an International Development Corporation could act as project(s) manager until local management can be arranged and local technicians trained to take over the project(s). The IDC would be staffed by experienced economists, businessmen, and technicians recruited on a world basis. It would (a) procure the material necessary and induce non-US suppliers to plan their production along the needs of the development countries and (b) be financed by capital subscribed by development areas Governments, by their nationals, by the IBRD, IMF, and private investors.

I. The General Problem of Development

- (A) Is the development of E. U. countries necessary?
- (B) In what realms of economic activity should development be undertaken?
 - 1.a. Agriculture
 - 1.b. Animal husbandry
 - 1.c. Forestry and forest industries
 - 1.d. Fisheries
 - 2. Metallic and mineral resources
 - 3. Industry
 - 4. Distribution
 - 5. Education
- (C) What should be the size of development?
- (D) Through whom should development be undertaken?

II. The Financing of Development

- (A) Difficulties inherent to private financing
- (B) Difficulties inherent to dollars investment
- (C) Restrictions placed on certain kind of loans

III. Development Within the Framework of a World Policy

- (A) Short-run
- (B) Long-run

IV. Prerequisites to Development

1. The General Problem of Development

In order to arrive at coherent conclusions, we deem it necessary to start from the very beginning and to investigate at first the very premises of our reasoning. Our first question is thus:

(A) Is the development of E. U. countries necessary?

The answer is affirmative for two reasons:

1. For the sake of the inhabitants of the countries under consideration development is necessary, for the standard of living of these people is generally extremely low.^(a) Many of these countries enjoy a democratic set-up; nevertheless, there are wide differences in the income of their inhabitants. Usually, a dominant group of rich landowners and industrialists and their families, mostly educated abroad, rule the country directly or indirectly. Practically all capital is concentrated in their hands. Their oligarchic group does not represent more than one-twentieth of the population. About ninety-five percent of the population is constituted of badly-educated farmers or workers enjoying little hygiene, usually undernourished, and unable to make the best of the little knowledge they have, because they are submitted to a social framework (like the system of the big Hacienda) which makes it impossible.

Theoretical measures have been taken to improve the lot of this proletariat. In Chile, for instance, the social legislation is one of the most progressive of the entire world. However, no amount of legislation will feed the workers.

At the root of this problem is an inadequate production, resulting from a lack of per capita efficiency, and this in turn is the result of a lack of education or scientific training. This in great part can only be corrected through years of education and a total revision of psychological attitudes toward life and work. However, this is a slow process which will not do in many cases, for the problem of low standards of living is urgent. Although it has existed for a considerable number of years without creating considerable disruption and chaos, it is taken at present as a political platform by communistic agitators who threaten to make the situation worse. Immediate measures are necessary.

2. For the sake of the world at large and especially for the sake of Europe, development in E. U. countries is necessary, because the world is short of practically every possible kind of goods.

It would be unrealistic, however, to predicate a policy of development on the proposition that everything should be produced because the world lacks everything. The world unfortunately is not yet in a position to purchase twice or three times the amount of goods currently produced, and this

(a) They have no access to a quantity of calories, vitamins, proteins, clothing, and housing sufficient to enable them to have US or European life expectancy.

is owed to the fact of extremely low per capita efficiency of large masses such as the Asiatic peoples. Most of the Chinese and Hindus are improperly fed and clothed; however, the product of their own labor has such a low economic significance that its value in exchange is practically nil. The clothing and the feeding of most Chinese and Hindus could only be justified on the basis of charity, and the world cannot afford this at the present moment.

A large region of the world exists, however, where the inhabitants have potential ability to pay in goods for the goods they receive. This part of the world is Europe - short of most foodstuffs and raw materials for its industry. A higher production in E. U. areas could and should be attained through development, thus, were it for the sake of the Europeans alone.

On the two bases above, the intensification of production is necessary, and development by definition is the technique conducive to such intensification.

(B) In what realm of economic activity should development be undertaken?

1.a. Agriculture The development of agriculture in most of the equatorial and subtropical parts of the world is difficult, for it brings about the phenomenon of laterisation which is no less than the sterilization of soils. In order to avoid laterisation it is necessary to select carefully proper soils and to introduce systems of erosion control. This implies reforestation, the plantation of nitrogenous plants, the building of dams and levees, etc.^(a) It is, therefore, a long-range proposition which must be studied very carefully.

Even where the terrains do not laterize, they are usually extremely poor except in such areas as Argentina or Uruguay.^(b) The expectation of high yields per acre on large scale development can, therefore, easily be disappointed.

Social difficulties hinder the development of agriculture even more. Where the land is in the hands of big landowners who practically dominate large masses of quasi serfs, there is little incentive for efficiency. The master of the property has a large income sufficient for him and for his family even when the methods of cultivation are completely out of date. The workers on the other hand are accustomed to such low incomes that they have absolutely no incentive to try to obtain better yields. Many countries like Mexico have attempted to break down the system through the redistribution of land to farmers. Unfortunately, they have gone far in the other direction and have split property so much that an exploitation on industrial scale becomes difficult. In order to back away from both inefficient systems, a

(a) The problem has been successfully tackled in Kiva (Central Africa) and in Northern and Central Peru.

(b) Regions of the highlands of Brazil f.i. are almost exhausted.

real revolution is necessary. This either takes time or involves bloodshed, and the latter method creates an atmosphere which is little conducive to developmental endeavors.

It should be noted here that the agricultural system in E. U. countries is one of the reasons for the small "capital formation".^(a) The quasi serfs or the very small farmers do not save. The big landowners do save, but as they do not trust the local political and financial setup, they convert their savings balances into foreign currencies and keep them in the United States or in Western Europe.

1.b. Animal husbandry offers little more possibilities of rapid development than agriculture. The control of diseases, which is absolutely essential as proven by the current hoof and mouth disease epidemic in Mexico, is a costly proposition, and the scientific up-keep and marketing of cattle has not yet been introduced very far in Latin America or in Africa.

1.c. Forestry and forest industries are better prospects for immediate yield. However, they imply the introduction of scientific methods of reforestation, the standardization of products, and the existence of a considerable know-how.

All of this, however, can be acquired in a few years. The progress in the exploitation of Parana Pine in Brazil is in this respect very encouraging.

1.d. Fisheries seem to have even better prospects than forestry. The only factors needed to develop this activity in E. U. countries are local and foreign capital, for where fish are abundant, the question of skill and know-how is practically negligible. The considerable growth of Chilean, Peruvian, and Mexican fish industries prove both points clearly.

2. The more intensive exploitation of metallie and mineral resources raises a completely different kind of problem.

Very large investments must be made in mining and petroleum exploitations before they can give any sizeable profit. This capital is not available in the economically underdeveloped countries because of the small amount of real savings; therefore, the exploitation of mining and petroleum must be left to foreign capital. Most of the backward countries are reluctant to let more foreign capital enter into these fields,^(b) for the profits, reserves, and the dividends of the foreign corporations are usually transferred abroad as soon as they are created. In Chile, for instance, about 25 percent of the value of the gross sales of copper leaves the country. In the case of small mining and petroleum enterprises the share of foreign exchange

(a) The little amount of real "savings" (or voluntary refrain from consuming) is the single most important factor which prevents a fast growth of E. U. countries.

(b) Brazil and Chile practically exclude foreign investments in petroleum fields.

which remains in the hands of foreign interests is much larger. In order to obtain a larger "cut" in the fruits of exploitation of their own natural resources, many Latin American countries utilize methods of taxation that are extremely discouraging to foreign capital, or insist on sharing the partnership, or in introducing their own technicians and administrators in foreign enterprises - and this results very often in a sterilization of the enterprises or in a reduction of efficiency.

In mining and petroleum as in the case of agriculture, little capital is formed for local use. Most of the savings are made by foreigners which transfer them abroad.

3. Industry The myth of industrialization at all costs has pervaded large developmental regions like Latin America or the Middle East. In certain cases when the condition of the soil is so bad as to make agricultural endeavors non-productive, a limited industrialization is justified. However, the creation of large industries requires considerable amounts of capital, know-how, and skills. Most of them are often lacking in L. A. countries. Industrial endeavors in the direction of self-sufficiency, such as the manufacture of jet-propelled pursuit planes in Argentina, are completely unjustifiable. The creation of a steel mill in Brazil, which is neither close to the iron ore deposits nor the coal deposits, might not have any beneficial effect.

However, a local steel mill in Chile at the proximity of coal fields, situated at the proximity of iron ore deposits, and close to a large market should not be dismissed as inefficient on the basis of cost calculation alone, for it might very well be efficient in terms of labor costs, and the monetary costs may spoil the picture, because of non-industrial factors such as inflationary situation or over-valued currency. But in general large industries in backward regions are expensive, their products cannot compete with foreign goods, and they do not help solve the world problems at all insofar as they expand lines of production which are practically the only ones left to areas such as Western Europe and where no shortage is foreseeable in the future.

Small industries can have a considerable better chance of success. Small textiles mills when cotton is available, small tools factories, manufactures of canned foodstuffs, beer, or copper appliances can be justified and productive, and, furthermore, they can constitute a strong basis for capital formation.

4. Distribution Where no market facilities exist or where they are extremely elementary, the organization of an efficient distribution system is sometimes much more helpful than the development of production itself. Cooperatives, warehouses, quick-freezing plants, canning plants, and packing manufactures can be organized on the basis of local capital, but require foreign technical knowledge. This is a line where much could be done at little expenditure.

New railroads involve large investments, and extremely careful consideration. In E. U. countries, as everywhere, the building of new railroads is a risky business at best, and even lines of old standing experience great difficulties. However, the creation of new lines in backward countries should not be always predicated on the basis of existing traffic. New lines open up new regions, and the demand for traffic follows the supply. It is unfortunate that the old free enterprise spirit which presided at the opening of most lines in the US and many in Africa, Asia, and Latin America seems to be replaced by the fear of risk which characterize present day Western European or US big investors, for large profits and immense economic improvements could accompany the creation of lines between Chile, Bolivia, Brazil, or across Africa. Owing to the present mentality, however, only the improvement of existing lines and the opening of "sure-fire" sections of railroads can be considered. This could, however, have beneficial effects.

The building of highways on the other hand seems to be the favorite manner of wasting money in many E. U. countries. It remains to be demonstrated that road transport is cheaper than the rail, and that the building of highways parallel to railroad lines present any economic advantage whatsoever.

5. Education The analysis of the four points above indicates that the development of practically all lines of economic endeavors is possible and desirable in backward countries, except in the domain of heavy and medium-heavy industry, but it is just as important to note that in practically no instance is that development possible without technical knowledge, know-how, and social reforms. This leads to the suggestion that, as the acquisition of more knowledge must come before the utilization of this knowledge, the first step which should be made in development should be along the lines of education. It may be that the most beneficial action which could be taken in favor of E. U. countries is the creation and financing of schools, laboratories, universities, and the dispatch of technicians, scientists, etc. on the spot.^(a)

(C) What should be the size of development?

Under North American psychological influence, the leaders of some backward countries seem often to have come to the conclusion that the one way to undertake development is to spend a considerable amount of money in magnificent and often completely useless public works which at best could be justified if they had a contra-cyclical effect. The building of huge dams, enormous airfields, four-lane super highways, and gigantic bridges will not solve any standard of living or production problem at all, but will raise considerable questions of repayment.

(a) The launching of small scale "agricultural" enterprises such as those created and projected by the F.A.O. small industries engineers could have the doubly beneficial effect of adding to the productivity of nations and to the skill and knowledge of their people on a self-financing basis.

As revealed by the analysis of Latin American or Middle Eastern budgets, the ability of the Governments to finance developmental expenditures is extremely small. As revealed by the study of the accumulation of savings, the ability of private people to finance such expenditures is just as moderate. However, the foreign and local borrowing already engaged in for such purposes has created a serious problem of transfer. In most cases it is extremely difficult to see how any of the M. U. countries will be able to reimburse what they owe to their creditors out of increased production; however, when all is said and considered, this is the only way for any country to redeem its indebtedness in the long-run.

New investments should, therefore, be as small as possible and give as large a productive yield as possible. The multitudinous unproductive public works undertaken or planned by Governments of economically underdeveloped countries should be avoided, for even if all undertakings financed with foreign capital are sound and productive, they will not have any beneficial effect at all if the Government and the private people of the borrowing countries stop their own productive expenditures and dedicate everything to non-productive investments.

The above suggests not only the need for a considerable modification in the attitude of Latin American Governments or Governments of M. U. countries, but too the need of a change in the mentality of the technicians which are hired by them to help in their economic troubles, but who in fact accelerate the trouble by introducing the grandiose US scale. Certain countries such as Venezuela are perfectly aware of that fact and try to secure the advice and opinion of people who will teach them to build at low cost and to find inexpensive solutions to large production problems. It is not necessary to have double super highways (to towns) if the traffic is small. It is not necessary to build a 60,000 k.w. dam if the foreseeable demand for the next 10 years does not exceed 12,000 k.w. It is not necessary to build a complicated dispatching system and a two-way railroad line where single track, low-speed, no ballast line can do the job.

In short, development should avoid the spectacular and turn towards the useful.

(D) Through whom should development be undertaken?

Where development is placed under the direct control and management of the Government or under a parastatal institution, risks are great that political considerations will influence the selection of projects and that the local Government will, in order to raise the local capital necessary for its undertakings, create such a pressure on private savings and private capital formation that private endeavors will be practically stopped. This seems to have occurred in Mexico during the execution of the 1941-46 plan. On the other hand, it would be unrealistic to expect that private interest will be interested only in those projects which produce more commodities for the good of the nation and the good of the entire world. The tendency would be rather to seek quick profits through the construction of buildings, purchase of real estate, and operation of soft or hard drinks factories.

Furthermore, the quantity of capital which private people in U. S. countries are able to mobilize is small, and this makes them poor partners to an international effort in the direction of the expansion of production.

Most of the time the only private capital able and willing to participate in positive and practical development is the foreign capital, but, unfortunately, with a few exceptions, the psychological effect of an expansion of foreign-owned enterprises in backward countries is bad for reasons expressed above.

II. The Financing of Development

Various difficulties seem to surround the problem of the financing of development expenditures with foreign capital.

(A) Difficulties inherent to private financing

The long history of defaults, expropriation, and abusive taxation in many E. U. countries and the difficulties which the large and sound foreign interests encounter in their dealings with Governments and private people alike in the last 15 years have changed considerably the nature of the new capital penetrating in these countries. At present the institutional investor or the large firm is reluctant in engaging in new investment activities, and often the Governments of economically underdeveloped countries are reluctant to welcome investment from a politically powerful source. Therefore, only small firms penetrate in E. U. countries which only have the intention of making a large profit and which will leave little, if any, equity in the country when they will have brought their activity to a close. (a) In order to reestablish confidence in that kind of investment which will be productive for both foreign interest and the countries concerned, many pre-requisites have to be filled.

Amongst others, default situations must be cleared one way or another. It is important to stress that the paying ability of backward countries is small and that debt settlements which involve too heavy a burden will not be successful.

It will be necessary also to establish a record of sound investment in backward countries. This could be done by institutions such as the Exim-bank or the International Bank which have the power to obtain from borrowing countries the execution of certain essential reforms, without which any new enterprise would be doomed to failure.

If the above were realized, it would be necessary furthermore to establish a set of rules governing the transfer to the creditors countries of these profits which result from their investment in E. U. countries.

Latin American, Middle Eastern, Asiatic, and African countries can barely afford normal growth on the basis of the benefits derived from foreign trade. It is, therefore, even more difficult for them to simultaneously take care of their own growth and to give large profits to foreigners. To expect a complete freedom in the disposition of profits is thus unrealistic. However, the rules governing exchange control, the maximum profits which can be made by the foreign companies, the maximum taxes to which a foreign company

(a) This finds another manifestation in the net annual yields from foreign investments in Latin America - from pre-war averages of 2½ to 4½ for non-US and US investments respectively, they jumped to 4 to 9% in 1946.

can be submitted should be set once and for all and possibly with the approval of a supreme body such as the United Nations. These rules should only be revised through negotiations with all parties.

(B) Difficulties inherent in dollars investment

1. Latin America suffers at present of a considerable dollar shortage. Its yearly indebtedness toward the US amounts to approximately \$2 billion.^(a) while its favorable balance toward Europe is about of the same size. The world as a whole suffers of a shortage of dollars ranging presently from 6 to 10 billion yearly.

In the short-run, the World's and Latin America's \$ shortages may be reduced or even eliminated through Marshall Plan loans or grants in aid. During this period, large US\$ loans to Latin America should be avoided: It can be surmised that the dollars which will be available to E. U. countries without any US\$ loans will already create a heavy inflationary pressure on the USA, so heavy as to justify export controls. There is no need in increasing that pressure.

In the long-run (after 1950/52 f.i.), the basic disequilibrium in balances between the US and the rest of the world would not present any difficulty if the US would be willing to invest abroad several billion US\$ a year for many years to come and would be willing after 25 to 30 years to lower its tariffs, reduce its production, and accept the repayment of its tariffs, reduce its production, and accept the repayment of its loans in goods.

Many indications exist that for political and psychological reasons the US will not adopt such measures in the long-run. Were they ready to invest billions abroad every year, it is doubtful that they are ready to organize after a period of years a national reduction of hours of labor or to submit to a widespread unemployment. And, nevertheless, these measures are necessary if the repayment of the loans is to come.^(b) Therefore, unless the US is ready to make gifts to the world for a long period, no definite improvement in the US\$ shortage is logically possible. Europe will thus have to take its share in financing E. U. countries as soon as possible.

(C) Restrictions placed on certain kind of loans

There has been and there is a considerable reluctance on the part of the Eximbank and the International Bank to finance local

(a)	Balance of trade deficit with US:	1.7 billion US\$ a year.
	Capital payments to US:	0.23 " " " "
	Balance of trade with world - US: (Assumed)	2.3 " " " "
	Capital payments to World - US:	0.25 " " " "
(b)	The former "creditor" nations of Europe have obviously enjoyed for years a standard of living which was not justified by local production alone. They were in fact benefiting of investments made in the pre-World War I "imperialistic" period.	

expenditures in development countries. Furthermore, the balance of payment loans have been rejected as non-productive. This reluctance may be explained for psychological reasons,^(a) but when it comes to hard economic facts, the effect and implication of any of these forms of loan are exactly the same as those of the loans for development. The success of the endeavors of a country will be determined by the totality of its policy, and not by the fact that it is tied to extremely stringent rules for a very small part of its national economy.

A balance of payments loan could enable a country to enjoy a considerable industrial and agricultural development, if industrial machines and agricultural implements constitute a large part of the country's imports. On the other hand, a straight development loan would be completely ineffective if the country spends the rest of its money on non-essentials and dedicates its local capital or foreign exchange surplus to the execution of political public works or to the up-keep of a large army.

Two factors, therefore, should only be considered in the making of a foreign exchange loan, and they are:

1. Is the overall policy of the country directed toward more production or toward more useless expenditures?
2. Will the production of the country increase sufficiently to enable it to service a loan of the size considered?

(a) Investors in INEB bonds might prefer to see "productive loans."

III. Development Within the Framework of a World Policy

(A) As described above, development countries will not suffer of a shortage of dollars or a shortage of any other currency in the short-run, i.e., until the Marshall financing is completed. During the "Marshall Period", development countries will in fact assume the position of creditors as they did during the World War. They could take care of their own development requirements if this did not mean an undue pressure on US and European equipment exports. It is, therefore, suggested that they utilize the few years of short-run financial help to put their house in order and plan for the large-scale development that will only be possible after 1951-52. In order to achieve that effect, they will have to avoid mistakes of the 1940-46 period during which they utilize their foreign exchange balance as a basis for an uncalled-for monetary expansion and then for the purchase of luxury items as soon as goods became available. In the drafting of such laws and regulations which will make sounder policies possible, the help of organization such as the International Bank and the International Monetary Fund would be valuable.

Simultaneously with the improvement of their financial and economic situation, development countries could engage in a form of limited development endeavors. The system they wanted to inaugurate in 1945-46 was one of large-scale developmental growth. In most cases, however, the E. U. countries failed to demonstrate that their administrative setup and the local availability of "know-how" and local capital were sufficient to warrant the success of the new creations. In the "Marshall Period," the E. U. countries could start again at the beginning and inaugurate skeleton organizations which would provide them by 1951-52 with a healthy framework upon which development can start on a large scale. Some form of financial and technical help may be required for the creation of this skeleton. It would be advisable that small dollar loans be made, earmarked for very small projects of great strategic value which could be and should be equipped with European material.

This condition seems to be essential, for further short-run expansion on the basis of American material would create an inflationary pressure in the States and at the same time close a little further the development markets for European goods. Marshall Europe cannot survive if it cannot import raw materials and export manufactured products. But then comes the problem of availability of material. Assuming even that Europe is ready to deliver goods on credit to Latin America, the ability of Europe to supply enough material in a short period of time should be demonstrated. It is believed that this ability is much greater than usually assumed. This might be illustrated by the fact that the yearly exports of Belgium will amount to nearly US\$1.8 billion a year in 1947 while the exports of the US will only reach about US\$14 billion. The difficulty is that most Latin American countries want to receive equipment too fast and that no effort is made to find sources of supply in Europe. Furthermore, European producers sell without consideration for the productive yield of their sales. They ignore the fact that 10,000 tons of rails sent to India or used in European yards will have a much smaller productive effect than the same weight of steel utilized in agricultural or mining sections of Venezuela or Peru.

(B) In the long-run it must be assumed that the industrial potential of Europe will be partially restored. In this case Europe will be in a position to finance through the International Bank or otherwise the development in E. U. countries which again are likely to be in a situation of balance of payments deficit. Furthermore, US dollar financing if available will be then sustained by US exports, and this will not disturb the internal price structure of the US. But, the availability of capital and funds will not by itself imply the existence of a situation conducive to harmonious development: the internal soundness of the countries to be developed is necessary, and a workable organization for development must exist. It is hoped that the first goal will have been achieved through the collaboration of the countries and international institutions during the "Marshall Period," but then the procurement and organization of the problem still will remain to be solved.

We have seen that for various reasons the existing institutions in charge of development are extremely sensitive to non-economic factors to which they should be immune. Furthermore, the procurement of material and skill has been adulterated by the dominant position of the US during the war and by the relative inadequacy of European sales organization in development countries.

Therefore, appears the necessity of the creation of an international board, which would be a clearing house for a part of the goods and commodities produced all over the world. It should be provided with a list of all the projects and plans of backward countries, study them at the point of view of production efficiency, and finance the operation of the transfer of these goods with IBRD or private funds, or on the basis of commodity exchange.

On the management side, such organization should set up independent development corporations with the financial participation of local governments, private nationals, foreign interests, and international funds. These would be staffed with or utilize international experts and would sell their creations after their successful operation to local interests. The sum total of the Board and of the instrumentalities created by it would in fact be an International Development Corporation.

IV. Prerequisites to Development

The above suggests that no loan can be successful if a set of rules is not imposed upon the country in which development should take place.

It would, however, be futile to set stringent laws as prerequisites to a loan. However, the following should be considered:

1. The country should make the best of the opportunities offered by the Marshall period, undertake a skeleton framework for large scale development to come, and be ready to participate to an International Development Corporation.

2. The country should clear its default situation.

3. The country should establish a set of clear rules governing foreign investment.

4. As much of the capital of nationals of E. U. countries is invested abroad and as local capital is almost always lacking, the nationals should be obliged either to repatriate their holdings or to invest them in an institution dealing with international investment, for the purpose of being used in E. U. countries.

5. The country should eliminate from its budget any non-productive item except the minimum required for the smooth administration of the country and the minimum required to meet its international obligations. Similarly, credit restrictions should be imposed on all non-productive endeavors.

6. The Governments of the countries should at least arrive at the point where the whole of their ordinary expenditures are covered by ordinary receipts. They should only borrow from the public or from their central bank for the execution of productive and long-range development projects.

7. A strict exchange control should avoid evasion of capital and prohibit unnecessary imports. If such controls cannot be imposed for psychological reasons, devaluation is the only alternative.

June 9, 1947

Dear Mr. McDougall:

In reply to your letter of May 5th concerning Mr. Maddox' suggestion that the whole theory of economic development should be recast, I find myself unable to take any definite position because of the generality of the proposal. While I do not know of any studies being conducted on the theory of economic development as a whole, I have the feeling that probably whatever theoretical work is necessary is being done in connection with specific problems.

If Mr. Maddox should care to make more definite the type of study that he has in mind, I should be glad to give his suggestion further consideration. Meanwhile, if you and Mr. Weintraub decide to go ahead with an informal meeting on this subject, I will be glad to arrange to have a member of the Bank's staff attend.

Sincerely yours,

Mr. F. L. McDougall
Counselor
Food and Agriculture Organization
of the United Nations
2000 Massachusetts Avenue N. W.
Washington 6, D. C.

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David & Selma

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*L. Demuth
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5 May 1947

Dear Mr. McCloy,

I am enclosing a copy of a letter which I have sent to David Weintraub of the U.N. Secretariat.

I think Maddox has a real point. Japan used self help to a very large degree during her half century of vigorous development before the war and the fact that militarists finally took control could hardly be regarded as an argument for not utilizing the experience to be gained from Japan.

Perhaps you would be good enough to let me know whether, from your point of view, an informal and I think off the record meeting along the lines suggested in my letter to Weintraub might prove useful.

With kind regards,

Yours sincerely,

F. L. McDougall

F. L. McDougall
Counselor

Mr. John J. McCloy
President
International Bank for
Reconstruction and Development
1818 H Street, N.W.
Washington, D.C.

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WBG ARCHIVES

PERSONAL

5 May 1947

My dear Weintraub,

I have had an interesting suggestion made to me by Jim Maddox to the effect that it would be very useful to get one or more first class economists to consider the main factors that have to be taken into consideration in securing the development of poverty stricken and over populated areas. He points out that

"The problem is vastly different from the 19th Century model. Apparently, Japan is the only actual example of a country which developed an industrial economy without vast new resources to exploit. I am convinced that the whole theory of economic development has to be recast if we are to make headway in this century. I really wish that you would give serious consideration to putting a man or two on this theoretical problem. We don't need to hold up action until they produce, but we do need guidance of a type which the history of last century does not give."

After thinking this over I decided to write to you and to Mr. McCloy suggesting that, in the first instance, it might be useful to have an informal meeting on this subject attended by expert members of the staff of U.N., the Bank and FAO, and possibly by two or three outside economists. At such a meeting the many factors that ought to be taken into consideration might be noted and the meeting might be asked to advise as to whether a useful purpose would be served if arrangements could be made for some distinguished economist or economists to prepare a document on the subject. Owing to the present pressure of work in each of our Organizations, such a meeting might perhaps be held somewhat later in the year.

I should be very glad to have your personal reactions to this idea.

With kind regards,

Yours sincerely,

F. L. McDougall
Counselor

MCD:RL

Mr. David Weintraub
Division of Economic Affairs
United Nations