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Pearson Commission Recommendations - Correspondence - Volume 6

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### Second Paragraph:

OK-but postpone contact of ED's until after the 3rd Replenishment. Part I Countries Agreement has been "signed", presumably at the 6/24 meeting.

### Third paragraph:

OK.

I would be inclined to report to the Board:

1. Unctad conclusion, i.e., support for Supplemental Finance if "additional funds" were made available.
2. "additional funds" are not likely to be made available.
3. Therefore, reluctantly conclude Supplementary Finance must be set aside.

*6/12 to Mr. Demuth from R. Demuth*

# OFFICE MEMORANDUM

TO: Mr. McNamara

DATE: May 28, 1970

FROM: Richard H. Demuth *RHD*

*7/11/5/32*

SUBJECT: Pearson Commission Recommendation on Supplementary Finance

The Pearson Commission recommended that discussions leading to a program of supplementary finance should be expedited and there is an outstanding request from UNCTAD to consider this matter. You have said that you did not wish to send forward to the Executive Directors a memorandum on this subject until agreement was reached on the IDA replenishment. Now that that agreement has just about been concluded, I suggest the following for your consideration:

I believe that the first step should be to find out from the Part I countries whether they are prepared to consider a supplementary financing scheme involving additional funds or whether, in agreeing to contribute to the Third Replenishment, their understanding was that these would be the only amounts to be contributed directly to IDA for the replenishment period. Denis Rickett could probably readily ascertain the position of these countries through the Executive Directors. In the unlikely event that there is support from the Part I countries for proceeding with supplementary finance with additional funds, we should prepare a staff proposal for discussion by the Executive Directors, and should inform the Directors of the date when we expect to submit the proposal to them.

*OK - but method contract of ED's control after the 3rd Replenishment Part I countries agreement has been signed, presumably at the 4th meeting.*

If, on the other hand, as seems probable, the Part I countries confirm that they are not prepared to consider contributing any additional funds to IDA for supplementary finance, at least for the time being, I believe that we should report this fact to the Board. The Board should also be told, however, that this circumstance would not preclude the possibility of using some part of the replenishment funds (and perhaps some Bank resources as well) for supplementary financing purposes. You should point out that, when UNCTAD's Trade and Development Board invited the Bank to consider working out and, if appropriate, introducing arrangements for a discretionary scheme of supplementary finance, it specifically directed the Bank's attention to the view of the Intergovernmental Group on Supplementary Finance that "it would be of little value merely to divert available resources from basic development finance for the purpose of supplementary financing." You should nonetheless tell the Directors, I believe, that, if they are disposed to consider supplementary finance as having as high a priority as basic development finance in the use of Bank and IDA resources, or wish to have a specific proposal to look at before deciding this issue, you will instruct the staff to prepare appropriate proposals and will schedule them for prompt discussion by the Board. You should add, however, that, before so instructing the staff,

*OK*

*I would be inclined to report to the Board:*  
1. "acted conclusively" support for Supplemental Finance if "additional funds" were made available  
2. "additional funds" are not likely to be made available  
3. therefore, reluctantly conclude Supplemental Finance must be set aside

Mr. McNamara

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May 28, 1970

you wish to have the views of the Executive Directors so that, if there is no disposition to go ahead with supplementary finance in the absence of additional funds, unnecessary staff time will not be spent in preparing proposals. Finally, I believe that you should tell the Directors that, if they do not wish to go ahead with supplementary finance in the absence of additional funds, you intend to put supplementary finance to one side for an indefinite period.

The approach I have proposed would also serve to put us in a position to respond to the request of the UNCTAD Trade and Development Board to report on the status of supplementary finance at their meeting in August.

May I have your reaction, please?

cc: Mr. Friedman, Sir Denis Rickett

711/5/31

DRAFT  
May 22, 1970

*6/12  
Dick, note the  
change: call me  
with your  
discussion.  
Rmw*

MEMORANDUM TO THE EXECUTIVE DIRECTORS

Subject: Pearson Commission Recommendation No. 13 Concerning Plans  
for Reaching Official Aid Target

Recommendation

"All member nations of the Development Assistance Committee should prepare plans for reaching the 0.70 per cent target, and the President of the World Bank should place discussion of these plans on the agenda of the 1971 meeting of the Board of Governors. The national plans should be submitted for publication to the Chairman of the DAC by January 1, 1971".<sup>1/</sup>

Comment

The reference to the 0.70 per cent target relates to the immediately preceding recommendation that "Each developed country should increase its commitments of official development assistance to the level necessary for net disbursements to reach 0.70 per cent of its Gross National Product by 1975 or shortly thereafter, but in no case later than 1980".<sup>2/</sup>

Underlying the recommendation to which this memorandum is addressed is the thought that, assuming that the aid-giving countries agree to accept a target for official development assistance and a timetable for reaching that target, plans for implementing the agreement ought to be discussed in a forum in which both donors and recipients are present. I

1/ Report, page 152.

2/ Ibid.

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If prior to the 1971 meeting of the Board of Governors, the members of the World Bank Group should indicate a preference for discussion of aid targets at the Annual Meeting, I shall make the necessary arrangements.

am sympathetic to that point of view. However, aid targets and timetables are already under consideration in various United Nations bodies (including the U.N. Conference on Trade and Development) (~~UNCTAD~~) as aspects of the strategy for the Second Development Decade (DD II), a process in which both developed and developing countries are participating. It may be assumed that some mechanism will be created for a continuing evaluation, including evaluation by United Nations bodies, of <sup>the goals and of</sup> progress made toward ~~reaching such goals as may be agreed.~~

*A the members of the World Bank Group may determine*  
~~I believe~~ that the meetings of the U.N. General Assembly, of the Economic and Social Council of the United Nations, and of UNCTAD provide a more appropriate forum for the discussion of aid targets by developed and developing nations than an Annual Meeting of the Board of Governors of the World Bank. <sup>IT</sup> Quite apart from the practical problems which would be raised by attempting to add an item of this character to the agenda of a five-day session, the Annual Meeting has traditionally been concerned with a review of the present and prospective activities and policies of the World Bank Group of institutions, rather than with attempts to influence the aid policies of developed countries through the medium of a public confrontation with the developing countries. Without deprecating the possible effects of such a public confrontation on the political processes of the developed countries, I believe that the appropriate forum for this purpose is the United Nations bodies referred to above, and that it is desirable, in the interests of all members of the Bank, to preserve the present non-political focus of our Boards of Governors' meetings.

*If prior to the 1977 meeting of the Board of Governors, the members of the World Bank Group should indicate a preference for discussion of aid targets at the Annual Meeting, I shall make the necessary arrangements.*

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In the circumstances, I do not believe that the action which the Commission has recommended should be taken.

Robert S. McNamara

7/11/5/30 To Mr. Demuth

MARK VI

DRAFT

PHenderson:RHDemuth:tf

May 13, 1970

MEMORANDUM TO THE EXECUTIVE DIRECTORS

Subject: Pearson Commission Recommendation No. 32 Concerning Criteria for the Allocation of IDA Credits

Recommendation

"IDA should formulate explicit principles and criteria for the allocation of concessional development finance and seek in its policies to offset the larger inequities in aid distribution."<sup>1/</sup>

Background

This recommendation of the Commission is made in the final chapter of the report, which deals with the broad international framework for development. The two parts of the recommendation are to be taken together: the main criterion for allocation which IDA is urged to adopt explicitly is that of taking into account, and so far as possible redressing, what the Commission regards as the inequities which arise as a result of the way in which official bilateral development assistance is distributed among countries.

The nature of these inequities is outlined in an earlier section of the report, in Chapter 6. It is there argued that additional aid to developing countries should be related primarily to economic performance; that for political and historical reasons the distribution of official bilateral aid has been extremely uneven, and bears little relation to economic factors; and that there is a tendency for large countries to receive less assistance per head than smaller ones. ~~Because of these features and effects of bilateral aid, the Commission advocates a very substantial increase in the amount of funds available to IDA. The recommendation is explicitly~~

*Handwritten notes:*  
You  
Dick with  
the changes.  
Debus  
with me in my  
y game  
from  
unacceptable  
R

<sup>1/</sup> Report, page 230.

formulated in relation to this increase: thus the need for IDA to take into account the policies pursued by other aid agencies is regarded by the Commission as a necessary corollary of the expansion in the scale of its activities which the Commission also favors.)

### Analysis

#### A. Inequities in Aid Distribution

The Commission has rightly drawn attention to a very important issue. The present distribution among developing countries of official development assistance appears to bear little relationship to need, performance, poverty or any other generally recognized criteria. The table below presents some salient features of this distribution in the most recent period for which figures are available, namely calendar year 1968. The figures relate to the grant equivalent of commitments of official development assistance by countries which are members of OECD's Development Assistance Committee and by multilateral agencies. It can be seen from the table that more than half of official aid thus defined was committed to a group of countries with less than 16 per cent of the total population of the developing world,<sup>1/</sup> while more than 13 per cent of the aid total went to countries with just 1.6 per cent of this total population. From the last column of the table it is clear that the very wide existing discrepancies in aid receipts per head cannot be accounted for by differences in the degree of poverty.

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<sup>1/</sup> Defined as comprising the 86 countries which are now Part II members of IDA, less Iceland and Ireland, which are not classed as aid recipients, and Libya and Saudi Arabia, which because of their oil revenues are not significant recipients, but with the addition of seven further countries. These latter consist of five developing countries which though members of the Bank are not members of IDA, namely Jamaica, Singapore, Trinidad and Tobago, Uruguay and Venezuela, together with Cambodia and Yemen, whose applications for membership in the Bank and IDA have been approved by the Boards of Governors.

It is not easy to regard such a distribution of aid as satisfactory, or even as fully reflecting the considered preferences and intentions of the bilateral donors taken as a group. If a workable and broadly acceptable method could be found of using IDA funds to "offset the larger inequities in aid distribution," as suggested by the Commission, there would be a strong case, in principle, for doing so. <sup>Although,</sup> ~~However,~~ for the reasons given in the following section of this memorandum, ~~I believe that, as a practical matter,~~ <sup>may</sup> it would not be feasible to adopt this suggested criterion as the ~~sole or even as a~~ principal consideration to be weighed in allocating IDA funds. <sup>I believe</sup> ~~The furthest that, in my~~ judgment, we can and should go in the direction pointed by the Commission <sup>we should</sup> ~~is to~~ add this criterion, as a general, unweighted factor, to the existing accepted criteria in reaching judgments about the allocation of IDA funds.

#### B. Use of IDA Funds to Offset Inequities

The question of how far IDA should have regard to the amount of aid that may be available to particular countries from other sources is not a new one: it has been raised and debated on a number of occasions. Most recently within the Bank, it was brought up at a meeting of the Executive Directors on July 23, 1968, which considered my memorandum on Criteria for the Distribution of IDA Funds. On that occasion a number of Executive Directors made explicit reference to the question, and widely differing views were expressed.

The issue, as I see it, <sup>need be</sup> ~~is~~ not one of a choice between two extreme positions. As I noted in the paper just referred to, IDA "can hardly escape giving consideration to the amount of assistance that prospective IDA borrowers may be receiving from other sources of finance." It is neither desirable nor practicable to try to devise a system of allocation for IDA in complete isolation from other aspects of the world situation, and without reference to the policies that are

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pursued by other donors. At the opposite extreme, it <sup>may be</sup> ~~would be equally~~ impracticable for IDA to adopt as the <sup>principal</sup> ~~sole~~ criterion for all its lending that of trying to ensure that countries judged to be in the same situation should receive equal amounts of per capita aid. There are several considerations which would appear to rule out such a course of action.

First, it would imply a direct and abrupt reversal of past decisions concerning the criteria that should be used. ~~In particular, it would not be consistent with the principle, now firmly adopted, of a wide geographical distribution of IDA credits among eligible countries. Nor would such a system be compatible with fixing specific maximum shares for individual countries which are substantial IDA recipients.~~ If the primary criterion for IDA allocations were to become that of redressing inequalities, IDA would ~~then~~ have to concentrate its assistance on those countries which according to some agreed test were judged to be receiving too little. This would <sup>lead to</sup> ~~probably imply a~~ very high degree of concentration on a limited group of countries, <sup>- a concentration</sup> including ~~those for which maximum shares have been established.~~ <sup>which the members of IDA have made clear they consider unacceptable.</sup>

Second, it is easy to state the broad principle that IDA should redress unwarranted inequalities in the distribution of aid, but very difficult to give it concrete expression in a form which would command general assent. The conceptual and technical problems of implementing the principle through any quantitative formula are formidable, ~~as shown by the analysis contained in the Annex to this memorandum.~~ Whatever precise method might be adopted would inevitably be open to question and indeed a matter of controversy, more particularly since large sums of money would be at stake.

A third factor is that the main sources of official bilateral development assistance are also the sources of IDA funds. It is open to question how

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far these countries would be willing to maintain, let alone increase substantially, the amounts that they were prepared to make available to IDA, if they knew that the ~~sole or~~ principal criterion <sup>for allocating</sup> on which IDA credits would be ~~extended was that of~~ offsetting or compensating for the collective results of their own development assistance policies.

It follows from these considerations that ~~the only step which it is~~ <sup>may not be</sup> practical for us to ~~take~~ <sup>do more at this time</sup> in implementing the Pearson Commission recommendation ~~at least at this time,~~ <sup>than</sup> is to accept as an additional criterion for the allocation of IDA credits that of securing greater equity in the over-all distribution of aid. Thus the fact that a country was judged to be receiving unduly low amounts of assistance from other sources would be one, but only one, factor to be weighed in determining its share of IDA financing.

Because of the ~~difficult~~ <sup>complex</sup> conceptual and technical issues described in the Annex, ~~I do not propose that we should try to agree on any precise formula~~ <sup>at would be difficult to</sup> for application of this proposed new criterion. The staff will, however, continue to examine, so far as possible in quantitative fashion, the possible implications and comparative merits of different ways in which the broad principle of redressing inequities in aid distribution might be given practical expression.

#### Conclusion

The broad principle embodied in the recommendation, that IDA funds should be specifically directed towards countries which are receiving unduly low amounts of aid from other donors, has merit. However, at least at this time, ~~I believe that~~ it should be regarded, not as displacing or superseding existing criteria for the distribution of IDA credits, but rather as introducing a new <sup>factor</sup> ~~criterion~~ to be added, ~~as a general, unweighted factor,~~ to the present accepted criteria in reaching judgments about the allocation of IDA funds.

Some Problems of Working out a Quantitative Formula for  
Implementing Pearson Commission Recommendation No. 32

This Annex describes some of the conceptual and technical problems involved in any attempt to apply, through a precise formula expressed in quantitative terms, the Commission's recommendation that IDA should seek in its policies to offset the larger inequities in aid distribution. Any such formula would have to start with an identification of the countries which appear to be receiving unduly small amounts of aid. This presupposes a set of figures relating to an actual or initial distribution of official development assistance, from which it can be seen how much each particular developing country received or might be expected to receive. It would also be necessary to form a fairly precise notion of what alternative distribution of aid it would be desirable to achieve:

this may be termed the preferred distribution. Only when these two distributions had been specified, with actual numerical allocations to particular countries, could the possible implications for IDA be derived with a reasonable degree of precision.

There are difficulties in trying to arrive at each of these distributions, and the second in particular gives rise to very serious problems.

In specifying the initial distribution, three main issues have to be resolved. These are:

- (i) which sources of official bilateral aid are to be taken into account;
- (ii) which time period should be taken; and
- (iii) what concept of aid should be adopted.

Differing opinions may reasonably be held concerning each of these.

As to the first issue, the most convenient course of action, which was followed in compiling the table presented in the memorandum, is to take into account only the official bilateral assistance flows from countries which are members of the Development Assistance Committee (DAC). Good data exist with respect to this group of countries, and they account for the great bulk of official bilateral aid. It may be, however, that in particular instances the inclusion of aid from other sources would make a considerable difference to the picture. A case in point under present circumstances is the United Arab Republic, which receives relatively little aid per head from the DAC countries, but has been the recipient of substantial amounts from other Arab countries since the closure of the Suez Canal in 1967.

The choice of time period might also make a significant difference to the relative claims of different countries, since the amount of per capita

aid which a particular country gets may vary appreciably from year to year. Ideally, what is needed is information concerning the prospective distribution of official aid among developing countries for a particular future time period, to which the allocation of compensatory IDA credits for the same period could be related. At present, however, the prospective distribution of official aid is not known. It would, therefore, be necessary to develop a system by which the intentions of the principal donors were made known in advance in fairly detailed and reliable form. Should this prove to be impracticable, it would be necessary to make use of actual data concerning the distribution of official development assistance for a recent period in the past. These figures, though firmly based, might in some respects be an uncertain guide to the future, given the frequency of changes in aid policies and programs.

As to the third issue, the definition of aid, there appears to be a clear choice between two alternatives. On the one hand, it is possible to use the actual estimated flow of funds or commitments of assistance, with no allowance for the terms on which this assistance is made available. On the other hand, one could use, again as in the table in the memorandum, some measure of the grant equivalent of the amounts committed in the period under review. Since the grant element of official commitments, as also the relation between commitments and actual net receipts for a given year, are both known to vary as between different developing countries, this choice also might affect significantly a compensatory allocation of IDA funds.

When one turns to the problem of specifying a preferred distribution of official aid, matters become much worse. What appears to be the Pearson Commission's conception of an equitable distribution of official development assistance can be stated simply and clearly. It is that countries which are in a similar situation, and hence can be regarded as equally deserving, should

receive as nearly as possible the same amounts of official aid per head. It is sometimes questioned, however, whether it is desirable to take explicit account of differences in population in arriving at a preferred distribution of official aid; and even if it is accepted that aid comparisons should be made in per capita terms, it is notoriously difficult to reach agreement on what is to be taken into consideration in determining whether and to what extent different countries can be regarded as equally deserving.

One possible ground for objection to the use of per capita comparisons is the belief that ideally the distribution of aid should be related to the estimated external financing requirements of each developing country. Although these requirements might be expected to bear on average some positive relationship to population, so that in general the more populous countries would need larger amounts of external finance, this relationship is likely to be a rather loose and uncertain one. Thus requirements should be estimated directly, and not on the basis of population. If there were an agreed and reliable method for calculating the future requirements of a country for external financing, and hence for official development assistance, this might well be the best way of deriving a preferred distribution of the latter. However, given the present limitations of our knowledge and predictive powers, and the very considerable margins of error which as a result of these limitations enter into all such estimates of requirements, it is questionable whether this direct approach to the problem can actually be used.

Even if it is agreed that it is impracticable to base the distribution of aid on estimated requirements, it might perhaps be argued that aid receipts should be related not to population but to other variables. Thus comparisons can be made between official aid flows and the national products of recipient countries, or the value of their imports of goods and services. A comparative

analysis of this kind appears in the most recent Report of the Chairman of the Development Assistance Committee, in a chapter which deals with the geographical allocation of assistance.<sup>1/</sup> It is clear from the figures which are presented there that the choice of a denominator makes a very considerable difference to the results derived, since there are wide variations among developing countries in per capita income and in the relation between national product and imports. Of the three possibilities, i.e., population, national product and imports, the per capita basis of comparison is the simplest and least regressive.

Even given general agreement on use of the per capita basis, there are no generally accepted criteria for determining the appropriate shares of different countries in concessional assistance. There are four main qualities that are commonly thought of as relevant to this question, namely poverty; economic performance; insufficiency of creditworthiness; and absorptive capacity, under which is included the availability of suitable projects. As the history of development assistance efforts clearly demonstrates, it is no easy task to classify or rank countries in relation to any of these characteristics, with the partial exception of poverty, for which there is broad agreement on using available measures of differences in national product per head. Despite the very useful work that has been done on the other three aspects, there is no simple and generally accepted way of measuring these qualities, and hence of ranking countries with respect to them. An act of informed judgment is necessarily called for.

Even where suitable measures or indicators can be devised, it is not clear how they should be used so as to derive a preferred distribution of aid. Suppose, for example, that it was agreed to rely on poverty alone as a test, with income per head as the appropriate indicator. A number of questions would still remain to be answered. How many degrees or gradations of poverty should there

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<sup>1/</sup> Chapter V of the Chairman's report for 1969, page 167 et seq.

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be? What should be the ceiling of income per head, above which countries would not qualify for consideration? And most serious of all, what premium should be placed on a given identified difference in income per head: if the per capita income of Country X is \$100, and that of Country Y is \$200, ought X to get twice as much aid per head, or fifty per cent more, or twenty per cent - or should it be entitled to only half as much on the grounds referred to above, that aid should be related not to population but to national product? It is evident that different answers can reasonably be given to such questions.

Finally, and still more intractable, there is the question of how different factors should be weighted. Should a very poor country which is thought to have shown indifferent performance be entitled to more or less aid per head than one that is significantly richer but is judged to have performed better? Should countries that are judged creditworthy for most, or all, of their external capital requirements continue to be regarded as ineligible for IDA credits, even if they are getting very little aid from other sources and have evinced good performance, or should their allocation merely be reduced - and if the latter, to what extent? Such issues are unavoidable, and once again there is plainly no agreed and straightforward way of resolving them.

Thus, it is clear that in implementing the recommendation a substantial element of judgment would be unavoidable. Given the difficulties and uncertainties of specifying both an actual and a preferred distribution of official development assistance, general agreement on a precise formula for allocating possible compensatory IDA credits is <sup>unlikely</sup> not to be expected. Nor ~~would the use of a mechanical formula be desirable.~~ <sup>In lieu of that we can strike</sup> The most that could be <sup>hoped for would be</sup> a set of working criteria by which the most significant

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inequities <sup>can</sup> ~~could~~ be identified, and a rough quantitative outline of the ad-  
justments that <sup>can</sup> ~~might~~ be made in the distribution of IDA funds to offset  
those inequities.