Folder Title: Role of the Bank – Correspondence 05

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McNamara papers

Role of the Bank
1978 - 1979 (Jan.)

7 11/4/40

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara
Mr. I.P.M. Cargill

DATE: January 10, 1979

FROM: Eugene H. Rotberg

SUBJECT: Capital Increase

On July 6, 1978 I held a seminar in Germany in which there were 10 representatives of various Ministries of Bonn and of the Bundesbank, as well as 74 bankers, 7 representatives of the insurance industry, 11 portfolio/trust managers, and 18 journalists. The seminar dealt basically with the case for a substantial capital increase in the Bank. After I spoke, Dr. Moltrecht made a public statement in support of a doubling of the Bank's capital and a payment of 10% of the subscribed payment in the form of paid-in capital. For your information I am enclosing a translation of one of the news accounts of Moltrecht's position. His support for paid-in capital and doubling was reported in 3 or 4 other newspapers at the time.

1/10

You may also be interested in a memo of First Boston dated November 14, 1978 which sets forth what they told the U.S. Treasury concerning an increase in capital, and two memoranda which summarize the views of Morgan Stanley and Salomon Brothers as expressed to the U.S. Treasury.

EHRotberg:mb

Attachments

cc: Mr. K. Georg Gabriel

TRANSLATION OF CLIPPING FROM "FRANKFURTER RUNDSCHAU" OF JULY 7, 1978

World Bank Wants More Capital

Lending Volume Now Up Against Ceiling

piz Frankfurt am Main. The management of the World Bank has recommended a capital increase to its governing bodies. Dr. Horst Moltrecht of the Federal Ministry for Economic Cooperation stated that in view of the significance of the World Bank in the development field, the Federal Government looked favorably on a proposed capital increase of \$30 - \$40 billion. As the Articles of Association call for 10% of the subscribed capital to be paid in cash, the Federal Republic, which holds 5.3% of the World Bank's capital, would be required to pay in between \$150 million and \$200 million over six to nine years. The remaining 90% remain on call as backing for possible liabilities.

As the Vice President of the World Bank, Eugene Rotberg, explained in Frankfurt, any real increase in the annual amount of lending (currently \$6 billion) would be possible only by increasing the capital, which currently stands at \$41 billion. According to the World Bank's Articles of Agreement, the total amount of loans outstanding may not exceed the sum of subscribed capital plus reserves.

To quote Rotberg, the World Bank had available at the end of 1977 to support its lending operations a total of \$21.6 billion in obligations outstanding with governments, central banks and the private capital market. In 1978/79 the Bank will raise \$4.2 billion equivalent largely in countries with balance of payments surpluses. In past fiscal years, it raised most of its funds in the United States, the Federal Republic of Germany, the OPEC countries, Japan and Switzerland. Sizable borrowings in Swiss francs, DM and

THE FIRST BOSTON CORPORATION

NEW YORK OFFICE

MEMORANDUM

November 14, 1978

TO: J.M. Hennessy

FROM: A.J. Freeman

RE: World Bank--U.S. Treasury Meeting

Joseph Winder and Thomas Hoopengardner of the U.S. Treasury Department visited Messrs. Hyland and Freeman on Thursday, November 9, to discuss the investment community's view of the World Bank. Their general focus was to develop an understanding of those features which were of critical importance to the continued marketability of the Bank's securities in the U.S. market. Their particular interest was the potential impact of possible changes in the U.S. role vis-a-vis the Bank. In this regard, we emphasized the following points:

1. Paid-in capital is important because it shows concrete support of the Bank. More particularly, as the largest component of the Bank's equity account, it lowers the Bank's overall cost of funds, lowers its debt-to-equity ratio and, if assigned a theoretical "maturity" of thirty years, extends the average life of the Bank's capitalization beyond the average life of its loan portfolio (after excluding central bank holdings of Bank debt, which are assumed to roll over). Winder cited the reduction in the percentage of callable capital from 20% to 10% in 1960, the year the Bank was first rated AAA. We responded that the Bank's superior financial ratios and coverage of outstanding borrowings by appropriated U.S. callable capital in 1960 mitigated the market impact of this change.

2. Appropriation of callable capital is important because it is immediately available solely to meet the Bank's obligations. This reinforces the market's view of the Bank as a lender's and not a borrower's institution. Authorized but not appropriated capital impairs this assurance, particularly in light of recent Congressional attempts to circumscribe the Bank's activities as a condition of appropriating funds.

3. Role of the U.S. as single largest member country is important because of its veto power over changes in the Bank's Articles (see below). Its importance as a source of callable capital is still significant, and is a critical component when grouped with other strong developed member nations (e.g. Germany and Japan).

4. Limitation on the Bank's lending imposed by the 1:1 ratio in its Articles is important as a reassurance to investors because such a limitation on lending implies a limit on borrowing.

5. No rescheduling policy on Bank loans is important as reassurance to investors that the Bank's ability to meet its debt service will not be impaired in a climate of concern over private sector lending to less developed countries.

mm

cc: Messrs. Buchanan
Toffey
Owen
Walsh
Hyland
Harrison
Fox

OFFICE MEMORANDUM

TO: Mr. K. Georg Gabriel

DATE: November 22, 1978

FROM: H.C. Hittmair

SUBJECT: Capital Increase

Following discussions here in the Bank with staff from the U.S. Treasury I made arrangements with our three managing underwriters and two rating services in New York to receive Treasury staff for discussions on financial matters in particular the prospective capital increase.

I have now been called by Mr. Henry from Morgan Stanley who told me that they had been visited by Messrs. McCutcheon and Winder from the U.S. Treasury. From Morgan Stanley Messrs. Vance Van Dine and Bob Henry attended the meeting. Mr. Henry told me that the key question to which they seemed to come back from various angles was whether investors would find it important that in the forthcoming capital increase the paid-in capital would remain at the 10% level. The questions were aimed in particular on whether a reduction of this percentage would be of any significance and whether there was any limit below which investors would take a negative attitude to the change. The answer by Morgan Stanley was that they consider the maintenance of a 10% portion of the subscribers' capital to be paid in as extremely important from a financial point of view and also from the point of view that it documented to the investing public the degree of support which the member countries were willing to extend to the World Bank.

On other questions concerning the capital increase Morgan Stanley was in their view as supportive as possible.

One point which came up in the meeting was that there were rumours that the activities concerning international financial institutions would be transferred from the U.S. Treasury to US AID. Morgan Stanley told the Treasury representatives that they would consider this as a very bad move because it would transfer the responsibilities for IFI's to an agency which would be much more politically exposed than the U.S. Treasury. The two U.S. Treasury representatives seemed to be pleased with this view.

HCHittmair:mb

cc: Mr. Cargill
Mr. Rotberg

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Eugene H. Rotberg

DATE: January 12, 1979

FROM: H.C. Hittmair

SUBJECT: Capital Increase

In the past we have received information from First Boston and Morgan Stanley about their discussions with the U.S. Treasury concerning various aspects of the proposed capital increase. In order to complete the picture I have today called Peter Gottesagen of Salomon Brothers in order to find out from him how their discussions went with the U.S. Treasury representatives. Peter confirmed the same approach and practically the same questions as were put to the other two underwriters and he mentioned that their response was also along the same lines. The general tenor of the reply was that any change of the current practices and policies would be perceived as negative by investors. This would apply to the question of the amount of paid-in capital, the question of appropriating callable capital and then, of course, any other major financial policies such as the one to one limitation on loan disbursements. He mentioned that the Treasury representatives appeared very smooth and very favorably disposed toward the World Bank and toward the proposed increase.

HCHittmair:mb

711/4/39

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Files

DATE: January 8, 1979

FROM: Joe Wood, Assistant Director, P & B

SUBJECT: Size of the Capital Increase: Reactions of the Executive Directors

1. On January 4 and 5 Messrs. Cargill, Gabriel and I met with several Executive Directors to discuss their views on the General Capital Increase. This note records the principal points made in these discussions.

2. Mr. Fried said that he would support a doubling of the IBRD capital with no paid-in. This support would be conditional upon settlement of the compensation question in the Board. In addition, prior to approval of the FY79 lending program, he would expect a Board discussion of "graduation policy" and of the desirable ultimate size of the Bank. He made it clear that the United States would not hold up a formal resolution on the General Capital Increase by insisting that the discussion of graduation take place first. On the subject of voting rights, he was clearly opposed to adjustments for the developing countries but did not rule out a special allocation to Japan from the currently unallocated shares. The only other issue which might pose a problem is maintenance of value. His preferred solution is to continue with the present practices and footnotes to the financial statements "for another couple of years."

3. Mr. Ryrie characterized the U.K.'s position as the most liberal of all: support for a doubling in capital with 10% paid-in. He would have no problem with a special allocation to Japan out of unallocated shares "because they have a case."

4. Mr. Mentre de Loye did not expect a firm French position to emerge until later this month when a council of ministers meeting is scheduled to consider French participation in all IFIs. Because of French budgetary concerns, it would be easier for France to support a doubling of capital if less than 10% were to be paid-in. He had understood from Fred Bergsten that the U.S. would probably accept a compromise figure of 5%. [Ed Fried explicitly denied this, saying that Mentre de Loye had misinterpreted some casual remarks Bergsten made over lunch.] He expected his minister to take a "hard" position on the Japanese question and to resist any increase which would raise Japan to (or above) the French level.

5. Mr. Narasimham promised support for a doubling of IBRD capital. He had no strong views on the proportion to be paid-in. He could agree to defer discussion of the distribution of shares among countries. When asked about the possibility of a special allocation for Japan, he said this was acceptable provided that it could be done without reducing

the voting power of Part II countries. He seemed unmoved by the point that an early capital increase for Japan could be very beneficial for the IDA 6 negotiations.

6. Mr. El-Naggar was also in favor of a doubling and would follow the majority on the paid-in question. The only important concern he had related to the distribution of shares. Somé of his constituents would expect a special increase. He was, however, prepared to leave this concern unstated at the Thursday meeting if other EDs (especially Mr. Murayama) would do likewise. When told about the Japanese problem, he was initially quite resistant to the idea of a special allocation out of unallocated shares. However, when Mr. Cargill mentioned the possibility of reviving the 15% OPEC share in the context of the General Increase, Mr. El-Naggar said this would make things much easier for him. With a management commitment to seek 15% for OPEC, he thought his constituents would accept a prior special increase for Japan.. Mr. Cargill promised to raise the 15% matter with Mr. McNamara and to give Mr. El-Naggar a response on January 8. X

7. Mr. Drake was away, but I confirmed my earlier understanding of Canada's position with Mr. Agostini. Canada was currently preoccupied with budgetary concerns and would be unable to support a doubling with 10% paid-in. Whether a lesser fraction paid-in would change this position was not entirely clear, because unlike other governments, Canada also had a problem with the notion of "head room." According to Agostini, they were in favor of 5% real growth and had concluded that this could be sustained with a capital increase of about $32 billion.

8. We did not meet with Mr. Murayama or Mr. Kurth. The impression prevailing among the other Directors was that both Germany and Japan were strongly in favor of 10% paid-in and were therefore inclined toward a capital increase smaller than $40 billion. d, 50

Before Wed Pay
chm
Japan - 40/?
FRG - 30/10
Belg -
Dutch - 40/10
Nordic - 3 40/10, 1 35/10, 1 might join maj.

cc: Messrs. Cargill, Broches, Nurick, Chenery, Damry, Stern, Gabriel

Canada [Peter ? talk] -
Aus - no instrmes;

JW:di

Fr - 30-35/10; with lower pd-in would support 40 [Peter ? talk]
UK - 40/10
US - 40/0
Italy - 40/10
LDC's - 40/

THE WORLD BANK

Office of the President

Fried 1/8/81
Our position (re [illegible]) is we will support a doubling of 02 paid-in

711/4/38

898

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: November 21, 1978

FROM: K. Georg Gabriel

SUBJECT: IBRD Capital Increase Proposal

1. Please find attached a draft memorandum which proposes a doubling in IBRD capital. The main question I have about the draft is whether it is sufficiently forthcoming on the issues which concern Japan and Germany. The Japanese re-emphasized to Frank Vibert on his recent visit their preoccupation about voting power. They will be looking for a "signal" in this memorandum and would no doubt find the language of the current draft quite disappointing. Similarly, the absence of any reference to maintaining the 10% paid-in ratio may be interpreted by the German Government as a "signal" that management is willing to settle for less. I believe that these concerns can be - and should be - dealt with by informal contacts with these two governments prior to distribution of the memorandum.

11/22

2. The Annex Tables have not yet been done because priority has been given to the financial projections which you requested to show the impact on the Bank of a Capital Increase with 0% paid-in. We hope to have the Annexes by the end of next week.

Distrib 12/1 for 1/11

Attachment

cc: General Capital Increase Steering Group
Mr. Bock

DJW:bc

review redraft for release on Fri.

Rmw

DRAFT
DJWood:bc

November 20, 1978

MEMORANDUM TO THE EXECUTIVE DIRECTORS

SUBJECT: Size of the IBRD General Capital Increase

Introduction

1. Nearly two years ago a memorandum entitled Future Role of the World Bank and its Associated Capital Requirements was submitted to the Executive Directors (R77-18, dated February 1, 1977). It identified a set of issues to be considered in defining the Bank's role over the next several years and in designing a Capital Increase appropriate to that role. No attempt was made to reach conclusions on the issues raised, but information was presented to show how the IBRD's capital requirements would be affected by its future rate of growth and by a series of other key assumptions.

2. In the period since that memorandum was submitted there have been numerous discussions both within and outside the Bank on the issues raised. Out of these discussions has emerged a broad consensus in favor of a substantial Capital Increase for the IBRD. What remains to be done is to translate this general consensus into a specific agreement. This memorandum attempts to lay the basis for an agreement on the central question of the size of the General Capital Increase.

3. Because the discussions have extended over a considerable period, it may be helpful to the Executive Directors and to member governments to review briefly the course of these discussions and to restate the main points made about the appropriate size of the IBRD Capital Increase. Such an overview is presented in the next section. A final section then gives the management view on these main points and concludes with a recommendation that the capital of the IBRD be doubled. It is recognized that a consensus on the size of the Capital Increase will necessarily be conditional upon subsequent agreement on other pending questions including timing, the distribution of shares among countries and the proportion of the Capital Increase to be paid-in.

Overview of Capital Increase Discussions.

4. A first meeting of the Executive Directors on the Future Role of the Bank memorandum took place on March 8, 1977. That meeting was mainly concerned with two operational questions: (a) the assumptions to be used in planning IBRD operations for FY78 and FY79; and (b) the timetable for negotiations of an IBRD Capital Increase. The question of political support for further growth in World Bank operations was addressed in several important meetings which took place in the months following the March 8 discussion. First, the representatives of the developing countries, meeting as the Group of 24 prior to the Development Committee session on April 27, 1977, issued a statement in which they urged that "the capital of the World Bank and the regional development finance institutions should have a sizable increase."

Second, the heads of state of seven major developed countries and the President of the European Community addressed the Bank's capital requirements in the communique issued at the conclusion of their meeting in London on May 8th. They expressed support for the World Bank and stated that its "general resources should be increased sufficiently to permit its lending to rise in real terms." Thirdly, the countries represented at the CIEC conference issued a report in June 1977 in which they affirmed their agreement on the following point:

> "The capital base of the World Bank should be increased sufficiently to permit its lending to rise adequately in real terms in the years ahead. Negotiations for a general increase in the capital of the Bank should be undertaken, as soon as possible, so as to allow the Bank to achieve its lending programme of $6.8 billion in FY1979 and thereafter further increase in its lending in real terms".1/

5. Against this background of political support for a Capital Increase a series of informal discussions was arranged to give the Executive Directors an opportunity to exchange views on the future growth rate of IBRD lending and to discuss several other matters which have a direct bearing on the size of the Capital Increase. The intent was that these informal discussions would help build a consensus on the specifics of a Capital Increase proposal, so that formal agreement could be reached in the Board in the early months of calendar 1978.

1/ The CIEC Report noted that this paragraph was to be read together with any agreed recommendations relating to the financing of energy and other priority sectors in other conference documents.

6. Real Rate of Growth. The first topic taken up in the informal meetings was the real rate of growth in IBRD commitments which ought to be used for planning purposes. A number of Executive Directors advocated a real growth rate of 7 - 9%, whereas others suggested that a growth rate more in line with that expected for the OECD countries - say 5% or a bit less - would be more appropriate. The significance of these growth rate assumptions for the sectoral distribution of lending and for the distribution of IBRD/IDA commitments among country income groups was also discussed. Technical notes were prepared to illustrate the kinds of sectoral shifts and shifts among country income groups which could be accommodated within an IBRD program which was growing at 5% per annum in real terms.[1/] Several Directors felt that the Bank's potential contribution in such areas as rural development, food production, urban employment generation, energy development and the exploitation of non-fuel minerals was a good foundation upon which to base the case for a substantial real rate of growth in Bank commitments.

7. The Bank's role in the overall transfer of resources to the developing countries and its non-financial contribution to development policy issues were also cited. At the request of the Executive Directors a technical note was prepared summarizing the case for a real rate of growth of 5 - 7% or more, with special emphasis placed upon the relative role to be played by the IBRD in the supply of external finance (Technical Note #2, dated November 30, 1977).

1/ Technical Note #1, #1a, #1b and #1c were issued in a revised form on December 27, 1977. Copies of these and other Technical Notes may be obtained from the Secretary's Office upon request.

8. While the discussion of real rates of growth in IBRD commitments resulted in some convergence of views, no attempt was made to reach agreement on a particular figure. On the contrary, several Directors stressed that the actual future growth rate for the IBRD should continue to be approved year by year in light of prevailing circumstances. From this point of view the decision on the size of the Capital Increase need not - and indeed should not - be linked to any particular growth rate. Instead the Capital Increase should be designed to give the IBRD a degree of flexibility or "head room" within which it can reasonably operate over the next several years.

9. <u>Inflation</u>. The IBRD's capital requirements will also be influenced by the level of international inflation in the years ahead. There was widespread agreement among the Executive Directors that it would be fruitless or even counter-productive to seek a consensus on a planning assumption regarding future inflation rates. A much better approach would simply be to acknowledge the relationship which exists between the level of future inflation and the number of years for which any given Capital Increase will meet the IBRD's requirements. If, for example, inflation were to average 5% a year in the future, then a Capital Increase ~~of about [$40] billion~~ which would represent [illegible] could support real IBRD growth of a rate of 5-7% over a six-year period.[1/]

[illegible]

1/ These calculations assume that commitments remain constant in nominal terms at the end of the growth period. At exchange rates prevailing on [illegible] This would represent an increase in capital of about [illegible] billion.

If inflation were to average 7% a year, the same size increase would only suffice to support IBRD growth for 5 years.[1/]

10. Planning Period. One implication of treating inflation in this way is that the planning period itself would be subject to a margin of uncertainty. Those Executive Directors who addressed the question of how many years of IBRD growth the Capital Increase should provide for all concluded that a period of at least 5 or 6 years was desirable. Most indicated they would favor a much longer period were it not for the very large capital requirements implied by a longer period.[2/]

11. Other Determinants of Size. During the course of the informal discussions some comments were also made on two other matters which may influence the appropriate size of the Capital Increase: (a) the interpretation of the notion of "non-disruptive adjustment", and (b) the repayment terms for future IBRD loans. The impact of these two factors on IBRD capital requirements had been analyzed in the Future Role of the Bank memorandum.[3/] Many Executive Directors found if difficult to take a position on the interpretation of "non-disruptive adjustment" without appearing to endorse an assumption which they regarded as implausible; namely, that the IBRD would receive no further Capital Increase at any time in the future. There was also a feeling expressed that the assumption regarding "non-disruptive adjustment", as well as the assumptions regarding repayment terms, could not realistically be discussed without recognizing

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1/ These calculations assume that commitments remain constant in nominal terms at the end of the growth period.

2/ ~~[The suggestion was made that the period could be lengthened by combining the Capital Increase with an amendment to the Statutory Limit. This possibility was examined in Technical Note #6 dated February 9, 1978.]~~ omit

3/ R77-18, paras. 109-115 and 120-123.

the trade-offs between these assumptions and the real rate of growth in IBRD commitments. A sensible approach, therefore, would be to consider the combinations or packages of assumptions which can be "bought" with Capital Increases of various sizes.

12. A table organized along these lines was distributed to the Executive Directors in December last year. An updated version is attached as Annex 1. The informal discussions which ended in early calendar 1978 did not lead to any consensus on the size of the Capital Increase. ~~For reasons well known to the Executive Directors~~ The discussions were adjourned in February at the request of the United States. The U.S. request for a change in schedule was accompanied by a clear statement of support for a planning assumption of 5% per annum real growth in IBRD commitments and for the significant increase in capital which such a lending program implies. omit?

13. Over the past several months there have been no further discussions within the Bank of the size of the Capital Increase, though a number of Governors did endorse a doubling of the IBRD's capital in their statements to the Annual Meeting. While many Governors did not indicate what size Capital Increase they could approve, there was unanimous support for proceeding promptly to bring the negotiations to a conclusion. {list for me]

Management Recommendations

14. In the final analysis the size of the IBRD Capital Increase will be a political decision. It is important that the nature of that decision

be clearly understood. Member governments are not being asked to decide on the particular rate of growth in IBRD commitments which should be maintained over the next several years. Nor are they being asked to commit themselves to a particular view on inflation, repayment terms or the interpretation of "non-disruptive adjustment". Their decision relates instead to the lending capacity of the IBRD. The use of that capacity is a separate matter, one which will inevitably be decided year by year in light of prevailing circumstances.

15. Obviously there is - and must be - a link between our current estimate of the IBRD's lending activities over the next several years and the recommended size of the Capital Increase. But it would be wrong to suppose that the appropriate size is simply the minimum required to sustain a desired growth rate. On the contrary, a margin of flexibility or "head room" is needed in order to allow realistically for the many uncertainties affecting the Bank's ability to carry out its intended role over the next several years. We cannot now anticipate the precise course of inflation, the pace of disbursements or the change in value of IBRD capital over the next several years. Hence the calculations of IBRD capital requirements should only be regarded as providing a rough benchmark or indication of general magnitude.

16. A margin of flexibility is also desirable for another reason; namely, that the demands placed upon the IBRD's lending capacity may change for reasons which we cannot now foresee. Five or six years ago, for

example, few observers would have anticipated increased IBRD lending for energy development. Allowing some margin for adjustment in the future will help avoid the situation in which member governments are faced with a de facto choice between reallocation of the IBRD lending activities and creation of new institutions to meet unforeseen needs.

17. For these reasons, I believe that the size of the Capital Increase ought to exceed the minimum calculated as being required to sustain growth at 5% per annum for five to six years. This minimum itself depends upon various assumptions about inflation, repayment terms, and so forth. ~~A range of $30 to $35 billion encompasses many, but not all, of the possible "packages" of assumptions. (Annex Table 2 has details)~~. Allowance for "head room" above this minimum would warrant ~~justify~~ a doubling of the ~~a~~ Capital ~~Increase of roughly $40 billion.~~ including the Selective Increase 1/ (Annex Table 2). Discussion of the Rather than tying the Capital Increase to a fixed U.S. dollar amount - with the number of shares implied varying from day to day - it seems preferable to express the recommended increase as a percentage of the current total. What is proposed therefore can be simply stated: it is doubling of the IBRD's capital base.

1/ This figure, assumes full subscription to the Selective Increase. A total of 326,790 shares have been allotted for subscription, whereas only 284,474 shares had actually been subscribed through November 15, 1978. The figure of $41,7 billion is based upon the 326,790 shares and assumes each share is worth $127,500.

41.7 doesn't assume anything re Sel Incr

18. It is predictable that member governments' reactions to this proposal will be influenced by a number of considerations other than those cited in this memorandum. ~~In particular, the question of~~ the budgetary impact of the proposed Capital Increase is bound to arise. There will ~~also be~~ questions about how a Capital Increase of this size is to be distributed among member governments. While the Capital Increase proposal which the Executive Directors finally approve for submission to the Governors will have to cover these points, it may be helpful at this stage to concentrate attention on the central issue of size. Some of the other pending issues, such as the proportion to be paid-in or the distribution of shares, are not closely tied to the size of the Capital Increase in any event. They would be likely to arise regardless of whether the proposed Increase were 75%, 100% or 150%. Moreover, a consensus on size - if it can be achieved - will lend valuable momentum to the negotiations as a whole.

omit?

19. In summary, then, the recommendations are that

- the size of the Capital Increase not be linked to any particular growth rate

- the negotiations proceed on the basis of a proposed doubling in IBRD capital.

F11/4/35

Fred 11/6/78

Cap Inc – on a purely personal basis – he will be back in time 11/15

He told Cargill he would give an ans re timing etc by 11/15 –

In reading the Gov's statements found them not as supportive as he had anticipated –

He believes US should go for doubling of capital with none paid-in –*

gives greatest chance of dealing with non-approp.

if pd-in is req'd, would go for a much smaller figure –

the same but better than amending the Articles.

McN: if there is a substantial trade-off, I personally favor the doubling + 0 pd-in –

Another major issue is the graduation policy –

what is our policy; how do we see the future –

he suggests: a growing basic need rational for the Brazils, Yugos, Rumanias, Koreas, Mexicos –

Re Human Rights trying to develop pragmatic approach among some OECD countries

Re salaries: wants to talk to Syndicate re how to finish it off –

if it comes a cropper, all bets are off –

Voting Rights: something must be done with Japan –

he was appalled at the scenarios re maintaining the LDC votes

(e.g. India replacing Japan) –

Re seats: I urged they weigh relation to votes –

Maintenance of Value – P+B is supposed to be doing a paper on the underlying economic issues – it cannot be settled as a legal matter –

what is the function of main. of value; what are we trying to do –

Hearings: believes House hearings before mid-Dec (IDA 6 Jan or Feb) –

*Treasury is sending people to NY to discuss with Jim Conn

765

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

7-11/4/36

OFFICE MEMORANDUM

TO: Mr. McNamara

DATE: November 2, 1978

FROM: P. N. Damry

SUBJECT: Views of Mr. Johnston and Others on Resumption of Capital Increase Discussions with Particular Reference to Voting Rights Issue

1. Mr. Johnston urges discussions should be resumed as soon as possible: however, like some others like the British and Canadian Directors, he feels this means "as soon as it is judged that the U.S. can engage in meaningful talks".

2. He feels the resumed discussions should commence informally simply because the earlier round of informal talks was left incomplete.

11/3 3. Voting Rights and Board Representation have special significance for his constituency. At the same time he recognizes that any precipitate attempt to secure a decision on Voting Rights could prove divisive and diversionary; so that the principal topic of the size of the increase should not go off at a tangent, he thinks we should aim initially only at some sort of broad understanding on Voting Rights and Representation and that a firm decision could await a firm decision on the size of the Capital Increase itself. He wants this broad understanding at an early stage to preclude a misunderstanding that the device of special share allocations is aimed principally at preserving particular constituencies (Latin American and African). Within the broad understanding to be arrived at he would like it understood that, in the final analysis, increasing Board seats would be resorted to not only to protect the Latins and Africans, but also any other constituency jeopardized by some circumstances like the splitting of the Middle East constituency.

4. He thinks his Australian authorities' attitude on Voting Rights is based on the premise that the Bank's integrity rests on the principle of relating voting power to the size of the subscriptions. At the same time, lest rigid adherence to this principle endanger the representation of non-oil developing countries, he would press for an increase in membership votes rather than special, selective share allocations designed solely to protect non-oil developing countries.

5. By contrast with Mr. Johnston, on the question of the importance of taking up the Voting Rights issue early, are Mr. Drake and other E.D.'s who feel that a conflict of interest is latent in this issue and its premature surfacing might indefinitely postpone a purposeful discussion on the Capital Increase itself. These Directors feel, therefore, that while there should be an early indication that no final recommendation on the Capital Increase would go to the Governors without a firm recommendation also on the Voting Rights question, the discussion of the size and timing of the Capital Increase should be resumed without any material discussion on the Voting Rights. The Nordic chair, which has always strongly supported greater representation to developing countries, at this stage, however,

would probably agree to avoid this divisive issue until a firm decision on the quantum of Capital Increase is taken. Nor is the membership-vote solution attractive to many Directors, including developing countries like India, because it is not easy to rationalize with reference to the normal criteria for fixing quotas in the IMF and shares in the Bank. The solution most acceptable would be a 21st or even a 22nd seat.

cc: Mr. Stern
Mr. Gabriel

PNDAMRY/at

757

711/4/37

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

TO: General Capital Increase Steering Group

DATE: November 2, 1978

FROM: K. Georg Gabriel, Director, PAB

SUBJECT: General Capital Increase Proposal: What Should It Say?

1. Assuming that a specific proposal for a General Capital Increase is to be distributed to the Board on or about December 1, what should it say? This note tries to identify the main issues and to present those alternative positions which might plausibly be taken. Four issues are covered: (a) the size of the increase; (b) the proportion to be paid-in; (c) the distribution of shares among countries; and (d) the timing of subscriptions.

Size of the Increase

2. Past discussion in the Board on the size of the General Increase has tended to focus on current dollar amounts: typically in the range of \$30 to \$40 billion. Some of the Governors' speeches, on the other hand, have referred to a "doubling" of the Bank's capital. Ambiguity of the doubling concept - that is, whether it refers to the capital before or after the Selective Increase - is generally recognized.

3. The plausible alternatives which might be proposed are as follows:

(a) \$40 billion. This could be justified in light of the higher than expected U.S. dollar inflation over the past year. It would give the Bank desirable "head room". The major shareholders (with the possible exception of the UK) would almost certainly regard such a proposal as an opening gambit inviting a lower counter-proposal from them.

(b) \$35 billion. This is the least ambitious figure which seems at all plausible. It could be presented as a genuine compromise between the higher figures advocated by the developing countries (and sympathetic developed countries) and the lower figures advocated by the United States and Germany.

(c) "doubling". This would be the boldest proposal. Currently authorized capital is SDR 34 billion. In current dollars, a doubling would amount to about \$45 billion. The current dollar figures would of course change in the future.

Paid-In Component

4. The issue with respect to the paid-in component is fairly clear: we can stick with the 10% proposal, letting the United States present the case for a lesser proportion, or we can try to structure the debate on this point ourselves by indicating the circumstances under which a lesser proportion paid-in might be in the interest of the Bank and its borrowers.

Yes
let's develop
strong argument
for 10% or 5%-

5. The latter approach would acknowledge the trade-off between paid-in capital and retained earnings. If other things are the same, a lesser volume of paid-in capital will mean that lending charges need to be higher. Borrowing countries would obviously prefer to have lower lending charges, but they are (or should be) even more concerned with a large and reliable flow of capital from the IBRD. If, therefore, the choice were between a doubling of capital with, say 7.5% paid-in and a $25 or $30 billion increase with 10% paid-in, a good case could be made that doubling would be more in the borrowing countries' interest.1/

6. Although we do not know the U.S. position on this point, I would expect them to argue that even $35 billion is obtainable only if the paid-in component is foregone. With 10% paid-in the politically feasible limit - from their point of view - might be $20 billion or less. The question for us is whether to try to pre-empt this choice by stating in the December 1st memorandum that the alternative to $35 billion with 10% paid-in ought to be a doubling of the Bank's capital with a lesser proportion paid-in.

What is
US position
what are trade-offs
for US

Allocation of shares

7. There are two main issues to be dealt with in the allocation of shares among member countries: (a) how to increase Japan's share, and (b) how to avoid a reduction in the voting power of the non-oil developing countries.

8. Japan's desire to increase its share could be accommodated either through a special supplementary subscription, which would come on top of the uniform general increase, or through a de facto reallocation of part of the subscription which would otherwise be allotted to the

I favor
this

1/ A higher statutory limit could accommodate more relaxed repayment terms and therefore lead to lower annual debt service payments by borrowers even with somewhat higher interest rates.

United States. The latter approach has the advantage of separating the "developed country" part of the voting rights problem from the question of the appropriate balance between developed and developing countries. It would also be responsive to the sense of the Congress resolution in favor of a reduced U.S. share in IBRD capital replenishments. The magnitudes involved are illustrated in the following table which notionally assumes a 75% increase in both authorized capital and shares allotted for subscription. what %? for IBRD

	After Full ~~to~~ Subscription to Selective Increase	After Notional 75% Capital Increase
Authorized Capital (shares)	340,000	595,000
Subscribed Capital (shares)	326,790	571,883
Japan's Capital (shares)		
- with pro rata increase	n.a.	23,693
- with voting power equal to Germany	n.a.	30,821
- difference		+ 7,128
U.S. Capital (shares)		
- with pro rata increase	n.a.	136,036
- 20% of increase	n.a.	126,754
- difference		- 9,282

As the figures show, there would be more than enough unallocated shares (13,210 at present) to accommodate a significant increase in Japan's voting power. Alternatively, the U.S. shares in excess of 20% of the GCI would also be sufficient to achieve this objective.

9. The decline in the voting power of the non-oil developing countries is probably best avoided through a supplementary allocation of shares (i.e., over and above the percentage increase allotted to all member countries), If this is the approach followed, it is necessary to specify both the total size of the supplementary allocation and its distribution among the non-oil developing countries. The size question hinges on whether the objective is to offset precisely the declining contribution of membership votes - thereby keeping total voting power for the group at roughly 30% - or to seek a modest increase in total voting power to, say, 33%. In the example cited above, the non-oil developing countries would need to subscribe to about 16,000 shares over and above the 75% GCI in order to maintain their voting power at just over 30%. ~33%?

10. The distribution of such a supplementary increase would be highly contentious. The best approach in the December paper might be to finesse the issue by simply stating management's support for a supplementary increase of a given size and leaving the distribution of the increase to be negotiated among the developing countries. Were the paper to propose a specific distribution, the most likely recommendation would be either: (a) an equal allocation to each country; or (b) an allocation which corrects the "low" subscriptions of those countries whose initial IBRD subscriptions were well below their IMF quotas; or (c) a combination of these two approaches. The equal allocation approach would be consistent with an attempt to offset the erosion in relative importance of membership votes. The second approach - sometimes referred to as the "Latin American twist" - would have political appeal in that it would help protect the Latin American constituencies which are most exposed to the threat of loss of Board representation.

Yes

Timing

11. The choice with respect to timing is whether to stick with the FY83 starting date or to accept the German suggestion that subscriptions should begin in FY82 and extend over five years. The German proposal would imply a test of Congressional willingness to support the GCI in FY81, i.e., the first year after the U.S. presidential elections.

Hold to FY83 [illegible] Use FY81 for [illegible]

Recommendations

12. While there are obviously a number of packages which would be acceptable, the essential choice would seem to be between a "compromise" proposal and an "advocacy" position. A reasonable "compromise" proposal would be a 75% increase in the Bank's capital with 10% paid-in. This would be equivalent at current exchange rates to an increase in authorized capital of about $34 billion. An advocacy proposal, on the other hand, could be based upon a doubling of authorized capital (about $45 billion).

13. My recommendation would be to proceed with an advocacy proposal but to indicate, either explicitly or implicitly, a willingness to accept less than 10% paid-in. A reduction in the paid-in component could be achieved by dividing the increased subscriptions into two tranches. The first tranche might be an across-the-board increase of either 33% or 50% (i.e., about $14 billion or $21 billion) with no paid-in. This would have the effect of reducing the average proportion paid-in in all shares to either 7.5% of 6.67%. The size of the second tranche would then be sufficient to bring the total of shares allotted to roughly double the current total (326,790 shares worth about $43 billion). Thus, depending upon the size of the first tranche, the second tranche might be as small as $22 billion or as large as $29 billion. The second tranche would have

[illegible] 75%, 10% No - don't indicate a paid-in component (of either 7.5% or 6.67%) and would be allocated so as to increase the relative voting power of Japan and maintain the relative voting power of the non-oil developing countries at 30.1%.1/ I would propose that the subscriptions begin in FY82 and that the non-oil developing countries be left to work out the detailed allocation of their "supplementary" shares.

14. The December memorandum would emphasize that a $43 billion capital increase would not imply any particular real rate of growth for the IBRD. The rate of growth would be determined by the Board in its annual review of the five-year lending program. The emphasis of the memorandum would be upon the need to give the Bank sufficient "head room" to sustain a significant real rate of growth over the next few years.

Agree

Yes

Distribution: Messrs. McNamara
Broches
Cargill (o/r)
Chenery
Damry
Koch-Weser
Stern
Wood

DJW:bc

1/ Assuming the United States is allotted 20% of a $22 billion increase involving 6.67% paid-in, the budgetary cost for the United States would be only $293 million spread over five years.

711/4/34

SALIENT POINTS ON CAPITAL INCREASE

EXECUTIVE SESSION OF THE BOARD, MARCH 16, 1978

The following comments or questions were raised by Executive Directors in connection with the capital increase:

Mr. JANSSEN:

* Would a positive decision by the Board on full cost-of-living increases for the staff politically antagonize and have a negative effect on the U. S. position regarding the capital increase?

* Given concern about what would happen to the Bank's lending program after FY79, it was necessary to avoid being caught in a time squeeze by coming to some formal conclusion on the capital increase by the beginning of next year. Advancing the capital increase by not one but two years beginning in 1981, with a five-year period for paying in the capital, should be carefully considered by the Board.

Mr. LOOIJEN:

* The premise that Bank salaries were, a priori, too high and it was up to the Bank to prove they were not, was illogical.

* Given that the U. S. Administration was known to support at least a five percent increase in real lending, it was not necessarily wise to postpone the entire discussion of the capital increase because one of the 130 member countries, albeit an important one, was not ready to participate in that discussion.

* Had there not been a formal Board decision to finish the capital increase discussions by July 1, 1978?

Mr. THAHANE:

* What timing was contemplated with regard to action on the capital increase? What could Directors tell their Governments when asked about this?

The following points and comments were made by Mr. McNAMARA:

* Further discussion leading to a formal decision on the capital increase should be deferred for at least the next two to three months. There was nothing to be gained by continuing the discussion

during that period. Although there was a critical point by which time a decision would have to be made affecting the Bank's ability to continue its lending program after FY79, the critical date for resumption of the capital increase discussion was several months away.

* Discussion should resume at the earliest possible moment, which would be when member governments were prepared to come to a formal decision. That moment was not likely to occur soon because several very complex issues, notably compensation and human rights, must be resolved before the United States would be able to take a formal position on the capital increase. Resolution of these fundamental issues would take at least six months, possibly nine, or even twelve. Developments would be monitored closely and the Board would be notified immediately if changes came about sooner.

* In the short run, it was imperative to continue working towards the objectives stated in the so-called Interim Program, along the lines of which work had been progressing for several years, while at the same time dealing with each of the controversies as intelligently and with as much unity as possible. Pursuit of the previously agreed-upon Interim Program would avoid penalizing the developing countries as a result of the delay in resolving the controversies.

* On the capital increase, the United States' position, as stated on several past occasions by Mr. Fried and reiterated now by Mr. Dixon, supported a continued increase of the Bank's lending by at least 5 percent in real terms and a modification of the capital structure to support that increase. However, the unresolved nature of the compensation and human rights issues made it difficult for the U. S. to act formally on a capital increase for the time being.

* On the Interim Program, the U. S. recognized that deferral of formal action by the Board in support of the necessary capital structure might compromise the FY79 lending program. The U. S. neither wished to see that program jeopardized nor to see deferral of the formal decision have an adverse impact on the Bank; it therefore supported the FY79 lending program at the previously planned level ($6.8 billion) which would have been associated with a formal decision on a capital increase at this time.

* On compensation, the U. S. position, again as previously stated by Mr. Fried, was that, in order for the Executive to obtain Congressional approval of a capital increase, it would be necessary to either see Bank staff salaries adjusted downward or, alternatively, to have evidence available showing that salaries should not be adjusted downward. The United States did not say the Bank could not have its capital increase unless there was a salary reduction.

* Regarding human rights, it was important to distinguish between its two components of civil and economic rights -- a distinction which Mr. McNamara had made in recent discussions with Messrs. Carter, Mondale, and Blumenthal. In Mr. McNamara's view, it was totally wrong to

2/8 To Mr. Gabriel
Has not Part II voting power fallen at certain times between 1960 and 1977. If so, show the data for appropriate dates.
Ernest

IBRD VOTING POWER
(%)

June 30:	1946[a/]	1950	1955	1960	1965	1970	1976	1977[b/]	After Selective Capital Increase[c/]
Non-Oil LDCs	26.19	25.97	25.29	23.25	28.37	30.06	30.85	31.11	29.98
Capital Surplus OPEC	-	-	-	.47	.78	.82	1.09	1.09	2.67
Other OPEC	1.26	1.61	2.71	2.39	3.51	3.94	3.97	3.95	6.47
Total Part II	27.45	27.58	28.00	26.11	32.66	34.82	35.91	36.15	39.12
Total Part I	72.55	72.42	72.00	73.89	67.34	65.18	64.09	63.85	60.88

a/ September 30.
b/ June 30, 1977; also includes memberships of Sao Tome & Principe and Maldives.
c/ Assumes that all subscriptions under the Selective Increase will be taken up.

P & B
2/6/78

use international financial institutions as instruments to advance civil rights, since this went beyond their charters and lay beyond the realm of their competence. However, it was entirely right for this institution to be made sensitive to the issue of economic rights, which did lie within its field of responsibility and with respect to which perhaps not enough attention had been paid in the past. This was a perfectly appropriate subject for Directors and Governments to raise, discuss in the Board, and ask Management to consider.

* The human rights issue and many others fell under the heading of politicizing the Bank. If politicizing the institution meant diverting it from the objectives of its Articles of Agreement and its creation, it was wrong, and must be resisted.

* Resolution of these difficult issues would be very time consuming. It was absolutely certain that there would be no decision by this Board on the compensation matter in June or July; this complicating factor should be taken into account in deciding how to deal with the cost-of-living adjustment matter.

* The Executive Directors were urged to convey to their Governments the clarifications made by Mr. Dixon regarding a March 16 Reuters news item on the purported U. S. Treasury Department guidelines for funding IFIs. The article did not correctly reflect the strongly supportive attitudes of the U. S. President, Vice-President, and Treasury Secretary for a strengthened World Bank and for requested congressional appropriations.

7 11/4/33

MEMORANDUM FOR THE RECORD

Meeting with Messrs. Solomon and Bergsten, U.S. Treasury, on IBRD Capital Increase, January 31, 1978

Present: Messrs. McNamara, Solomon, Bergsten, Fried

Mr. Solomon said that Treasury would be as forthcoming as possible on the General Capital Increase and supported an increase of lending in real terms of 5% per year. However, in view of the various issues raised on the Hill with regard to the Bank, the tactical scenario was of utmost importance. Treasury could not make a formal commitment to the capital increase until sufficient progress had been shown in those areas of concern to the Hill. According to Mr. Bergsten, there were two more general and three more precise, administrative issues:

(a) Policy leverage with recipient countries, i.e., to demonstrate maximum usage of such leverage;

(b) Human rights, i.e., to meet last year's legislative requirements;

(c) Salaries;

(d) Travel; and

(e) Accountability.

Policy Leverage

Mr. Bergsten argued that the Bank's use of policy leverage could best be documented through country reviews by the Board. Mr. McNamara replied that he had suggested a more thorough country review by the Board than was intended but he had not found Board support. The U.S. had finally to understand that ~~Mr. McNamara and the~~ U.S. was ~~were~~ not running the Bank. However, the issue of country reviews did not really relate to the first point. The Bank had just answered Mr. Fried's questions on policy leverage and effectiveness of Bank operations for a number of countries. These country notes demonstrated (i) substantial policy influence of the Bank, and (ii) influence in the right direction. Leverage was effected not only through policy dialogue but also through projects; it was more significant and more effective than in the case of other agencies because the Bank was more powerful.

Mr. Bergsten said that, in order to satisfy the Hill, specific cases should be cited where the Bank had successfully applied leverage to change recipient country policies. This would demonstrate that this mode of foreign assistance was more effective than other modes. He said that the underlying Congressional concern was control, and U.S. control could only be exerted through the Board. Mr. McNamara said that the Bank was much tougher through its staff and management than through its Board where LDCs and OPEC countries would vote against the full use of leverage (e.g., to stop lending), and also some Part I countries in the case of specific regions or countries (e.g., France in the case of West Africa). The Board had a narrower, political concept. Mr. Bergsten said that unfortunately these facts could not be quoted publicly.

It was agreed that Treasury would determine whether the country notes supplied to Mr. Fried were a satisfactory response to this first concern.

Human Rights

With regard to the second area of concern, Mr. McNamara said that the U.S. Government had no policy on human rights and that the Bank could not conform with a policy which had not been stated. He pointed to the inconsistencies in the present U.S. approach (e.g., South Korea or Indonesia versus Argentina) and suggested that Messrs. Blumenthal and Vance get together and agree on such a policy. He called attention to Mr. Fried's suggestion of (i) agreeing on clearly extreme cases of human rights violators among countries, and (ii) judging the other countries on a trend basis.

Mr. Bergsten (i) agreed that the present loan-by-loan procedure did not constitute a serious approach; (ii) proposed to differentiate by countries ("good and bad guys"); (iii) reported that a U.S. team was presently discussing the issue with other OECD governments; and (iv) promised that there would soon be a U.S. policy on human rights. It was agreed that the Bank would have to wait for such a policy to emerge.

Accountability

Mr. McNamara emphasized that he felt fully accountable to member governments. However, the content of certain documents had to be changed if they were sent to the Board. These trade-offs had to be clearly understood. Mr. Bergsten said that the Hill demanded end-use audits, i.e., detailed public scrutiny of the Bank's invoice and disbursement procedures. Mr. McNamara replied that the Bank had extremely well-developed disbursement procedures and he was prepared to have them examined by independent auditors, e.g., Price Waterhouse.

Mr. Fried disagreed with Mr. Bergsten. Congress was not so much enquiring about the Bank's disbursement system but rather asking whether the ultimate benefits of Bank projects accrued to the intended target groups. Mr. McNamara replied that these questions were addressed by OED and he explained OED's comprehensive system of auditing each individual project. He said that management was presently considering the benefits and risks of publishing OED's annual review of project performance audit results and that, in spite of the risks involved, he personally was in favor of publishing these reviews.

Messrs. Solomon and Bergsten were clearly impressed by the comprehensiveness of OED's activities; Mr. Bergsten recommended an early publication of the annual review (i.e., before Treasury had to testify) and expected a major beneficial impact on the Hill.

Operational Travel Policy

Mr. McNamara said that, as a responsible manager, he had to ensure that the operational travel policy reflected cost and efficiency criteria. The Bank's policy would probably soon be changed to an all-economy policy with limited exceptions, over the fierce opposition of the Staff Association. Staff believed that the proposed change in policy constituted a further unreasonable caving-in and that Mr. McNamara was yielding to U.S. pressures; the possibility of disorder could therefore not be excluded if a change in policy was announced. Mr. Bergsten said that any disorder would have a disastrous impact with Congress.

Salaries

Mr. McNamara said that the Bank was facing very serious problems on compensation. He reported on the actions he had demanded from the Kafka Committee, namely (i) to agree--in its next meeting--on a set of alternative principles, (ii) to hire consultants to collect the data required for evaluating the impact of the alternative principles, and (iii) to inform the two Boards that a conclusion could not be drawn before about six months from now. Messrs. Solomon and Bergsten argued that the consultants' report (of January 16, 1978) had greatly advanced the basis for arriving at a final conclusion within a considerably shorter period of time. A six-months' deadline would pose serious problems for advancing the capital increase. Mr. McNamara pointed to the complex implications of any change in compensation policies (e.g., on the pension fund system) and emphasized that a decision affecting the salaries of 5,000 staff members had to be based on a thorough analysis which required a time-consuming collection of data. However, he agreed to speed up such data collection to the extent possible.

In response to a question by Mr. Solomon, Mr. McNamara said he would not hold off action on a cost-of-living increase; together with Mr. Witteveen, he would recommend a full cost-of-living increase, effective March 1, to the Board. He did not want staff to be penalized for the inaction of governments, i.e., the delays of the Joint Committee in dealing with the issues. However, he expected the Board to agree to a less than 100% offset because the Board might be willing to sacrifice the strength of the institution for legislative action in the U.S.; it would thus be one of the rare occasions where he would lose in a Board vote. Mr. Solomon said that, under such circumstances, the staff might rally and the U.S. position would be weakened by Mr. McNamara's recommendation. As a compromise, he suggested an increase of about 3% for six months by March 1, 1978. Mr. McNamara agreed that this was a possibility the Board might adopt, but he was not prepared to recommend it.

Mr. McNamara pointed to the deviation between the consultants' recommendations and the recent U.S. proposal (by Mr. Cross to the Joint Committee), which made the U.S. position appear rather weak. There was a basic difference in position between the U.S. and him: he wanted to analyze and judge the issue of whether staff were overpaid or underpaid on a professional basis; the U.S. Government wanted the salaries to be cut and the staff to be penalized in order to obtain Congressional action.

Mr. Solomon admitted that the U.S. proposal was obviously to be negotiated. The U.S. would agree to certain changes and might, for example, propose recruitment bonuses for certain skills or nationalities. Mr. McNamara said that he might accept a compensation package corresponding to the U.S. private sector with certain recruitment bonuses, etc. It was agreed to establish alternative principles, collect and evaluate the necessary data as soon as possible, and then have bottom-line negotiations.

Capital Increase

Mr. McNamara said that it was an untenable position to let action on the capital increase hang on the salaries issue. Mr. Bergsten suggested that, as a compromise, the Board could ease the lid on the lending ceiling. Mr. McNamara agreed that this might be a possibility; the U.S. might tell the Board that (i) it could not make a formal commitment to the capital increase before the salaries issue had been settled, but (ii) in view of the importance attributed to a satisfactory growth of foreign aid, there would be no limitation imposed on the FY79 lending program. Mr. Solomon confirmed that this approach could be supported by Treasury.

CKW
February 3, 1978