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THE WORLD BANK

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McNamara pages

Role of the Bank
1977 (Nov.)

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Role of the Bank - Correspondence 04

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711/4/32

MEMORANDUM FOR THE RECORD

Meeting on Concluding Remarks to the Informal Meeting of EDs on the IBRD Capital Increase, November 17, 1977

Present: Messrs. McNamara, Knapp, Damry, Chenery, Gabriel, Wood

Mr. McNamara said that he wanted to propose a further meeting on the Capital Increase for Tuesday, December 13, which would focus on (i) questions and comments received on technical notes to be prepared and circulated, and (ii) the issues of non-disruptive adjustment and repayment terms. The borrowing issue could be left for a subsequent meeting in January 1978. He asked Messrs. Gabriel and Wood to prepare the following three technical notes for distribution to the EDs: (i) a matrix giving the pattern of Bank lending through 1983 by type of lending, i.e., new-style urban and rural projects, nonfuel minerals, etc; (ii) rationale for an increase in IBRD lending in real terms; and (iii) impact of alternative rates of real growth on nominal lending, staff levels, quality of projects and efficiency of administration. The third note should state that there would be no dramatic increase in staff and that the improvement of quality and efficiency of administration could only be achieved through expansion, i.e., was a function of size. It should argue that the decentralization five years ago had been carried out at a below-optimal size for such a reorganization. The issue of regional decentralization and of grassroots work on new-style projects should not be raised.

CKW
November 23, 1977

711/4/31

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: November 16, 1977

FROM: Attila Karaosmanoglu *AK*

SUBJECT: A Briefing Note on Inflation

I am enclosing a briefing note on inflation for tomorrow's Board discussion.

Att.

c.c. Mr. Chenery
Mrs. Hughes/Mr. Laursen
Mr. Wood (2 copies)

HHughes/kg

11/16

DRAFT
EYSachse/KLaursen:hmr
November 16, 1977

A BRIEFING NOTE ON INFLATION

I. INTRODUCTION

1. Our recent work on the inflation prospects to 1985 has modified the views expressed a year ago.^{1/} As measured by the U.S. dollar deflator, inflation in the developed countries of the OECD is projected to average 7.5% per annum in 1978-80 and 7% per annum during 1981-85 but the parallel movement in the "index of international inflation", the index of c.i.f. U.S. dollar prices of manufactured exports^{2/} no longer appears likely.

Table I.1: BANK STAFF PROJECTIONS OF RATES OF INCREASE IN US DOLLAR GDP DEFLATORS OF OECD NORTH AND INDEX OF INTERNATIONAL INFLATION a/

(Percent per annum)

	November 1976		November 1977	
	GDP Deflator	Trade Deflator	GDP Deflator	Trade Deflator
1975	12.9	12.6	12.3	12.6
1976	3.4	1.5	3.2	0.2
1977	7.5	7.5	7.7	7.0
1978	8.0	8.0	8.0	6.0
1979	7.5	7.5	7.5	5.5
1980	7.0	7.0	7.0	5.0
1981-85	7.0	7.0	7.0	5.0
1986-90 b/	n.a.	n.a.	6.0	4.0

a/ 1975 historical, 1976-1977 estimates, 1978-1990 projections.

b/ Extended for World Development Report.

^{1/} See Technical Note: Deflators SecM 76-803, November 29, 1976.

^{2/} Categories 5-8 in the Standard International Trade Classification (SITC).

2. Such projections are quite uncertain, however. Both because our understanding of past inflation experience is incomplete, and because inflation depends largely on institutional factors, it is more difficult to analyze and project than changes in real economic variables. Our point projection of the U.S. dollar deflator should be viewed as a "central tendency" around which the variation could be rather wide. While it is above targets agreed on by the Ministerial Council of the OECD it appears to be centrally located within the range that we feel is realistic.

3. The relationship between GDP deflators and export prices is of course also uncertain. Economic theory would perhaps suggest a somewhat higher rate of inflation for the former than for the latter because productivity gains may be expected to be lower for GDP as a whole than for exports. This tendency could be reversed in periods of steeply rising commodity prices because of their greater weight in exports than in GDP. Conversely this tendency would be strengthened during periods of moderate commodity price increases. Historical developments appear to confirm these hypotheses: During the 1960's trade prices rose less rapidly than GDP deflators whereas the reverse was true in the first half of the 1970's. In 1975 the two inflation rates were about equal, but in 1976 the GDP deflator rose significantly faster than the export price index. Given this recent development, the moderate price increases projected for commodities and the above mentioned theoretical relationship, we feel reasonably confident that trade prices should now be projected to lag behind GDP deflators. This is also the position taken by the OECD Secretariat.

4. Section II of this note contains a survey of inflationary factors and some problems of measurement as a background to a more detailed discussion of our projections in Section III.

II. DEFINITION, MEASUREMENT AND "CAUSES"

5. Inflation may be defined as an increase in the general level of prices as distinct from a change in relative prices. Conceptually one may distinguish between "demand pull" inflation and "cost push" inflation, the former being

a situation where demand causes prices to go up because supply is inelastic, and the latter a situation where costs go up even if capacity is not fully utilized and are shifted on to prices. In practice, however, this distinction has not proved to be particularly relevant, mainly because an increase in demand may be inflationary rather than expansionary even at considerable unemployment levels.

6. Normally inflation is measured by the increase in the GDP deflator for a given economy which is taken to be representative of the average price increase. This procedure is, of course, subject to the usual index problem of correct weighting because the products entering into GDP are continuously changing in relative importance.

7. Obviously this problem is exacerbated when one seeks a measure of international inflation even if exchange rates are fixed. With variable exchange rates the additional problem arises that international inflation will be different whether expressed in one currency or another. Suppose, for example, that Germany's GDP deflator rises by 3% in deutsche marks while that of the U.S. goes up by 6% in dollars and that the deutsche mark appreciates 3% relative to the dollar. If measured in deutsche marks inflation in both countries and, hence, world inflation is 3%; if measured in dollars it is 6%. In other words, if the numeraire currency is appreciated, world inflation is understated; if it is depreciated, world inflation is overstated.^{1/}

8. There is no general consensus as to the causes behind such inflationary developments. On the one hand the "monetarists" argue that inflation is created by excessive monetary expansion and that price stability may be brought about by careful monetary management. On the other hand, the "structuralists" argue that "bottlenecks" in the economy combined with labor union

^{1/} An extreme example is the German hyperinflation in the early 1920's which was accompanied by daily exchange rate devaluations. Measured in marks inflation rates reached 10,000%; measured in dollars prices were fairly stable.

pressures cause prices and wages to go up in key sectors from where they "spill over" on the rest of the economy. The "structuralists" therefore conclude that high employment is only possible with high inflation rates. This is the trade-off depicted by the so called Phillips curve. The "monetarists" take the view that only under fairly stable prices will the economic climate be conducive to investment, innovations and growth so that there is no trade-off between growth and inflation.

9. Postwar inflation-growth experience appears, by and large, to support the "monetarist" position that the relationship between growth rates and inflation rates is negative. This is also the view taken by OECD's recent "McCracken Report". But some highly regarded economists are not convinced that this relationship will also apply in the future.

Table II.1: GDP DEFLATORS AND REAL GROWTH IN OECD NORTH^{a/}
(Percent per annum)

	<u>1956-58</u>	<u>1959-65</u>	<u>1966-69</u>	<u>1970-75</u>	<u>1976-77</u>
GDP Deflators					
in U.S. dollars:	3.0	2.2	3.4	10.3	5.4
in national currency:	3.5	2.4	3.9	7.9	7.6
Real GDP Growth	2.3	5.2	4.9	2.8	4.8

a/ OECD North includes all OECD members except Greece, Spain and Turkey.

Source: Annex A.

III. PROJECTIONS

10. The core of the Bank's inflation indices are the GDP deflator expressed in U.S. dollars and the price index for manufactured exports. The former may be said to be of particular relevance in judging interest rate

conditions on the international capital market, while the latter is of importance in assessing the Bank's future lending needs.

GDP Deflator

11. The details of the historical series on GDP deflators are set out in Table III.1.

Table III.1: GDP DEFLATORS IN OECD NORTH: 1955-77
(Percent per annum)

	<u>1956-58</u>	<u>1959-65</u>	<u>1966-69</u>	<u>1970-75</u>	<u>1976-77</u>
In U.S. dollars:					
North America	3.2	1.6	4.0	6.7	5.6
Japan-Oceania	2.4	3.7	4.2	12.8	9.0
Western Europe	<u>2.8</u>	<u>2.9</u>	<u>2.5</u>	<u>13.0</u>	<u>4.0</u>
Major	<u>2.8</u>	<u>2.7</u>	<u>2.2</u>	<u>12.5</u>	<u>2.7</u>
Other	2.6	3.7	3.4	14.3	7.5
TOTAL	<u>3.0</u>	<u>2.2</u>	<u>3.4</u>	<u>10.3</u>	<u>5.4</u>
In national currency:					
North America	3.2	1.7	4.0	6.6	5.8
Japan-Oceania	2.3	3.9	4.4	9.4	7.3
Western Europe	<u>4.6</u>	<u>3.4</u>	<u>3.8</u>	<u>8.7</u>	<u>9.2</u>
Major	<u>4.8</u>	<u>3.4</u>	<u>3.5</u>	<u>8.8</u>	<u>9.6</u>
Other	3.6	3.6	4.4	8.4	8.1
TOTAL	<u>3.5</u>	<u>2.4</u>	<u>3.9</u>	<u>7.9</u>	<u>7.6</u>

Source: Annex A.

12. Paralleling this overview of inflation, an overview of real economic growth is presented in Table III.2.

Table III.2: REAL GROWTH IN OECD NORTH: 1955-77
(Percent per annum)

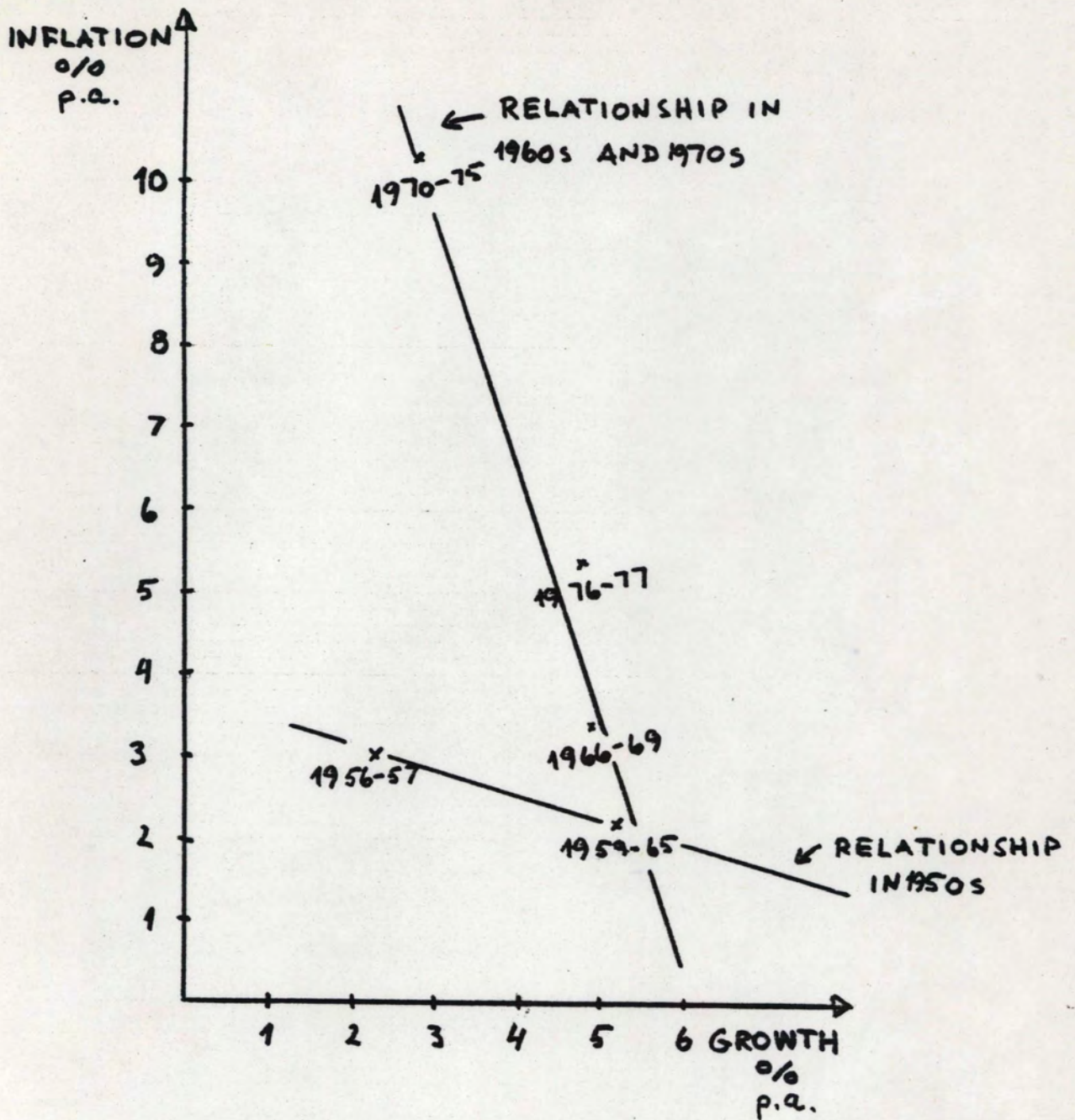
	<u>1956-58</u>	<u>1959-65</u>	<u>1966-69</u>	<u>1970-75</u>	<u>1976-77</u>
North America	1.0	4.6	4.3	2.1	5.5
Japan-Oceania	6.2	9.0	10.3	5.8	5.6
Western Europe	<u>3.6</u>	<u>5.2</u>	<u>4.4</u>	<u>3.0</u>	<u>3.6</u>
Major	4.0	5.2	4.4	2.8	3.8
Other	2.4	5.2	4.4	3.3	3.0
TOTAL	<u>2.3</u>	<u>5.2</u>	<u>4.9</u>	<u>2.8</u>	<u>4.8</u>

Source: Annex A.

13. Comparing the above inflation and growth tables suggests a rather dramatic change in the relationship between the two variables. It thus appears that since about 1960 reductions in growth rates are associated with much larger increases in inflation rates than in the 1950's. This relationship is shown in the graph below. Neither its slope nor its shift are very well understood, and this is an important area for further empirical analysis that will be undertaken by the International Economy Division. As yet, however, there is no convincing evidence for revising the projections presented in Table I.1. But while our inflation forecasts for the near term seem to hold, recently published data for major OECD countries suggest that our low growth projections for 1978-80 may be more realistic than the medium, base-case projections used in "Prospects." 1/

1/ Prospects for Developing Countries, 1978-1985, November 1977, p.16

INFLATION - GROWTH RELATIONSHIP 1956 - 1977



SOURCE : TABLE II.1

We have therefore adopted the following "guidelines" being used in our present global analysis for the World Development Report. (Table III.3)

Table III.3: OECD NORTH REAL GROWTH AND INFLATION: 1978-90

(Percent per annum)

	<u>Real Growth</u>	<u>Inflation</u>	
		<u>GDP Deflator</u>	<u>Trade Deflator</u>
1978-80	4.0	7.5	5.5
1981-85	4.2	7.0	5.0
1986-90	4.2	6.0	4.0

International Trade Deflators

14. We noted a year ago that:

Until the late 1960's, export prices rose significantly less rapidly than domestic prices. In the early 1970's, both export and domestic prices rose at about the same rate, but since 1973 export prices have risen faster than domestic prices. ^{1/}

Data recently published by the U.N. will permit major improvements in the analysis of this relationship.^{2/} We have now been able to develop export unit-value series for all developed countries covering more disaggregated groups of commodities than previously, including chemicals (SITC 5), machinery and equipment (SITC 7) and other manufactures (SITC 6 and 8), and weighted by these countries' trade with developing countries rather than their total trade. Table III.4 compares the "old" series with the "new" ones.

^{1/} SecM 76-803, para. 7.

^{2/} U.N., Monthly Bulletin of Statistics, Special Table F, "Exports of Developed and Developing Areas: In, Within and Between the Areas".

Table III.h: COMPARISON OF RATES OF CHANGE IN INDICES
OF U.S. DOLLAR DEFLATORS AND "OLD" AND "NEW"
EXPORT UNIT-VALUES: 1956-1975

(Percent per annum)

	US Dollar GDP Deflator	Export Unit-Values			
		SITC 7		SITC 5-8	
		Old	New	Old	New
1956-60	2.4	0.1	3.1	1.0	1.8
1961-65	2.4	0.9	1.4	0.5	0.9
1966-70	4.0	2.3	1.7	2.4	1.2
1971-75	11.1	12.4	15.0	12.6	15.1
1971	7.2	7.8	13.0	5.2	7.7
1972	9.7	10.0	12.4	8.0	10.1
1973	14.3	15.2	16.5	17.4	19.8
1974	12.1	13.9	11.5	20.4	23.4
1975	12.3	15.4	21.8	12.6	15.5

15. The new data broadly confirm the description in last year's statement, but there are certain important differences. In the first ten years, the discrepancy between the "new" series and GDP deflators is narrowed compared to the "old" series; indeed in 1956-60, SITC 7 prices rose faster than GDP deflators. The discrepancy widens in 1966-70; but in 1971-75 the reversal is not only sharpened but manufactured export prices rise faster than GDP deflators in every year, rather than commencing in 1973. Particularly noteworthy is the fact that the prices of these exports to developing countries tended quite consistently to rise faster than did the prices of the same export categories to all countries. This discrepancy cannot at present be fully explained. It appears to be due, in part at least, to a different commodity composition of exports to developing countries than of total exports. Thus the prices of capital equipment for such sectors as petrochemicals,

fertilizers and mineral development, which weigh heavily in exports to developing countries, have risen rapidly.

16. As indicated above in paragraph 3, the relationship between export unit-values and GDP deflators is quite complicated. Depending on the particular circumstances export prices may rise more or less rapidly than GDP deflators. This was the background for our agnostic position last year that a parallel movement should be projected for the two series. The situation this year, however, appears to be sufficiently clear to warrant a projection of export prices on the "old" definition rising somewhat more slowly than GDP deflators. Our tentative estimate is that the difference in these inflation rates will be about 2 percentage points. With further staff work, scheduled in the coming months, we intend to improve our understanding of this relationship and in particular the one between "new" export prices and GDP deflators.

ANNEX A: Historical Real Growth, GDP Deflator and Exchange-
Rate Data

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1956-74 (percent)
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^{1/} All data are reproduced from memos of the International Economy
Division of January, February, and August 1977.

A.1: HISTORICAL RATES OF REAL GDP GROWTH IN OECD NORTH 1956-74

(percent per annum)

	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974
<u>North America</u>	2.3	1.5	-0.7	5.8	2.5	2.0	6.5	4.0	5.5	6.3	6.7	2.8	5.0	2.8	0.7	3.4	6.1	5.7	-1.5
United States	1.8	1.5	-0.8	6.1	2.4	1.9	6.5	3.9	5.5	6.3	6.6	2.8	5.0	2.6	0.5	3.2	6.1	5.6	-1.9
Canada	8.7	1.2	1.3	3.3	2.4	3.0	6.8	5.6	6.3	6.7	7.1	3.4	5.6	5.2	2.7	5.9	5.9	6.9	2.8
<u>Japan-Oceania</u>	6.4	6.4	5.9	8.2	11.1	10.8	6.7	9.4	11.8	5.2	8.3	11.4	11.7	10.0	9.8	6.9	7.9	9.3	-0.6
Japan	8.0	8.0	5.4	9.2	14.1	14.5	7.1	10.5	13.4	5.1	9.8	12.9	13.4	10.8	10.9	7.3	8.9	9.8	-0.9
Australia	2.0	2.2	7.5	5.3	3.3	-0.2	6.2	6.2	6.4	5.3	2.3	6.8	5.6	6.9	5.2	5.3	2.9	6.5	1.2
New Zealand	5.1	5.9	4.1	4.6	8.1	3.2	3.1	6.2	6.2	5.9	3.9	-0.9	2.1	5.0	3.7	2.5	4.4	6.4	2.2
<u>Western Europe</u>	4.4	4.2	2.2	5.1	6.7	5.4	4.2	4.3	6.0	4.4	3.3	3.1	5.2	5.9	5.1	3.3	3.9	5.3	2.3
<u>Major Countries</u>	4.7	4.6	2.7	5.1	6.9	5.4	4.1	4.3	5.8	4.4	3.4	2.9	5.5	5.7	4.9	3.2	3.8	5.5	2.0
France	5.0	6.0	2.6	2.9	7.1	5.7	6.4	5.4	6.4	5.9	4.0	4.7	4.7	6.9	5.9	5.4	5.7	5.6	3.9
Germany	6.9	5.6	3.2	7.0	8.8	5.7	4.1	3.4	6.8	5.6	2.9	-0.2	7.1	8.1	5.9	2.9	3.4	5.1	0.5
Italy	4.7	5.4	4.9	6.6	6.3	8.0	6.2	5.5	2.7	3.2	5.7	7.1	6.2	5.7	5.0	1.6	3.1	6.3	3.4
U.K.	2.0	2.1	0.9	3.8	4.8	3.3	0.9	3.9	5.9	2.2	1.9	2.5	3.4	1.1	2.1	2.5	2.5	5.5	0.8
<u>Others</u>	3.5	3.1	0.7	5.1	6.0	5.5	4.6	4.0	6.9	4.3	2.9	3.7	4.5	6.4	5.7	3.4	4.5	4.4	3.2
Austria	5.1	5.9	4.1	4.6	8.1	5.6	2.7	4.1	6.2	3.4	5.0	2.3	4.5	5.8	7.8	5.3	6.4	5.8	4.4
Belgium	2.9	2.5	-0.6	2.5	5.5	5.0	5.2	4.4	7.0	3.7	3.0	3.9	4.3	6.6	6.4	4.1	5.7	6.3	3.8
Denmark	2.2	5.0	2.7	6.9	6.2	6.4	5.6	0.7	9.2	4.5	2.9	4.2	3.8	8.6	2.7	3.4	4.6	3.3	0.5
Finland	1.9	1.5	-0.1	7.4	9.9	8.0	4.3	2.5	6.5	5.1	2.4	2.6	2.3	10.5	8.2	2.4	7.0	6.5	4.2
Ireland	-1.3	0.6	-2.0	4.1	5.4	4.7	3.6	4.9	4.1	2.1	1.3	5.2	7.4	6.8	2.9	3.5	4.7	5.4	0.4
Netherlands	3.7	2.8	-0.3	4.9	8.4	2.8	4.4	3.3	8.6	5.3	2.8	5.4	6.7	6.8	6.8	4.4	3.9	4.3	3.3
Norway	5.1	0.8	1.2	3.4	3.6	6.5	4.7	5.4	5.0	5.7	4.5	5.6	4.0	5.0	3.5	4.6	4.9	4.2	3.7
Sweden	3.1	3.1	2.6	5.5	3.5	5.6	4.3	5.3	6.8	4.2	2.4	3.4	4.0	5.1	4.9	0.7	2.6	3.5	4.2
Switzerland	6.0	2.9	-1.8	7.2	5.8	7.3	5.0	4.7	5.0	3.9	2.4	1.6	3.6	5.5	5.6	4.0	3.7	2.6	1.8
TOTAL OECD North	3.3	2.7	0.8	5.7	4.6	3.9	5.7	4.5	6.2	5.5	5.6	3.7	5.8	4.6	3.2	3.8	5.5	6.0	-0.1

Source: OECD.

A.2: RATES OF CHANGE IN US DOLLAR GDP DEFLATORS OF OECD NORTH: 1956-74 ^{a/}
(percent)

	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974
<u>North America</u>	3.6	4.0	2.2	2.0	1.7	0.6	1.5	1.6	1.5	2.3	3.5	2.9	4.5	5.0	5.5	5.2	4.3	6.0	10.3
United States	3.5	3.8	2.3	1.8	1.8	0.9	1.9	1.7	1.4	2.3	3.4	2.9	4.6	5.1	5.3	5.1	4.1	5.9	9.7
Canada	5.4	5.7	0.7	3.9	0.4	-3.7	-4.0	0.7	2.8	3.1	4.5	3.7	3.4	4.3	8.0	6.6	6.8	6.6	16.9
<u>Japan-Oceania</u>	4.1	3.9	-0.8	2.7	5.6	3.3	2.9	3.8	3.5	4.5	4.2	4.0	3.7	4.9	6.8	7.7	18.0	27.6	13.0
Japan	4.7	5.6	-1.7	2.7	7.1	5.5	4.2	4.3	4.3	5.3	4.8	4.7	4.9	4.9	7.0	7.2	18.7	26.3	12.3
Australia	5.0	2.8	0.4	2.4	4.4	0.9	1.2	3.4	2.4	3.1	3.1	2.8	3.3	4.5	5.5	9.0	14.4	36.0	18.1
New Zealand	3.3	0.5	2.3	2.5	2.8	0.1	4.9	2.6	3.0	1.9	0.3	1.7	-14.2	4.7	9.6	15.8	16.7	26.8	6.0
<u>Western Europe</u>	4.8	2.4	1.0	-5.0	6.1	4.1	4.2	3.7	4.5	3.0	3.5	2.4	-0.1	4.0	6.8	10.0	14.2	19.5	9.0
<u>Major</u>	4.7	2.3	1.2	-6.6	7.0	4.2	4.4	4.4	3.5	2.5	3.2	2.0	-0.5	4.0	7.0	10.1	13.8	18.2	7.7
France	5.2	0.7	-3.3	-7.8	3.4	3.4	4.8	6.3	4.1	-2.6	2.7	2.7	4.2	1.9	-0.8	6.0	16.1	21.5	2.9
Germany	3.2	3.1	4.0	-19.5	29.6	8.2	4.6	3.4	3.0	3.2	3.2	1.6	1.5	5.3	15.2	13.0	15.6	26.4	10.1
Italy	4.1	2.0	2.4	0.3	2.2	2.8	5.7	8.6	5.8	3.6	2.4	2.9	1.6	3.7	6.7	8.1	12.3	10.1	4.7
United Kingdom	6.5	3.6	4.1	1.2	1.2	3.2	4.0	1.8	2.0	6.4	4.4	1.3	-9.0	5.3	7.6	12.2	9.1	5.4	7.8
<u>Other</u>	4.8	2.8	0.2	1.1	2.7	3.8	3.7	1.3	8.3	5.3	4.5	3.8	1.4	4.0	6.0	9.6	15.5	23.6	12.7
Austria	4.3	4.5	0.3	2.3	3.0	5.0	4.1	3.7	3.0	5.4	2.9	3.4	2.2	3.5	3.8	9.2	15.6	28.8	16.4
Belgium	4.2	3.0	2.0	0.6	1.0	1.1	1.4	3.0	4.9	5.1	4.0	3.2	2.2	3.7	5.6	7.6	16.4	21.5	12.8
Denmark	5.0	1.3	2.0	3.8	1.7	4.3	6.8	5.8	4.5	7.5	2.5	4.4	2.9	4.9	7.9	6.9	14.5	27.1	10.4
Finland	9.0	-4.7	-12.4	1.4	2.2	3.1	2.6	5.6	7.7	4.3	5.1	-0.9	-9.7	3.4	3.1	6.9	8.7	23.5	21.3
Ireland	3.2	3.1	6.3	2.2	0.4	2.4	4.8	2.3	8.7	4.6	4.2	2.0	-8.3	7.8	9.3	12.2	15.6	11.7	2.3
Netherlands	3.2	5.8	2.9	2.1	2.8	6.3	4.0	5.1	8.2	6.4	5.2	4.6	3.5	5.9	5.6	12.1	18.8	24.0	13.3
Norway	7.4	5.4	-1.6	2.9	2.4	2.3	3.0	2.2	5.5	4.9	4.4	4.1	3.5	3.3	11.6	7.4	11.7	24.6	14.3
Sweden	5.9	4.2	2.3	0.8	5.2	4.5	3.7	-11.6	22.0	5.8	5.7	5.4	2.0	3.2	6.0	8.5	13.5	16.3	7.0
Switzerland	1.4	2.4	4.0	-0.6	3.7	4.3	5.5	4.6	5.0	3.6	4.8	4.7	4.2	2.9	4.9	14.5	17.4	29.8	13.0
TOTAL	4.0	3.4	1.6	0.3	3.3	1.7	2.4	2.5	2.7	2.8	3.6	2.8	2.8	4.7	6.0	7.1	9.8	14.3	12.1

NOTE: All averages are weighted averages where the weights are shares in nominal GDP in the preceding year; the relevant GDP figures appear in Table II.A.

^{a/} No distinction was made between GDP and GNP in this table.

^e Preliminary estimate.

A.3: RATES OF CHANGE OF REAL GROWTH AND US DOLLAR GNP DEFLATORS: 1975-77

(Percent per annum)

	1974 GNP (billion \$US)	Real GDP Growth			\$US GDP Deflator		
		1975	1976	1977	1975	1976	1977
<u>North America</u>	<u>1,543.30</u>	<u>-1.53</u>	<u>5.98</u>	<u>5.02</u>	<u>9.02</u>	<u>5.83</u>	<u>5.32</u>
U.S.	1,398.00	-1.8	6.1	5.2	9.3	5.1	5.8
Canada	145.30	1.1	4.9	3.3	6.4	12.9	1.0
<u>Japan-Oceania</u>	<u>547.05</u>	<u>2.14</u>	<u>5.74</u>	<u>5.41</u>	<u>5.29</u>	<u>6.31</u>	<u>11.71</u>
Japan	455.30	2.4	6.3	6.0	5.5	6.5	13.5
Australia	78.39	1.5	3.6	2.7	5.7	6.3	0.5
New Zealand	13.36	-3.0	-1.1	0	-5.1	-1.9	11.0
<u>Total Europe</u>	<u>1,330.88</u>	<u>-1.94</u>	<u>4.26</u>	<u>2.94</u>	<u>19.13</u>	<u>-0.77</u>	<u>8.85</u>
<u>Major</u>	<u>989.43</u>	<u>-2.09</u>	<u>4.69</u>	<u>2.92</u>	<u>19.03</u>	<u>-2.54</u>	<u>8.18</u>
France	266.10	0.1	5.2	3.2	26.7	-1.7	4.5
Germany	384.53	-3.2	5.6	4.2	13.9	0.7	10.0
Italy	149.81	-3.5	5.6	1.5	16.8	-7.6	11.7
U.K.	188.99	-1.8	1.4	1.0	20.0	-6.1	7.5
<u>Other</u>	<u>341.45</u>	<u>-1.50</u>	<u>3.02</u>	<u>2.99</u>	<u>19.43</u>	<u>4.44</u>	<u>10.65</u>
Austria	33.00	-2.0	5.2	4.0	16.8	2.7	12.5
Belgium	53.42	-1.9	2.3	2.8	19.0	3.8	14.5
Denmark	30.40	-1.1	5.5	1.9	18.7	3.5	10.2
Finland	22.03	0.5	0.2	3.0	18.8	7.9	9.0
Ireland	6.73	-0.5	3.0	4.0	16.4	-2.5	8.9
Netherlands	69.18	-1.1	4.2	4.0	18.0	4.3	13.5
Norway	23.30	3.5	6.0	7.0	16.6	4.1	11.0
Sweden	56.10	0.6	1.5	1.0	22.6	5.8	11.6
Switzerland	47.29	-7.6	0.5	1.7	23.0	5.0	0.5
TOTAL OECD NORTH	3,421.23	-1.10	5.28	4.29	12.30	3.19	7.69

NOTE: 1975 figures are revised; those for 1976 are preliminary; those for 1977 are forecasts based partly on very preliminary data.

A.4: INDICES OF US DOLLAR GDP DEFLATORS OF OECD NORTH: 1955-74 ^{a/}

(1970=100)

	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974
North America	66.0	68.4	71.1	72.6	74.0	75.3	75.7	76.8	78.1	79.2	81.1	83.9	86.4	90.3	94.8	100.0	105.2	109.8	116.3	128.3
United States	65.8	68.1	70.7	72.3	73.6	74.9	75.6	77.0	78.3	79.4	81.2	84.0	86.4	90.4	95.0	100.0	105.1	109.4	115.9	127.1
Canada	68.7	72.4	76.5	77.0	80.0	80.3	77.3	74.2	74.7	76.8	79.2	82.8	85.9	88.8	92.6	100.0	106.6	113.8	121.3	141.8
Japan-Oceania	57.2	59.6	61.9	61.4	63.0	66.6	68.8	70.8	73.4	76.0	79.4	82.8	86.1	89.3	93.6	100.0	107.7	127.1	162.1	183.2
Japan	51.3	53.7	56.7	55.9	57.4	61.5	64.9	67.6	70.5	73.5	77.4	81.1	84.9	89.1	93.5	100.0	107.2	127.2	160.7	180.5
Australia	64.0	67.2	69.1	69.4	71.1	74.2	74.9	75.8	78.4	80.3	82.8	85.4	87.8	90.7	94.8	100.0	109.0	124.7	169.6	200.3
New Zealand	78.6	81.2	81.6	83.5	85.6	88.0	88.1	92.4	94.8	97.6	99.5	99.8	101.5	87.1	91.2	100.0	115.8	135.1	171.3	181.6
Western Europe	64.2	67.3	68.9	69.6	66.1	70.1	73.0	76.1	78.9	82.5	85.0	88.0	90.1	90.0	93.7	100.0	110.0	125.6	150.1	163.6
Major	65.7	68.8	70.4	71.3	66.6	71.3	74.2	77.5	80.8	83.1	85.8	88.5	90.3	89.8	93.4	100.0	110.1	125.3	148.1	159.5
France	79.0	83.1	83.7	80.9	74.6	77.1	79.7	83.5	88.8	92.4	90.0	92.4	94.9	98.9	100.8	100.0	106.0	123.1	149.6	153.9
Germany	53.9	55.6	57.3	59.6	48.0	62.2	67.3	70.4	72.8	75.0	77.4	79.9	81.2	82.4	86.8	100.0	113.0	130.6	165.1	181.9
Italy	58.6	61.0	62.2	63.7	63.9	65.3	67.1	70.9	77.0	81.5	84.5	86.5	89.0	90.4	93.7	100.0	108.1	121.4	133.7	140.0
United Kingdom	65.7	70.0	72.5	75.5	76.4	77.3	79.8	83.0	84.5	86.2	91.7	95.7	96.9	88.2	92.9	100.0	112.2	122.4	129.0	139.0
Other	59.1	62.0	63.7	63.8	64.5	66.2	68.8	71.3	72.2	78.3	82.4	86.1	89.4	90.7	94.4	100.0	109.6	126.6	156.5	176.4
Austria	60.3	62.9	65.7	65.9	67.4	69.4	72.9	75.9	78.7	81.1	85.5	88.0	91.0	93.0	96.3	100.0	109.2	126.2	162.5	188.6
Belgium	64.3	67.0	69.0	70.4	70.8	71.5	72.3	73.3	75.5	79.2	83.2	86.5	89.3	91.3	94.7	100.0	107.6	125.3	152.2	171.7
Denmark	53.2	55.7	56.4	57.5	59.7	60.7	63.3	67.6	71.5	74.7	80.3	82.3	85.9	88.4	92.7	100.0	106.9	122.4	155.6	171.8
Finland	84.3	91.9	87.6	76.7	77.8	79.5	82.0	84.1	88.8	95.6	99.7	104.8	103.9	93.8	97.0	100.0	106.9	116.2	143.5	174.1
Ireland	60.2	62.1	64.0	68.0	69.5	69.8	71.5	74.9	76.6	83.3	87.1	90.8	92.6	84.9	91.5	100.0	112.2	129.7	144.9	148.2
Netherlands	49.7	51.3	54.3	55.9	57.1	58.7	62.4	64.9	68.2	73.8	78.5	82.6	86.4	89.4	94.7	100.0	112.1	133.2	165.2	187.1
Norway	55.1	59.2	62.4	61.4	63.2	64.7	66.2	68.2	69.7	73.5	77.1	80.5	83.8	86.7	89.6	100.0	107.4	120.0	149.5	170.9
Sweden	54.4	57.6	60.0	61.4	61.9	65.1	68.0	70.5	62.3	76.0	80.4	85.0	89.6	91.4	94.3	100.0	108.5	123.2	143.3	153.4
Switzerland	58.2	59.0	60.4	62.8	62.4	64.7	67.5	71.2	74.5	78.2	81.0	84.9	88.9	92.6	95.3	100.0	114.5	134.4	174.4	197.6
TOTAL	64.2	67.5	69.2	71.0	70.8	73.1	74.3	76.1	78.0	80.1	82.3	85.2	87.7	90.1	94.3	100.0	107.2	117.6	134.4	150.6

Sources: Tables A.5 and A.6.

^{a/} No distinction was made between GDP and GNP in this table.

^e Preliminary estimate.

A.5: INDICES OF NATIONAL CURRENCY GDP DEFLATORS OF OECD NORTH: 1955-76 ^{a/}
(1970 = 100)

	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
North America	65.8	68.1	70.7	72.3	73.5	74.9	75.6	76.9	78.2	79.4	81.2	84.1	86.6	90.4	95.0	100.0	104.9	109.2	115.9	127.6		
United States	65.8	68.1	70.7	72.3	73.6	74.9	75.6	77.0	78.3	79.4	81.2	84.0	86.4	90.4	95.0	100.0	105.1	109.4	115.9	127.1	139.7	147.4
Canada	65.7	68.2	70.2	71.6	73.5	74.6	75.0	76.0	77.2	79.3	81.8	85.4	88.7	91.6	95.5	100.0	103.1	108.0	116.2	132.8	147.0	161.0
Japan-Oceania	56.4	58.6	61.0	60.4	62.0	65.1	68.0	70.1	73.0	75.7	79.1	82.6	86.1	89.7	93.8	100.0	105.0	110.9	124.0	148.0	161.1	173.7
Japan	51.7	54.0	57.0	56.2	57.7	61.2	65.4	68.1	71.2	74.3	78.1	82.0	85.8	89.6	93.6	100.0	104.4	109.4	122.1	146.9	157.8	167.9
Australia	64.1	67.2	69.1	69.0	70.8	73.9	74.7	75.5	78.3	80.4	82.8	85.5	87.9	90.8	95.0	100.0	106.9	116.5	133.3	155.4	180.1	205.0
New Zealand	63.4	65.4	65.8	66.9	68.6	70.6	70.8	74.1	76.2	78.7	80.1	80.4	84.0	87.2	91.4	100.0	113.3	126.0	140.6	144.8	160.1	189.5
Western Europe	56.1	58.8	61.1	64.2	65.6	67.1	69.6	72.5	75.7	78.7	81.2	84.2	86.6	89.6	94.0	100.0	107.4	114.3	123.0	136.0	154.8	168.1
Major	56.2	59.0	61.3	64.7	66.3	67.8	70.4	73.5	76.8	79.6	81.7	84.5	86.5	89.2	93.8	100.0	107.5	114.2	122.5	135.5	155.3	171.2
France	50.0	52.6	55.7	62.3	66.2	68.4	70.7	74.0	78.7	81.9	79.8	82.1	84.5	88.6	94.8	100.0	105.6	112.3	120.5	133.9	151.2	165.7
Germany	62.2	64.1	66.0	68.5	69.4	71.1	74.2	77.2	79.6	81.7	84.7	87.7	88.8	90.2	93.4	100.0	107.9	114.2	121.0	129.3	139.8	144.0
Italy	58.4	60.8	62.0	63.5	63.3	64.6	66.4	70.2	76.3	81.1	84.2	86.1	88.6	89.9	93.7	100.0	106.6	112.9	124.3	145.2	170.3	200.6
United Kingdom	56.4	60.0	62.2	64.4	65.2	66.0	68.2	70.8	72.3	74.0	78.6	82.1	84.7	88.3	93.1	100.0	111.0	117.4	126.2	142.5	180.7	208.9
Other	55.8	58.2	60.7	62.1	63.0	64.6	66.7	69.0	71.7	75.7	79.7	83.5	87.1	90.7	94.5	100.0	107.0	114.8	124.6	137.3	153.4	166.7
Austria	60.4	63.0	65.9	66.1	67.7	69.8	73.2	75.9	78.6	81.0	85.4	87.9	90.9	93.0	96.3	100.0	105.2	112.8	123.0	136.3	148.3	156.9
Belgium	65.0	67.4	69.8	70.7	71.2	71.8	72.6	73.5	75.8	79.3	83.2	86.8	89.4	91.8	95.6	100.0	105.3	111.1	119.5	134.7	151.3	164.9
Denmark	49.0	51.3	51.9	52.9	54.9	55.8	58.3	62.2	65.8	68.9	74.0	75.8	80.0	88.2	92.9	100.0	105.6	113.9	125.5	139.6	156.2	170.0
Finland	46.1	50.3	54.1	58.3	59.1	60.4	62.3	63.9	67.9	73.1	76.2	80.1	84.6	93.7	96.9	100.0	106.8	114.9	130.4	155.4	181.0	204.0
Ireland	51.7	53.2	54.9	58.0	59.3	59.6	61.1	63.9	65.5	71.5	74.6	77.9	80.9	85.0	91.7	100.0	110.0	124.4	141.6	153.1	188.3	226.0
Netherlands	52.4	54.3	57.4	58.5	59.6	61.2	62.7	64.7	67.9	73.6	78.1	82.7	86.1	89.5	94.9	100.0	108.4	118.2	127.7	139.1	154.4	168.3
Norway	55.0	59.1	62.3	61.3	63.0	64.6	66.2	68.1	69.7	73.6	77.1	80.5	83.8	86.6	89.6	100.0	105.8	110.6	120.6	132.5	145.8	158.4
Sweden	54.3	57.2	59.8	61.3	61.8	64.9	67.8	70.1	72.3	75.5	80.0	85.1	89.2	91.1	94.0	100.0	105.9	113.1	120.7	131.3	150.5	167.0
Switzerland	57.9	58.7	60.1	62.5	62.6	64.8	67.6	71.4	74.7	78.4	81.3	85.6	89.3	92.7	95.4	100.0	109.3	119.1	128.1	136.6	145.6	148.1
TOTAL	62.2	64.6	67.0	68.9	70.3	71.8	73.0	74.9	77.0	78.9	81.0	84.0	86.5	90.1	94.5	100.0	105.8	111.3	119.5	134.0	149.0	160.0

Sources: OECD, Growth Triangles, 1955-1973.
 OECD, National Accounts, 1962-1973.
 OECD, Economic Outlook, No. 20, December 1976.

a/ No distinction was made between GDP and GNP in this table.

A.6: EXCHANGE-RATE INDICES OF OECD NORTH: 1955-76
(national currency/US dollar; 1970=100)

	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976
Australia ^{a/}						99.56	99.75	99.55	99.83	100.11	100.00	100.08	100.10	100.10	100.24	100.00	98.04	93.40	78.59	77.60	85.07	91.11
Austria	100.21	100.21	100.31	100.32	100.41	100.52	100.46	99.94	99.92	99.90	99.89	99.93	99.93	99.96	100.02	100.00	96.32	89.36	75.69	72.26	67.33	69.35
Belgium	101.17	100.54	101.16	100.47	100.64	100.42	100.43	100.23	100.43	100.19	99.97	100.36	100.07	100.56	100.97	100.00	97.86	88.64	78.49	78.46	74.07	77.74
Canada	95.68	94.24	91.82	92.97	91.86	92.85	97.02	102.37	103.31	103.31	103.25	103.19	103.32	103.20	103.13	100.00	96.71	94.88	95.78	93.65	97.41	94.43
Denmark	92.07	92.07	92.07	92.07	91.91	91.93	92.11	92.02	92.06	92.22	92.21	92.12	93.17	99.80	100.26	100.00	98.76	93.03	80.67	81.27	76.62	80.61
Finland	54.72	54.72	61.74	75.99	75.99	75.99	75.99	75.99	76.46	76.44	76.43	76.45	81.44	99.94	99.88	100.00	99.95	98.86	90.90	89.28	87.54	91.52
France	63.30	63.30	66.54	76.98	88.71	88.71	88.73	88.64	88.64	88.64	88.65	88.88	89.00	89.58	94.05	100.00	99.67	91.23	80.56	87.00	77.53	86.45
Germany	115.39	115.29	115.23	114.99	114.61	114.38	110.21	109.64	109.32	109.01	109.54	109.66	109.32	109.47	107.64	100.00	95.47	87.45	73.29	71.08	67.48	69.05
Ireland ^{a/}	85.84	85.70	85.77	85.27	85.30	85.33	85.49	85.33	85.56	85.81	85.69	85.78	87.34	100.10	100.23	100.00	98.05	95.92	97.76	102.48	108.31	133.30
Italy	99.66	99.66	99.66	99.61	99.03	99.00	99.03	98.99	99.11	99.57	99.64	99.57	99.51	99.40	100.02	100.00	98.60	92.99	92.96	103.70	104.10	132.71
Japan	100.74	100.47	100.47	100.47	100.51	100.49	100.84	100.75	100.93	100.07	100.93	101.17	101.12	100.67	100.06	100.00	97.43	86.00	76.00	81.39	82.87	82.80
Netherlands	105.41	105.89	105.65	104.66	104.37	104.29	100.43	99.63	99.57	99.73	99.55	100.07	99.61	100.09	100.02	100.00	96.62	88.74	77.30	74.35	69.93	73.11
New Zealand ^{a/}	80.67	80.55	80.61	80.14	80.17	80.21	80.36	80.23	80.42	80.64	80.52	80.57	82.77	100.10	100.24	100.00	97.85	93.28	82.06	79.72	92.86	111.61
Norway	99.88	99.88	99.88	99.88	99.75	99.81	99.94	99.87	100.03	100.15	100.05	100.05	100.05	99.94	99.96	100.00	98.55	92.18	80.67	77.51	73.13	76.35
Sweden	99.74	99.35	99.75	99.76	99.79	99.66	99.64	99.41	100.05	99.33	99.46	100.07	99.54	99.65	99.69	100.00	98.49	91.83	84.21	85.60	80.06	83.99
Switzerland	99.43	99.42	99.44	99.45	100.25	100.20	100.21	100.32	100.26	100.20	100.40	100.37	100.41	100.13	100.06	100.00	95.47	88.60	73.46	69.12	59.88	57.99
United Kingdom	85.84	85.70	85.77	85.27	85.30	85.34	85.50	85.33	85.56	85.80	85.69	85.78	87.39	100.10	100.24	100.00	98.05	95.93	97.80	102.49	108.31	133.28

^{a/} These indices are derived from annual figures which differ slightly from those in the country pages of IFS.

Source: IMF Data Fund; 'af' rates

Table A.7: "NEW" AND "OLD" US DOLLAR INDICES OF UNIT VALUES OF EXPORTS OF MANUFACTURES FROM DEVELOPED COUNTRIES; GLOBAL WEIGHTS_{a/}
(1970 = 100)

	Machinery SITC 7		Other Manufactures SITC 5, 6, 8		Total Manufactures SITC 5-8	
	New	Old	New	Old	New	Old
1954	70.0		87.1		79.8	
1955	70.0	84.5	88.6	80.8	80.7	82.4
1956	73.0	86.4	92.5	83.1	84.0	84.6
1957	76.0	88.2	93.3	85.8	85.6	86.9
1958	80.0	85.3	92.6	86.2	86.9	85.8
1959	80.0	83.4	90.2	85.8	85.8	84.7
1960	81.0	85.0	91.9	88.6	87.2	86.9
1961	83.0	85.9	91.7	88.4	87.8	87.2
1962	85.0	86.7	91.1	86.9	88.4	86.8
1963	85.0	87.6	90.8	86.8	88.2	87.2
1964	86.0	88.7	91.5	86.4	89.1	87.5
1965	89.0	89.5	93.4	88.3	91.4	88.9
1966	91.0	91.2	94.7	90.2	93.1	90.7
1967	92.0	91.9	93.2	90.3	92.7	91.1
1968	91.0	90.6	92.2	90.6	91.7	90.6
1969	89.0	93.7	94.0	94.3	91.6	94.0
1970	100.0	100.0	100.0	100.0	100.0	100.0
1971	112.0	107.8	101.2	103.4	106.1	105.2
1972	123.0	118.6	109.6	108.1	115.7	113.6
1973	142.0	136.6	134.0	130.0	137.7	133.4
1974	159.0	155.6	172.2	165.4	166.0	160.6
1975	188.0	179.6	186.8	182.0	187.4	180.8

a/ International Price Index (IPI). The "old" series are based on fixed 1972 shares of each of the major industrial countries (U.S., Japan, France, West Germany, Italy, U.K.) in their combined exports; the series are based on moving shares in 1970 prices for all developed countries.

Source: "Old" series: EPD/IE, "Price" memo of January 25, 1977.
"New" series: U.N., Monthly Bulletin of Statistics, 1966-71 and June 1977 issues.

Table A.8: "NEW" US DOLLAR INDICES OF UNIT VALUES OF EXPORTS OF
MANUFACTURES FROM DEVELOPED COUNTRIES: BILATERAL WEIGHTS^{a/}
(1970 = 100)

	Chemicals SITC 5	Machinery SITC 7	Other Manuf. SITC 6 & 8	Total Manuf. SITC 5-8
1954	123	73	83	81.6
1955	120	74	84	82.4
1956	123	76	88	84.9
1957	124	80	89	87.4
1958	119	83	88	88.2
1959	114	84	87	88.2
1960	113	86	89	89.9
1961	110	87	89	90.3
1962	106	88	88	90.0
1963	104	88	89	90.2
1964	104	89	91	91.6
1965	107	92	93	94.2
1966	105	93	94	94.9
1967	102	97	93	96.2
1968	94	89	89	89.7
1969	97	87	93	90.3
1970	100	100	100	100.0
1971	103	113	102	107.7
1972	107	127	111	118.6
1973	140	148	134	142.0
1974	215	165	177	175.3
1975	221	201	198	202.3

^{a/} Bilateral weights: shares in exports from developed to developing countries.

Source: U.N., Monthly Bulletin of Statistics, 1966-71 and June 1977.

MFN/EPDIE
10/18/77

711/4/30

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara
FROM: I.P.M. Cargill *Shaw*
SUBJECT: Future Role of the Bank

DATE: November 15, 1977

Messrs. Gabriel, Wood and I have seen most of the Executive Directors either together or separately. There are some patterns in their thinking now emerging.

11/16
Mr. Fried came to see me early last week and the three of us saw him together last Friday. In addition, he has talked to several other Executive Directors and to Mr. Damry. When he saw me, he said that he would like to have the discussion on November 17 kept to 'procedural' matters. When I questioned him about the meaning of this he was very vague and so I suggested that after we had talked to other Executive Directors we should meet with him. On Friday evening he was a bit clearer. He said he had had no instructions from the Treasury and would certainly have none for some time. The Treasury was completely preoccupied with problems that seemed more pressing, e.g., the supplemental appropriation for IDA 4. However, he understood that some position had to be taken by the end of March and felt that by then the Administration's position would be clarified. However, in the meantime, he and his colleagues in the Treasury were concerned lest the word should get out that a major capital increase for the Bank was about to be agreed without any consultation with Congressional leaders, and for this reason he would prefer to have the discussion about the amount taken up later in the schedule of talks but had no objection to discussing other issues, both those that would be relevant to the size of the capital increase and others that were tangential to this issue. Yesterday he spoke to Mr. Damry and to some Executive Directors and is reported to have said again that he would prefer to keep the discussions next Thursday confined to procedural matters. I have the impression that he is quite confused.

In addition, it could be said that the Part II countries, Belgium, the Netherlands, and the Scandinavian countries support our proposals. Other countries have reservations on several points.

A consensus seems to be emerging among the developed countries in favor of a figure of \$30 billion for the increase. Mr. Fried says that this is the outer limit that could be supported by the United States. Mr. Drake believes anything larger than this would raise difficulties in Canada. The United Kingdom says that the figure of \$40 billion was deliberately taken out of Mr. Healey's Annual Meeting speech and vaguer words were substituted for it; they believe they could support a figure above \$30 billion but not as high as \$40 billion. The Germans are already planning on \$30 billion but Mr. Janssen indicated that there is some, if not great, flexibility in this figure. Mr. Janssen emphasized that a capital increase

of this size had the full support at ministerial level of all the ministries concerned. Mr. Murayama has neither instructions nor views on this point. He said that Japan was doing what it normally did, namely to wait to see what Germany and the United States would do. Mr. Wahl sees the capital increase as but one element in a broader negotiation between the North and South. He thinks France will be reluctant to play this "trump card" before the other negotiations (e.g., on the Common Fund) reach the decision stage. Mr. Johnston said that he could take no position on account of the elections in Australia next month; but in general he said the attitude towards further growth in Bank operations has gained increasing support over the last year in Canberra. Subject to certain reservations, which I mention below, he expected Australia to fall in with the consensus that emerged.

With regard to the rate of growth, the range of 10-12% per annum in nominal terms seems to be where most people would reach agreement. However, Mr. Janssen, Mr. Drake and others are much exercised about the rate of inflation that the Bank has forecast on the grounds that it is politically unacceptable. Fair support seems to be emerging for a suggestion that we not discuss projections of the rate of inflation not only on political grounds but because forecasts of this kind are extremely unreliable and might result in long basically irrelevant discussions about the methodology used. In other words, it is suggested that if a consensus can be reached for, say, 11% growth rate in nominal terms, it should suffice simply to note that this will permit substantial growth in real terms.

With regard to the order in which the various topics should be discussed, there seems to be support, albeit for different reasons, for Mr. Fried's wish to leave the amount of the capital increase until the end. Mr. Murayama says his authorities are very concerned lest word should get out that agreement was being reached on a figure such as \$30 billion at a time when a budget is about to be presented for a special increase and he would therefore prefer on this point not to take a position until the end of February or the beginning of March. Indeed, he would prefer not to have any discussions about it until then.

A number of Executive Directors wish to have discussions about the implications of continuing IBRD growth at a rate of 10-12% per annum. As Mr. Johnston put it, such discussion will be useful in providing officials with material they can use in selling the capital increase to parliaments. While he has no doubt that his government will support a major capital increase, he thinks it important to satisfy officials in the Treasury on "how the money will be used" as a means of obtaining full support for a large capital increase. He has asked Canberra to give a list of "businessman's questions" concerning the future operations of the Bank, but he has not yet received a reply.

Other Executive Directors (Ryrie, Drake, Murayama, Fried) echoed this theme. The issues they suggested for discussion fall into three categories. First, on the lending side they wish to discuss what might be called the absorptive capacity question. The issue is not whether there are

November 15, 1977

sufficient good projects to support real growth of 5%, but rather whether growth at this rate is compatible with the emphasis we are placing on new style projects. No doubt the Wall Street Journal article on Indonesia has helped to crystalize this issue. The second and closely related question concerns the size and administrative character of the Bank. This was raised by Fried, Ryrle, Murayama and Johnston. The third issue is the capacity of the financial markets to support the IBRD borrowings needed to fund a commitment program growing at 12% per annum. In Janssen's mind, as well as others, this issue is closely related to the Bank's financial position and especially its reserve adequacy. ✓
✓

While each of these issues could be considered "tangential" to the political decision which will eventually be made about the size of the capital increase, I believe that on the 17th we will have to bend in the direction of accepting a limited discussion of them at subsequent meetings.

cc: Mr. Knapp
Mr. Damry

IMPC/DJW:aj

7/11/4/29

OFFICE MEMORANDUM

CONFIDENTIAL

TO: Mr. McNamara

FROM: P. N. Damry *P. N. Damry* 11/15

SUBJECT: Capital Increase Discussions

DATE: November 15, 1977

DECLASSIFIED

NOV 30 2012

WBG ARCHIVES

11/16

1. Mr. Cargill will have given you a fuller account of talks with Directors; but I should bring to your notice that Mr. Fried has twice in the last week taken it upon himself to tell me that he thought the meeting on the 17th would deal with what he calls procedural aspects, i.e. "discuss as to what the Directors should discuss". He made the point strongly that a great deal of time would be required simply to identify the determinants regulating the size and character of the increase. I told him that, while no doubt these determinants would have to be identified—and we have indeed pointed out two for discussions on the 17th,—I understood that it was the desire of the Executive Directors generally to commence substantive talks in a purposeful and a business-like fashion on the 17th. Mr. Fried accepted this statement with reserve. Mr. Fried would almost certainly start off by asking that we discuss questions like "Is the Bank too big?, are we too relaxed in our lending procedures?"—in other words, the sort of questions we hoped were well behind us. If he does so start with these, there will be a great deal of impatience on the part of LDCs, among whom, Dr. Sen for one would argue "let us start with a figure of \$40 billion and if we find that the inflation rate is smaller, that will last us for many more years than anticipated; but if inflation is higher we may have to come back for a further increase sooner than we expected". Dr. Sen's \$40 billion is based simply on the doubling of the capital increase recommended by many Governors. I do not think that the more cautious Part I Directors like Messrs. Drake and Janssen or the French would go along with such an argument.

2. Mr. Fried seems meanwhile to have been talking to Messrs. Sen, El-Naggar and others on the same lines and I have advised that the LDCs should not merely confine themselves to G-9 meetings but should try to arrange a meeting of minds with Messrs. Janssen, Drake, Magnussen and Looijen.

3. Messrs. El-Naggar and Sen as late as this afternoon told me they had a clear impression from Mr. Fried that he wanted to go no further on the 17th than procedure (in the loose sense described above) and were perturbed with what they saw as delaying tactics. They feel, about Mr. Drake also, that while he will be ready to take a constructive attitude towards discussions leading to a range of figures as the upper limit of the capital increase, before even bringing such a figure to a semi-final stage Mr. Drake would want a review of the other (including "tangential") issues, particularly administrative implications.

Mr. McNamara

November 15, 1977

4. The question then is how one starts on the 17th: can we assume a desired rate of real growth in lending without first going into the nominal rate and if that comes to 14 per cent, can we avoid a seemingly premature discussion of our administrative and physical capacity to handle that extent of growth? Another question which could be asked at this point could be regarding the absorptive capacity of borrowers. If so, Mr. Sen would argue that since we are talking only of commitments and not actual withdrawals, absorptive capacity is not relevant; but this argument can be carried too far because commitments must become disbursements within a reasonable period.

5. My advice, *subject to paragraph 6 below,* would be that you should commence with the details of a case for a real rate of growth of 7 per cent in lending. That will focus attention on a point of departure which would give the succeeding talks some direction; otherwise, with Mr. Murayama only too anxious to procrastinate and Messrs. Drake and Magnussen only too keen to start parallel talks on "tangential" issues, we may, if the meeting is simply thrown open to the Executive Directors, without an initial and somewhat detailed "presentation", get a somewhat discursive and unpurposeful discussion over a wide range of subjects, with no real step achieved towards establishing a figure for lending to serve as a starting point for the next round.

6. One other way, which I favour, could be to start with a case for a 14 per cent growth in nominal terms and to say nothing at this stage, about growth in real terms. That gets over the difficult discussion of inflation in which that we might otherwise get bogged down. I have a feeling Mr. Janssen would be relieved if we confined our initial talks to "nominal" figures. He would be strongly opposed to accepting an assumed inflation rate of 7 per cent, in the initial stages.

7. At the same time, clearly we would not want, nor would the Executive Directors be ready, to come to any very definite conclusions on any sort of numbers on the very first morning. I suggest we aim to bring ~~with~~ matters, within the first two sessions, to ^{such} a stage of tentative conclusions on the growth of lending as would permit the Executive Directors to report to their Governments for instructions.

PNDamry:ets

11/17/77

①

The World Bank

Joussier - Tandy & urgent

Range of assumptions re rate of real growth
then effect of size on: absorption

How long should it last - at least 6 yrs

Bks int. coverage rate } need
vs rates } improvement

Pay in 102 + start pay to early '80

'83 to improve rates -

le 72 cap. assumption

pub. of it by Bk would have
unmistakable character -

link growth of Bk to growth of GDP
of OECD, real & nominal -

come to tentative conclusion early next yr -

"low. should be inc. in real terms"

∴ Govt favors a cap inc large
enough for at least 6 yrs -

U. Nazzer - Hopes for decision before 3/31 -

Should provide for at least 6 yrs.
The context:

a. We are not talking of assistance by
DE's to LDC's but rather of borrowing
from surplus countries to lend to LDC's
disengage from pay of aid given -

b) Paris in Bk a wonderful deal.

- constraint: 50b of devel for 5b. per in
- c) BRK has managed to combine a solid
 fine stone with an effective development
 ∴ doesn't agree with being growth in BRK
 leading to growth in OECD countries
- d) A cap line is a constitutionally binding ceiling
- e) We are not starting from scratch
 (BRD Com: North part)
- | | | |
|-------|-------|---------|
| 64-68 | 10 pa | } 11.12 |
| 69-73 | 7.7 | |
| 74-78 | 15.8 | |

The Determinants of Real Rate of Growth

I. Cap Regs of OECD

II. Pattern of External Fin

III. The place of the BRK in the Fin

I Cap Regs of OECD:

W. Europe proj^o 402 cap reg^o 402 for '80

based on 1.62 per + 13.12 per for cost of money

1.62 per too low - after 50 yrs, a substantial
 prop. would be below poverty line -

For this + other reasons = 406 too low an est.

II Re the supply of ext fin.

OPEC^{ODA} has been at 1.8% - this is not likely to rise
 DAC at 0.32 - some are likely but not great.
 R ODA would be: faces constraints + unclear

favorable assumptions will fall short -
demand for Bk fin for growth will be
to match the

Flow of com. Bk lending will be less
rapidly than in the past -

There will be a reallocation of DA
a rapid one in debt serv.

∴ they will substantially meet their request
of fin from BTD -

WBK would not replace com Bk, but
supplement it -

III The role of the Bk in the further Jett fin
The demand for an expanded role of the
Bk, even in traditional fields, will be
quite high -

But the effect in education on the
networks - i.e.

- a) fuel & iron - fuel minerals
- b) new style projects are an important
initiative & should be expanded -
- c) guarantee power should be retroacted -
- d) non-fin work of Bk.

presence of Bk influences compliance of
LDC's

presence of Bk efforts create a better
environment in dealing with debt prob.
Emigrants

... long & research carried out by the Bk -
all of these require & substantially greater
presence

∴ Should aim at real rate of growth of 7.7%
& recover 92 -

The Capital should not be less than
doubled, i.e. 40B as a bottom -

Re inflation: agree on real rate of growth
& size of capital rise - i.e. do not need
to bring inflation -

Re frequency: it is a buffer variable -

"We are in possession of a wonderful
development instrument. Let us make
use of it".

Fried - w/o instructions -

Agrees we should arrive at conclusion
of end of war or early 60s -

NS favors an rise in cap & rise leading
in real terms -

Bk is the most effective channel we
have in transferring capital -
pace of growth should not reduce this

Bk leading should rise 32.5% p.a
over next 5 yrs

if you Bk maintain others: banking is at
a size of 100B

The World Bank

- e) Will new style projects be bought by BIS
- f) De. lending could reduce commitments on policy advice
- d) How will graduation effect rate
- e) Can BK borrow rigid funds
- f) The admin + manage funds of BK staff should grow 50% -

Re inflation: 72 too high - both unlikely & politically unacceptable - would prefer an assumption lower than 72 -

France - London Summit, CIEC, Common Conf, Gov at Annual Mtg supported decline in lending - several Gov suggested a doubling of output - rate of growth should be as large as possible -

assumes:

- 1. Share of BK in multilateral loans will remain constant
- ∴ nominal rate of 11 1/2%

4. On assumption of 0% rate? interest at 1973

3. On past record, 1972
 Re Inflation: unlikely to fall & levels of 71 - better to err on high side -

∴ Support nominal rate of growth of 7 1/2%

Pyrie - UK wishes to see a rise in lending on real terms + an effort of the role of this marginal rate -

Cap De should carry Bk there
with 80's

Should restore a reasonable degree of
breadth & flexibility even in 50's
& 60's -

but can't decide now on how fast
Bk lending should grow -

will have to take a/c of factors such
as fixed record: size of Bk; absorption
capacity of LDC's; ability to borrow -

For illustrative purposes, it can
endorse figs in paper: 52 as real
terms a desirable fig to have in
mind -

72 up to 80's a bit too high - if
proceeded on 72, Cap De could last
longer -

Character of 1/4 of the roughly
doubling + that is the figure they
have in mind -

Proprio - with during annual 10% growth
substantial cap inc -
should cover at least 5 yrs -
" believes an inc. on order of
150% is req'd to permit a
real inc of 5 to 7% pa + that

Future role of Reg Bks will affect size of W Bk & would like to discuss

Yugo - real inc should not be less than 7% - absorptive cap of LDC's is rising rapidly - cap mltis of world are offering larger funds size & ∴ Bk borrowing should be accommodated -

∴ pure fin. by Bk loans help stabilize DC efforts -

∴ inter. cooper. contrib. by the Bk is a plus

∴ prog. of rate of growth in DC's at 2 low rates of growth, ∴ Bk can help LDC's -

W/ps dialogue has come to a standstill - one of the main issues the parties get on is of par of Bk - it should not be delayed

Well - in context of W/ps dialogue, En. has equal lending should not be in red terms & substantially inc fin of energy & inc - fuel investment - (What is share of BRD in program fin)

Re rate of infla - can't extrapolate from the past - end of lower figs than prog. by accepting a shorter period between cap replen ∴ he prefers on the 6.82 '74 & 3.2 in '81 -

The World Bank

(8)

Can agree to 52 for one in next terms
as basis for future work -

Believes this would require a doubling
of capital on basis of 8% interest -

Jan - Main emphasis should be on real rate of
growth & an inc. to avoid too
frequent cap. inc.

We shouldn't be too modest: :: with
real rate of growth of 112 over 15 yrs.
should plan on 73-92 -

to infla: reluctant to mention a figure
set a cap inc that isn't required
too frequent a review -

He suggests 40 to 50 -

Main interval 6 yrs - even better
would be 10 yrs -

What is absorbing cap. of DC's:
has improved over time -
and we are thinking of new fields:
e.g. mining

There is increasing emphasis on
basic needs & this requires
new style projects

But old style projects haven't become
unimportant -

Transfer of capital is not aid but
benefit to both parties -

The World Bank

Take a look at state of cap mkts -
in recent yrs, cap mkts have
expanded faster than GNP -
and there is a change in character -
they have been internationalized
with much greater mobility -

Johnston - All this constatement have been 200 million
+ recog its value -

Not yet prepared to put just the views
of this countries re work.

Need a rational justification for the
figures -

What is at the Bk wishes to do -

Ans. locait want Bk to
lose sight of impact of
shifting lending on cap
mkt + size -

Thailand - Should inc. relative share of Bk in
at least 5%

Real growth rate should not be less
than 7.2%

Comeca - supports: 7.2% in real terms
+ 4.0% rise in cap

Link infla with freq. of cap inc +
not with size -

Trade has increased at high rate +
supports need for higher lending com.

The World Bank

late of real one - must take a/c of net transfer -

LA Govs support a doubling of cap

Duke - Comb countries attach importance to inc the cap & lending - haven't been specific but believe they would support

52 -

Duke want a rationale for an inc.

Canada -

Support a inc in lending + a substituted inc in capital -

"Officials" would endorse Janesick's statements -

Re format & time-table

Disapp'd that initial idea to consider level of B's etc prior to considering level of lending has not been pursued -

Bd dis. should refer to Prospects paper re cap. flows & growth thru '85 -

2 pla rates of 7.72 too high, should reduce. prefer deflator of 3.52 - this would reduce cap inc req'd thru '85 by 52 from the level of 3.02 & 4.06 should show alternative inflows -

52 real growth can be guess on basis grounds & should be within DECD growth rates -

Concerned re implications of the one-
don't want to sacrifice quality &
efficiency -

want to be sure that goods (LDC) put
same priority on cap exp in Bk

Magnussen - From a sub. cap exp + support
realise in thinking for many
years to come -

Not prepared to state specific figs -
will place wgt on that all the
implications of other lending rates
re what we hope to achieve
by other lending programs + their
effect on admin probs -

Pesquera - In view of 11% growth in past
15 yrs, why accept 5%
for the future when LDC
needs are increasing -

Support as long as doubling
the capital -

Oppose linkage of growth rate
to OECD growth rate because
LDC need an increasing

influence with one the judgement
Hope for agreement early next yr.

Abdullahi - supports El Wazir
Real rate of growth of 5% less than

to 7 part 15 yrs:

∴ real growth not 100% by absorptive capacity but by donor willingness-

Inflation + "freedom" can be 10% -
but rate of growth no less than 7%
+ cap exp of at least 40% -

Budget - largely w/o interest -

All (KOR 2020 2021) credit cost are
in real terms

want real growth cap & maintain

Bk share at less than percent -

this means 5% at minimum -

could we compromise on nominal rate

of 10% + i. i.e. real lending
at 5% 78% -

Neerajana - Japan will double ODA in 5 yrs -
But resources are 10% -

200% of cap exp must be financing -

Difficult to find basis for choice of

5% - have to consider "supplier side" -

GNP 7% DECD may be less than 4% -

7% infla. rate too high -

Share of BK set to be constant - but
apparent to be inc. from 52 to 100 -
[still to provide]

Concerned re growth & size of organ-
¹⁰⁴⁴ 755 to large to manage

Rsta - no opportunity to make an cap - but
we need is a quantification of what
we need re borrowing & know how
much cap we need to borrow -

But not ready for gran. now -

∴ don't meet soon again

Yvesi Towner - agrees with El Vezger

favor real line 8592
Supports realloc of ODA to "poorest"
Desires capacity for quarterly auth.
Supports 403 cap 2nd

Logajidube - supports El Vezger + Janssen -
Supports 5592 + doubling of cap -

Office of the President

I Constructive

II Met 14/13

III 3 Tech Notes

1. Matrix - J. R. R. R.

2. Returns for a level process
and terms

3. List of other red terms one in
staff, goal, + office J. R. R. R.

IV Respond to queries or comments on
~~the notes~~

Non-descriptive etc

Refugee terms