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JANUARY-
JUNE 1974

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara, President **DATE:** June 19, 1974

FROM: Hollis B. Chenery, VP, Development Policy

SUBJECT: Themes for Governors' Speech

Before suggesting a new outline, I have tried to identify more clearly the themes around which your annual speech can be developed. A partial summary is attached. William and I plan to discuss it with a few people who have been concerned with the analytical work and to give you a revised draft on Friday.

Attachment

cc: Mr. William Clark, Director, IPA
Mr. E. Stern, Director, Development Policy
Mr. J. Maddux, IPA

HBChenery:di

McN notebook

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT ASSOCIATION

INTERNATIONAL FINANCE CORPORATION

6/26 To Messrs. Chenery
Stern

I was disappointed to find no proposals directed to "terms of trade"; "commodity agreements"; etc. I told Dave Bell if Ford Foundation would work with you both to develop research work on the subject, I would join with Ford to help finance (from my contingency reserve).

RMcN

cc: Mr. B. King
Mr. W. Tims

(HBC handwritten note:
Ben Perhaps you could see whether there is any interest in EPD or ECD in taking up McNamara's offer.)

7/2

Ford Foundation
List of proposals received
in worldwide research
competition on international
economic problems

6/26 To Messrs Chenery
Stern
I was disappointed
to find no proposals
directed to "terms of
trade", "commodity
agreements", etc.
I told Dave Bell
of Ford Foundation
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(from my contingency
reserve).
RSM

TABLE 1

IEO OUTLINES BY COUNTRY OF ORIGIN

(First Round - May 15, 1974)

Total Outlines Received	74
Austria	1
Belgium	1
Canada	4
Chile	1
France	2
Great Britain	2
Israel	4
Italy	1
Japan	1
Kenya	1
Netherlands	1
Switzerland	5
U.S.A.	50

TABLE 2

IEO PROPOSALS BY COUNTRY OF ORIGIN

(May 15, 1974)

Total Proposals Received	47
Belgium	1
Canada	2
Chile	1
Israel	2
Great Britain	2
Italy	1
Switzerland	3
U.S.A.	35

TABLE 3

IEO PROPOSALS BY RESEARCH AREAS

(May 15, 1974)

	Area	Number
I.	The International Transmission of Economic Disturbances	16
II.	The Organization of the World Monetary, Investment, and Trade Systems	10
III.	The Relationships among Trade and Investment, Income Distribution and Economic Policy	10
IV.	Trends and Policies in Commodity Supply and Demand	6
V.	International Economic Aspects of Environmental Problems	2
VI.	Other	3
		47

The average amount requested for all proposals received is in the $80-90,000 range.

Of the 26 IEO Competition Referees, 18 are Americans, 8 are foreign nationals; from Great Britain 3, France 1, Switzerland 1, India 1, Cuba 1, Sweden 1.

OUTLINES
FIRST ROUND
INTERNATIONAL ECONOMIC ORDER COMPETITION
1974-75

Received from:

1. Robert E. Baldwin, University of Wisconsin
2. Lawrence R. Klein, Wharton School of Finance and Commerce, University of Pennsylvania
3. Herbert G. Grubel, Simon Fraser University (Canada)
4. Gian S. Sahota , Vanderbilt University (Georgescu-Roegen)
5. John S. Chipman, University of Minnesota
6. James B. Ramsey, Hamermesh, Kreinin, Rasche, Michigan State University
7. Robert M. Stern, University of Michigan
8. J. M. Blin, Northwestern University
9. Michael J. Brenner, Harvard University
10. Flournoy A. Coles, Vanderbilt University
11. Ingo Walter, New York University
12. N. N. Franklin, International Labour Office (Geneva)
13. Lester C. Thurow, Massachusetts Institute of Technology
14. Jagdish Bhagwati, University of California, Berkeley
15. G.S. Sahota, Vanderbilt University
16. Roy D. Laird, University of Kansas
17. Frieder Roessler, Graduate Institute of Int'l. Studies (Switz.)
18. J. L. Reiffers, Faculté de Sciences Economiques d'Aix-en-Provence, via Yves Sabolo of ILO (Geneva)
19. Melvin M. Fagen, EEC (Geneva)

OUTLINES
FIRST ROUND
INTERNATIONAL ECONOMIC ORDER COMPETITION
1974-75

Received from:

20. Rodrigue Tremblay, University of Montreal (Canada)

21. Theodore Morgan, University of Wisconsin

22. Cagan, Phillip, Columbia U. and National Bureau of Economic Research, via Robert E. Lipsey, NBER

23. Anthony Y. C. Koo, Michigan State University

24. Peter R. Odell, Erasmus University (Rotterdam)

25. Walter C. Labys, Graduate School of International Studies (Geneva), projects 1, 2, 3

26. R. K. Berky, UNIDO (Vienna)

27. T. Takayama, S.C. Schmidt, U. of Illinois

28. Peter Frevert, Mohamed A. El-Hodiri, U. of Kansas

29. Elisha Pazner, Tel-Aviv University (Israel)

30. Richard N. Cooper, Yale University

✓31. Robert E. Krainer, University of Wisconsin (Madison)

✓32. John M. Culbertson, University of Wisconsin (Madison)

33. Akira Takayama, Sheng Cheng Hu, Yoshihiko Otani, via Jay W. Wiley, Purdue University

34. Claude d'Aspremont, Henry Tulkens, via Mgr. E. Massaux, Catholic University of Louvain (Belgium)

35. George H. Borts, Brown University

36. M. June Flanders, Tel-Aviv University (Israel)

37. Donald R. Hodgman, University of Illinois (Urbana-Champaign)

OUTLINES
FIRST ROUND
INTERNATIONAL ECONOMIC ORDER COMPETITION
1974-75

Received from:

38. Willard F. Mueller, Robert T. Aubey, Peter C. Carstensen, U. of Wisconsin

39. George Alibaruho, Institute for Development Studies, U. of Nairobi (Kenya)

40. Henry N. Goldstein, Raymond F. Mikesell, U. of Oregon

41. Rachel McCulloch, Janet Yellen, Harvard University

42. Weir M. Brown, OECD (Paris)

43. Henry N. Goldstein, Raymond F. Mikesell, U. of Oregon

44. Jacob A. Frenkel, Rudiger Dornbusch, Harry G. Johnson, University of Chicago

45. Richard J. Herring, Richard C. Marston, University of Pennsylvania, via Edward J. Parker

46. Thomas R. Stauffer, W. S. Comanor, Harvard

47. Dominique Florimond Turcq, University of Kobe (Japan)

48. G. K. Helleiner, University of Toronto (Canada)

49. V. Kerry Smith, State University of New York at Binghamton

50. Raveendra Batra, William R. Russell, Southern Methodist University

51. Giancarlo Barbiroli, Palmira Mazzaracchio, Giancarlo Santoprete, Vladimiro Ballini, University of Bologna (Italy)

52. Douglas K. Adie, Ohio University

53. Alex Cukierman, Edi Karni, Tel-Aviv University (Israel)

54. Franz Gehrels, William P. Travis, Indiana University

OUTLINES
FIRST ROUND
INTERNATIONAL ECONOMIC ORDER COMPETITION
1974-75

Received from:

55. Maryanna C. Boynton, California State University, Fullerton, via Dr. Ivan L. Richardson

56. Robert W. Boatler, University of Texas

57. Peter B. Kenen, Princeton University via William G. Bowen

58. John Kareken, Neil Wallace, University of Minnesota

59. David L. Huff, Robert T. Green, U. of Texas, Austin

60. Michael Connolly, Dean Taylor, U. of Florida (Gainesville)

61. Robert M. Stern, U. of Michigan, via James R. Randolph

62. Gerard Curzon, Victoria Curzon, Graduate Institute of International Studies (Geneva)

63. C. M. Cooper, Science Policy Research Unit, U. of Sussex, via C. Freeman (England)

64. John H. Makin, Yoshio Niho, University of Wisconsin (Milw.)

65. Stephen P. Dresch, An-loh Lin, National Bureau of Research, via Robert E. Lipsey (see IEO#22)

66. Haim Ben-Shahar, Michael Adler, Bernard Dumas, Tel-Aviv University (Columbia) (Israel)

67. J. B. L. Akumu, Oxford Professional Consultancy (England)

68. J. R. Zecher, D. N. McCloskey, University of Chicago

69. William R. Cline, Brookings Institution

70. R. Robert Russell, University of California (San Diego)

71. John O. Ward, University of Missouri (Kansas City)

72. Robert A. Mundell, University of Waterloo (Canada)

73. Fritz Machlup, New York University

74. E. E. Barandiarán, F. Ossa, Catholic University of Chile

INTERNATIONAL ECONOMIC ORDER COMPETITION
PROPOSALS
1974-75

Applicant	Outline No.	Subject	Requested Amount
Vanderbilt University G. S. Sahota	15	Trade, aid, growth, income distribution and economic policy in Asia	$ 62,868
University of Wisconsin (Madison) Robert E. Krainer	31	Economic integration and macro-economic policy: a study of the production, financing and investment decisions of multi-national firms and their bearing on economic policy	34,670
Vanderbilt University Nicholas Georgescu-Roegen, G. S. Sahota	4	The laws of matter energy and the econo-nomics of natural resources	133,758
University of Pennsylvania Richard J. Herring, Richard C. Marston	45	The integration of national and international money markets: an econometric study of international monetary linkages	89,302
University of Toronto Gerald K. Helleiner	48	Importers, trade barriers and manufactured exports from less developed countries	51,255
Massachusetts Institute of Technology Lester C. Thurow	13	The income distribution effects of inter-national trade in agricultural commodities in the U.S. and the U.K.	36,208
Tel-Aviv University Elisha A. Pazner Assaf Razin	29	Welfare implications of exchange rate uncertainty	60,000
University of Kansas Peter Frevert Mohamed El-Hodiri	28	International transmission of economic disturbances	81,724

Applicant	Outline No.	Subject	Requested Amount
Michigan State University Anthony Y. C. Koo	23	A comparative constraint approach to trade theory	$ 45,996
University of Bologna (Italy) Giancarlo Barbiroli Palmira Mazzaracchio Giancarlo Santoprete Vladimiro Ballini	51	The dynamics of the world trade of: manganese, beryllium, zirconium, cobalt, titanium, vanadium, zinc, copper, lead, silver	45,000
Ohio University Douglas K. Adie	52	The international transmission of business fluctuations through the monetary link	59,700
University of Illinois T. Takayama S. C. Schmidt	27	Projection and evaluation of trends and policies in agricultural commodity supply, demand, international trade, and food reserves	205,000
University of Texas Robert W. Boatler	56	A technology-adoption-adjustment model of less developed country trade in manufactured goods	15,000
European Economic Comm. Melvin M. Fagen	19	Organized economic cooperation among countries having different systems -- new approaches and new insights for policy	90,000
Indiana University Franz Gehrels William P. Travis	54	The magnitude and distribution of welfare gains from specified foreign investment, trade, and migration policies	97,231
California State University Maryanna C. Boynton	55	Effects of t ugar programs of the industrialized consuming nations on the economies of the	9,546

INTERNATIONAL ECONOMIC ORDER COMPETITION
PROPOSALS
1974-75

Applicant	Outline No.	Subject	Requested Amount
University of Wisconsin Robert E. Baldwin	1	An empirical approach to equilibrium and disequilibrium effects of international economic policy on efficiency, employment and distribution	$110,032
Princeton University Peter B. Kenen	57	Aspects of international financial integration	71,854
University of Minnesota John Kareken Neil Wallace	58	A welfare analysis of alternative international economic policy regimes	84,522
Brown University George H. Borts James A. Hanson	35	International adjustment to monetary disturbances	103,557
University of Texas David L. Huff Robert T. Green	59	Hierarchical structure of international trade and dependency relationships	46,160
Catholic University of Louvain Claude d'Aspremont Henry Tulkens	34	Stability and game theoretic analyses of international negotiations on transfrontier pollution	66,018
Massachusetts Institute of Technology Jagdish N. Bhagwati	14	Protection, adjustment costs and compensation mechanisms: theoretical and empirical analyses	53,900
University of Florida Michael Connolly Dean Taylor	60	Adjustment devaluation with money and non-traded goods	72,722

INTERNATIONAL ECONOMIC ORDER COMPETITION
PROPOSALS
1974--75

Applicant	Outline No.	Subject	Requested Amount
University of Michigan Robert M. Stern	61	Determinants of the commodity composition of trade	$111,488
Graduate Institute of Int'l. Studies Gerard Curzon Victoria Curzon	62	Reform of the international trade system: issues before the Tokyo round of GATT negotiations	176,780
New York University Robert G. Hawkins Richard Levich Tracy Murray Ingo Walter	11	Balance of payments adjustment under floating exchange rate system: a multi-country model under varying degrees of international capital mobility	42,133
National Bureau of Economic Research Stephen P. Dresch An-loh Lin	65	International trade, foreign investment, and production-induced pollution	170,800
Michigan State University Mordechai E. Kreinin James B. Ramsey Robert H. Rasche Norman Obst	6	Time reaction lag (and time path) of the domestic economy and the balance of payments to exchange rate adjustments	159,500
National Bureau of Economic Research Phillip Cagan	22	The effects of world commodity prices on U.S. manufacturing prices	96,600
University of Wisconsin(Mil.) John H. Makin Yoshio Niho	64	Optimal ti paths for multiple policy instrumen ı an open economy	40,287

INTERNATIONAL ECONOMIC ORDER COMPETITION
PROPOSALS
1974--75

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INTERNATIONAL ECONOMIC ORDER COMPETITION
PROPOSALS
1974-75

Applicant	Outline No.	Subject	Requested Amount
University of Sussex (Eng.) C. M. Cooper, et al	63	Technology and the supply and demand for primary commodities in international trade	$156,000
University of Pennsylvania F. Gerard Adams Lawrence R. Klein	2	Linkage of international commodity market models and analysis of international commodity price inflation	99,560
University of Chicago Tulane University D. N. McCloskey J. R. Zecher	68	Prices, growth and the balance of payments under the gold standard, 1840-1940	
Oxford Professional Consultancy J. B. L. Akumu et al	67	The significance of socio-economic underdevelopment of the less developed countries and its effects on the transmission of economic disturbances	£48,000 $
Tel-Aviv University Haim Ben-Shahar Michael Adler Bernard Dumas	66	Risk determinants of international trade and investment	54,211
Purdue University Akira Takayama	33	International transmission of inflation and the balance of payments	158,103
Brookings Institution William R. Cline	69	Trade and employment effects of multilateral trade liberalization	70,000

INTERNATIONAL ECONOMIC ORDER COMPETITION
PROPOSALS
1974-75

Applicant	Outline No.	Subject	Requested Amount
University of Chicago Rudiger Dornbusch Jacob A. Frenkel Harry G. Johnson	44	The international transmission of real and monetary disturbances	$ 97,130
University of Cal. (San Diego) R. Robert Russell John Hooper	70	A multilateral model of international trade flows	87,074
Graduate Institute of International Studies (Geneva) Frieder Roessler	17	The legal design of the international economic system	
Harvard University Michael J. Brenner	9	International monetary reform and transnational monetary reform and transnational actors: the decision to establish flexible exchange rates	43,862
U. of Waterloo (Canada) or Columbia Robert A. Mundell	72	International currency systems, factor price differentials and the international monetary order	176,000
New York University Fritz Machlup	73	Open problems of the international monetary system and its reform	72,279
University of Minnesota John S. Chipman	5	A neo-classical econometric model of international trade	79,737
Catholic University of Chile Edgardo E. Barandiarán Fernando Ossa	74	Harmonization of national macroeconomic policies in an interdependent world of regional blo the alternatives for the Andean cou s	81,400

INTERNATIONAL ECONOMIC ORDER COMPETITION
PROPOSALS
1974-75

Applicant	Outline No.	Subject	Requested Amount
Southern Methodist University William Ross Russell Raveendra N. Barta	50	The analysis of international trade between centrally controlled and decentralized economies	$ 93,205

Mr. Robert S. McNamara, President June 17, 1974

Hollis B. Chenery, VP, Development Policy

Technical Notes for Governor's Speech

1. Attached are two technical notes on Terms of Trade by Commodity and by Country Groups in connection with your Governor's Speech. This material is summarized in a more general framework in section II.A of the Energy Paper.

2. Other notes requested are being forwarded by Mr. Stern.

cc: Mr. J.L. Maddux

Attachments

HBC:gss

HBC

Mr. W. Tims, Director, EPD June 7, 1974

E. Stern, Director, Development Policy

Annual Speech

We discussed the draft annual speech with Mr. McNamara on Wednesday. He indicated that he would turn this version over to Mr. Maddux even though he thought there was little in the present draft that he could use. To assist Mr. Maddux, he asked that the following technical notes be prepared. They should be submitted to Mr. McNamara, with a copy to Mr. Maddux, no later than close of business on June 14:

1. Trade Patterns. A short technical note (about 5 pages) describing the movements in international trade, volume and prices of principal commodities by category, source and destination. This will be background to a more detailed understanding of the movements of the terms of trade discussed in the paper. He expects to use the terms of trade table which is in the Five-Year Operations Program. The note should also cover the specifics as to why the share of trade of developing countries in primary commodities has decreased (Page 10) and give examples of the supply-limiting policies mentioned on Page 11.

2. A separate technical note on the terms of trade of selected individual developing countries to expand the discussion in Paragraph 3 of Page 11; and regional terms of trade to back up the discussion on Page 17.

3. A technical note on the capital flows from the oil producing countries. The recipients are to be distinguished by income group, and we should make estimates to the extent possible of disbursements per year. He recognizes that information on commitments is weak and on disbursements non-existent, but would like to have our best possible estimates on this (check with Messrs. Vibert and El Fishawy).

4. A technical note on the impact of inflation on different groups in developing countries, recognizing that no general propositions may hold. Therefore, country examples should be used to demonstrate the impact on small farmers, landless laborers, urban poor, rural-urban income distribution, etc. You might enlist the assistance of Mr. Yenal or Mr. Ahluwalia on this.

DRAFT--KPekonen/ad'A

June 14, 1974

Terms of Trade by Country Groups

According to the latest estimates (CPP run May 30, 1974) the terms of trade of the 40 non-oil exporting developing countries are projected to deteriorate by 5.6 percent over the period 1974-1980. There are, however, sharp differences in the projected trends between individual countries, regions and groups of countries classified by income levels resulting from the different compositions of their trade patterns.

On the basis of income level distinction the terms of trade of the low income group are projected to worsen most, by 10.8 percent. The deterioration of the middle/high income group is relatively modest, 3.0 percent.

On the regional basis East Africa and South Asia are hit hardest by a worsening of their terms of trade of 13.6 percent and 9.0 percent respectively. Mineral producers are expected to suffer a relatively sharp deterioration in their terms of trade (17.5%) in the latter part of the 1970's, which however is partly due to a high initial level of their export prices in 1974.

Table 1 gives a detailed picture of the main trends of the terms of trade in the 1970's by various country groups and regions.

Table 1

Terms of Trade of LDC's by Country Groups and Regions
(1967-69 = 100)

	1973	1974	1980	Percentage Change 1974-80
47 countries	116.6	142.6	134.6	-5.6
40 countries	108.5	101.3	95.6	-5.6
Oil Exporters	131.0	292.5	282.9	-3.3
Middle/High Income	110.4	102.1	99.0	-3.0
Low Income	94.6	89.3	79.6	-10.8
Mineral Producers	114.4	113.8	93.9	-17.5
Latin America	125.1	113.2	111.3	-1.7
West Africa	110.6	108.6	105.6	-2.8
East Asia	96.6	88.1	85.4	-3.1
East Africa	104.2	100.4	86.7	-13.6
Mediterranean	102.3	99.0	91.6	-7.5
South Asia	89.9	83.8	76.3	-9.0

Terms of Trade, Country Examples

For a number of developing countries, the composition of their trade as such that they face a more rapid increase in prices in imported primary commodities than in those of their exported commodities. Here again considerable differences between individual countries exist. In table 2, the terms of trade projections for some selected countries are given.

Table 2

Terms of Trade, Selected Countries
(1972 = 100)

	1973	1974	1980	Percentage change 1974-80
Ethiopia	120.8	99.6	93.2	-6.4
India	88.2	74.2	72.7	-2.0
Malaysia	116.1	114.2	104.6	-8.4
Morocco	95.9	120.9	95.9	-20.7
Pakistan	78.2	94.6	71.7	-24.2
Sri Lanka	92.8	86.5	75.6	-12.6
Thailand	120.1	113.0	96.0	-15.0
Turkey	96.7	90.0	81.8	-9.1
Uruguay	111.5	79.5	76.5	-3.8

In the following tabulation the main factors affecting some selected countries' terms of trade trends between 1974-80 are shown. Export and import price changes of the main internationally traded commodity groups are given in the first column and their share in 1974 as percentage of total exports/imports in the second.

		Import/Export prices Percentage change 1974-80	Share in 1974 (%)
Ethiopia			
Imports:	"Other goods"	57	62
	Fuel	59	33
Exports:	"Other goods"	48	42
	Coffee	43	37
India			
Imports:	"Other goods"	48	54
	Fuel	64	27
Exports:	"Other goods"	42	58
	Jute	45	14
	Tea	- 4	9
	Eng. goods	66	8
	Cotton	23	7
Malaysia			
Imports:	"Other goods"	83	67
	Food	64	17
	Fuel	59	16
Exports:	Rubber	33	28
	"Other goods"	54	22
	Logs	58	12
	Tin	62	11
Morocco			
Imports:	"Other goods"	42	82
	Fuel	42	18
Exports:	"Other goods"	48	53
	Phosphate	-29	47
Pakistan			
Imports:	"Other goods"	63	23
	Food	17	17
	Fuel	63	14
Exports:	CYR (?)	13	27
	Manufactured goods	63	20
	Rice	-24	19

		Import/Export prices Percentage change 1974-80	Share in 1974 (%)
Sri Lanka			
Imports:	Food	24	37
	"Other goods"	59	33
Exports:	Tea	-3	44
	"Other goods"	55	25
	Rubber	33	19
Thailand			
Imports:	"Other goods"	48	73
	Fuel	59	23
Exports:	"Other goods"	48	39
	Rice	-9	15
	Rubber	33	12
	Maize	19	12
Turkey			
Imports:	"Other goods"	54	79
	Fuel	55	19
Exports:	Cotton	13	24
	Fruits	50	16
	"Other goods"	8	12
	Zinc	-4	10
Uruguay			
Imports:	Fuel	54	32
Exports:	Beef	70	39
	Wool	-1	30

E.G. Ethiopia's worsening terms of trade results from relatively modest increase of export prices of coffee and "other goods" as compared with the price expectations of her main import categories. Export prices of phosphate in Morocco, rice in Pakistan and Thailand, tea in Sri Lanka and India and zinc in Turkey are projected now to decline

over the period 1974-1980. The exports of these goods are of crucial importance for some of the developing countries and their declining prices cause considerable losses under world wide inflation and consequently increasing import prices mainly of fuels and industrial goods.

Generally LDC's import prices of the "other goods" rise considerably faster than their export prices under the same heading, reflecting mainly projected price trend differences between manufactured goods imported by LDC's and less sophisticated goods exported by them.

* * *

DRAFT
JNusbaumer:jl
June 13, 1974

DEVELOPMENTS IN PRIMARY COMMODITY TRADE AND IN DEVELOPING COUNTRIES TERMS OF TRADE

1. During the decades of the 1950's and 1960's the share of developing countries in total world exports fell from 31.2 to 19.4 percent. This reflected both a slower growth of export volume and a slower rise in export unit values compared with developed areas. In 1970, the volume of developing countries' exports was 1.8 times larger than in 1950, but the volume of developed countries' exports was 4.4 times larger. Export unit values of LDC's were very high in the early 1950's, then fell gradually until the early 1960's. From 1963 onwards export unit values rose again, but slower than those of developed areas.(Table 1). The movements in LDC's terms of trade reflected these developments: after falling continuously until the early 1960's, they remained fairly stable (around 100) during the rest of the last decade (Tables 2 and 3).

2. The divergence in the movements of prices of primary commodities and of manufactures which was typical of the 1950's, did not continue during the 1960's, but the rise in primary product prices in that period was comparatively slow (Table 2 and Diagram 1). Primary commodities exported by developing countries show price movements similar to those of the same commodities exported by the developed world. Therefore, unless it is assumed that unit values of manufactures exported by the LDC's did not follow the general rising trend of prices of these products, changes in the terms of trade of LDC's are attributable to the large share of primary products in their exports. However, the nearly constant level of their terms of trade with developed areas in the larger part of the 1970's is

clearly due to the stagnation of petroleum prices. If these are excluded from the index, some improvement in the terms of trade of LDC's with developed areas can be discerned in the latter years of the decade (Tables 3 and 4 and Diagram 2).

3. Among the primary products exported by developing countries, average export unit values rose most for non-ferrous metals; these nearly doubled in price between 1960 and 1970. The next largest rise in export unit values occurred in food products. The export prices of minerals increased little while those of agricultural non-food commodities were at best stable in the 1960's (Table 5). The international market prices of the 35 major primary commodities (excluding petroleum) exported by developing countries followed roughly the same trends (Table 6). The pattern of year-to-year changes is different, however, due to the fact that these 35 commodities represent a small sample of the many varieties and quality types of primary products exported by LDC's. These international prices fluctuate more than export unit values because they respond to short-term supply and demand factors in narrower markets.

4. In terms of volume, world trade in manufactures increased faster than in primary products, with the exception of fuels (Table 7). World exports of food products (SITC 0 + 1)and of other raw materials (SITC 2 +4) rose at approximately the same rate from the early 1950's to 1970, i.e., by 4.5 percent per annum compared with 7.3 percent for total trade. The increase in the volume of exports of food and raw materials was considerably greater for developed market economies than for LDC's and it is noteworthy that developed countries' exports of these products to developing countries also increased faster than the exports of the latter to the former.

5. The volume of developing countries total exports of 35 major primary commodities (excluding petroleum) increased by 3.1 percent per annum between 1955 and 1970. There was a marked slowdown in the first half of the last decade and a partial recovery in the latter half due to the growth in the volume of exports of metals and minerals. The volume growth of exports of agricultural products, food and non-food, declined sharply in the late 1960's compared with the earlier period (Table 8).

6. In part, the DC's recently increased share of world trade of primary commodities reflects the rapid development of food production in these countries, particularly in Western Europe. The creation of the EEC has resulted in a dynamic rise of agricultural output and exports in the participating countries, thanks to the price support schemes and the protention against imports which are the mainstay of the common agricultural policy. In turn, the growth of output in Western Europe has given rise to important trade flows between this area and other developed countries because of particular input-output relationships in some productions. An example is the rapid development of EEC imports of soybeans for livestock feed from the United States. Another development which has affected the share of developing countries in primary commodity exports is the rapid growth of production of minerals in developed countries of the Southern Hemisphere. This is particularly relevant for lead, zinc and manganese ore.

7. In addition, export availabilities of some primary commodities from developing countries have been reduced by a number of factors, notably demand for food and weather. While production of food in LDC's increased at about the same rate as in developed countries during the 1960's, the

increase was not sufficient to meet the growth of demand for food due to higher population growth rates. Consequently, developing countries have been increasingly dependent on food imports from developed areas and this also accounts for the rise in the share of these areas in total world exports of primary commodities. Unfavorable weather conditions have notably affected the production of groundnuts in West Africa and this favored the growth of trade in competing oilseed products, among which palm oil, which is produced in LDC's, but also soybeans, rapeseed and sunflowerseed, which are mainly produced in developed countries

8. Comparison of the growth rates of total exports by income groups of developing countries and main areas of distribution (Table 9) shows that during the last two decades trade developing countries was growing in relative importance for low and high income LDC's, but not for oil-exporting countries. A higher ratio of total exports of low income countries goes to other developing countries than for either of the other two categories, the dependence on developed country markets being highest of oil-exporting countries.

9. Table 10 shows the estimated commodity terms of trade for different groups of developing countries. These were calculated on the basis of information concerning exports of 36 major primary commodities (including petroleum). The total terms of trade of the different country groups would probably be higher if manufactures were included in exports. However, apart from the "high income" group, the difference is not likely to be large. The shares of commodity categories (out of a total of 36 commodities) in total primary exports of LDC's were as follows in 1967-69:

	Low Income	High Income	Oil-exporting
Food	53.95	50.04	13.99
Agric. non-food	28.77	22.60	7.39
Metals and Minerals	12.88	18.06	4.23
Petroleum	4.40	9.30	74.39

Table 1: QUANTUM AND VALUE EXPORTS INDICES 1950-1972
(1963 = 100)

Year	Developing Countries			Developed Countries		
	Quantum	Implicit Price Index/1	Value	Quantum	Implicit Price Index /1	Value
1938	56	33.9	19	36	41.7	15
1948	51	107.8	55	35	100.0	35
1950	89	69.7	62	43	83.7	36
1951	60	128.3	77	50	100.0	50
1952	57	117.5	67	50	100.0	50
1953	62	108.1	67	53	96.2	51
1954	64	109.4	70	56	94.6	53
1955	68	110.3	75	61	95.1	58
1956	72	109.7	79	67	98.5	66
1957	74	109.5	81	72	100.0	72
1958	75	105.3	79	70	97.1	68
1959	80	102.5	82	75	97.3	73
1960	85	102.4	87	84	97.6	82
1961	89	100.0	89	88	98.9	87
1962	95	97.9	93	93	98.9	92
1963	100	100.0	100	100	100.0	100
1964	107	102.8	110	111	101.8	113
1965	113	101.8	115	120	103.3	124
1966	118	103.4	122	130	104.6	136
1967	124	103.2	128	137	105.1	144
1968	136	102.9	140	155	103.9	161
1969	147	106.1	156	173	108.1	187
1970	160	108.1	173	189	113.8	215
1971	169	112.4	190	201	119.9	241
1972	182	117.6	214	219	130.1	285

Note: Includes petroleum.

/1 Calculated from value and quantum indices published by: United Nations, Monthly Bulletin of Statistics.

Table 2: UNIT VALUE OF WORLD EXPORTS OF MANUFACTURES COMPARED WITH OTHER GOODS, 1950-1970 (1963 = 100)

	Manuf. Goods	Other Goods
1950	81	98
1951	96	121
1952	98	114
1953	94	109
1954	92	108
1955	93	107
1956	97	107
1957	98	109
1958	97	105
1959	97	102
1960	99	101
1961	100	100
1962	100	98
1963	100	100
1964	101	103
1965	104	102
1966	106	103
1967	107	102
1968	107	100
1969	110	102
1970	117	106

* Preliminary figures.

Source: United Nations Statistical Office, Statistical Yearbook 1969, plus data supplied by United Nations Statistical Office.

Table 3: TERMS OF TRADE INDEX NUMBERS OF DEVELOPED MARKET-ECONOMY AND DEVELOPING COUNTRIES AND TERRITORIES BY MAJOR REGIONS, 1955-1970
(1963 = 100)

	1955	1956	1957	1958	1959	1960	1961	1962	1964	1965	1966	1967	1968	1969	1970
Developed Market Economy Countries	92	93	92	96	97	98	99	100	100	100	100	101	101	101	102
Developing Countries and Territories	110	107	104	104	105	104	100	98	101	100	101	100	101	102	101
excluding petroleum	111	108	103	101	103	104	99	96	103	102	104	103	103	107	108

Source: United Nations, Monthly Bulletin of Statistics, October 1971.

Table 4: TERMS OF TRADE OF LDC'S WITH DEVELOPED AREAS 1953-1970
(1963 = 100)

	1953	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967	1968	1969	1970
Developed areas/ Developed areas/1	113	120	119	116	111	107	104	104	100	98	100	102	99	100	98	99	102	100
Developing areas less fuels/Developed areas/1 /2	114	125	119	115	109	103	102	103	99	96	100	104	101	103	101	102	106	105

Source: UN Monthly Bulletin of Statistics, November 1971, Statistical Yearbook 1969.

/1 Unit value index of exports from the first region to the second divided by unit value index of export from the second to the first.

/2 Export prices of fuels for developing countries and territories are based on the posted prices concept.

Table 5: EXPORT PRICE INDEXES BY DEVELOPED AND DEVELOPING AREAS AND BY COMMODITY GROUPS, 1955-1970
(1963 = 100)

	Code/1	1955	1956	1957	1958	1959	1960	1961	1962	1964	1965	1966	1967	1968	1969	1970
Primary Commodities	X	102	104	105	97	96	96	97	96	104	105	107	103	100	104	107
	Y	112	111	113	108	103	102	98	96	103	102	102	100	100	104	107
Food	X	97	97	97	96	95	94	94	96	105	105	108	107	102	105	108
	Y	114	113	117	111	97	94	91	91	107	101	102	101	102	108	116
Agricultural Non-Food	X	110	111	112	98	98	99	100	96	103	103	106	98	96	100	100
	Y	118	115	111	100	110	114	104	99	101	102	100	94	94	101	98
Minerals	X	101	113	113	101	96	97	98	98	105	106	107	105	104	107	122
	Y	104	105	110	111	103	101	100	100	102	103	103	102	102	103	104
Non-Ferrous Base Metals	X	113	121	106	96	103	106	104	101	116	129	144	135	142	158	187
	Y	135	136	98	86	101	104	99	99	124	146	177	156	165	167	191

Source: United Nations, Monthly Bulletin of Statistics, March 1971.

X - Indexes representing exports of developed areas.

Y - Indexes representing exports of developing areas.

Table 6: COMMODITY PRICE INDEX
(1967-69 = 100)

	36 Commodities (Incl. Pet.)	35 Commodities (Excl. Pet.)	Agriculture Food	Agriculture Non-Food	Metals, Minerals and Ores
1950	114	100	106	145	54
1951	123	117	116	188	68
1952	118	107	110	140	79
1953	119	100	111	113	73
1954	127	108	129	113	71
1955	126	107	111	129	84
1956	126	108	116	119	85
1957	121	103	115	117	76
1958	116	95	104	107	69
1959	106	94	97	119	72
1960	103	93	94	120	73
1961	99	88	89	108	72
1962	98	88	90	108	71
1963	100	94	101	105	72
1964	102	101	105	106	90
1965	102	102	99	103	105
1966	103	104	96	105	114
1967	99	97	97	98	95
1968	99	98	98	98	98
1969	102	105	104	104	109
1970	105	109	114	99	108
1971	114	104	109	103	96
1972	128	113	121	114	97
1973	187	169	170	189	140

Source: Commodities & Export Projections Division
Economic Analysis & Projections Department

Table 7: QUANTUM INDEX OF EXPORTS OF MARKET ECONOMIES
(1963 = 100)

Exports to → / SITC Sections / Exports from ↓ Year	MARKET ECONOMIES – TOTAL ECONOMIES DE MARCHE – TOTAL: Total	0+1	2+4	3	5	7	6+8	DEVELOPED MARKET ECONOMIES: Total	0+1	2+4	3	ECONOMIES DE MARCHE DEVELOPPEES: 5	7	6+8	DEVELOPING MARKET ECONOMIES ECONOMIES DE MARCHE EN VOIE DE DEVELOPPEMENT: Total	0+1	2+4	3	5	7	6+8	SITC Sections / Années
	0-9	0+1	2+4	3	5	7	6+8	0-9	0+1	2+4	3	5	7	6+8	0-9	0+1	2+4	3	5	7	6+8	
MARKET ECONOMIES — TOTAL...	1953	63	65	65	50	34	42	55	62	64	64	47	30	40	43	68	67	65	77	51	64	74	1953
	1958	71	72	75	69	56	64	69	69	78	75	64	51	58	61	86	84	75	89	66	91	94	1958
	1959	75	80	85	72	65	71	76	73	92	85	66	61	64	71	97	97	85	88	73	88	92	1959
	1960	84	88	94	79	74	81	84	81	85	94	75	72	75	80	94	97	93	93	79	94	98	1960
	1961	88	91	95	84	81	87	87	85	90	96	81	78	83	83	96	97	93	96	88	96	98	1961
	1962	93	96	95	93	89	92	97	92	96	95	90	87	91	90	95	94	99	102	93	95	96	1962
	1963	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	1963
	1964	113	104	107	109	119	112	113	111	103	106	110	120	114	115	108	109	108	103	115	107	108	1964
	1965	117	109	105	116	132	125	123	119	108	108	119	134	128	126	112	110	111	106	121	116	114	1965
	1966	127	112	113	126	150	141	133	128	111	112	130	153	145	137	122	117	115	114	143	126	119	1966
	1967	134	117	114	140	167	150	138	137	116	114	144	173	159	143	124	121	118	124	153	139	121	1967
	1968	151	122	122	155	183	176	151	151	121	120	163	203	188	168	138	123	123	129	176	149	136	1968
	1969	170	125	132	168	210	194	163	165	125	128	173	234	210	191	155	123	131	144	188	171	135	1969
	1970	188	137	139	195	243	225	183	189	139	140	197	259	241	204	166	141	148	135	207	183	167	1970
	1971	197	149	143	211	262	247	203	202	148	138	227	282	268	215	178	150	180	155	220	204	191	1971
DEVELOPED MARKET ECONOMIES	1953	64	68	63	62	33	45	60	62	68	65	53	30	40	43	68	66	59	116	42	63	75	1953
	1958	70	76	70	75	56	66	69	64	74	70	70	51	58	61	90	83	82	123	67	92	96	1958
	1959	75	80	80	72	65	72	76	73	78	81	67	61	64	71	88	86	72	108	75	89	93	1959
	1960	84	85	91	83	71	81	85	83	82	94	78	71	75	80	95	98	88	121	81	95	101	1960
	1961	88	92	94	85	81	87	87	85	91	95	81	78	83	83	97	98	89	114	89	97	100	1961
	1962	92	95	93	92	89	92	92	92	95	93	91	86	91	91	95	94	94	102	95	93	96	1962
	1963	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	100	1963
	1964	111	107	110	99	118	112	114	112	105	109	103	121	114	115	108	109	116	97	113	107	108	1964
	1965	119	112	109	104	133	125	124	121	113	104	126	134	128	128	113	108	119	93	123	116	113	1965
	1966	127	118	114	113	147	140	124	131	117	113	137	152	145	138	124	122	118	107	141	128	118	1966
	1967	137	120	118	125	165	153	139	142	122	116	127	173	159	143	126	127	124	107	120	129	121	1967
	1968	155	127	126	127	195	176	162	151	127	126	141	205	187	169	139	126	145	106	173	148	135	1968
	1969	176	132	134	147	222	205	183	162	134	132	149	237	216	192	157	126	154	125	185	171	151	1969
	1970	191	147	145	176	244	223	197	197	148	141	181	262	240	204	169	143	169	137	204	183	160	1970
	1971	204	160	144	184	264	249	204	211	161	138	192	284	266	216	182	159	206	127	216	202	164	1971
DEVELOPING MARKET ECONOMIES	1953	64	75	84	46		48		57	77	83	37		43		70	69	95	70		57		1953
	1958	76	85	85	65		62		75	84	84	62		62		80	87	89	83		63		1958
	1959	81	88	93	72		70		81	86	93	66		72		83	90	95	85		65		1959
	1960	89	91	94	77		79		85	90	94	73		81		88	95	99	88		74		1960
	1961	89	89	97	84		82		87	85	97	80		82		92	94	98	93		81		1961
	1962	94	96	99	93		89		94	96	96	90		90		97	96	104	102		84		1962
	1963	100	100	100	100		100		100	100	100	100		100		100	100	100	100		100		1963
	1964	106	103	102	113		112		106	98	102	115		112		107	110	100	105		113		1964
	1965	112	103	107	121		116		112	101	108	126		115		111	112	103	109		118		1965
	1966	118	104	111	131		130		119	102	111	137		130		116	109	111	115		130		1966
	1967	124	107	109	146		135		125	106	109	153		137		119	110	102	127		129		1967
	1968	137	113	114	163		162		135	112	112	174		166		121	117	121	133		152		1968
	1969	149	113	127	177		194		149	112	124	188		195		149	117	147	148		191		1969
	1970	159	121	128	189		216		151	122	127	204		211		152	116	134	134		200		1970
	1971	174	130	140	223		212		175	129	137	245		205		167	132	155	161		227		1971

Source: United Nations, Statistical Yearbook, 1972

1 (i) Developed Market Economies: United States, Canada, Western Europe (incl. Turkey and Yugoslavia), Australia, New Zealand, South Africa and Japan.

(ii) Developing Market Economies: countries other than those listed in (i) and Centrally Planned Economies except Cuba which is included in this area.

Table 8: QUANTUM INDEX OF DEVELOPING COUNTRIES
EXPORTS OF 35 MAJOR COMMODITIES
(1967-69 = 100)

	36 Commodities (Incl. Pet.)	35 Commodities (Excl. Pet.)	Agriculture Food	Agriculture Non-Food	Metals, Minerals and Ores
1955	47	68	70	85	52
1956	48	70	69	86	62
1957	51	72	72	80	66
1958	52	73	77	82	57
1959	59	77	77	87	65
1960	63	82	82	89	71
1961	67	86	87	97	75
1962	70	88	88	95	78
1963	75	89	90	102	76
1964	80	89	96	94	72
1965	84	92	100	101	74
1966	87	93	103	99	79
1967	93	97	100	94	94
1968	100	100	103	96	98
1969	107	104	98	109	105
1970	111	108	104	111	112
1971	111	108	108	100	109
1972	110	105	107	96	110

Source: Commodities & Export Projections Division
Economic Analysis & Projections Department

Table 9: GROWTH RATES OF VALUE OF EXPORTS TO AND FROM LDC'S, BY COUNTRY GROUPS, 1950-52 TO 1969-71

	Average Annual Percentage Changes		Value ($ billion)			
	Total Developed	Developed	Total Developing		Developed	
			1950-52	1969-71	1950-52	1969-71
Low Income/1	4.0	2.4	1.2	2.6	2.3	3.7
High Income/2	10.3	5.6	2.4	10.4	8.2	24.3
Oil-Exporting	5.3	8.7	1.5	4.2	2.7	14.1
Developed	6.5	9.3	16.5	58.5	29.6	160.4

Source: IMF Direction of Trade.

/1 Per capita income below $200.

/2 Per capita income above $200.

Table 10: TERMS OF TRADE OF DEVELOPING COUNTRIES, BY INCOME GROUP AND AREA /1
(1967-69 = 100)

	Latin America Country Groups			Africa/2 Country Groups			Asia/2 Country Groups			All LDCs/2 /3 Country Groups		
	1	2	3	1	2	3	1	2	3	1	2	3
1955	108	123	139	123	118	147	129	130	156	123	123	150
1956	107	123	140	120	117	145	128	125	154	121	121	148
1957	98	117	132	114	110	135	122	117	143	116	114	138
1958	93	111	130	107	104	135	116	112	145	109	109	138
1959	93	108	116	109	104	122	114	114	128	109	108	124
1960	93	105	112	107	103	117	112	114	123	108	105	119
1961	88	99	107	100	96	112	104	105	118	100	99	115
1962	89	100	107	101	97	111	105	106	117	102	100	114
1963	91	104	110	105	102	110	108	104	114	105	103	111
1964	101	107	107	107	106	106	109	106	106	107	106	106
1965	106	104	104	104	104	105	104	106	105	104	104	105
1966	108	102	101	102	103	104	101	106	103	102	103	103
1967	97	98	100	98	98	101	99	99	102	98	98	102
1968	99	99	100	99	99	100	99	99	101	99	100	100
1969	104	102	100	103	103	99	102	102	98	102	102	98
1970	101	101	100	100	101	95	100	96	93	100	100	95

/1 Export unit value index for 36 major primary commodities divided by weighted index of export price of manufactures and primary products. The price index of exports of manufactures by developed countries with a weight of 70% and the price index exports of primary commodities by LDC's with a weight of 30% were used to calculate the weighted index, which represents an estimated import price index for LDC's.

/2 Country Group 1 = per capita income below $200, Group 2 = per capita income above $200, Group 3 = oil exporting countries.

/3 Excludes LDC's in Oceania.

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Diagram 1: UNIT VALUE INDEX OF MANUFACTURE OF GOODS AND OF OTHER GOODS FOR TOTAL WORLD TRADE

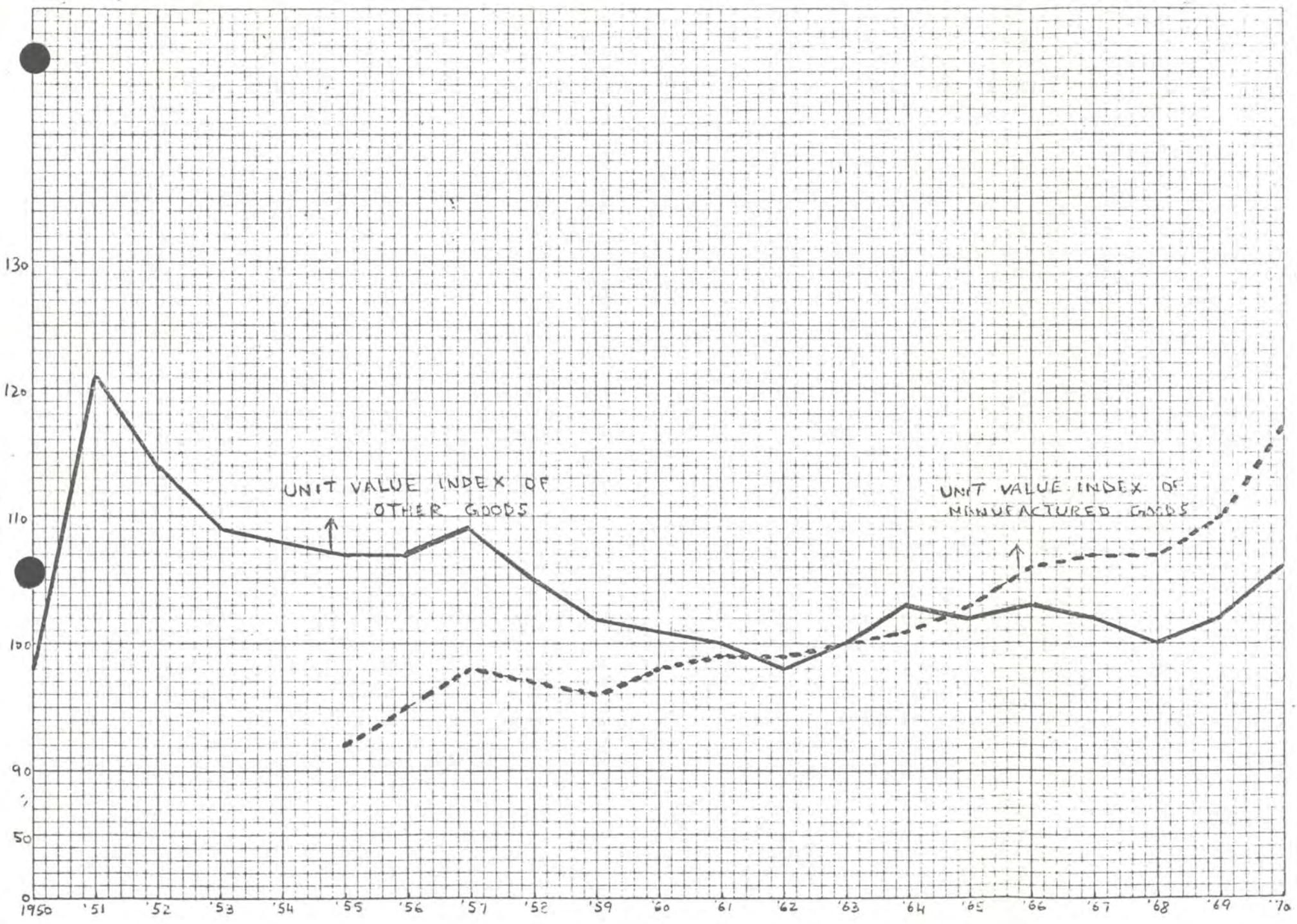

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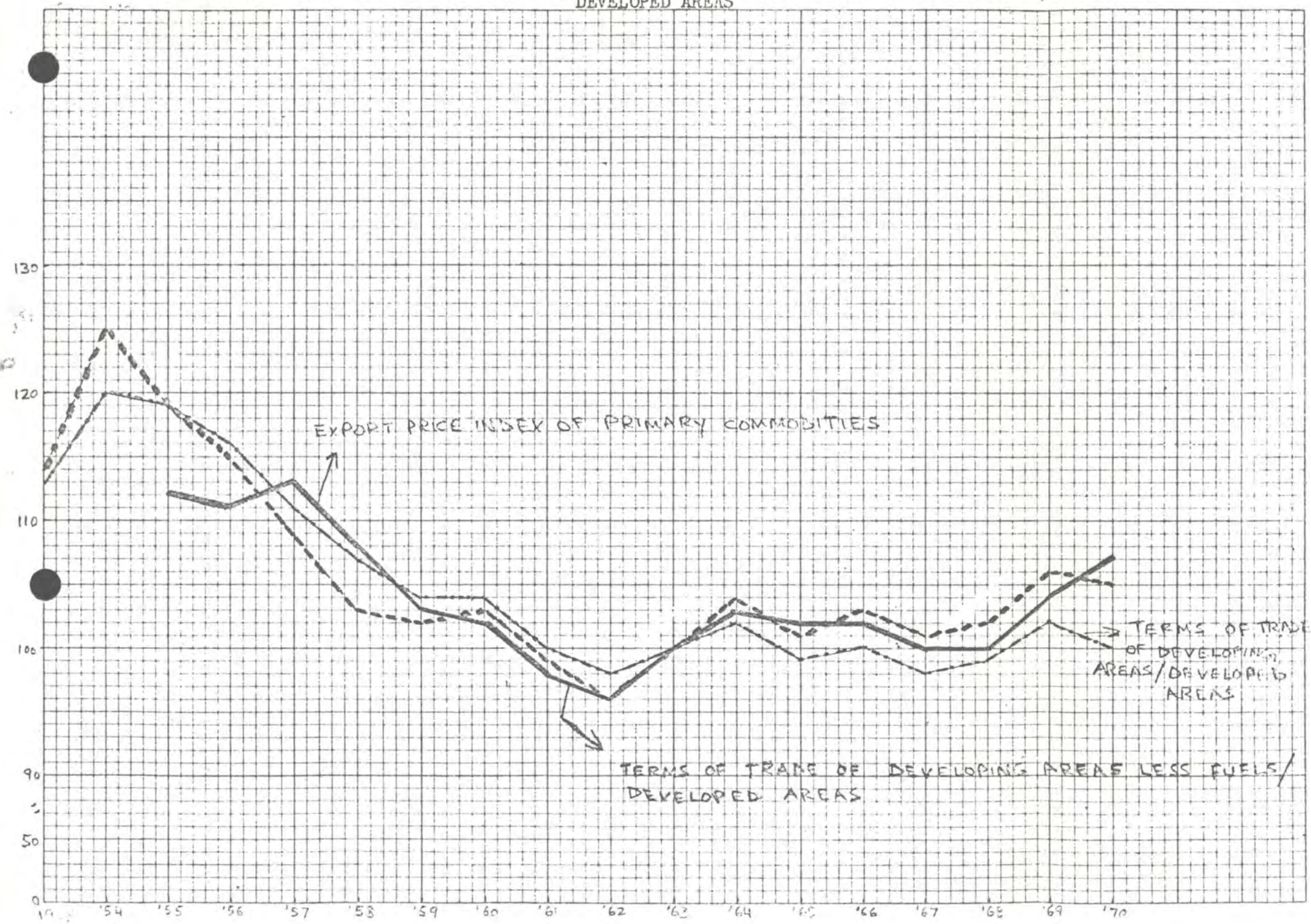
Diagram 2: UNIT VALUE INDEX OF LDC EXPORTS OF PRIMARY COMMODITIES AND LDC TERMS OF TRADE WITH DEVELOPED AREAS



INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

HBC File
HBC McN Sundries

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara, President DATE: June 14, 1974

FROM: Mr. S. Aldewereld, Vice President, Finance
Mr. Hollis B. Chenery, VP, Development Policy

SUBJECT: Euro-currency Markets

We have asked Messrs. Rotberg and Saxe to propose the best method of keeping you informed of developments in Euro-currency markets. They feel that a periodic report from the International Economy Division of the DPS (a sample covering the first quarter of 1974 is attached) supplemented with information from Mr. Rotberg would be the most effective procedure, as outlined in the attached memorandum from Mr. Saxe. We suggest that we start on this basis and that we review how well the system meets your requirements after a reasonable interval.

Attachments
Memorandum from Mr. Saxe
Publicized Euro-currency Credits

cc: Messrs. I.P.M. Cargill
J. Adler
E. H. Rotberg
J. Saxe

HBChenery:di

Mr. Robert S. McNamara, President June 3, 1974

Hollis B. Chenery, VP, Development Policy

Technical Note for Governors' Speech

1. Attached is a draft of the technical note for the 1974 Annual Speech. As you requested, it summarizes the principal points that emerge from the longer term energy paper and the 5-year program.

2. The present draft is weak on policy conclusions. This is in part because it is difficult to formulate them in the areas outside the Bank's operational concern without having a clearer idea from you as to how far you wish to go on such matters as trade liberalization and buffer stocks. In addition, the draft covers too wide a variety of subjects; once it is focused more sharply, the policy message also will become clearer.

3. I should like to meet with you after you have read the draft to discuss the direction and timing of the additional work.

Attachment

cc: Mr. William Clark
Mr. J. Maddux
Mr. E. Stern
Mr. W. Tims
Ms. E. Yudin

HBChenery:di

Mc 24

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara, President DATE: May 30, 1974

FROM: Hollis B. Chenery, VP, Development Policy

SUBJECT: Progress Report on the Energy Paper

To help in establishing the relations between the Bank's five year program and the forthcoming "energy paper", I attach the current outline of the latter and a draft of the introductory summary. Staff seminars on the four main sections will take place next week.

5/30

Attachment

cc: Messrs. Knapp, Cargill, Adler, Stern

HBChenery:di

Draft Outline
May 28, 1974

EFFECTS OF CHANGING TRADE PATTERNS ON DEVELOPMENT PROSPECTS AND CAPITAL REQUIREMENTS

fter/Editor			Dates Draft	Dates Seminar	Draft Pages
Chenery	I.	INTRODUCTION: THE NATURE OF THE ADJUSTMENT PROBLEM	6/10		3
	II.	CHANGES IN THE WORLD ECONOMY, 1970-1980	5/31	6/4	30
		Introduction			(2)
Tims/Chenery	A.	Recent Changes in Commodity Markets 1. Petroleum: 2. Other Primary Commodities:			(8)
Tims/Chenery	B.	Impact on Developed Countries and World Trade			(10)
Tims/Chenery	C.	Future Supply and Demand for Energy 1. Alternative Sources of Energy 2. Alternative Projections of Petroleum Prices			(10)
Karaosmanoglu/ Hulley	III.	DEVELOPMENT OF OPEC COUNTRIES	5/31	6/5	12
	A.	Growth and Absorption			
	B.	Accumulation of External Capital			
	IV.	ADJUSTMENT PROBLEMS OF DEVELOPING COUNTRIES	6/4	6/7	28
Tims/Chenery	A.	Growth Prospects and Capital Requirements			(8)
Ray/Hulley	B.	Internal Adjustment to Higher Energy Costs			(4)
Thompson/ Hulley	C.	Adjustment in Representative Countries			(8)
Tims/Saxe/ Hulley	D.	Impact on Creditworthiness			(8)
Vibert/Stern	V.	ROLE OF THE INTERNATIONAL COMMUNITY	6/6	6/10	15
		(Introduction)			(2)
	A.	Terms of Lending and Burden Sharing			(6)
	B.	Commodity Policy			(4)
	C.	Other Measures to Provide Additional Resources			(2)
		ANNEXES		Total	88*

I. Commodity Projections
II. World Supply and Demand for Energy (Section II C)
III. Growth of OPEC Countries (Section III)
IV. Growth Prospects of LDCs (Section IV A)
V. Sectoral Adjustment to Higher Energy Costs (Section IV B)
VI. Adjustment in Representative Countries (Section IV C)

MCN notebook

Mr. Robert S. McNamara

May 22, 1974

Messrs. H. B. Chenery and W. C. Baum

Rural Development Policy Paper: Draft Outline

1. In accordance with your request, there is attached a draft outline of the Rural Development Policy Paper.

2. Overall responsibility for preparation will be with the Agriculture and Rural Development Department. Mr. Turnham of that department will be mainly responsible for preparing the initial drafts: he will be assisted by other departmental staff and by DPS staff members, Messrs. Burki and Krishna.

3. Experience with earlier papers (e.g., agricultural credit and land reform) indicates that more time is required for staff discussion and review than has been allowed for. This is particularly likely to be the case for the rural development paper, which will be of considerable operational significance to regional staff. In other respects the present timetable is also likely to prove too tight. We therefore propose that the date of Board presentation, presently scheduled for October 29th, be slipped by two months. This would imply a staff review in the third week of October (presently scheduled for August 20th), your review in mid-November (presently scheduled for September 17th); distribution to the Executive Directors would be at the beginning of December (presently scheduled for October 1st).

Attachment

DTurnham/MFudelman:pdn

RURAL DEVELOPMENT POLICY PAPER

OUTLINE

A. Rural Development: A Multi-Dimensional Action Program Directed to the Alleviation of Rural Poverty /6 Pages/

A brief introduction summarizing the evolution of the Bank approach to Rural Development, to draw upon the Nairobi speech, Mr. Yudelman's Rural Development paper of January 1973, relevant discussions in the Rural Credit and Land Reform Policy Papers and other recent Bank papers, for example, those dealing with village electrification, rural water supplies and employment.

The thrust will be to discuss the possible multiple objectives of rural development but to bring the focus to raising the productivity of the rural poor. This will lead into an analysis of rural income distribution with special reference to "target groups"--notably the small-scale farmers (culminating with a workable definition). The task is to devise an effective minimum cost package for provision of significant benefits, mainly productive benefits, to as wide a segment of the rural poor as possible.

B. Design and Implementation of an RD Program /9 Pages/

This part will draw upon experience in and out of the Bank relating to ongoing or past programs, and attempt to distill from this experience some guidelines for improved project design (perhaps the crucial problem). As well as national commitment, emphasis will be given to the importance of a nationwide planning approach to RD, having regard to:

1. The need to determine specific program actions by reference to the overall availability of program resources, and the claims of other target groups or regions.

2. A time perspective that takes into account the likelihood that RD in many circumstances would only pay off after a long preparatory or gestation period.

3. Making the most effective use of the particularly scarce resources--managerial talent or technical services and foreign assistance.

The availability of such a national planning framework for rural development programs may have a considerable impact on the type of Bank support to be undertaken--for example, regarding the choice between single sector and multi-sectoral integrated approaches. But, in any event, there would be a need either to evaluate an ongoing overall program, or to construct a substitute for it. In this process the critical issues to be resolved relate basically to the determination of an appropriate level and mix of program elements, having regard, on one side, to the specifics of need among the small farmers and other target groups as related to ecological and societal characteristics, and, on the other side, to resource availability.

Questions for detailed consideration are:

1. Doing more to identify and promote the use of relatively less sophisticated (and less expensive) delivery systems in respect of agricultural services--credit, extension, etc.--and in respect of technology of agricultural hardware;

2. Making more appropriate use of social service elements in rural development projects;

3. Minimizing the recurrent cost burden to government of operating the facilities associated with RD programs;

4. Determining administrative and organizational arrangements to ensure (a) effective coordination at high levels; (b) appropriate decentralization of decision-making and day-to-day administration of the program to local levels; and (c) the promotion of institutional developments "from below" so that farming and other rural populace are given a chance to develop the type of social group action and rural institutions they best respond to and can be motivated by.

C. Issues Concerning Bank Group Involvement in Rural Development /9 Pages/

1. An overview of past and ongoing efforts, having regard to (a) lending programs for rural development; (b) country and sector studies; and (c) research. Separate consideration will be given to the regional dimension, where relevant, and lending operations will be examined in the light of the guidelines established in Section B of the paper in as much detail as possible.

2. Conclusions Based on the Overview:

   a. More effort is now focused on identification and preparation of rural development projects (refer to CPPs and regional submissions) than previously and operational procedures have also been clarified. (Refer to Burke Knapp memorandum of March 4, 1974).

   b. Experience shows, however, that while it is possible to prepare a limited number of RD projects with the degree of thoroughness generally expected in Bank projects, the type of specification described under Section B is hard to attain. For the Bank, rural development projects tend to be resource intensive relative to amount lent in terms of the effort necessary during preparation, appraisal and supervision. Problems reported during the implementation phase indicate that borrowing countries too sometimes have difficulties with them.

c. While general operational procedures are not a major difficulty, processes relating to the identification, preparation, appraisal and supervision of projects may need to be modified. For example, we should examine new approaches such as using rural development agencies as intermediaries for a wide range of sub-projects, lending through local governments, etc., to see whether this will facilitate reaching our goals.

d. There is also a need to develop a long-term approach toward rural development, including programs, countries and regions in which it would be most appropriate for the Bank to initiate action, having regard to the considerable country differences in receptivity to RD programs now.

D. A Five-Year Action Program for the Bank in Rural Development /6 Pages/

In the light of the above, actions will be proposed covering:

a. A tentative lending program.

b. Sector work.

c. Research on policy work.

d. The special country of concentration program.

e. Estimate of the impact of the program.

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

COPY FOR MCNAMARA NOTE-BOOK

TO: Mr. Robert S. McNamara, President DATE: May 22, 1974

FROM: Hollis B. Chenery, VP, Development Policy

SUBJECT: Revisions in the IBRD/IDA Program, FY74-78

I attach proposed revisions on a line-in, line-out basis. The major changes are in paragraphs 2.3-2.6 and in the discussion of creditworthiness (paragraphs 2.24-2.28). The changes are summarized and reasons given in the attached summary. We may have a few more suggestions at the time of the Friday discussion.

cc: Mr. Knapp, Senior VP
Mr. Adler, Director, P¢B
Mr. Saxe

HBChenery:di

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara, President DATE: May 8, 1974

FROM: Hollis B. Chenery, VP, Development Policy

SUBJECT: Progress Report on the July Energy Paper for the Board

1. Following the Board discussion of our Interim Report on the oil and commodity problem on March 19, you approved a draft outline and work program for the preparation of a July report to the Board covering the longer term aspects of this problem. This report is designed to provide a basis for better international understanding of the adjustment problems facing the developing countries as well as a background for the Bank's five year operational program. In the past month the immediate issues have been widely debated in the U.N. Special Session, but there has been relatively little attention to the structural changes required over the longer term.

2. The Bank work for the July paper has proceeded on schedule and the background papers requested are largely complete. I have held two rounds of discussions with the working groups preparing these papers and have tried to focus the proposed Board paper on aspects of the problem that are central to the Bank's lending policies and country programs.

3. An annotated outline of the proposed paper is attached. Before starting on the drafting, I would like to discuss it with you and have made an appointment for Wednesday, May 8 for this purpose. The subsequent schedule calls for a draft of the paper to reach you on June 10 (after staff discussion) and for submission to the Board by July 1.

Attachment

cc: Messrs. W.C. Baum
E. Stern
W. Tims
M. Haq

HBC:gss

"grace-full kept" complete with tables by 6/10.

Returned

AUG 5 1974

Revised Draft
H.B. Chenery
5/7/74

EFFECTS OF CHANGING TRADE PATTERNS ON DEVELOPMENT PROSPECTS AND CAPITAL REQUIREMENTS

A Report to the Board on changes in primary product markets and their consequences for developing countries and Bank operations

I. INTRODUCTION: THE NATURE OF THE ADJUSTMENT PROBLEM

A. Sources of Disequilibrium

-- Oil markets: increase in OPEC surplus to $65 billion in 1974.

-- Other primary products: major price increases in grains, fertilizer, metals,etc.

-- World inflation: now over 10%

B. Problems of Adjustment

-- Short term (1974-75): only capital flows, reduction in growth of demand and GNP. (Discussed in March Interim Report).

-- Medium term (1975-80): shifts in energy supply and demand, growth of absorptive capacity of OPEC countries, reallocation of investment and trade in OECD and LDC. Main focus of present paper.

-- Longer term (1980-85): limited analysis of energy prospects needed to evaluate medium term strategies.

C. Scope of Paper

-- Purpose: to provide analytical framework for international action by Bank, LDCs, and other agencies.

-- Focus: bring together principal elements in the adjustment process in global framework to determine magnitude and relative importance of several types of policy needed.

II. CHANGES IN THE WORLD ECONOMY, 1973-80

Introduction. Our analysis of the principal structural changes in the world economy is based on a study of the relations among three groups of countries--OECD, OPEC, and LDC--each of which is further subdivided into three or more sub-groups according to the needs of the analysis. The analysis starts from the changes in commodity markets and relative prices that have taken place in the last several years, which have produced the current trade imbalance. We then take up the main elements in the adjustment process for the medium term: (i) further changes in relative prices, (ii) adjustments in the supply and demand for energy, (iii) increasing absorptive capacity of the oil producing countries, and (iv) changes in the pattern of OECD investment, trade and growth. These changes in the world environment provide the basis for more detailed analysis of the developing countries in section III and of the needs for international action in section IV.

A. Changes in Commodity Markets and Relative Prices

1. Petroleum: recent price increases have raised the share of petroleum from 30% to 65% of the value of total world primary exports. Future adjustments in the volume and price of petroleum exports are considered in section B.

2. Other Primary Commodities: there have been rapid increases in prices and volumes in 1972-74, which are now expected to taper off. For selected commodities, projections will be made under two assumptions: expected prices with present market organization and possible increases in prices resulting from producer action or commodity agreements. The difference between the two will illustrate the possible scope for increased earnings from these agreements.

3. Manufactured Goods: prices of manufactured goods exports have been increasing at 10% per year. The rate of increase is expected to decline to 7% per year by the end of the decade.

B. World Supply and Demand for Energy

1. Alternative Sources of Energy. Summary of increased supplies expected from the principal alternative sources in the OECD countries (coal, oil, gas, nuclear power) at the present delivered cost of oil imports. These are based on OECD estimates for 1980 and 1985 as modified by the Bank. (Details given in Annex I).

2. Alternative Projections of Prices and Production. Since a difference of $1 per barrel in OPEC revenues is equal to $10 billion per year in the balance of payments deficit of the consuming countries, it is important to determine the probable price range as accurately as possible. In 1974 f.o.b. prices the likely range for 1980 is now thought to be between $8.60 (the present Persian Gulf price) and $7.00 with a possible rise in 1975-76 before declining. Alternative projections of demand and of supplies from non-OPEC and OPEC sources will be made on this basis. This range is somewhat lower than the present OECD projections but higher than those of Houthakker and other U.S. analysts. (Details of the projections will be given in Annex II).

C. Development of OPEC Countries

1. Growth and Absorptive Capacity. The prospective growth patterns of the OPEC countries will determine their needs for imports, attitudes toward price and output of petroleum, balance of payments surplus and willingness to finance flows to other developing countries. We have analysed the prospective growth of each country separately and will aggregate the results into three groups: Gulf States, intermediate countries (Iran, Algeria, Libya, Venezuela), and least developed (Indonesia, Nigeria). The balance of payments surplus of the OPEC group is predicted to fall from $63 billion in 1974 to $45 billion (in current prices) in 1980 on the high price assumption and to $35 billion on the lower price assumption. (Details in Annex III.)

2. Price and Production Behavior. The division of oil revenues among the producers will affect their willingness to maintain a given price policy. If Saudi Arabia is the only country that restricts production, it would have to hold its exports at about their current levels to maintain the present price level (in constant prices). Saudi Arabia would suffer from a reduction in its markets beyond 1980 because of the growth of non-OPEC energy sources and is therefore likely to try to hold prices down to the lower level, at which its exports and revenues will continue to rise. (An Annex is being prepared illustrating alternative production patterns for the OPEC countries, but we do not propose to include it in the Board document).

3. External Investment. We will estimate total external investment by OPEC countries in relation to total OECD investment and to LDC investment on the two price assumptions. (Uses of investment are taken up in section D).

D. Growth of OECD Countries

The effects of the adjustment process on the OECD countries will be analysed briefly in order to determine:

-- Alternative growth possibilities for 1974-80 (3.7% to 4.5%, compared to the past 4.8%) and investment requirements.

-- Inflation in international prices (14% in 1974, falling to 7.5% from 1976 onward). Domestic prices rise at about 10%.

-- Demand for imports from developing countries.

-- Capital inflows from OPEC countries (and possible uses?)

III. ADJUSTMENT PROBLEMS OF DEVELOPING COUNTRIES

A. Growth Prospects and Capital Requirements (Draft:Tims)

1. External Factors. Changes in commodity prices discussed in IIA will have a substantial effect on the foreign exchange availabilities and growth prospects of developing countries. These were analysed by income level in the Interim Report and have now been studied for seven regional groupings. Estimates of additional external capital requirements to maintain adequate rates of growth are on the order of $12 billion per year for the rest of the decade on favorable growth assumptions for the OECD.

2. Internal Adjustments and Growth Prospects. The more developed of the LDCs--Korea, Brazil, Yugoslavia, etc.--have substantial possibilities for reallocating resources and adjusting to worsened terms of trade fairly quickly. The least developed countries are less flexible and will take longer to adjust to increased import costs. These differences are discussed below and allowed for in the projections of growth prospects for several groups of countries. (Detailed projections in Annex IV).

B. Adjustment to Higher Energy Costs

We have studied the impact of higher energy costs on the principal sectors affected in some detail (results given in Annex V). On the whole the substitution possibilities in the developing countries are much more limited than in the

industrialized ones. Higher prices are expected to have their main impact on investment in alternative local energy sources, with relatively little effect on the growth of energy use. The main adjustment will therefore be on import substitution and export expansion elsewhere in the economy to absorb the higher cost of imported fuels.

C. Adjustment in Representative Countries (Draft:Thompson)

We have made detailed analyses of the adjustment prospects and effect on future growth in 16 selected countries, half of which are in the lowest income group. They illustrate several patterns of readjustment to the initial increased cost of oil, foodstuffs and other imports. These include: (i) increased investment in domestic energy sources; (ii) shift to more profitable primary exports; (iii) more rapid expansion of industrial exports; (iv) increases in borrowing at Bank terms. These general prospects will be summarized in the text with greater detail in Annex VI.

D. Impact on Creditworthiness (Draft:Saxe)

Several factors in the present situation have affected the prospective creditworthiness of developing countries: (i) the large increase in loanable funds generated by the oil exporter surpluses; (ii) the effects of world inflation on service on prior debt; (iii) changes in terms of trade of individual countries; (iv) greatly increased demands for capital to finance the transitional adjustment period. These will be analysed in general terms and applied to several representative countries to show the relative importance of different factors. As in the past, results will be given for groups of countries rather than individual cases.

IV. ROLE OF THE INTERNATIONAL COMMUNITY (Draft:Haq/Vibert)

(It is not clear at this point how much discussion of the possible reactions of the OECD and OPEC countries should be included in the present paper. Drafts are being prepared on the following topics).

A. Actions to Date (Introductory)

B. Terms of Lending and Burden Sharing

It is clear that the DAC approach of GNP shares is only relevant to long-term development loans but does not reflect the need for transitional assistance nor the differences in liquidity and short-term impact on different lenders. An approach combining the two types of factor will be discussed.

C. Commodity Policy

1. Short term reactions to food and fertilizer problems.

2. Role of commodity agreements and trade liberalization.

D. Other Measures to Provide Additional Resources.

A N N E X E S

I. World Supply and Demand for Energy (Section II B1)

II. Oil Production and Prices (Section II B2)

III. Growth of OPEC Countries (Section II C)

IV. Growth Prospects of LDCs (Section III A)

V. Sectoral Adjustment to Higher Energy Costs (Section III B)

VI. Adjustment in Representative Countries (Section III C)

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara, President DATE: May 2, 1974

FROM: Hollis B. Chenery, VP, Development Policy

SUBJECT: FY1975 DPS Budget

1. Pursuant to your budget instruction, P & B have reduced their earlier recommendation on the DPS budget for FY1975 to allow for no increase in staff, discretionary resources or research funds. Our budget, as originally agreed with P & B, took the constraints the Bank faces in FY1975 into account and, consistent with your guidelines, did not seek an increase of discretionary resources per staff member. There are, however, two areas in which we sought specific increases which I should like to discuss with you.

The International Economy Division

2. The Economic Analysis and Projections Department was created in October 1972 to centralize the Bank's data collection and projections work and to place our analysis in the context of evolving world economic trends. Since then, the oil crisis and the rise in commodity prices have increased the need to view prospects for LDC growth and trade in the context of demand in industrialized countries, trade and aid policies, and worldwide inflation. The available staff in this department is far from adequate to collect the data and prepare an analysis of the world economic outlook. In the FY1974 budget proposal, we proposed staff for this purpose but, within the limited slots available, had to give priority to strengthening the work on economic and social data.

3. This year has demonstrated the importance of this function as well as our limited capability. While we utilize fully the work of the IMF and the OECD, this does not meet our requirements, since the analyses of both organizations have a different focus. The assessment of the second round impact of higher energy costs, the demand effects of high rates of inflation over an extended period of time, and the evolution of capital markets all require considerable analysis on our part and an ability to link them to the prospects of developing countries.

4. To meet these needs, we propose to establish an International Economy Division, separate and distinct from the work on debt and financial flows which will continue to be the function of the International Finance Division. (A proposed restructuring of other aspects of the department is now under discussion with Mr. Kearns but does not bear directly on the proposed new division). The two divisions

would have the following functions:

International Economy Division. The division would be responsible for:

- analyzing and projecting economic growth in industrialized countries, relying to a maximum extent on the work of other organizations;

- assessing the effect of trade policies on exports from developing countries;

- analyzing and projecting international trade in goods and services to provide a global framework for Bank estimates of developing country prospects.

~~International Finance~~ Division (called the International Economy Division in FY1974). The division would be responsible for:

- collecting data on capital flows and debt;

- preparing creditworthiness analyses for the Bank's country lending programs;

- extending the coverage of the debt reporting system to the Euro-currency market and other private flows;

- analyzing alternative forms of lending.

5. We estimate the net increase in staff required, after taking into account internal adjustment of priorities, at 5 professionals, including one in the Commodities Division which would be assigned responsibility for trade in manufactured products. Given the budget stringency, it may be possible to start the division with one less staff position than planned, and a further adjustment of other work could yield another position--but an increase of 3 professional staff positions is the minimum necessary. We have gone about as far as possible in trying to do this work with temporary assignments, utilizing partial time of

selected staff. Given the importance of the ongoing changes in the world economy to the Bank, I think that the creation of the International Economy Division is essential.

Research Budget

6. The second issue relates to the research budget. The Board discussion of the program clearly indicated support for an enlarged effort, and you indicated that 1-2% of the Bank's budget might be an appropriate level. The 1974 program is $1,750,000 and in earlier discussions with P & B, we had reached agreement on a level of $2.1 million in 1974 dollars. Although there is a sound basis for an expansion of this magnitude, in view of the budget situation it is of course necessary to review all priorities. However, no increase in real terms seems to me inconsistent with the substantive achievements of the program and the expressed views of both Management and Directors.

7. I would suggest therefore a FY1975 research program of $1,900,000 (in 1974 dollars). This is a modest increase (8%) for this program. The External Research Program is only in its third year and it has taken time to institute the necessary quality control and educate the staff to the standards expected. The pipeline of operationally oriented research proposals is growing steadily. To allow for no increase in resources, in real terms, would force the rejection of projects in high priority areas and retard the development of this program on which much of our intellectual leadership rests.

cc: Mr. J. Adler
Mr. Stern
Mr. Tims
Mr. Gulhati
Mr. Haq
Mr. Duloy

EStern:HBChenery:gss

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Messrs. Alter, Bell, Benjenk, Chaufournier, S.S. Husain, Weiner } Hand-carried 2 p.m.

DATE: April 25, 1974

FROM: Hollis B. Chenery, VP-DP HBC

SUBJECT: Revised Lending Program for FY1974-78

Mr. McNamara has authorized me to circulate to you my comments on the Regional programs as summarized in P & B memos of April 16, 17 and 18. I understand from Mr. Knapp that he will be having meetings with you early next week to discuss possible revisions in these programs.

Attachment

cc: Mr. Knapp

HBC:di

bcc: Stern, Nag, Chenery

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

Returned 5/15 Xeroxed to ES

MCN notebook

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara, President DATE: April 23, 1974

FROM: Hollis B. Chenery, VP, Development Policy

SUBJECT: Revised Lending Program for FY1974-78

1. Our Interim Report of March 5 defined the changes in the world economy that necessitate a revision in our previous five-year program in the following terms:

- More rapid inflation requires an increase in Bank lending (and borrowing) in current prices; it will also cut the value of the IDA program by some 10%.

- The adverse consequences of the changes in relative prices of oil, other raw materials, and manufactured goods will be concentrated in an identifiable group of "most affected" countries; the principal ones are listed in table 9 of the Interim Report. Additional financing of $10 billion--half on intermediate or concessionary terms--was estimated to be needed for the two years 1974 and 1975, with increasing amounts through 1978.

- A number of countries that have been receiving IDA funds are benefitting from these price changes and now have increased creditworthiness for Bank borrowing.

2. A full response by the Bank Group to these changed circumstances will require revision of the lending rate, since (a) the present rate is too low to provide an adequate surplus over expenses; (b) the anticipated grant equivalent of the present rate has risen from perhaps 25% to 50% as a result of accelerated inflation, equal to a fall in the real rate from 5% to 2-3%. (This form of comparison must be adjusted for changes in the terms of trade for individual countries; the real rate would be harder for a country such as India.) Whenever it is politically feasible, a shift to a dual rate structure (or third window) would permit the Bank to respond more adequately to the needs of its borrowers. In the meantime, we should recognize the softening of Bank terms that has taken place (even if the rate is raised somewhat) in our assessment of creditworthiness for future Bank lending.

Criteria for Allocation of Bank and IDA Funds

3. There are several ways in which the Bank/IDA can adjust lending criteria to meet the changed world situation:

	FY75	76	77	78	74-78
DPS	780	940	970	300	
Reg	60 / 140	60 / 180	60 / 210	60 / 240	770

(a) Reserve IDA for the poorest countries and those most seriously affected by the changed terms of trade.

(b) Reduce IDA and expand Bank lending to countries whose creditworthiness for the (now softer) Bank terms has improved.

(c) Expand Bank lending to countries that are creditworthy and have been negatively affected by changes in their terms of trade.

(d) Shift toward more rapidly disbursing forms of lending to countries having inadequate access to other sources of funds to meet current account deficits induced by price changes.

4. While these needs and opportunities were suggested in the Interim Report and in the instructions to the Regions for revision of their lending programs, the response has on the whole been quite limited. The increase in Bank lending in constant dollars is less than $100 million per year, considerably less than the loss in the value of IDA through higher rates of inflation. None of the four means of readjusting to the changed needs of the borrowers has been fully utilized. Furthermore, it is unlikely that the "bottom up" approach that has been followed in proceeding from projects to country totals to regional totals will produce an adequate readjustment in the Bank/IDA program without more explicit guidance based on an overall assessment of these preliminary results.

Suggested Revisions

5. Application of the above criteria leads to a number of possible revisions in the lending program. These should be treated as illustrative, since they have not been discussed with the Regions. We have focussed primarily on FY75, rather than the five-year period, both because it is operationally more relevant and because we have more information as to the nature of the lending program and financial needs of the developing countries for this year. We are also preparing a summary table for the period FY74-78, by Regions, which reflects the adjustments that we think should be made in the lending program to be submitted to the Board.

Reallocation of IDA

6. It should be possible to reduce or eliminate IDA allocations to several marginal countries (Indonesia, Philippines, Thailand, Zaire, Morocco and Bolivia) in order to release IDA resources for more seriously affected borrowers such as Bangladesh, India and some of the small least developed countries in Africa. Our concrete proposals to reallocate

about $155 million of IDA in FY75 are given in Annex I. Similar reductions should be made in future years unless more concessionary resources become available. In most cases these IDA cuts should be made up by increased IBRD lending, since the countries concerned can absorb more Bank funds. In some cases, we must also consider whether the termination of IDA would seriously compromise the social aspects of the existing lending program or our leverage with the country concerned.

Increased IBRD Lending

7. We have identified a number of possibilities for increased IBRD lending. The amounts will depend somewhat on future changes in terms. Our specific suggestions for increasing the IBRD program by about $540 million for FY75 are given in Annex II. In many cases these increases can be absorbed by raising the proportion of the project cost to be covered by the Bank. In addition, it appears that the Regions have not made an adequate adjustment for the probable increases in the cost of projects; a correction for this factor could easily add another 7 or 8 percent to the IBRD program in FY76-78. I think that a request to the Regions to reexamine this aspect could easily result in a higher financial lending program for the assumed level of operational activity; such a reexamination can be completed in a fairly short time.

Lending to OPEC

8. It is questionable whether the oil exporting countries should account for some 20 percent of the proposed increase in IBRD lending for FY74-76. While some of the OPEC countries are large potential sources of Bank borrowing and are likely to request Bank development assistance, the amount of lending seems excessive for this purpose. I propose a cut of at least $50 million each in the allocations for Algeria and Iran in FY75 and a somewhat larger annual reduction in the total for the OPEC countries for the five-year period.

Forms of Lending

9. Given the need for quick disbursements to cover the increased payments gap in the problem countries, the proposed expansion of program lending to $500 million, or 10 percent of the total commitments in FY75, is quite modest. We have identified additional possibilities for program lending of some $250 million in FY75 which are listed in Annex III. These suggestions are based on an analysis of countries which have been most severely affected by the energy situation and have inadequate access to other sources of funds. Program lending

has been suggested against both IDA and IBRD funds, although it would probably not be necessary to show such a breakdown in the Board paper.

Total Program

10. Our tentative suggestions for the overall size of the lending program for FY74-78 are summarized in Annex IV. If the size of the program is increased in this fashion, it would lead to an increase in Bank lending of a magnitude commensurate with the analysis of requirements given in the Interim Report. Such a response on the part of the Bank/IDA is important to our effort to secure a more adequate response from other sources.

Attachments

cc: Messrs. Knapp
Cargill
Aldewereld
Adler
Stern
Haq

HBChenery:MHaq:di

Annex I

ILLUSTRATIVE MODIFICATIONS IN FY75 IDA ALLOCATIONS
(Million $)

A. Candidates for Reduction

	Allocation Suggested by Regions	Proposed Cut	Proposed Allocation
Indonesia	35	35	-
Philippines	20	20	-
Thailand	35	35	-
Uganda	25*	25	-
Zaire	40	25	15
Morocco	10	10	-
Bolivia	11	5	6
	175	155	21

B. Candidates for Increase

	Allocation Suggested by Regions	Proposed Increase	Proposed Allocation
Bangladesh	145	45	190
India	570	70	640
Reserve Pool (for small poorest countries worst hurt, particularly in Africa)**	75	40	115
	790	155	945

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* Assuming the zero lending program for Uganda releases at least one-third of its $75 million IDA IV allocation.

** Possibly including: Somalia, Rwanda, Chad, Upper Volta, Niger, Mali, Mauritania.

Annex II

ILLUSTRATIVE MODIFICATIONS IN FY75 IBRD ALLOCATIONS
(Million $)

A. Candidates for Increase

	Allocation Suggested by Regions	Proposed Increase	Proposed Allocation
India	60	140	200[1/]
Korea	300	50	350
Philippines	171	20	191
Thailand	106	35	141
Zaire	80	25	105
Mexico	197	60	257
Colombia	60	65	125
Chile	40	30	70
Lebanon	-	20	20
Panama	11	15	26
Uruguay	10	25	35
Tanzania	25	30	55
Guyana	3	5	8
Cameroon	10	15	25
Bolivia	6	5	11
	1,079	540 - 180 = 444	1,619

B. Candidates for Reduction

Algeria	203	50	153
Iran	267	50	217
	470	100	370

1/ For the subsequent years of the FY74-78 period, the allocation is projected to rise progressively to $380 million by FY78.

Annex III

ILLUSTRATIVE ADDITIONS TO PROGRAM LENDING FOR FY75
(million $)

Country		Allocations Suggested by Regions[1/]	Proposed Increase	Total
Uruguay	IBRD	-	25	25
Guyana	IBRD	3	5	8
India	IDA	100	100	200
Bangladesh	IDA	40	40	80
Korea	IBRD	100	50	150
Tanzania	IBRD	-	30	30
Sri Lanka	IDA	25	-	25
Laos	IDA	12	-	12
Vietnam	IDA	50	-	50
Egypt	IDA	65	-	65
Jamaica	IBRD	15	-	15
Kenya	IBRD	50	-	50
Chile	IBRD	40	-	40
Totals	IBRD	208	110	318
	IDA	292	140	432
GRAND TOTAL		500[1/]	250	750

1/ From E Tables.

REGIONAL SUMMARY - ILLUSTRATIVE MODIFICATIONS IN THE REVISED LENDING PROGRAM FY74-78
(Million $ in Current Prices)

Region	Regions Proposals Table E IBRD	IDA	TOTAL	DPS Proposals[1] IBRD	IDA	TOTAL	Proposed Change IBRD	IDA	TOTAL
EASTERN AFRICA	1,526	1,502	3,028	1,718	1,304	3,022	+192	-198	-6
WESTERN AFRICA	1,692	733	2,425	1,807	900	2,707	+115	+167	+282
ASIA	5,262[2]	5,233	10,495	7,037	5,318	12,355	+1,775[3]	+85[4]	+1,860
EMENA	7,360	640	8,000	6,955	610	7,565	-405[5]	-30	-435
LATIN AMERICA & CARIBBEAN	6,717	200	6,917	8,128	176	8,304	+1,411[6]	-24	+1,387
TOTAL	22,557	8,308	30,865	25,645	8,308	33,953	+3,088	-	+3,088
P & B Adjustment Factor	.924	.989	.942	.924	.989	.942			
Adjusted TOTAL	20,850	8,217	29,067	23,696	8,217	31,913	+2,846	-	+2,846

1/ Based upon country analysis of needs and possibilities as well as an adjustment correcting for underestimation by the Regional Offices of the inflation impact on project costs in FY75-78.
2/ Regional lending program estimate used by P & B.
3/ Includes increased lending of $770 million for India, $145 million for Thailand, $125 million for Korea, and $80 million for the Philippines.
4/ Result of IDA reallocations shown in Annex I and projected to FY78.
5/ The decline largely reflects proposed cuts in OPEC countries.
6/ The increase largely reflects proposed additions to the Mexico program and the restoration of the Brazil lending program as of December 1973.

I. REGIONAL BREAKDOWN OF PRD ADJUSTMENT FOR PROJECT COST UNDERESTIMATION

Region	FY75	FY76	FY77	FY78	FY74-78
EAST AFRICA			4	6	10
WEST AFRICA	10	20	30	40	100
ASIA	10	25	40	55	130
EMENA		5	8	12	25
LAC	35	95	170	235	535
TOTAL	55	145	252	348	800

II. REGIONAL DISTRIBUTION OF DPS PROPOSED CHANGES IN LENDING PROGRAM (PERCENT)

	IBRD	IDA	TOTAL
EAST AFRICA	12.6	-13.2	-0.2
WEST AFRICA	6.8	22.8	11.6
ASIA	33.7	1.6	17.7
EMENA	-5.5	-4.7	-5.4
LAC	21.0	-12.0	20.1
TOTAL (FROM E TABLES)	13.7	-	10.0
ADJUSTED TOTALS	13.6	-	9.8

WESTERN AFRICA - ILLUSTRATIVE MODIFICATIONS IN REVISED LENDING PROGRAM 1974-78
($ Millions in Current Prices)

		FY75		FY76		FY77		FY78		FY74-78 Program		
		Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Change
Cameroon	IBRD	9.5	25.0	58.5	58.5	35.0	35.0	55.0	55.0	206.5	222.0	+15.5
	IDA	7.5	7.5	11.5	11.5	23.0	23.0	17.0	17.0	83.0	83.0	-
Other Countries	IBRD	279.0	279.0	335.0	335.0	304.0	304.0	437.0	437.0	1,485.0	1,485.0	-
	IDA 1/	128.5	166.5	115.0	153.0	125.0	163.0	180.0	232.0	650.5	816.5	166.0
TOTAL Region	IBRD	288.5	304.0	393.5	393.5	339.0	339.0	492.0	492.0	1,691.5	1,707.0	+15.5
	IDA	136.0	174.0	126.5	164.5	148.0	186.0	197.0	249.0	733.5	899.5	166.0
	IBRD/IDA	424.5	478.0	520.0	558.0	487.0	525.0	689.0	741.0	2,425.0	2,606.5	181.5

1/ Including $166 m. IDA from reserves pool.

EASTERN AFRICA - ILLUSTRATIVE MODIFICATIONS IN REVISED LENDING PROGRAM FY74-78
($ Millions in Current Prices)

		FY75		FY76		FY77		FY78		FY74-78 Program		
		Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Change
Botswana	IBRD	-	-	7.8	10.8	0.5	3.5	4.9	4.9	20.7	26.7	+6.0
	IDA	-	-	3.0	-	3.0	-	-	-	6.0	-	-6.0
Tanzania	IBRD	25.0	55.0	24.0	34.0	23.0	31.0	10.0	16.0	105.8	159.8	+54.0
	IDA	40.0	40.0	31.0	31.0	34.0	34.0	49.0	49.0	186.0	186.0	-
Uganda	IDA	-	-	38.0	-	37.0	-	40.0	-	115.0	-	-115.0
Zaire	IBRD	80.0	105.0	14.2	44.2	22.6	42.6	69.2	116.2	186.0	308.0	+122.0
	IDA	40.0	15.0	45.0	15.0	35.0	15.0	62.0	15.0	192.0	70.0	-122.0
Sub-Total	IBRD	105.0	160.0	46.0	89.0	46.1	77.1	84.1	137.1	312.5	494.5	+182.0
	IDA	80.0	55.0	117.0	46.0	109.0	49.0	151.0	64.0	499.0	256.0	-243.0
Other Countries	IBRD	224.3	224.3	230.1	230.1	286.1	286.1	222.4	222.4	1,213.6	1,213.6	-
	IDA 1/	201.5	211.5	170.5	180.5	203.5	213.5	251.0	266.0	1,003.0	1,048.0	+45.0
TOTAL	IBRD	329.3	384.3	276.1	319.1	332.2	363.2	306.5	359.5	1,526.1	1,708.1	+182.0
	IDA	281.5	266.5	287.5	226.5	312.5	262.5	402.0	330.0	1,502.0	1,304.0	-198.0
		610.8	650.8	563.6	545.6	644.7	625.7	708.5	689.5	3,028.1	3,012.1	-16.0

1/ Include $45 million IDA from Reserves Pool for period 1975-78.

ILLUSTRATIVE MODIFICATIONS — THE REVISED LENDING PROGRAM FY74-78

($ millions in current prices)

	FY74		FY75		FY76		FY77		FY78		FY74-78 Program		
	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l Prop.	DPS Prop.	Reg'l. Prop.	DPS Prop.	Change
Region (E Table-New)													
IBRD	910.4	910.4	971.0		1327.0		1680.0		1828.0	1828.0	6716.4		
IDA	37.3	37.3	51.0		24.0		47.0		41.0	41.0	200.3		
IBRD/IDA	947.7	947.7	1022.0		1351.0		1727.0		1869.0	1869.0	6916.7		
Mexico IBRD			197.0	257.0	329.0	399.0	369.0	444.0	317.0	362.0	1521.0	1771.0	+250.0
Panama IBRD			11.0	26.0							94.0	109.0	+15.0
Uruguay IBRD			10.0	35.0							108.5	133.5	+25.0
Colombia IBRD			60.0	125.0							714.2	779.0	+64.8
Brazil IBRD	234.0	246.0	390.0	514.0	330.0	527.0	510.0	605.0	560	625.0	2024.0	2517.0	+493.0
Guyana IBRD			(3.0)	(8.0)							(53.7)	(58.7)	(+5.0)
IDA			(4.0)	(4.0)							(9.0)	(9.0)	(-)
IBRD/IDA			7.0	12.0							62.7	67.7	+5.0
Bolivia IBRD			(6.0)	(11.0)	(10.0)	(15.0)	(10.0)	(17.0)	(33.0)	(40.0)	(59.0)	(83.0)	(+24.0)
IDA			(11.0)	(6.0)	(10.0)	(5.0)	(12.0)	(5.0)	(12.0)	(5.0)	(57.2)	(33.2)	(-24.0)
IBRD/IDA			17.0	17.0	20.0	20.0	22.0	22.0	45.0	45.0	116.2	116.2	0
Total above countries: IBRD	234.0	246.0	677.0	986.0	669.0	941.0	889.0	1066.0	910.0	1027.0	4574.4	5451.2	+876.8
IDA	-	-	15.0	10.0	10.0	5.0	12.0	5.0	12.0	5.0	66.2	42.2	-24.0
Total	234.0	246.0	692.0	996.0	679.0	946.0	901.0	1071.0	922.0	1032.0	4640.6	5493.4	+852.8
All other countries with no changes:													
IBRD	676.4	676.4	294.0	294.0	668.0	668.0	838.0	838.0	918.0	918.0	2142.0	2142.0	0
IDA	37.3	37.3	36.0	36.0	14.0	14.0	35.0	35.0	29.0	29.0	134.1	134.1	0
IBRD/IDA	713.7	713.7	330.0	330.0	682.0	682.0	873.0	873.0	947.0	947.0	2276.1	2276.1	
Region: Regional vs. DPS Proposal:													
IBRD	910.4	922.4	971.0	1280.0	1327.0	1609.0	1727.0	1904.0	1828.0	1945.0	6716.4	7593.2	+876.8
IDA	37.3	37.3	51.0	46.0	24.0	19.0	47.0	40.0	41.0	34.0	200.3	176.3	-24.0
IBRD/IDA	947.7	959.7	1022.0	1326.0	1351.0	1628.0	1727.0	1944.0	1869.0	1979.0	6916.7	7769.5	+852.8
Additional Inflationary Adjustments												+535.0	+535.0
New Total: IBRD												8128.2	1411.8
IDA												176.3	-24.0
IBRD/IDA												8304.5	1387.8

EMENA: Suggested Program Changes

		FY75		FY76		FY77		FY78		FY74-78		
		Reg.	DPS	Reg.	DPS	Reg.	DPS	Reg.	DPS	Reg.	DPS	Change
ALGERIA	IBRD	203	153	200	160	220	170	230	180	932	742	-190
FINLAND	IBRD			50	-					70	20	-50
IRAN	IBRD	267	217	200	150	180	120	130	80	985	775	-210
LEBANON	IBRD	-	20							80	100	+20
MOROCC	IBRD					UNCHANGED						
	IDA	10	-	10	-	10	-			30	-	-30
SUBTOTAL:	IBRD	470	390	440	310	400	310	360	260	2067	1637	-430
(5 Countries)	IDA	10	-	10	-	10	-			30	-	-30
Regional Total:	IBRD	1323	1243	1525	1385	1680	1590	1738	1638	7360	6930	-430
	IDA	127	117	125	115	120	110	162	162	640	610	-30
TOTAL:		1450	1350	1650	1500	1800	1700	1900	1800	8000	7540	-460

ILLUSTRATIVE MODIFICATIONS IN THE REVISED LENDING PROGRAM FY74-78
($ millions in current prices)

Countries		FY75 Reg'l Prop.	FY75 DPS Prop.	FY76 Reg'l Prop.	FY76 DPS Prop.	FY77 Reg'l Prop.	FY77 DPS Prop.	FY78 Reg'l Prop.	FY78 DPS Prop.	FY74-78 Program Reg'l Prop.	FY74-78 Program DPS Prop.	Change
Bangladesh	IDA	145	190	145	190	145	190	205	225	714.1	869.1	+155.0
India	IBRD	60	200	60	240	60	270	60	300	240.0	1010.0	+770.0
	IDA	570	640	570	640	570	640	800	850	2875.0	3135.0	+260.0
Indonesia	IBRD	261 (250)	261	380 (325)	380	430 (400)	430	565 (400)	565	1711.0 (1375)	1711.0	-
	IDA	35	-	35	-	35	-	-	-	186.0	81	-105.0
Korea	IBRD	300	350	200	225	220	245	230	255	1044.0	1169	+125.0
Philippines	IBRD	171	191	240	260	240	260	235	255	1041.6	1121.6	+ 80.0
	IDA	20	-	20	-	20	-	20	-	89.5	9.5	- 80.0
Thailand	IBRD	106	141	119	154	125	160	156	196	644.0	789.0	+145.0
	IDA	35	-	35	-	35	-	40	-	152.0	7.0	-145.0
Total	IBRD	898	1143	999	1259	1075	1365	1246	1571	4680.6	5800.6	-1120.0
	IDA	805	830	805	830	805	830	1065	1075	4016.6	4101.6	+ 85.0
Other countries	IBRD	192	192	247	247	220	220	222	222	1106.8	1106.8	-
	IDA	237	237	249	249	270	270	373	373	1216.3	1216.3	-
Total all countries			+ 245		+ 260		290		320			
	IBRD	1090	1335	1246	1506	1295	1585	1468	1793	5787.4	6907.4	+1120.0
After interim adjustments made by Region		-98		-113		19				-525		
		992		1133		1176		1335		5262.0		+1645.4
	IDA	1042	1067	1054	1079	1075	1100	1438	1448	5232.9	5317.9	+ 85.0

RSM notebook

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: April 18, 1974

FROM: Warren Baum and Hollis Chenery

SUBJECT: Board Paper on Fertilizer

1. The staff review of the Fertilizer Policy Paper on April 17 raised several controversial issues. We met with Messrs. Stern, Qureshi, Haq, van der Tak, Fuchs and Yudelman to determine how much revision would be needed to resolve these issues and how long it should take. We concluded, and Mr. Qureshi agreed, that the revisions would take about one week and that a new draft could be submitted to you by Friday, April 26.

2. We will be glad to discuss this at your convenience.

HBChenery:WBaum:di

President has seen

April 3, 1974

ENERGY, RAW MATERIALS AND DEVELOPMENT

Notes on the Agenda of the Special Session
of the U.N. General Assembly

INTRODUCTION

Although the world's attention has focused on the rise in the price of petroleum and its consequences, this is only the most dramatic aspect of a general shift from surpluses to scarcities of many primary products. The resulting changes in relative prices have favored the development of some countries while hampering the continued growth of a large majority. Since these changes have been concentrated in the past few months, the nature of the adjustment process that is required to restore a process of orderly development is still a matter of debate.

The Special Session of the General Assembly provides an opportunity to clarify the relations between these commodity questions and the broader problems of development. The objectives of international action should be twofold -- (a) to bring about a readjustment in trade and production patterns that will restore orderly growth processes, while safeguarding the weaker economies that have suffered from the recent rise in commodity prices, and (b) to reassess the volume and sources of real resource transfers to the developing countries in light of the changed international economic situation. Before considering appropriate forms of international action, it is important to have a clearer understanding of the nature of the forces that have led to the present situation.

DIAGNOSIS

The basic factor underlying recent increases in prices of primary products is the unprecedented growth of the world economy since 1960 and particularly that of the industrial countries since 1970. Since the prices of several years ago did not signal the future growth of demand, the specific shortages of today are largely attributable to the long lead times required to increase primary production and processing capacity. Given the past history of oversupplies of wheat, fertilizer, petroleum products, etc., together

with the low price elasticity of demand, it is quite understandable that supply did not keep up with the accelerated growth in demand. The large increases in price for a number of commodities are the result.

While these phenomena may be regarded as largely a consequence of rapid growth, they have been augmented by several fortuitous events, most notably the effects of the Middle East war on the oil producers and the combination of bad weather and crop failures in several countries that produced the grain crisis in 1973. In both wheat and oil these events accelerated the evolution of forces already at work. It is therefore not reasonable to seek a return to the supply and price conditions of 1970. Instead, it is necessary to make up the deficiencies in investment and productive capacity in shortage areas -- grains, fertilizer, some metals, energy sources -- and to facilitate the reallocation of resources that is needed to restore a process of normal growth with higher energy costs.

Studies conducted in the World Bank, the OECD and elsewhere lead to the following conclusions as to the likely consequences of the energy crisis:

(i) Petroleum and natural gas have been undervalued in relation to future demands and alternative sources of supply; as a result they have replaced other sources of energy in the industrial countries to an undesirable degree.

(ii) Given the lead time of 5-10 years or more for the development of alternative energy sources, a rise in marginal energy prices to the level needed to stimulate these developments is desirable. This level also has considerable appeal as a basis for a "reasonable" world price for oil. Current estimates of the marginal cost of substantial alternatives to OPEC oil imports are in the range of $7-9 per barrel (in 1973 prices) in the industrial countries as compared to the present landed cost of imports from the Persian Gulf of $10 per barrel. Opinions differ as to whether the OPEC price could be temporarily reduced below this level, but the probability of a substantial reduction seems low.

(iii) The current level of oil prices will produce an increase in the value of oil exports of the OPEC countries of about $60 billion in 1974 and $75 billion in 1975 compared to 1973 revenues of $23 billion. This is the equivalent of a transfer to them of over 1.5% of world GNP and 10% of the total value of world exports. While the total resource cost will not be a serious impediment to growth once demand and production patterns have adjusted to it, the balance of payments impact amounts to 15-20% or more of total foreign exchange supplies in a number of developing countries and will require some difficult adjustments in world trade patterns. During the period of trade adjustment, there is a real danger of major trading countries adopting incompatible policies that will hamper the growth of total world output.

(iv) In a third of the principal developing countries and most of the developed ones, the oil impact will be largely offset by increased export earnings plus ready access to external capital, and their development prospects will not be seriously affected. International action should therefore focus on the problems of the remaining countries (which contain over a billion people) for which the transition to a viable balance of payments position will be difficult.

In most commodities other than oil the combination of reduced growth of demand in the next 2-3 years and increased supply is expected to check the rise in prices and lead to a considerable fall in the terms of trade of most producer countries from their present favorable levels. The principal commodities for which there is cause for concern about supplies in the medium term are petroleum, grains and fertilizer.

As pointed out in the Bank's Interim Report, the impact of changes in commodity prices on developing countries has been very uneven. Countries that are not large exporters of minerals or other products in short supply have suffered from a substantial worsening in their terms of trade. Even assuming that growth rates in the United States and other advanced countries are quickly restored to normal levels, we project that the growth of many of the poorest and most

populous countries will be substantially reduced because of the higher cost of their imports and their limited supplies of foreign exchange. In the absence of international action to offset this effect, this group of poor countries is likely to suffer most severely from the subsequent adjustments in the world economy. Some of them could even suffer negative growth in per capita incomes for the remainder of the decade.

TYPES OF INTERNATIONAL ACTION

The preceding diagnosis suggests that the most useful focus for discussing the commodity problem at the Special Session would be the types of international action that would facilitate the needed structural changes and move the world economy to a condition of orderly and equitable development. The kinds of international action that have some chance of success are likely to be those which increase total world income and from which most countries stand to benefit.

Two kinds of international action to deal with the commodity problem need to be considered:

- short-term measures to mitigate the effects of high prices or shortages of food, fertilizer, oil, etc., on countries that do not have the means to secure them.

- measures to facilitate the internal and external adjustments in the economic structure that are necessary for a resumption of orderly development.

The adjustment process will require a period of several years in both the consuming countries that have suffered and the producers that have benefited from the rise in commodity prices. There are 7-8 OPEC countries that will not be able to make full use of their additional resources for their own development in the next five years, while there are a number of developing countries (including India, Bangladesh, Sri Lanka, Kenya, the Philippines, Thailand, Korea and several smaller poor countries) in which it will take several years to bring about the needed reallocation of resources. Some of the industrial countries will also need to finance large additional import costs. Since the commodity boom is expected to taper off in the next year or two and be followed by a worsening of terms of trade for most primary producers (apart from the oil exporters), a number of other developing countries will then face similar adjustment problems.

Short-Term Measures

Although the increased balance of payments deficits of the advanced countries can be financed more or less automatically through the capital markets, this is not true of most of the developing countries. As pointed out in the Bank's Interim Report, special measures will be needed to provide the additional $10 billion that they will require in the two-year period 1974-75 to maintain their development programs, and only half of this amount can be financed at conventional terms. The magnitude of the requirement is such that some contribution is needed from both the OPEC countries and the industrial countries.

The need for additional lending on concessional terms is estimated in the Interim Report to be about $3 billion in 1975 and somewhat larger in each of the next several years. One means to finance this requirement would be through a tax on oil exports. If the full amount were financed in this way, it would require a tax of 25 cents per barrel at the export volumes projected for 1975. The burden of such a tax would be shared between oil producers and consumers. In effect, some of the OPEC countries are moving in this direction by making concessional loans to developing countries to finance the increased cost of petroleum imports.

Although it may appear to the advanced countries that the use of OPEC revenues is the best way of financing the impact on the countries that are worst affected, the OPEC countries are unlikely to accept the full responsibility for this problem. Apart from the fact that the problem arises largely from the suddenness in the rise of the price of oil, it is not at all clear that they should. Since concessional lending from the sale of natural resources constitutes a gift of part of their capital stock, there is a strong case for arguing that other rich countries should help to meet the increased need for external capital in a comparable way.

One of the most painless and efficient ways for the advanced countries to contribute to the short-term financial requirement would be through a debt moratorium for the countries most seriously affected. This procedure would enable the recipients to use their own foreign exchange earnings to pay for increased import costs for a limited period and hence would be appropriate to the short-term problem. For example, if a billion dollars were made available in this way, it would reduce the debt service of the developing countries in 1975 by 8%.

Whatever measures are chosen to meet the short-term financial requirement, it is clear that the conventional notions of burden-sharing will have to be modified. Applying the existing DAC average (.35% of GNP) for official aid to the GNP of the richer OPEC countries would produce only some $300 million per year, a level which they already meet but which is quite inadequate to the problem. Since the advanced countries will be the recipients of most of the capital flows generated by the increase in oil prices, it is also incumbent on them to facilitate its relending on appropriate terms to the poor countries that have not benefited from the changes in commodity prices.

Medium-Term Measures

Although the immediate financial problem is acute, the world also faces a transition to a viable pattern of production and trade at the higher costs of energy. This will require large additional amounts of investment and may take five years. Both the short and medium-term problems greatly complicate the development efforts of the poorer countries. For many of them the additional investments required to adjust to the higher cost of energy are added to increased import bills due to inflation in the advanced countries and rising costs of such products as food. Under these circumstances, it will be exceedingly difficult for the developing countries as a group, and particularly for the poorest among them, to reach the objectives set for the Second Development Decade. While the international community must take measures to bring about the adjustment of the world economy with a minimum of disruption, it must also take measures to assure that the most vulnerable economies will not be adversely affected and that they are provided the resources necessary to increase their incomes. This requires that:

1. Efforts to balance trade focus on the expansion of total trade rather than on restricting markets or competing for a larger share of stagnant markets.

2. The developing countries be enabled to earn the increased foreign exchange necessary to finance their higher import costs by increasing their exports of manufactured products to advanced countries.

3. The increased savings generated by the increased price of oil, which will increase the resources available for investment, be used by the advanced

countries not only to finance their domestic investment requirements but also to increase both private and public investment in the developing countries.

4. Special measures be taken to allocate strategic commodities in short supply -- such as food and fertilizer -- in such a way that the minimum requirements of the poorer countries will be met.

POSITION OF THE U.S.

The position the United States will take on the issues outlined above will have a critical impact on the treatment of these problems, though the results should not be expected in the form of General Assembly action. The developing countries are groping for an approach to help them over the immediate impact of increased oil prices and to increase the flow of real resources in support of their development. Their efforts are still inchoate. In the absence of leadership the danger of confrontations on such matters as raw material supplies, even if they should prove ultimately unsuccessful, will increase substantially. The U.S. can play a major role in channeling the discussion of these issues -- which are likely to occupy the world for some time -- into constructive channels. The U.S. is in a position to take the initiative because:

(a) the U.S. is one of the industrialized countries which, on a net basis, has suffered least from the changes in commodity prices;

(b) the U.S. is likely to be one of the countries which will attract a substantial part of the investable resources from the OPEC countries; and

(c) the U.S. is a major supplier of food and fertilizer.

The willingness of the U.S. to contribute to an effective adjustment process, and to the special problems of the developing countries, will have a substantial effect on the actions of other countries -- industrialized, oil producers and other developing countries. To promote effective action on some of the general measures discussed in the preceding section, the U.S. should consider proposing the following initiatives:

1. A pledge by all countries, and in particular the industrialized countries, not to engage in

restrictions on trade or payments in an effort to adjust to the higher commodity prices. (This proposal was made by the U.S. in the C-XX and may be raised in the OECD, but it is worth repeating here.)

2. Recognizing the importance of increased trade for the developing countries, the U.S. should call for elimination of non-tariff barriers on imports of manufactured goods and agricultural products from developing countries. (The U.S. must also reiterate the importance it attaches to the Generalized System of Preferences.)

3. Since concessional assistance in the amounts required in 1974 and 1975 is not likely to become available through normal parliamentary procedures, a moratorium on debt payments during 1974 and 1975 could be negotiated as a way of matching OPEC contributions of concessional assistance to the developing countries.

4. Re-emphasize the importance of an early replenishment of IDA and urge other countries, not now members, to contribute resources, since an existing organization will be able to assure quick and effective disbursement.

5. Offer to make available for export to developing countries amounts of fertilizer no less than the volume exported in 1972, provided other industrialized countries will join in the effort.

6. Reiterate the importance the U.S. attaches to the rebuilding of food grain stocks and state explicitly that the U.S. is prepared to finance a reasonable share of the investment required to provide and maintain an adequate emergency reserve for the world.

7. Recognizing that the problem of providing a more adequate transfer of resources to the developing countries is a complex issue and that the concept of appropriate contributions from different countries is in need of re-examination, the U.S. should suggest this as an appropriate topic for the Conference of Producing and Consuming Countries which it has already proposed.

8. State that the U.S. believes it appropriate that the increased economic strength of oil producers and other countries be recognized in international organizations and that their voting power be increased relative to that of the industrialized countries.

INTERNATIONAL DEVELOPMENT ASSOCIATION | INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT | INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara DATE: April 4, 1974

FROM: Hollis B. Chenery

SUBJECT: Paper for the Special Session of the General Assembly

I am making several minor corrections in the paper and will re-run copies to take to the State Department after lunch. Please let me know if you have any changes to suggest.

Do you want to send copies over to the State Department in advance of our appointment?

HBChenery:tk

Mr. Robert S. McNamara April 2, 1974

Hollis B. Chenery

Analysis for U.N. Special Session

1. The attached notes follow the line of our discussion on Saturday. The first two sections give a summary diagnosis of the interacting oil and commodity problems and suggest actions to meet them. These are equally relevant to the Bank's position and to that of the U.S. Section III considers these problems from the standpoint of the U.S. Government. Other suggestions that we advocate for the U.S. are already included in this draft.

2. Much of the material in sections I and II will be covered in our July paper to the Board. After discussing this draft with you, we can try to develop points that you think are of particular interest at the present stage. — Discussed Apr 3 11 am

Attachment

cc: Mr. Stern

HBChenery:di

(All figures to be checked)

DRAFT
H.B. Chenery
April 1, 1974

ENERGY, RAW MATERIALS AND DEVELOPMENT

Notes on the Agenda of the Special Session of the U.N. General Assemby

The following notes focus on the issues directly related to "the commodity problem" -- the supply and prices of oil and other raw materials -- which led to the Special Session. The traditional UNCTAD agenda is treated only to the extent that new possibilities for action may have been opened up by recent developments.

DIAGNOSIS

The basic factor underlying recent increases in prices of primary products is the unprecedented growth of the world economy since 1960 and particularly among industrial countries since 1970. Specific shortages are largely attributable to the long lead times required to increase primary production and processing capacity and to lags in adjustment mechanisms, since the prices of several years ago did not signal the future growth of demand. Given the past history of oversupplies of wheat, fertilizer, petroleum products, etc., together with the low price elasticity of demand, it is quite understandable that supply has not kept up with demand, with consequent large increases in price for a number of commodities.

While these phenomena may be regarded as largely a consequence of rapid growth, they have been augmented by several fortuitous events, most notably the effects of the Middle East war on the oil producers and the combination of bad weather and crop failures in several countries that produced the grain crisis of 1973. In both these cases, however, the effect was more that of a trigger that accelerated the evolution of forces already at work. It is therefore not reasonable to seek a return to the supply and price conditions of 1970. Instead, it is necessary to make up the deficiencies in investment and productive capacity in shortage areas -- grains, fertilizers, some metals, energy sources -- and to facilitate the reallocation of resources that is needed to restore a process of normal growth with higher energy costs.

Since energy studies are numerous and controversial, I will only state my own conclusions from the work done in the Bank, the OECD and elsewhere as to the likely consequences of the energy crisis.

(i) Petroleum and natural gas have been undervalued in relation to future demands and alternative sources of supply; as a result they have replaced other sources of energy in the industrial countries to an undesirable degree.

(ii) Given the lead times of 5-10 years or more for the development of alternative energy sources, a rise in marginal energy prices to

the level needed to stimulate these developments is desirable. This level also has considerable appeal as a basis for a "reasonable" world price for oil. Current estimates of the marginal cost of substantial alternatives to OPEC oil imports are in the range of $7-9 per barrel (in 1973 prices) in the industrial countries. Opinions differ as to whether the OPEC price could be temporarily reduced below this level (I think the probability is low).

(iii) The current level of oil prices will produce an increase in the value of the oil exports of the OPEC countries of about $60 billion in 1974 and $75 billion in 1975 compared to 1973 revenues of $23 billion. This is the equivalent of a transfer to them of some 2% of world GNP and 10% of the total value of world exports. While the total resource cost will not be a serious impediment to growth once demand and production patterns have adjusted to it, the balance of payments impact amounts to 15-20% or more of total foreign exchange supplies in a number of developing countries and will require some difficult adjustments in world trade patterns. During the period of trade adjustment, there is a real danger of individual countries following incompatible policies that will hamper the growth of total world output.

(iv) In a third of the principal developing countries and most of the developed ones, the oil impact will be largely offset by increased export earnings plus ready access to external capital, and their development prospects will not be seriously affected. International action should therefore focus on the problems of the remaining countries for which the transition to a viable balance of payments position will be more difficult.

In most commodities other than oil the combination of reduced growth of demand in the next 2-3 years and increased supply is expected to check the rise in prices and lead to some fall in the terms of trade of producer countries from their present favorable levels. The principal commodities for which there is cause for concern about supplies in the medium term are petroleum, grains and fertilizer.

TYPES OF INTERNATIONAL ACTION

The preceding diagnosis suggests that the most useful focus for discussing the commodity problem at the Special Session would be the types of international action that would facilitate the needed structural changes and move the world economy to a condition of orderly and equitable development. The kinds of international action that have some chance of success are likely to be those which increase total world income and from which most countries stand to benefit. The case for pure transfers of resources from one group of countries (e.g. oil producers) to another is less persuasive.

Two kinds of international action to deal with the commodity problem need to be considered:

- short-term measures to mitigate the effects of high prices or shortages of food, fertilizer oil, etc. on countries that do not have the means to secure them.
- measures to facilitate the internal and external adjustments in the economic structure that are necessary for a resumption of orderly development.

The adjustment process will require a period of several years in both the consuming countries that have suffered and the producers that have benefited from the rise in commodity prices. There are 7-8 OPEC countries that will not be able to make full use of their additional resources for their own development in the next five years, while there are a number of developing countries (including India, Bangladesh, Sri Lanka, Kenya, the Philippines, Thailand, Korea and several smaller poor countries) in which it will take several years to bring about the needed reallocation of resources. Some of the industrial countries will also need to finance large additional import costs.

Since the commodity boom is expected to taper off in the next year or two and be followed by a worsening of terms of trade for most primary producers (apart from the oil exporters), a number of other developing countries will then face similar adjustment problems.

Short-Term Measures

Although the increased balance of payments deficits of the advanced countries can be financed more or less automatically through the capital markets, this is not true of most of the developing countries. As pointed out in the Bank's Interim Report, special measures will be needed to provide the additional $10 billion that they will require in 1974 and 1975 to maintain their development programs, and only half of this amount can be financed at conventional terms.

Most of the proposals that have been made so far to meet the needs of the developing countries have focused on the developmental aspects of the problem rather than the need to maintain import levels in the face of higher prices. The magnitude of the requirement is such that some contribution is needed from both the OPEC countries and the industrial countries if it is to be met.

The need for lending on concessional terms is estimated in our Interim Report to be about $3 billion in 1975 and somewhat larger in the next several years. One means to finance this requirement would be through a tax on oil exports. If the full amount were financed in this way, it would require a tax of 25 cents per barrel at the export volumes projected for 1975. The burden of such a tax would be shared between oil producers and consumers. In effect, some of the OPEC countries are moving in this direction by making loans to developing countries to finance the increased cost of petroleum imports.

Although it may appear to the advanced countries that the use of OPEC revenues is the best way of financing the impact on the countries that are worst affected, the OPEC countries are unlikely to accept the full responsibility for this problem. Apart from the fact that it arises largely from the suddenness in the rise of the price of oil, it is not at all clear that they should. Since concessional lending from the sale of natural resources constitutes a gift of part of their capital stock, there is a strong case for arguing that other rich countries should help to meet the increased need for external capital in a comparable way.

One of the most painless and efficient ways for the advanced countries to contribute to the short-term financial requirement would be through a debt moratorium for the countries most seriously affected. This procedure would enable the recipients to use their own foreign exchange earnings to pay for increased import costs for a limited period and

hence would be appropriate to the short-term problem. For example, if a billion dollars were made available in this way, it would reduce the debt service of the developing countries in 1975 by ____%.

Whatever measures are chosen to meet the short-term financial requirement, it is clear that the conventional notions of burden-sharing will have to be modified. Applying the existing DAC average (.35% of GNP) for official aid to the GNP of the richer OPEC countries would produce only some $300 million, a level which they may well meet under existing proposals but which is quite inadequate to the problem. Since the advanced countries will be the recipients of most of the capital flows generated by the increase in oil prices, it is also incumbent on them to facilitate its relending on appropriate terms to the poor countries that have not benefited from the changes in commodity prices.

Medium-Term Measures

The transition to a viable pattern of production and trade for the world economy will require large amounts of investment and will probably take at least five years. The objectives of international action should be to bring about this readjustment with minimum disruption of normal growth processes and with safeguards for the most vulnerable economies. To meet these objectives, it is essential that more balanced trade be achieved by expansion of the total rather than through competitive efforts to achieve larger shares of stagnant export markets.

Since the developing countries cannot support continued increases in debt to finance their increased import costs, those countries having larger deficits must move to reduce them by expanding exports. Much of this increase must take the form of manufactured exports to the advanced countries. The most important contribution that the latter can make to this process is to reduce the existing barriers to access to their markets.

There are increased requirements for investment in both developed and less developed countries to increase energy supplies, expand exports and substitute for imports. The net effect of the rise in prices of oil and some other commodities will be to increase the resources available for investment although by a lesser amount than the savings initially generated in the OPEC countries. Since the bulk of the OPEC funds will flow to the advanced countries, they will be in a better position to increase both public and private investment in the developing countries. This indirect route seems more likely than a direct channeling of OPEC funds to other developing countries in large volumes.

Although it is not possible to foresee with any accuracy the full impact of the adjustment process, it is likely to take place more easily in the stronger economies and to retard growth in some of the weaker ones. Given the limited supplies of some essentials such as fertilizer and

grains at the present time, special measures to protect these economies should be considered. It may, for example, be necessary to ration fertilizer in order to secure the necessary minimum for India and other poor countries until supplies become more plentiful.

The rebuilding of grain stocks requires special attention in the present situation, since they are dangerously low and no mechanism now exists to ensure adequate investment in stocks for the world as a whole.

THE POSITION OF THE UNITED STATES

The position taken by the United States will have a critical impact on most of the problems outlined above. Unlike most of the advanced countries, it has not suffered from the changes in commodity prices and it is likely to attract a substantial part of the investment flow from the OPEC countries. Its willingness to contribute to the solution of the short- and medium-term problems of readjustment will have a substantial effect on the actions of other developed countries.

Apart from the general measures outlined in the preceding section, the United States is in a position to take the initiative in several fields in which it is a major supplier. For example, its willingness to allocate fertilizer or supply wheat on concessional terms to the worst affected countries might be an important element in a cooperative effort in which the oil producers were being urged to take similar actions.

Similarly, an offer to defer debt service from these countries during a period of acute balance of payments stringency would be likely to elicit similar offers from other creditor countries.

The attitude of the United States in the IBRD and other international institutions will affect their ability to respond constructively to the present crisis. For example, an increase in voting power in IDA, based on contributions to the fourth replenishment, might make OPEC contributions to IDA more likely. As one of the prospective recipients of capital flows from the OPEC countries, the United States will also be in a position to help in financing the short-term deficits of the less developed countries, either through the international institutions or directly.