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Folder Title: Irving S. Friedman Chron files - Correspondence 04

Folder ID: 1784922

ISAD(G) Reference Code: WB IBRD/IDA 03 EXC-10-4482S

Series: Presidential chronological files of Economic Advisor Irving Friedman

Sub-Fonds: Records of President Robert S. McNamara

Fonds: Records of the Office of the President

Digitized: June 14, 2013

To cite materials from this archival folder, please follow the following format:
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Washington, D.C.

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Friedman: Presidential Chron files / Interview with Jan. 1969
Dutch "Algemeen Handelsblad"

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1784922
A1995-169 Other #: 1 210707B
Irving S. Friedman Chron files - Correspondence 04

Sir Denis Rickett (through Mr. Friedman)

January 21, 1969

Ugo Sacchetti

Proportion of Bank Lending in Aid
to Less Developed Countries

The attached calculations are based on the most readily available data. It should be emphasized that the percentages represent very rough indicators but they may do for your purposes. Strictly speaking, the numerators and the denominators of the ratios are not comparable and this is the most important factor to be borne in mind in using the ratios. Moreover, even though I provide a period of three years, and an average for that period, this may not be sufficiently revealing. It is possible that one would obtain a different picture by using commitments instead of disbursements. Moreover the figures for the IBRD could be different if loans to developed countries (such as Japan) and repayments from such countries (e.g. France) are excluded.

If you wish to have more precise ratios, we would be glad to compute them but some time would be required to obtain the basic data.

Attachment

USacchetti:fm

Calendar Year Data in \$ Million

	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>Average 1965-67</u>
(A) Total net flow of financial resources from DAC countries to LDCs and multilateral agencies	11,493	10,471	11,306	11,090
(B) Total net loan disbursements to LDCs from bilateral and multilateral sources	2,554	2,699	3,250	2,834
(C) Net IBRD loan disbursements	290	446	405	380
(C) as % of (A)	2.5	4.3	3.6	3.4
(C) as % of (B)	11.4	16.5	12.5	13.4

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- (A) Includes net official and private flows from all DAC countries including Japan in the form of grants, grant-like assistance and loans as well as private investment capital plus capital subscriptions and other contributions (e.g. bond issues) to multilateral agencies.
- (B) Includes net disbursements (i.e. gross disbursements less repayments) on loans to LDCs on bilateral account from DAC countries (but excluding net disbursements on loans repayable in recipients' currencies) and net disbursements by multilateral agencies. The latter are net of loan repayments and net of LDCs' capital and other contributions to them.
- (C) Includes disbursements to all member countries (not only LDCs); and it does not include capital subscriptions to IBRD or changes in IBRD bond holdings by member countries.

Source: Statistical Tables to the 1968 Annual Aid Review Second Revision DAC/AR(68)4 of October 30, 1968. Figures for net IBRD loan disbursements are from IBRD Treasury's Department.

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

FROM: Irving S. Friedman

SUBJECT: Dutch newspaper "Interview"

DATE: January 2, 1969

As I mentioned over the phone today, the attached set of answers were sent to Mr. Clark with respect to the questions for the Dutch newspaper "interview". I have confined myself thus far to the following three questions.

1. How do you propose to raise the money you will need to double the Bank Group's financing over the next five years, in view of:
 - A. The scarcity of funds in the capital markets;
 - B. The balance of payments difficulties of many rich countries and the consequent reduction of their aid;
 - C. The concern that expansion threatens the Bank's reputation as a sound and successful institution.
2. Are you worried about the increasing debts of some developing countries?
5. Do you believe that your announced view of the World Bank as being at least as much a development institution as a bank diminishes confidence in its bonds in the money markets, and thereby creates problems for the Bank when it makes bond issues?

I am preparing another paper for you which goes into these matters in somewhat greater depth. The attached answers are designed for a more general audience whereas I assume that the "White Paper" that you have requested might be more technical at least in the first instance. Mr. Rotberg indicated that he would like for the time being to work on this thought independently.

Attached: as stated

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President has seen

Answer to Question 1

1. Generally speaking I propose to raise the money needed to finance the World Bank over the next year by borrowing in capital markets of the developed countries and from other investors such as central banks throughout the world who find the holding of World Bank bonds attractive. Before entering into more detail aspects of the question, I would like to emphasize my conviction that the Bank's position in capital markets is based essentially on its record of well-conceived operations, resulting in a diversified and balanced portfolio and a satisfactory earning record, and its insistence on high standards from the borrowing countries. The Bank makes its own careful appraisals of investment opportunities and the conditions of the national economies, including the creditworthiness of its borrowers. It does everything possible to insure that loans from the Bank are used for productive purposes, including close scrutiny of the execution of projects, which add to the economic strength of the borrowing countries and lay the basis not only of servicing of debt to the Bank, but also to other public and private investors.

Answer to l.a.

l.a. The Bank can operate successfully in the capital markets of the world as they now exist. As in other markets, the market for loanable funds is determined by demand and supply conditions which are adjusted by the mechanism of prices, in this case by the rise in the price of money, i.e. the rate of interest. It is the rise in interest rates which give us the basis of speaking of a "scarcity" of capital rather than amount of loanable funds available in such capital markets. This scarcity is not related to a reduction of funds in capital markets. Savings in the developed countries have increased markedly together with the extraordinary rise in national income (insert some figures). More particularly sales of new bonds in major capital markets have increased sharply; such sales amounted to the equivalent of -- billion in 1965, ^{\$45} billion in 1966, ^{\$64} billion in 1967, and available information indicates further increases in 1968.

In comparison with these overall totals, the borrowings of the World Bank are relatively small. We assume that the World Bank would need to borrow over the coming years about a billion or so annually on a gross basis, and three-fourths of a billion on net basis. This would be between 1% and 1.5% of the aggregate long term funds raised in the United States and other industrial countries. Moreover, even the largest issues by the Bank in the United States (250 million) does not exceed in magnitude any of the several largest long-term offerings by corporations, states and municipalities and also far less than the largest offerings of Federal agencies. Similarly in Europe we attempt with the assistance of trained and experienced bankers to keep our offerings in line with the practical possibilities of absorption by the public in capital markets or through private placements.

1.a

It may be argued that most bonds sold in the capital markets of the industrialized countries are domestic rather than foreign bonds. The floatation of World Bank bonds might be regarded as much larger proportionately if they are compared to issues made by foreign and international institutions rather than domestic. The bonds of the World Bank are, however, of a somewhat unique nature. They are denominated in the domestic currencies of the countries in which the issue is made. They are backed by the Bank's financial resources, held in a variety of currencies, mostly of the major industrial countries, as well as by a guarantee of all member countries of the Bank. For example, ~~A~~ German investor in a World Bank bond is buying a security of an institution which is guaranteed by his own Government as well as by others. These Investors can buy World Bank bonds with virtually the same degree of confidence as they buy the bonds of their own national government. Our experience thus far indicates that except for the occasional inevitable misjudgement of local market situations at any particular time, there is no indication that the World Bank is reaching the limits of its borrowing ability. Indeed in many countries there are many signs that the World Bank could borrow much more than it has been doing and anticipates doing in the foreseeable future. The reason, in the briefest form, is that the World Bank bond is a sound and attractive investment.

Answer 1 b.

1.b The persistence of balance of payments difficulties in some of the industrial countries, particularly the United States and the United Kingdom, have been an important factor in the fund raising activities of the Bank. The Bank is eager to do its utmost not to enhance such balance of payments difficulties, while at the same time fulfilling the responsibilities given to it in its Articles of Agreement, namely, assisting the development of the less developed countries of the world. In ~~those~~ ^{of the United Kingdom} cases where balance of payments difficulties have led to drastic restrictions of exports of capital, such as ~~the United Kingdom~~, the World Bank has not tried to borrow money in their capital markets in recent years. In the case of the United States, which is the largest capital market, there has fortunately been a recognition by the United States authorities that exports of capital to the developing countries should be maintained. This recognizes the basic principle that poor countries are not in a position to carry on development unless they receive new inflows of capital from abroad on a continuing basis. The United States in response to its balance of payments difficulties has "tied" its development assistance to purchases in the United States. In the case of the World Bank, however, such tying is incompatible with its multilateral character and the principle of international competitive bidding which must guide the Bank in its lending operations. Thus funds disbursed by the Bank to its borrowers can be used in any member country plus Switzerland, and the amount of exports which any industrial country receives as a result of Bank loans depends on its international competitiveness. The United States authorities have continued to allow the World Bank to have access to the United States capital market. In this connection, it may be noted

that the cumulative effect of all World Bank transactions has been to make a very large positive contribution to the United States balance of payments and it is expected that it will continue to do so. The World Bank is not only a borrower in the U.S. capital market, but is also an investor. It holds a large portion of its current cash and securities in the United States. As of latest available date, the Bank's holdings of cash and securities amounted to about \$___ billion.

I should like to take this opportunity to suggest that, as in the case of Germany, the countries which experience large balance of payments surpluses should permit the Bank to take advantage of these conditions by borrowing more heavily than otherwise in the markets of such countries.

Question 1.c.

1.c As for the question regarding the threat to the Bank's reputation as a sound and successful institution, I would like to assure readers of this interview and all others that I am determined to make sure that this threat does not materialize. First of all I should like to emphasize that the increase which is taking place in Bank lending is a result of a careful country by country review of investment possibilities conforming to the high standards of the World Bank. From my past experience, I know an increase in the size of a corporation's activities need not jeopardize its strength. Indeed such increase can enhance its reputation if the investing public is confident that the corporation is well managed.

The World Bank's reputation rests on a number of factors which might be summed up in terms of financial management. The Bank has a broad and diversified portfolio. After more than 20 years of experience the Bank's ability to appraise and evaluate projects is more efficient than ever and we are constantly improving our techniques. The Bank limits its lending to any one country to amounts that are well within the creditworthiness of the country, i.e. its ability to service its obligations to the Bank. Moreover, the Bank maintains continuous relations with its borrowers be they public or private institutions. It advises, persuades and, where necessary, insists that governments pursue policies designed to insure effective use of funds borrowed from the Bank and to make possible repayment to the Bank. The Bank adjusts its lending rate to longer-run changes in its borrowing rate. The Bank has earned substantial net income, now amounting to a net of \$180 million a year. It has built substantial reserves and has a strong liquidity position.

Before the Bank enters new fields of investment such as education or new countries, a most careful examination is made to make certain that the investment will increase the capacity of the country to produce and its capacity to repay debt. The Bank has had a continuous history of expanding its scope of investments to new fields, as for example, entering into agriculture. However, such expansion should not jeopardize the reputation of the Bank, because the Bank does not intend to make loans, for whatever the purpose may be, unless it has a sound basis to believe that the funds will be well used and the loans repaid.

Question 2

The increasing debts of some of the developing countries is becoming one of the most critical problems for certain developing countries, but I believe that the problem is manageable, if handled in time. At present the annual debt service on amortization and interest of developing countries accounts on average of about 8% of their earnings from exports of goods and services. In some countries however external debt service is 20% or even more of exports. In such cases, concern over the ability to repay is inevitable. Experience teaches us however, that other factors such as growth and diversification of exports, debt servicing record, ability to attract private capital, political stability, etc., all should be weighed in the judgement of creditworthiness. These factors, where unfavorable, can frequently be changed by proper policies.

We regard it as part of our job in the Bank to do all possible to assist countries to pursue those policies which strengthen their capacity, both at present and in the future, to service debt. Developing countries cannot hope to develop satisfactorily without increasing their external debt. However, some external debt has been incurred for very poor reasons and on excessively onerous terms. Our aim should be to insure that debt is incurred on reasonable terms for productive purposes and that the ability of the country to repay debt constantly strengthened. Many developing countries are showing a much more responsible attitude in incurring more external debts, e.g., by severely limiting increases in short-term external debt. For those countries which reach the limits of their debt servicing capacity, the World Bank is simply not in a position to make any new loans. This is why we have attached urgent importance to the replenishment of the resources of the

International Development Association, which by providing funds from national budgets, enables credits to be made on a fifty-year basis virtually interest-free.

Question 5

I do not believe that regarding the World Bank as a development institution diminishes confidence in its bonds. The World Bank is a special type of a bank whose characteristics are clearly set forth in the Articles of Agreement. These Articles have guided the institution for over 20 years. Under these Articles, the World Bank has a clear responsibility to help bring about the economic development of its member countries. It is for this reason that countries have subscribed over \$22 billion, of which over \$2 billion has already been paid in and the remainder still uncalled for becomes in effect a guarantee fund. To help pursue its development objective countries have given the Bank access to capital markets and in other ways have enabled the Bank to raise funds in the developed countries for use in productive investment in the developing countries. It is its special responsibilities which make the World Bank a development institution, while at the same time retaining its essential character as a bank operating on the principle of maintaining and strengthening its financial structure and insuring its liquidity in the short run and its financial soundness in the long run. I am sure that if we adhere to the principles of sound financial management, as summarized above, the Bank will continue to enjoy the confidence of the world's capital markets as expressed by the high rating of World Bank's bonds and the success we have had in expanding our borrowing operations.

QUESTIONS AND ANSWERS

1. How do you propose to raise the money you will need to double the Bank Group's financing over the next five years, in view of:
 - a. The scarcity of funds in the capital markets;
 - b. The balance of payments difficulties of many rich countries and the consequent reduction of their aid; and
 - c. The concern that expansion threatens the Bank's reputation as a sound and successful institution.

ANSWER:

1.a. First of all, I don't accept the idea that there is an absolute scarcity of funds. As in other markets, the prices for loanable funds, i.e., the rate of interest, are determined by supply and demand and we have been going through a period of heavy demand. However, there has not been a reduction of available funds in capital markets. On the contrary savings in the developed countries have increased markedly together with the extraordinary rise in national income. As to the Bank itself, I would point out that we raised without difficulty over \$800 million in the first six months of our 1969 fiscal year. More generally, sales of new bonds in major capital markets have increased sharply; such sales amounted to the equivalent of about \$37 billion in 1965, \$45 billion in 1966, \$64 billion in 1967, and available information indicates further increases in 1968.

President has seen

In comparison with these overall totals, the borrowings of the World Bank are relatively small. We assume that the World Bank would need to borrow over the coming years about a billion dollars or so annually on a gross basis, and three-fourths of a billion on a net basis. This would be between 1% and 1.5% of the total of long-term funds raised in the United States and other industrial countries. Moreover, even the largest World Bank issues in the United States (\$250 million) compare in size to long-term offerings by large corporations, states and municipalities and are far less than the largest offerings of Federal agencies. Similarly in Europe, with the assistance of trained and experienced bankers, we attempt to keep our offerings in line with the practical possibilities of absorption by the public in capital markets or through private placements.

You will note that I am comparing the Bank's bonds to domestic rather than foreign obligations. That is because of their unique nature. They are denominated in the domestic currencies of the countries in which the issue is made. They are backed by the Bank's financial resources, held in a variety of currencies, mostly of the major industrial countries, as well as by a guarantee of all member countries of the Bank. A German investor in a World Bank bond is buying a security of an institution which is guaranteed by his own Government as well as by others. Taken together, the guarantees of the countries belonging to the European Common Market, the United Kingdom and the United States, amount to approximately \$11.6 billion. Investors can buy World Bank bonds with the same or greater degree of confidence as they buy the bonds of their own national government.

There is no indication that the World Bank is reaching the limits of its borrowing ability. Indeed in many countries there are many signs that the World Bank could borrow much more than it has been or anticipates borrowing in the foreseeable future. The reason, in the briefest form, is that World Bank bonds are a sound and attractive investment.

ANSWER:

1.b. Balance of payments difficulties in some of the industrial countries have had an effect on the fund raising activities of the Bank. The Bank wishes to do its utmost not to increase such balance of payments difficulties, while at the same time fulfilling the responsibilities given to it in its Articles of Agreement, namely, assisting the development of the less developed countries of the world. In the case of the United Kingdom where balance of payments difficulties have led to drastic restrictions of exports of capital, the World Bank has not been active in its capital market in recent years.

In the case of the United States, which is the world's largest capital market, there has fortunately been a recognition by the United States authorities that exports of capital to the developing countries should be maintained. This recognizes the basic principle that poor countries are not in a position to carry on development unless they receive new inflows of capital from abroad on a continuing basis. The United States in response to its balance of payments difficulties has "tied" its own development assistance to purchases in the United States. In the case of the World Bank, however, such tying is incompatible with its multilateral character and the principle of international competitive bidding which must guide the Bank in its lending operations. Thus

funds disbursed by the Bank to its borrowers can be used in any member country, or in Switzerland, and the amount of export orders which any industrial country receives as a result of Bank loans depends on its international competitiveness. The United States authorities have continued to allow the World Bank to have access to the United States capital market.

I might also point out that countries which experience large balance of payments surpluses (such as Germany) are permitting the Bank to take advantage of these conditions by borrowing more heavily than otherwise in their markets. The Bank in fact borrowed almost \$394 million equivalent in Germany in 1968.

ANSWER:

l.c. As to any possible threat to the Bank's reputation as a sound and successful institution, I am determined that this question will not arise. First of all I should like to emphasize that the increase which is taking place in Bank lending is the result of a careful country-by-country review of investment possibilities conforming to the traditionally high standards of the World Bank.

The World Bank's reputation rests on a number of factors which might be summed up in terms of financial management. The Bank has a broad and diversified portfolio. After more than 20 years of experience the Bank's ability to appraise and evaluate projects is higher than ever and we are constantly improving our techniques. The Bank limits its lending to any one country to amounts that are within the creditworthiness of the country, i.e., its ability to service its obligations to the Bank. Moreover, the Bank maintains continuous relations

with its borrowers, whether governments or private corporations. It advises, persuades and, where necessary, insists that borrowers pursue policies designed to insure effective use of its funds and their repayment on schedule. Generally, it disburses funds only against invoices for specified goods and equipment, and it follows a careful program of field inspections of projects to make sure that progress is satisfactory.

The Bank has kept its interest rate on loans adjusted to longer-run changes in its borrowing rate. The Bank has earned substantial net income, now amounting to about \$180 million a year. It has built substantial reserves and has a strong liquidity position. This cash and liquid investment represents a substantial asset for the production of Bank income. It exceeds 40% of the Bank's present funded debt and is almost 40 times the Bank's yearly sinking fund requirements. Looked at another way, it puts the Bank in an exceedingly favorable cash flow position to meet its anticipated disbursements and its debt servicing obligations.

Before the Bank enters new fields of investment, and before beginning to lend in new countries, a most careful examination is made to make certain that the investment will increase the capacity of the country to produce and its capacity to repay debt. The Bank has had a continuous history of expanding its scope of investments to new fields, as for example, agriculture and education. However, such expansion should not jeopardize the reputation of the Bank, because the Bank does not intend to make loans, for whatever the purpose may be, unless it has a sound basis to believe that the funds will be productively used and the loans repaid. In fact agriculture and education are both keys to successful development, and development is the best guarantee of solvency and repayment capacity.

QUESTION 2:

Are you worried about the increasing debts of some developing countries?

ANSWER 2:

The increasing debt of some of the developing countries is becoming a serious problem but I believe that it is a manageable one, if handled in time. At present the annual debt service on amortization and interest of developing countries accounts on average for about 8% of their earnings from exports of goods and services. In some countries, however, external debt service is 20% or even more of exports, and such cases naturally cause concern. Experience teaches us however, that other factors such as growth and diversification of exports, trends in domestic savings and investment, and ability to attract foreign private capital, should be weighed in the judgement of creditworthiness. These factors, where unfavorable, can frequently be changed by proper policies, and much depends upon a borrowing country's demonstration of its will to development and its readiness to take the measures necessary to this end.

We regard it as part of our job in the Bank to do all we can to help countries pursue those policies which strengthen their capacity, both at present and in the future, to service debt. Developing countries cannot hope to develop satisfactorily without increasing their external debt. However, some external debt has been incurred for very poor reasons and on excessively onerous terms. Our aim should be to insure that debt is incurred on reasonable terms for productive purposes and that the ability of the country to repay debt is constantly strengthened. Many

developing countries are showing a much more responsible attitude in incurring more external debts, e.g., by severely limiting increases in short-term external debt.

Even countries which follow sound borrowing policies, however, may reach the limits of their debt servicing capacity when they still present opportunities for productive development investment. The World Bank cannot meet the needs of such countries and this is why we have attached urgent importance to the replenishment of the resources of the International Development Association, or IDA. This institution, since it is supported by funds from national budgets, can extend credits on a fifty-year basis virtually interest-free.

QUESTION 3:

What are the prospects for the areas in which you have said the Bank wishes to make a particular effort, education, agriculture and population control? With regard to the latter, what criteria will you use in setting up programs, and how will you avoid adverse reactions on religious or ethnic grounds?

ANSWER 3:

In my speech to the Bank's Governors, I outlined the prospects for our agricultural and educational lending by saying that we intended to quadruple the volume of the former and triple the volume of the latter over the next five years. As far as population control is concerned, I should stress that this is a new field of operation for the Bank, and we are still working our way into the subject. The process of deciding how best to assist population control is not made easier by the fact that

far too little research has been done on this subject anywhere in the world.

But I must stress again that it is not the absolute size of a country's population which worries us, but its rate of population growth. We are seriously concerned that the rate of growth of countries' populations should not be so high as to negate the rate of their economic development. For example, if a country's gross domestic product is rising at a level of 4% per annum and population at a rate of 2.5% per annum, there is painfully little room for the improvement in the standard of living which we as a development agency want to see -- and which humane people all over the world hope for. It simply cannot provide the roads, the schools, the power and other basic facilities needed to cope with a rapidly growing population. Our aim is to give children in developing countries the possibility of growing up in a world where they can live with at least some degree of human dignity. In some cases this can only be achieved by limiting the growth of population to levels with which countries' efforts to promote their economic development can keep pace.

We fully realize, of course, the religious and ethnic and national sensitivities in the area of population control. Those pose thorny and difficult problems, but fundamental to our approach are respect for the dignity of man and for the right of nations to determine their own approaches to the population question. We are resolved however that the dangers of rapid population growth must be pointed out, and we are determined to extend help when asked.

QUESTION 4:

Do you believe that your announced view of the World Bank as being at least as much a development institution as a bank diminishes confidence in its bonds in the money markets, and thereby creates problems for the Bank when it makes bond issues?

ANSWER 4:

Certainly not.

In the first half of the current fiscal year the Bank has raised \$804 million equivalent in capital markets. This is a large amount by any standards, and can hardly be taken as a sign of wavering investor confidence in the Bank.

I do not believe that regarding the World Bank as a development institution diminishes confidence in its bonds. The World Bank is a special type of a bank whose characteristics are clearly set forth in the Articles of Agreement. These Articles, which also specify the high standards to be used in lending operations, have guided the institution for over 20 years. Under these Articles, the World Bank has a clear responsibility to help bring about the economic development of its member countries. It is for this reason that countries have subscribed over \$22 billion, of which over \$2 billion has been paid in, and with the uncalled remainder serving in effect as a guarantee fund. To help pursue its development objectives developed countries have given the Bank access to capital markets and in other ways have enabled the Bank to raise funds for use in productive investment in the developing countries. It is its special responsibilities which make the World Bank a development institution, while at the same time retaining its essential

character as a bank operating on the principle of maintaining and strengthening its financial structure, insuring its liquidity in the short run and its financial soundness in the long run. I am sure that if we adhere to the principles of sound financial management, as summarized above -- and we are determined to do so -- the Bank will continue to enjoy the confidence of the world's capital markets as expressed by the high rating of World Bank bonds and the success we have had in expanding our borrowing operations.

ROUTING SLIP

Date

December 30, 1968

OFFICE OF THE PRESIDENT

Name

Room No.

Mr. William Clark

0413

To Handle

Note and File

Appropriate Disposition

Note and Return

Approval

Prepare Reply

Comment

Per Our Conversation

Full Report

Recommendation

Information

Signature

Initial

Send On

Remarks

Attached are two copies of redrafts of answers to questions 1, 2 and 5. Can I be of any help on questions 3 and 4? I would appreciate having your reaction to the attachment.

From Irving S. Friedman

A1221

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Answer to Question 1

1. Generally speaking I propose to raise the money needed to finance the World Bank over the next year by borrowing in capital markets of the developed countries and from other investors such as central banks throughout the world who find the holding of World Bank bonds attractive. Before entering into more detail aspects of the question, I would like to emphasize my conviction that the Bank's position in capital markets is based essentially on its record of well-conceived operations, resulting in a diversified and balanced portfolio and a satisfactory earning record, and its insistence on high standards from the borrowing countries. The Bank makes its own careful appraisals of investment opportunities and the conditions of the national economies, including the creditworthiness of its borrowers. It does everything possible to insure that loans from the Bank are used for productive purposes, including close scrutiny of the execution of projects, which add to the economic strength of the borrowing countries and lay the basis not only of servicing of debt to the Bank, but also to other public and private investors.

Answer to l.a.

l.a. The Bank can operate successfully in the capital markets of the world as they now exist. As in other markets, the market for loanable funds is determined by demand and supply conditions which are adjusted by the mechanism of prices, in this case by the rise in the price of money, i.e. the rate of interest. It is the rise in interest rates which give us the basis of speaking of a "scarcity" of capital rather than amount of loanable funds available in such capital markets. This scarcity is not related to a reduction of funds in capital markets. Savings in the developed countries have increased markedly together with the extraordinary rise in national income (insert some figures). More particularly sales of new bonds in major capital markets have increased sharply; such sales amounted to the equivalent of ^{\$37} billion in 1965, ^{\$45} billion in 1966, ^{\$64} billion in 1967, and available information indicates further increases in 1968.

In comparison with these overall totals, the borrowings of the World Bank are relatively small. We assume that the World Bank would need to borrow over the coming years about a billion or so annually on a gross basis, and three-fourths of a billion on net basis. This would be between 1% and 1.5% of the aggregate long term funds raised in the United States and other industrial countries. Moreover, even the largest issues by the Bank in the United States (250 million) does not exceed in magnitude any of the several largest long-term offerings by corporations, states and municipalities and also far less than the largest offerings of Federal agencies. Similarly in Europe we attempt with the assistance of trained and experienced bankers to keep our offerings in line with the practical possibilities of absorption by the public in capital markets or through private placements.

1.a

It may be argued that most bonds sold in the capital markets of the industrialized countries are domestic rather than foreign bonds. The floatation of World Bank bonds might be regarded as much larger proportionately if they are compared to issues made by foreign and international institutions rather than domestic. The bonds of the World Bank are, however, of a somewhat unique nature. They are denominated in the domestic currencies of the countries in which the issue is made. They are backed by the Bank's financial resources, held in a variety of currencies, mostly of the major industrial countries, as well as by a guarantee of all member countries of the Bank. ~~For example,~~ A German investor in a World Bank bond is buying a security of an institution which is guaranteed by his own Government as well as by others. ~~These~~ I investors can buy World Bank bonds with virtually the same degree of confidence as they buy the bonds of their own national government. Our experience thus far indicates that except for the occasional inevitable misjudgement of local market situations at any particular time, there is no indication that the World Bank is reaching the limits of its borrowing ability. Indeed in many countries there are many signs that the World Bank could borrow much more than it has been doing and anticipates doing in the foreseeable future. The reason, in the briefest form, is that the World Bank bond is a sound and attractive investment.

Answer 1 b.

1.b The persistence of balance of payments difficulties in some of the industrial countries, particularly the United States and the United Kingdom, have been an important factor in the fund raising activities of the Bank. The Bank is eager to do its utmost not to enhance such balance of payments difficulties, while at the same time fulfilling the responsibilities given to it in its Articles of Agreement, namely, assisting the development of the less developed countries of the world. In ~~these~~ ^{of the United Kingdom} cases where balance of payments difficulties have led to drastic restrictions of exports of capital, ~~such as the United Kingdom,~~ the World Bank has not tried to borrow money in their capital markets in recent years. In the case of the United States, which is the largest capital market, there has fortunately been a recognition by the United States authorities that exports of capital to the developing countries should be maintained. This recognizes the basic principle that poor countries are not in a position to carry on development unless they receive new inflows of capital from abroad on a continuing basis. The United States in response to its balance of payments difficulties has "tied" its development assistance to purchases in the United States. In the case of the World Bank, however, such tying is incompatible with its multilateral character and the principle of international competitive bidding which must guide the Bank in its lending operations. Thus funds disbursed by the Bank to its borrowers can be used in any member country plus Switzerland, and the amount of exports which any industrial country receives as a result of Bank loans depends on its international competitiveness. The United States authorities have continued to allow the World Bank to have access to the United States capital market. In this connection, it may be noted

that the cumulative effect of all World Bank transactions has been to make a very large positive contribution to the United States balance of payments and it is expected that it will continue to do so. The World Bank is not only a borrower in the U.S. capital market, but is also an investor. It holds a large portion of its current cash and securities in the United States. As of latest available date, the Bank's holdings of cash and securities amounted to about \$___ billion.

I should like to take this opportunity to suggest that, as in the case of Germany, the countries which experience large balance of payments surpluses should permit the Bank to take advantage of these conditions by borrowing more heavily than otherwise in the markets of such countries.

Question 1.c.

1.c As for the question regarding the threat to the Bank's reputation as a sound and successful institution, I would like to assure readers of this interview and all others that I am determined to make sure that this threat does not materialize. First of all I should like to emphasize that the increase which is taking place in Bank lending is a result of a careful country by country review of investment possibilities conforming to the high standards of the World Bank. From my past experience, I know an increase in the size of a corporation's activities need not jeopardize its strength. Indeed such increase can enhance its reputation if the investing public is confident that the corporation is well managed.

The World Bank's reputation rests on a number of factors which might be summed up in terms of financial management. The Bank has a broad and diversified portfolio. After more than 20 years of experience the Bank's ability to appraise and evaluate projects is more efficient than ever and we are constantly improving our techniques. The Bank limits its lending to any one country to amounts that are well within the creditworthiness of the country, i.e. its ability to service its obligations to the Bank. Moreover, the Bank maintains continuous relations with its borrowers be they public or private institutions. It advises, persuades and, where necessary, insists that governments pursue policies designed to insure effective use of funds borrowed from the Bank and to make possible repayment to the Bank. The Bank adjusts its lending rate to longer-run changes in its borrowing rate. The Bank has earned substantial net income, now amounting to a net of \$180 million a year. It has built substantial reserves and has a strong liquidity position.

Before the Bank enters new fields of investment such as education or new countries, a most careful examination is made to make certain that the investment will increase the capacity of the country to produce and its capacity to repay debt. The Bank has had a continuous history of expanding its scope of investments to new fields, as for example, entering into agriculture. However, such expansion should not jeopardize the reputation of the Bank, because the Bank does not intend to make loans, for whatever the purpose may be, unless it has a sound basis to believe that the funds will be well used and the loans repaid.

Question 2

The increasing debts of some of the developing countries is becoming one of the most critical problems for certain developing countries, but I believe that the problem is manageable, if handled in time. At present the annual debt service on amortization and interest of developing countries accounts on average of about 8% of their earnings from exports of goods and services. In some countries however external debt service is 20% or even more of exports. In such cases, concern over the ability to repay is inevitable. Experience teaches us however, that other factors such as growth and diversification of exports, debt servicing record, ability to attract private capital, political stability, etc., all should be weighed in the judgement of creditworthiness. These factors, where unfavorable, can frequently be changed by proper to policies.

We regard it as part of our job in the Bank to do all possible to assist countries to pursue those policies which strengthen their capacity, both at present and in the future, to service debt. Developing countries cannot hope to develop satisfactorily without increasing their external debt. However, some external debt has been incurred for very poor reasons and on excessively onerous terms. Our aim should be to insure that debt is incurred on reasonable terms for productive purposes and that the ability of the country to repay debt constantly strengthened. Many developing countries are showing a much more responsible attitude in incurring more external debts, e.g., by severely limiting increases in short-term external debt. For those countries which reach the limits of their debt servicing capacity, the World Bank is simply not in a position to make any new loans. This is why we have attached urgent importance to the replenishment of the resources of the

International Development Association, which by providing funds from national budgets, enables credits to be made on a fifty-year basis virtually interest-free.

Question 5

I do not believe that regarding the World Bank as a development institution diminishes confidence in its bonds. The World Bank is a special type of a bank whose characteristics are clearly set forth in the Articles of Agreement. These Articles have guided the institution for over 20 years. Under these Articles, the World Bank has a clear responsibility to help bring about the economic development of its member countries. It is for this reason that countries have subscribed over \$22 billion, of which over \$2 billion has ~~already~~ been paid in and the remainder still uncalled for becomes in effect a guarantee fund. To help pursue its development objective countries have given the Bank access to capital markets and in other ways have enabled the Bank to raise funds in the developed countries for use in productive investment in the developing countries. It is its special responsibilities which make the World Bank a development institution, while at the same time retaining its essential character as a bank operating on the principle of maintaining and strengthening its financial structure and insuring its liquidity in the short run and its financial soundness in the long run. I am sure that if we adhere to the principles of sound financial management, as summarized above, the Bank will continue to enjoy the confidence of the world's capital markets as expressed by the high rating of World Bank's bonds and the success we have had in expanding our borrowing operations.

To: Mr. Irving S. Friedman

From: Frank M. Tamagna

Subject: Questions and Answers

Questions

1. How do you propose to raise the money you will need to double the Bank Group's financing over the next five years, in view of:
 - A. The scarcity of funds in the capital markets.
 - B. The balance of payments difficulties of many rich countries and the consequent reduction of their aid.
 - C. The concern that expansion threatens the Bank's reputation as a sound and successful institution.

Answer 1.A

1. Scarcity or abundance of financial resources are relative terms. The tremendous expansion that has taken place in the advanced countries over the current decade has been made possible only through an unprecedented generation of savings and its absorption in production investments; actually, the high demand for capital has been a determinant factor of the high level of income, that has in turn made possible the high savings formation. Large availability of funds frequently accompanies an inadequate rate of economic expansion, which would be contrary to the aims of the World Bank as a development institution.
2. Within this context, it should be noted that the amount of financial resources this Bank needs is comparatively small in terms of the total supply and demand for capital. There is no reason why

it could not continue to be accommodated, as it has been in the past, within the framework of free and flexible markets. In 1967, for instance, nearly \$40 billion of long term local public and corporate issues (bonds and stocks) were placed in the United States market (omitting the exceptionally large financing by the Federal Government and its agencies for about \$28 billion in shorter maturities), and approximately the same amount has been placed this year. In recent years, the aggregate amount of bonds and stocks offerings (public and private) in individual European countries has been approximately equivalent to the capital raised in the United States, but fragmented over many smaller markets with lower absorptive capacity. The development of an Euro-bond market, overcoming national barriers, has offered new and unexpected opportunities for large issues; thus far this year, it has absorbed over \$3 billion of foreign and international issues, or about double the amount placed last year. This is in addition to over a billion of new foreign issues absorbed by individual countries - about four times more than in 1967.

3. In our program, we estimate that the World Bank would need to borrow, over the coming years, about a billion or so annually on a gross basis, and three-fourths of a billion on a net basis. This would be only between 1 and 1.5 percent of the aggregate long term funds raised in the United States and other capital-producing countries and their international markets. Moreover, even the largest

issues by the Bank in the United States (\$250 million) does not exceed in magnitude any of several largest long term offerings by corporations or states and municipalities, and would also be far less than the largest offerings by Federal agencies. Similarly, in Europe any one of the Bank offerings would not be out of line with the funds raised by private or public institutions in any national market, or the Euro-bond market.

4. The problem, therefore, should be viewed in terms of how the Bank's borrowing can be appropriately fitted into the total flow of funds. Our issues are subject to authorization by the governments and what we are asking for is that this power should not be used in a restricted and discriminatory sense; ~~we should be allowed a free access to markets, subject to the conditions prevailing for other borrowers.~~ ^{our activities} ^{All we require is} ^{capital} ^{same} access to markets, subject to the conditions prevailing for other borrowers. This is fundamentally an allocation problem of resources - whether the developed countries would use their enormous accretions to their capital resources exclusively to raise themselves, ^{a other developed countries} still above the level of developing nations, or allow for some part of their additional resources to be used for the development of the rest of the world. Will the base of the growth pyramid remain a narrow one as it is today, or will it broaden to include the many countries of the developing world as well as the few of the developed? I believe that a broad based pyramid offers not only greater stability, but also the likelihood of more sustained overall rate of advance.

Answer 1.B

5. As to the balance of payments problem, it is perfectly true that this had led to a deterioration in a flow of resources from some of the rich countries to the poor, but this ^{can be offset} should be compensated (and in part it has been) by an increasing flow of resources from those developed countries that benefit from an improvement in their balance of payments conditions. I believe, ~~also~~, that a distinction ought to be made between capital outflow to other developed countries on the one hand, and outflow to the developing world on the other hand. The United States, in asking the cooperation of business and banks for protecting the balance of payments, has recognized this point, restricting the capital outflow to the former in the measure needed to sustain a continuing flow to the latter. Money spent on development is not a once-and-for-all loss to the rich countries, for the simple reason that it does not stay in the developing nations' pockets. They cannot afford to hoard ^{them} marks, or dollars, or gold. They must use the resources they receive to buy the products which only the developed world can supply. Funds invested in sound ^{development activities} projects in the less developed countries therefore return very rapidly to the developed countries, in the form of orders for goods and services.

6. The World Bank is an intermediary, that facilitates the flow of financial resources from developed to developing countries. As such, I believe that it should be exempted from any restrictions that developed countries might apply with respect to transfers of

(Setting aside the controversial question of the merits of controls and restraints over ~~the~~ any capital movements abroad,

capital to other developed countries. These may, of course, give rise to a reallocation of resources, as some advanced countries may be more competitive in their exports than others, and therefore obtain a larger share of the orders by developing countries. It is only natural that countries which can supply goods more competitively should benefit more than their less competitive neighbors. But this only underlines the fundamental point about the balance of payments disequilibria of the advanced countries - that they reflect the relative strength in world markets of the developed countries vis-a-vis each other.

Answer 1.C

7. The World Bank's reputation rests on a number of factors, which may be summed up in terms of 'financial management'. The Bank has been seeking, and has been successful in achieving a broad diversification of its portfolio in high quality loans. It has assisted 85 countries with 579 loans, and the average borrowing of any one country has been \$135 million only, of every individual project \$20 million; repayments and sales have reduced the outstanding indebtedness to the Bank by 69 countries to an average of \$113 million each. Only one country, India, has received over \$1 billion - of which \$630 million remain outstanding. Should any one, or even a group of countries fail to meet its obligations on schedule, it could hardly impair the ~~solidity~~ ^{financial strength} of the Bank and its ability to continue its operations. The Bank is further protected by an accumulated reserve, held in liquid assets in an amount of over \$1 billion, available on short term to meet disbursements on

its loans or repayments of its debt.

8. The loans of the Bank have been in most part for specific projects, which have been appraised, evaluated and supervised not only by our technical staff, but also by outside experts. Our technical assistance is an essential part of our financial management and our techniques are constantly being revised and adapted to new fields of resource development and lending. About half of our loans have been for basic infrastructural projects - power and transportation; the other half broadly distributed between industry, agriculture, communications, water supply and others.

9. Because of the broad diversification and quality that the Bank has already achieved for its portfolio, it is in a stronger position to ~~take into consideration special risks in financing~~ ^{finance} projects in some countries which are just beginning to develop and whose levels of sophistication may be relatively low. This is not a new situation for the Bank. To use one area of the world as an example, when we began lending in Latin America almost 20 years ago those countries knew very little about project or sectoral or national planning. But we worked with them, and others worked with them, and the results, while far from perfect, have really been ~~very~~ gratifying. Today most of the Latin American countries - and many countries in other areas which started from the same low base - have become very

also make it easier to improve its quality through education and skills, and therefore to raise altogether its productivity. This better balance between economic growth, population and education should make it easier for developing countries to achieve a better balance between living standards, saving formation, and investment opportunities. ~~As for education, population control has also indirect, but measurable benefits, helping the country to a sustainable development in the long run.~~

12. The Bank has also been mindful of the importance to conduct its financial management in accordance with financial conditions. As a bank, it must keep an appropriate balance between the cost of the money in the market and the ability of 'good risk' customers to borrow and meet their obligations. As a development institution, it must seek to direct funds from the advanced to the developing countries at the most reasonable terms it can. In seeking and obtaining the countries' authorization to borrow in their own markets, the Bank has also recognized a necessity to adapt its borrowings to the national interest and the financial policies of national authorities.

13. In placing its issues it must, of course, choose the country and the time offering the best opportunities. It will continue to seek its funds in the most economic markets, and exclude from its issues those markets which ~~have priced themselves out of general~~ ^{or experiencing interest rates and yields much higher than general} norms. From time to time, the Bank has made adjustments in its ^{own} lending rates, whenever market conditions and long term considerations

This is not practical for an institution with the magnitude and variety of the Bank's lending operations

Mr. Irving S. Friedman

DRAFT

warranted. It cannot and does not propose to make continuing changes in its ^{lending} interest rate on short terms basis, ^{however} following the ^{up and down} whims of fluctuating markets. The large ^{cash} ~~reserve~~ ^{of the bank} position gives the Bank flexibility in choosing the time, amount and place of its borrowings in accordance with a realistic evaluation of long range trends.

14. I ~~should also mention that~~ ^{Bank} investors in ~~our~~ bonds have an ultimate safeguard in the Bank's uncalled capital, which represents an unrestricted guarantee by each and all of its members to meet the Bank's obligations to investors. I would ~~prefer to regard this as a~~ ^{however,} measure of 'last resort', recourse to which should be considered by this Bank ~~except as an extreme safety factor, under conditions of~~ ^{as most unlikely in practice.} universal catastrophe, which I cannot possibly foresee. In evaluating its soundness, we in the Bank think that it is and will continue to be based on ^{a strong firm ad structure and} firm financial management, supported by the skills of technical assistance.

The existence of uncalled capital much larger than our funded debt provides the additional safeguard which, taken all together, give the World Bank bonds its very high standing in the capital markets of the world

figures?

It has regarded its own lending rates as following, not leading, market trends.

*more on actual experience among
more on actual cost factors*

OFFICE MEMORANDUM

TO: Mr. Irving S. Friedman

DATE: December 27, 1968

FROM: David Kochav DK

SUBJECT:

I am afraid some of the replies are repetitive. This is because several questions (especially 1, 3, 4, 5) deal with the same issues. Perhaps we could rearrange the questions, so that the answers will read better.

Best Regards

DRAFT
D. Kochav
Dec. 26, 1968

Question 1. How do you propose to raise the money you will need to double the Bank Group's financing over the next five years, in view of:

- A. The scarcity of funds in the capital markets;
- B. The balance of payments difficulties of many rich countries and the consequent reduction of their aid;
- C. The concern that expansion threatens the Bank's reputation as a sound and successful institution.

Answer

1A. Sales of new bonds in the capital markets of 13 major industrial countries amounted to \$64 billion in 1967, and have exceeded \$70 billion in 1968. These include bonds of central governments, local governments and corporations, in both domestic as well as international capital markets. Most of such bonds, perhaps \$65 billion in 1968 are domestic, which are sold by governments and private corporations in their home countries. Less than \$5 billion are bonds sold by governments and corporations in markets of other countries or in the Euro-bond market.

The bonds of the World Bank are of a somewhat unique nature: they are denominated in domestic currencies, e.g., bonds sold in U.S. markets are U.S. dollar bonds, those sold in Germany are in Deutschmarks, etc., and are backed by reserves held in a variety of currencies, as well as by a guarantee of all major governments. From the point of view of the investor, they are actually domestic bonds for all practical purposes. At the same time, the proceeds of bonds are used not for domestic investments,

but for productive investments in the lesser developed countries. In brief, they actually form domestic bonds, the proceeds of which are used for international development.

If related to the total amount of bonds sold in capital markets, up to \$1,000 million worth of bonds we plan to sell a year in all markets are not a large share, constituting less than 1.5% of the total. If compared merely to foreign and international bonds, then the World Bank bonds form a considerable share. However, I should hasten to add that the World Bank is perhaps the most established borrower in international markets, and in fact can be considered as having established an international market for bonds on a continuous basis.

Now when one talks about a scarcity in the capital markets, let us be specific about the meaning of such scarcity. Obviously, there is no reduction in the supply of funds in the markets, as can be seen from the plain fact that the sales of new bonds are increasing at a rapid rate: Sales of new bonds in major capital markets amounted to \$37 billion in 1965, \$45 billion in 1966, \$64 billion in 1967, and have again considerably increased in 1968. Thus the actual supply of funds has expanded rapidly, but at the same time the demand for funds has increased at a more rapid rate. The faster growth rate in demand for funds, relative to its supply, led to an increase in interest rates.

As all markets, the market for loanable funds is determined by demand and supply conditions, which are adjusted by the mechanism of prices, in this case by a rise in the price of money--the interest rate. By the very definition of a free market, there is no "scarcity" or shortage

of funds at the going interest rate. Instead of a "scarcity" of capital funds, I would rather say that capital markets are rapidly expanding, although they operate at a higher level of interest rates.

As other financial institutions, the World Bank has also adjusted its operations to a higher level of interest rates. We borrow at market rates which have indeed increased last year, and we also had to raise our lending rate.

I believe that in the expanding markets there is room for a considerable increase for World Bank bonds. After all, we are in a very strong financial position, as can be seen by some well-known facts, which I would like to summarize.

The Bank has a paid-in capital of \$2,300 million^{1/} at the end of 1968. In addition, it has a "special reserve" of \$290 million, which has been accumulated from commissions received. According to the Articles of Agreement the Special Reserve is to be held in liquid form

^{1/} Following figures are an approximation for December 1968. Exact figures would have to be used when available.

and to be used only for the purpose of meeting liabilities of the Bank on its bonds and guarantees. In addition to the above, the Bank has a Supplemental Reserve of over \$900 million, accumulated from retained earnings against losses on loans and guarantees and from currency devaluations. Altogether the Bank has a paid-up capital and reserve position of about \$3,500 million. Although the present financial strength of the Bank rests mainly on the above amount of paid-in capital and reserves, it has also capital subscribed but not called of \$20.6 billion, which forms a guarantee of all major governments to holders of Bank bonds and obligations. This includes not only the guarantee of the U.S. Government, but also of several other governments, the financial position of which is considered very strong in international financial markets. The uncalled capital is considered by the Bank only as a guarantee to be used as a last resort. The prospective operations of the Bank do not indicate any need to call on this part of the subscribed capital. The Bank has a consistent record of high net earnings, as follows:

FY 1962	\$ 98 million
1963	113 "
1964	131 "
1965	138 "
1966	140 "
1967	170 "
1968	147 "

On the basis of conservative projections, net earnings are expected to amount to about an annual level of \$170 million in the next five years. The Bank expects to retain up to half (check) of such earnings, in order to strengthen its Supplemental Reserve.

As another evidence of the great elasticity of capital markets I would mention the very rapid increase in the Euro-bond market, which in a matter of a few years has grown to sales of new bonds worth about \$3.5 billion in 1968.

In brief, my belief is that in the expanding capital markets, there is room for a considerable increase in sales of bonds of the World Bank, which is one of the strongest financial institutions in the world. At the same time, we as everybody else in the financial markets would have to adjust to a higher level of interest rates.

1B. It has to be emphasized that the balance of payments difficulties represent basically an imbalance between the industrial countries. For the industrial countries as a group, development assistance does not lead to a balance of payments deficit. This is simply because all development aids form a transfer of goods and services, but not as a drain on the reserves of the industrial countries. Money "spent" on development is not a once-and-for-all balance of payments loss to the rich countries, for the simple reason that it does not stay in the developing nations' pockets. They cannot afford to hoard deutsche marks, or dollars, or gold. They must use the resources they receive to buy the products which only the developed world can supply. Loans made to the less-developed countries therefore return rapidly to the developed countries in the form of orders for goods and services.

Of course, some advanced countries may make greater gains than others from this return flow; those which can supply goods more competitively benefit more than their less competitive neighbors.

In this form development loans may have some net effects on the balance of payments of particular industrial countries, inasmuch as such loans are not "tied" to purchases in these particular countries.

In principle I believe that development loans should be "insulated" from effects of balance of payments problems of the industrial countries. This position has been strongly endorsed by the DAC ministerial committee, which represents all the major providers of development assistance. However, little if anything has as yet been done to carry out this and similar resolutions; and we have to live with present realities.

Now we have of course to distinguish between the surplus and deficit countries. For those countries with a balance of payments surplus, export of capital is in fact one of the best ways to reduce such surpluses and still benefit in the future from returns on exported capital. This has been clearly recognized by the Government and financial authorities of the Federal Republic of Germany, which have encouraged capital exports, and the World Bank has been fortunate to be able to borrow largely in this market.

The major problem in this respect has been the U.S., which of course has the largest and most sophisticated capital markets, and at the same time faces a balance of payments deficit. To overcome this problem, the Bank made a special arrangement with the U.S. Treasury by which sales of new World Bank bonds in the U.S. would be matched by investments of the Bank funds in U.S. securities, so that there would be no adverse effects on the U.S. balance of payments. I should add that this arrangement has been working satisfactorily. The Bank has been able to step up the sales of bonds in the U.S. market, while the U.S. balance of payments has not been adversely affected in any way.

In summary, I would conclude that in sales of bonds we have not encountered insurmountable difficulties due to the balance of payments problems of the industrial countries, and I do not expect any deterioration in this respect.

10. I have already mentioned several basic facts and figures related to the financial strength of the Bank. I think I should add a few comments on our lending policies, since after all our financial strength rests ultimately on the strength of our loans.

Over the years under my predecessors the Bank has worked out most effective procedures for appraising and evaluating the projects we finance, and for supervising them once a loan is made. These techniques are constantly being refined, and adapted to new fields of lending as we move into them. Today they are, because of experience, more efficient than ever before.

It is of course true that we shall in the future be financing projects in some countries which are just beginning to develop, and whose level of sophistication may be relatively low. But that is not a new situation for the Bank. To use one area as an example, when we began lending in Latin America almost twenty years ago those countries knew very little about project or sectoral or national planning. But we worked with them, and others worked with them, and the results, while far from perfect, have really been very gratifying. Today most of the Latin American countries--and many countries in other areas which started from the same low base--have become much better at planning and carrying out development projects and programs.

One of the Bank's great strengths both in its operations and its reputation for soundness is that it works with borrowers over the long term. When it makes a loan, it does not write a check and walk away. It lives with the country and the project for many years. It concerns itself with problems that may arise during construction, and later during operation. It advises, persuades, insists. The result is an evolving sophistication on the part of our borrowers. We have already seen many of them develop great capabilities; and I am certain that as we move more deeply into some of the newer countries where we have not yet been very active the same learning process will occur.

I would like to emphasize that loans for agriculture, education and population control are economically as sound as the loans we have made for other sectors, such as power, transportation and irrigation. I should make here a distinction between financial and economic benefits of a loan. If we make a loan for power, the power authority would get increased revenues from the sale of electricity from which the loan could be amortized. Now, if we make a loan for highway construction, unless this is a toll road, the highway authority would not gain any additional revenue. This does not of course mean that a loan for highways nets smaller returns or benefits than a port loan. Rather, the benefits from the highway loan accrue to the users of the road and to the economy as a whole rather than to a particular authority. In other words, the benefits from the road loan are economic and not financial, but nobody would use it as an argument against loans for road building.

I think the same principle applies to loans for certain agricultural projects as well as to education and population control.

Even if no particular authority can show direct financial revenues resulting from such investments, they could carry great economic benefits to the national economy, if properly used. Agricultural loans are carefully chosen to raise the food production, and thus to increase the food intake and its nutritional content in the less-developed countries. This would certainly result in a higher productive capacity. After all, even the hardest and soundest financier would recognize that countries in which a considerable share of people are subject to malnutrition cannot be expected to raise their productivity at a satisfactory rate. In addition, the less-developed countries presently spend over \$4 billion a year for imports of food and agricultural materials. Agricultural development in their own countries could result in considerable foreign exchange savings, and thus directly strengthen their balance of payments.

Loans for education carefully scrutinized to raise the skill potential in developing countries will also make a direct contribution to raise their productive capacity. It has long been recognized that the lack of skills is perhaps as strong a constraint on productivity growth in these countries as the shortage of capital.

Loans for population control have perhaps the highest benefits of all. Take two different developing countries with similar standards of living, each with a birth rate of 40 per 1,000. Now estimate what would happen if the birth rate in one of those countries, in a period of 25 years, were to be halved to 20 per 1,000. The country which lowered its population growth would raise its standard of living 40% above the other country in a single generation. This is some measure of the benefits obtainable from population control investment.

Question 2. Are you worried about the increasing debts of some developing countries?

Answer The Bank has always paid close attention to the external debt position of the borrowing countries. This is required by the Bank's Articles of Agreement which read: "In making or guaranteeing a loan, the Bank shall pay due regard to the prospects that the borrower, and, if the borrower is not a member, that the guarantor, will be in position to meet its obligations under the loan; and the Bank shall act prudently in the interests both of the particular member in whose territories the project is located and of the members as a whole." [Article III, Section 4, (v)].

One of the requirements for lending is that the country regularly report to the Bank on every external loan it undertakes or guarantees. These reports form the basis for an evaluation of the indebtedness of borrowing countries, as well as the future prospects for debt servicing. And we are quite selective in making developing countries eligible for Bank lending. Some member countries have been made ineligible for Bank or IDA lending on grounds of inadequate economic and financial policies. A number of countries with a reasonable record of performance but which face long-term balance of payments difficulties are eligible only for IDA credits, not for Bank lending. Only those countries which have adequate policies combined with creditworthiness and ability to prepare and execute good projects receive Bank loans.

At present, the annual debt service of amortization and interest of 92 developing countries accounts for about 8% of their earnings from exports of goods and services. This of course is an average ratio, with great variations. In some countries external debt service is about 20%

or sometimes more of exports. On the basis of this ratio alone it is difficult to say whether debt servicing forms an excessive burden. A country which has good prospects for rapid export growth, as well as an inflow of private capital, a ratio of 20% or even 25% of debt service to exports, does not form a heavy burden. A good example for this group is Mexico, which has a very good credit standing.

In fact, export growth of the major debtors of the Bank has been fairly rapid (examples of some countries in Latin America could be added). In addition to the expansion of exports in traditional commodities, the Bank has actively encouraged diversification of exports to manufactures and other commodities with good marketing prospects. We do not generally finance expansion of productive capacity of "surplus commodities" in international markets (e.g., coffee, sugar).

I also note with some satisfaction that the use of short-term credits, such as suppliers' credits, which in the past has been excessive in some developing countries has not been restricted, either on the initiative of their governments or by their mutual agreements with the Bank or the IMF.

In brief, we feel that we make every effort to evaluate the creditworthiness of prospective borrowers from the Bank. And the projects we finance are expected to strengthen the debt servicing capacity of these countries.

There are some countries which have a satisfactory economic performance and have good projects, but cannot be expected to service loans of World Bank terms, because of their poorer long-term balance of payments prospects or because of extreme poverty. A good example is India or some

African countries. To these countries we give IDA credits, for 50 years at only 3/4% interest, to the extent IDA resources are available. We do not consider these countries creditworthy for large amounts of Bank loans, except for self-liquidating investments.

Question 3. How do you think the efficiency of the Bank's aid might be increased?

Answer The efficiency of the Bank's activities has been well proved over the last twenty years, and we are constantly working to increase it. Today, there are a number of kinds of development assistance which can have a particularly high payoff: one example is a sector of investment which the Bank considers extremely important--agriculture. Recent breakthroughs in the development of high-yielding strains of wheat and rice have made it possible to obtain yields per acre two or three times as high as could have been produced with normal types of seed. It has also been found that the new high-yielding varieties are particularly responsive to irrigation and fertilizer inputs. An important way to increase the Bank's total impact on development, therefore, is to increase the proportion of that total represented by investment in the new agriculture.

I have already commented on the high benefits of education loans. I should also add that we shall continue to finance projects and programs in our more traditional fields--transportation, power, irrigation, and industrial development. We have recently begun to finance infrastructure projects (such as roads, water supply, etc.) for tourism development, which is a rapidly increasing sector with foreign exchange earnings.

In all these fields we operate on the basis of a close and careful evaluation of a country's overall economic prospects and policies, giving advice to the best of our knowledge on what ought to be improved and how it could be done. In addition, we carefully select those projects with high economic returns and we require that measures be taken to attain high standards of all aspects of projects--in management and institution building, as well as the technical and financial aspects.

Question 4. What are the prospects for the areas in which you have said the Bank wishes to make a particular effort, education, agriculture and population control? With regard to the latter, what criteria will you use in setting up programs, and how will you avoid adverse reactions on religious or ethnic grounds?

Answer In my speech to the Bank's Governors, I outlined the prospects for our agricultural and educational lending by saying that we intended to quadruple the volume of the former and triple the volume of the latter over the next five years. As far as population control is concerned, I should stress that this is a new field of operation for the Bank, and we are still working our way into the subject. The process of deciding how best to assist population control is not made easier by the fact that far too little research has been done on this subject anywhere in the world.

But I must stress again that it is not the absolute size of a country's population which worries us, but its rate of population growth. We are, seriously concerned that the rate of growth of countries' populations should not be so high as to negate the rate of their economic development. For example, if a country's gross domestic product is rising at a level of 3% per annum and population at a rate of 2.5% per annum, there is painfully little room for the improvement in the standard of living which we as a development agency want to see--and which humane people all over the world hope for. Our aim is to give children in developing countries the possibility of growing up in a world where they can live with at least some degree of human dignity. In some cases this can only be achieved by limiting the growth of population to levels with which countries' efforts to promote their economic development can keep pace.

We fully realize, of course, the religious and national sensitivities in the area of population control. These pose thorny and difficult problems, but fundamental to our approach are respect for the dignity of man and for the right of nations to determine their own approaches to the population question. We are resolved however that the dangers of rapid population growth must be pointed out, and we are determined to extend help when asked.

Question 5. Do you believe that your announced view of the World Bank as being at least as much a development institution as a bank diminishes confidence in its bonds in the money markets, and thereby creates problems for the Bank when it makes bond issues?

Answer The stepping-up of our lending as well as the sale of bonds might naturally raise some questions. I believe however that a closer look in our financial situation and the prospects for the Bank itself and its major borrowers could go a long way towards the realization that the Bank is a sound financial institution and will continue to be so in the future. I shall not repeat the various factors which I have already mentioned. I would only want to summarize the various points made. The Bank has an established 20-year record of sound and well-conceived operations. Although the Bank has always recognized its major responsibility as a development finance institution, it has not compromised the high standards ^{it} requires from the borrowing countries. The Bank would continue to insist on high standards of creditworthiness and performance, of its debtor countries, as well as of the particular projects and programs it finances. The Bank's future lending program which indicates doubling of operations is based on a careful country-by-country evaluation which

has taken into account the creditworthiness, economic and financial policies and project availability prospects of the major developing countries. The Bank's financial position is strong and we shall make every effort to maintain its financial soundness. I hope that we shall continue to enjoy the full confidence of the capital markets, as expressed by the high rating of our bonds.

Working Paper

DRAFT

D. Kochav

Dec. 26, 1968

Question 1. How do you propose to raise the money you will need to double the Bank Group's financing over the next five years, in view of:

- A. The scarcity of funds in the capital markets;
- B. The balance of payments difficulties of many rich countries and the consequent reduction of their aid;
- C. The concern that expansion threatens the Bank's reputation as a sound and successful institution.

Answer

1A. Sales of new bonds in the capital markets of 13 major industrial countries amounted to \$64 billion in 1967, and have exceeded \$70 billion in 1968. These include bonds of central governments, local governments and corporations, in both domestic as well as international capital markets. Most of such bonds, perhaps \$65 billion in 1968 are domestic, which are sold by governments and private corporations in their home countries. Less than \$5 billion are bonds sold by governments and corporations in markets of other countries or in the Euro-bond market.

The bonds of the World Bank are of a somewhat unique nature: they are denominated in domestic currencies, e.g., bonds sold in U.S. markets are U.S. dollar bonds, those sold in Germany are in deutschemarks, etc., and are backed by reserves held in a variety of currencies, as well as by a guarantee of all major governments. From the point of view of the investor, they are actually domestic bonds for all practical purposes. At the same time, the proceeds of bonds are used not for domestic investments,

but for productive investments in the lesser developed countries. In brief, they actually form domestic bonds, the proceeds of which are used for international development.

If related to the total amount of bonds sold in capital markets, up to \$1,000 million worth of bonds we plan to sell a year in all markets are not a large share, constituting less than 1.5% of the total. If compared merely to foreign and international bonds, then the World Bank bonds form a considerable share. However, I should hasten to add that the World Bank is perhaps the most established borrower in international markets, and in fact can be considered as having established an international market for bonds on a continuous basis.

Now when one talks about a scarcity in the capital markets, let us be specific about the meaning of such scarcity. Obviously, there is no reduction in the supply of funds in the markets, as can be seen from the plain fact that the sales of new bonds are increasing at a rapid rate: Sales of new bonds in major capital markets amounted to \$37 billion in 1965, \$45 billion in 1966, \$64 billion in 1967, and have again considerably increased in 1968. Thus the actual supply of funds has expanded rapidly, but at the same time the demand for funds has increased at a more rapid rate. The faster growth rate in demand for funds, relative to its supply, led to an increase in interest rates.

As all markets, the market for loanable funds is determined by demand and supply conditions, which are adjusted by the mechanism of prices, in this case by a rise in the price of money--the interest rate. By the very definition of a free market, there is no "scarcity" or shortage

of funds at the going interest rate. Instead of a "scarcity" of capital funds, I would rather say that capital markets are rapidly expanding, although they operate at a higher level of interest rates.

As other financial institutions, the World Bank has also adjusted its operations to a higher level of interest rates. We borrow at market rates which have indeed increased last year, and we also had to raise our lending rate.

I believe that in the expanding markets there is room for a considerable increase for World Bank bonds. After all, we are in a very strong financial position, as can be seen by some well-known facts, which I would like to summarize.

The Bank has a paid-in capital of \$2,300 million^{1/} at the end of 1968. In addition, it has a "special reserve" of \$290 million, which has been accumulated from commissions received. According to the Articles of Agreement the Special Reserve is to be held in liquid form

^{1/} Following figures are an approximation for December 1968. Exact figures would have to be used when available.

and to be used only for the purpose of meeting liabilities of the Bank on its bonds and guarantees. In addition to the above, the Bank has a Supplemental Reserve of over \$900 million, accumulated from retained earnings against losses on loans and guarantees and from currency devaluations. Altogether the Bank has a paid-up capital and reserve position of about \$3,500 million. Although the present financial strength of the Bank rests mainly on the above amount of paid-in capital and reserves, it has also capital subscribed but not called of \$20.6 billion, which forms a guarantee of all major governments to holders of Bank bonds and obligations. This includes not only the guarantee of the U.S. Government, but also of several other governments, the financial position of which is considered very strong in international financial markets. The uncalled capital is considered by the Bank only as a guarantee to be used as a last resort. The prospective operations of the Bank do not indicate any need to call on this part of the subscribed capital. The Bank has a consistent record of high net earnings, as follows:

FY 1962	\$ 98 million
1963	113 "
1964	131 "
1965	138 "
1966	140 "
1967	170 "
1968	147 "

On the basis of conservative projections, net earnings are expected to amount to about an annual level of \$170 million in the next five years. The Bank expects to retain up to half (check) of such earnings, in order to strengthen its Supplemental Reserve.

As another evidence of the great elasticity of capital markets I would mention the very rapid increase in the Euro-bond market, which in a matter of a few years has grown to sales of new bonds worth about \$3.5 billion in 1968.

In brief, my belief is that in the expanding capital markets, there is room for a considerable increase in sales of bonds of the World Bank, which is one of the strongest financial institutions in the world. At the same time, we as everybody else in the financial markets would have to adjust to a higher level of interest rates.

1B. It has to be emphasized that the balance of payments difficulties represent basically an imbalance between the industrial countries. For the industrial countries as a group, development assistance does not lead to a balance of payments deficit. This is simply because all development aids form a transfer of goods and services, but not as a drain on the reserves of the industrial countries. Money "spent" on development is not a once-and-for-all balance of payments loss to the rich countries, for the simple reason that it does not stay in the developing nations' pockets. They cannot afford to hoard deutsche marks, or dollars, or gold. They must use the resources they receive to buy the products which only the developed world can supply. Loans made to the less-developed countries therefore return rapidly to the developed countries in the form of orders for goods and services.

Of course, some advanced countries may make greater gains than others from this return flow; those which can supply goods more competitively benefit more than their less competitive neighbors.

In this form development loans may have some net effects on the balance of payments of particular industrial countries, inasmuch as such loans are not "tied" to purchases in these particular countries.

In principle I believe that development loans should be "insulated" from effects of balance of payments problems of the industrial countries. This position has been strongly ^{taken} endorsed by the DAC ministerial committee, which represents all the major providers of development assistance. However, little if anything has as yet been done to carry out this and similar resolutions; and we have to live with present realities.

Now we have of course to distinguish between the surplus and deficit countries. For those countries with a balance of payments surplus, export of capital is in fact one of the best ways to reduce such surpluses and still benefit in the future from returns on exported capital. This has been clearly recognized by the Government and financial authorities of the Federal Republic of Germany, which have encouraged capital exports, and the World Bank has been fortunate to be able to borrow largely in this market.

The major problem in this respect has been the U.S., which of course has the largest and most sophisticated capital markets, and at the same time faces a balance of payments deficit. To overcome this problem, the Bank made a special arrangement with the U.S. Treasury by which sales of new World Bank bonds in the U.S. would be matched by investments of the Bank funds in U.S. securities, so that there would be no adverse effects on the U.S. balance of payments. I should add that this arrangement has been working satisfactorily. The Bank has been able to step up the sales of bonds in the U.S. market, while the U.S. balance of payments has not been adversely affected in any way.

In summary, I would conclude that in sales of bonds we have not encountered insurmountable difficulties due to the balance of payments problems of the industrial countries, and I do not expect any deterioration in this respect.

10. I have already mentioned several basic facts and figures related to the financial strength of the Bank. I think I should add a few comments on our lending policies, since after all our financial strength rests ultimately on the strength of our loans.

Over the years under my predecessors the Bank has worked out most effective procedures for appraising and evaluating the projects we finance, and for supervising them once a loan is made. These techniques are constantly being refined, and adapted to new fields of lending as we move into them. Today they are, because of experience, more efficient than ever before.

It is of course true that we shall in the future be financing projects in some countries which are just beginning to develop, and whose level of sophistication may be relatively low. But that is not a new situation for the Bank. To use one area as an example, when we began lending in Latin America almost twenty years ago those countries knew very little about project or sectoral or national planning. But we worked with them, and others worked with them, and the results, while far from perfect, have really been very gratifying. Today most of the Latin American countries--and many countries in other areas which started from the same low base--have become much better at planning and carrying out development projects and programs.

One of the Bank's great strengths both in its operations and its reputation for soundness is that it works with borrowers over the long term. When it makes a loan, it does not write a check and walk away. It lives with the country and the project for many years. It concerns itself with problems that may arise during construction, and later during operation. It advises, persuades, insists. The result is an evolving sophistication on the part of our borrowers. We have already seen many of them develop great capabilities; and I am certain that as we move more deeply into some of the newer countries where we have not yet been very active the same learning process will occur.

I would like to emphasize that loans for agriculture, education and population control are economically as sound as the loans we have made for other sectors, such as power, transportation and irrigation. I should make here a distinction between financial and economic benefits of a loan. If we make a loan for power, the power authority would get increased revenues from the sale of electricity from which the loan could be amortized. Now, if we make a loan for highway construction, unless this is a toll road, the highway authority would not gain any additional revenue. This does not of course mean that a loan for highways nets smaller returns or benefits than a port loan. Rather, the benefits from the highway loan accrue to the users of the road and to the economy as a whole rather than to a particular authority. In other words, the benefits from the road loan are economic and not financial, but nobody would use it as an argument against loans for road building.

I think the same principle applies to loans for certain agricultural projects as well as to education and population control.

Even if no particular authority can show direct financial revenues resulting from such investments, they could carry great economic benefits to the national economy, if properly used. Agricultural loans are carefully chosen to raise the food production, and thus to increase the food intake and its nutritional content in the less-developed countries. This would certainly result in a higher productive capacity. After all, even the hardest and soundest financier would recognize that countries in which a considerable share of people are subject to malnutrition cannot be expected to raise their productivity at a satisfactory rate. In addition, the less-developed countries presently spend over \$4 billion a year for imports of food and agricultural materials. Agricultural development in their own countries could result in considerable foreign exchange savings, and thus directly strengthen their balance of payments.

Loans for education carefully scrutinized to raise the skill potential in developing countries will also make a direct contribution to raise their productive capacity. It has long been recognized that the lack of skills is perhaps as strong a constraint on productivity growth in these countries as the shortage of capital.

Loans for population control have perhaps the highest benefits of all. Take two different developing countries with similar standards of living, each with a birth rate of 40 per 1,000. Now estimate what would happen if the birth rate in one of those countries, in a period of 25 years, were to be halved to 20 per 1,000. The country which lowered its population growth would raise its standard of living 40% above the other country in a single generation. This is some measure of the benefits obtainable from population control investment.

Question 2. Are you worried about the increasing debts of some developing countries?

Answer The Bank has always paid close attention to the external debt position of the borrowing countries. This is required by the Bank's Articles of Agreement which read: "In making or guaranteeing a loan, the Bank shall pay due regard to the prospects that the borrower, and, if the borrower is not a member, that the guarantor, will be in position to meet its obligations under the loan; and the Bank shall act prudently in the interests both of the particular member in whose territories the project is located and of the members as a whole." [Article III, Section 4, (v)]. One of the requirements for lending is that the country regularly report to the Bank on every external loan it undertakes or guarantees. These reports form the basis for an evaluation of the indebtedness of borrowing countries, as well as the future prospects for debt servicing. And we are quite selective in making developing countries eligible for Bank lending. Some member countries have been made ineligible for Bank or IDA lending on grounds of inadequate economic and financial policies. A number of countries with a reasonable record of performance but which face long-term balance of payments difficulties are eligible only for IDA credits, not for Bank lending. Only those countries which have adequate policies combined with creditworthiness and ability to prepare and execute good projects receive Bank loans.

At present, the annual debt service of amortization and interest of 92 developing countries accounts for about 8% of their earnings from exports of goods and services. This of course is an average ratio, with great variations. In some countries external debt service is about 20%

or sometimes more of exports. On the basis of this ratio alone it is difficult to say whether debt servicing forms an excessive burden. A country which has good prospects for rapid export growth, as well as an inflow of private capital, a ratio of 20% or even 25% of debt service to exports, does not form a heavy burden. A good example for this group is Mexico, which has a very good credit standing.

In fact, export growth of the major debtors of the Bank has been fairly rapid (examples of some countries in Latin America could be added). In addition to the expansion of exports in traditional commodities the Bank has actively encouraged diversification of exports to manufactures and other commodities with good marketing prospects. We do not generally finance expansion of productive capacity of "surplus commodities" in international markets (e.g., coffee, sugar).

I also note with some satisfaction that the use of short-term credits, such as suppliers' credits, which in the past has been excessive in some developing countries has ^{now} ~~not~~ been restricted, either on the initiative of their governments or by their mutual agreements with the Bank or the IMF.

In brief, we feel that we make every effort to evaluate the creditworthiness of prospective borrowers from the Bank. And the projects we finance are expected to strengthen the debt servicing capacity of these countries.

There are some countries which have a satisfactory economic performance and have good projects, but cannot be expected to service loans of World Bank terms, because of their poorer long-term balance of payments prospects or because of extreme poverty. A good example is India or some

African countries. To these countries we give IDA credits, for 50 years at only 3/4% interest, to the extent IDA resources are available. We do not consider these countries creditworthy for large amounts of Bank loans, except for self-liquidating investments.

Question 3. How do you think the efficiency of the Bank's aid might be increased?

Answer The efficiency of the Bank's activities has been well proved over the last twenty years, and we are constantly working to increase it. Today, there are a number of kinds of development assistance which can have a particularly high payoff: one example is a sector of investment which the Bank considers extremely important--agriculture. Recent breakthroughs in the development of high-yielding strains of wheat and rice have made it possible to obtain yields per acre two or three times as high as could have been produced with normal types of seed. It has also been found that the new high-yielding varieties are particularly responsive to irrigation and fertilizer inputs. An important way to increase the Bank's total impact on development, therefore, is to increase the proportion of that total represented by investment in the new agriculture.

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In all these fields we operate on the basis of a close and careful evaluation of a country's overall economic prospects and policies, giving advice to the best of our knowledge on what ought to be improved and how it could be done. In addition, we carefully select those projects with high economic returns and we require that measures be taken to attain high standards of all aspects of projects--in management and institution building, as well as the technical and financial aspects.

Question 4. What are the prospects for the areas in which you have said the Bank wishes to make a particular effort, education, agriculture and population control? With regard to the latter, what criteria will you use in setting up programs, and how will you avoid adverse reactions on religious or ethnic grounds?

Answer In my speech to the Bank's Governors, I outlined the prospects for our agricultural and educational lending by saying that we intended to quadruple the volume of the former and triple the volume of the latter over the next five years. As far as population control is concerned, I should stress that this is a new field of operation for the Bank, and we are still working our way into the subject. The process of deciding how best to assist population control is not made easier by the fact that far too little research has been done on this subject anywhere in the world.

But I must stress again that it is not the absolute size of a country's population which worries us, but its rate of population growth. We are, seriously concerned that the rate of growth of countries' populations should not be so high as to negate the rate of their economic development. For example, if a country's gross domestic product is rising at a level of 3% per annum and population at a rate of 2.5% per annum, there is painfully little room for the improvement in the standard of living which we as a development agency want to see--and which humane people all over the world hope for. Our aim is to give children in developing countries the possibility of growing up in a world where they can live with at least some degree of human dignity. In some cases this can only be achieved by limiting the growth of population to levels with which countries' efforts to promote their economic development can keep pace.

We fully realize, of course, the religious and national sensitivities in the area of population control. These pose thorny and difficult problems, but fundamental to our approach are respect for the dignity of men and for the right of nations to determine their own approaches to the population question. We are resolved however that the dangers of rapid population growth must be pointed out, and we are determined to extend help when asked.

Question 5. Do you believe that your announced view of the World Bank as being at least as much a development institution as a bank diminishes confidence in its bonds in the money markets, and thereby creates problems for the Bank when it makes bond issues?

Answer The stepping-up of our lending as well as the sale of bonds might naturally raise some questions. I believe however that a closer look in our financial situation and the prospects for the Bank itself and its major borrowers could go a long way towards the realization that the Bank is a sound financial institution and will continue to be so in the future. I shall not repeat the various factors which I have already mentioned. I would only want to summarize the various points made. The Bank has an established 20-year record of sound and well-conceived operations. Although the Bank has always recognized its major responsibility as a development finance institution, it has not compromised on the high standards ^{it} requires by it from the borrowing countries. The Bank would continue to insist on high standards of creditworthiness and performance, of its ~~or~~ debtor countries, as well as of the particular projects and programs it finances. The Bank's future lending program which indicates doubling of operations is based on a careful country-by-country evaluation which

has taken into account the creditworthiness, economic and financial policies and project availability prospects of the major developing countries. The Bank's financial position is strong and we shall make every effort to maintain its financial soundness. I hope that we shall continue to enjoy the full confidence of the capital markets, as expressed by the high rating of our bonds.

Question 1.c.

1.c As for the question regarding the threat to the Bank's reputation as a sound and successful institution, I would like to assure readers of this interview and all others that I am determined to make sure that this threat does not materialize. First of all I should like to emphasize that the increase which is taking place in Bank lending is a result of a careful country by country review of investment possibilities conforming to the high standards of the World Bank. From my past experience, I know an increase in the size of a corporation's activities need not jeopardize its strength. Indeed such increase can enhance its reputation if the investing public is confident that the corporation is well managed.

The World Bank's reputation rests on a number of factors which might be summed up in terms of financial management. The Bank has a broad and diversified portfolio. After more than 20 years of experience the Bank's ability to appraise and evaluate projects is more efficient than ever and we are constantly improving our techniques. The Bank limits its lending to any one country to amounts that are well within the creditworthiness of the country, i.e. its ability to service its obligations to the Bank. Moreover, the Bank maintains continuous relations with its borrowers be they public or private institutions. It advises, persuades and, where necessary insists that governments pursue policies designed to insure effective use of funds borrowed from the Bank and to make possible repayment to the Bank. The Bank adjusts its lending rate to longer-run changes in its borrowing rate. The Bank has earned substantial net income, now amounting to a net of \$180 million a year. It has built substantial reserves and has a strong liquidity position.

Before the Bank enters new fields of investment such as education or new countries, a most careful examination is made to make certain that the investment will increase the capacity of the country to produce and its capacity to repay debt. The Bank has had a continuous history of expanding its scope of investments to new fields, as for example, entering into agriculture. However, such expansion should not jeopardize the reputation of the Bank, because the Bank does not intend to make loans, for whatever the purpose may be, unless it has a sound basis to believe that the funds will be well used and the loans repaid.

Question 1.c.

1.c. Concern has been expressed that the large expansion contemplated in the Bank's financing threatens its reputation as a sound and successful institution. I would like to assure readers of this interview and all others that I am determined to make sure that this threat does not materialize. From my past experience, I know an increase in the size of a corporation's activities need not jeopardize its reputation. Indeed such increase can strengthen its reputation if the investing public is confident that the corporation is well managed. The World Bank's reputation raises a number of factors which might be summed up in terms of financing management. The Bank has a broad, diversified portfolio of high quality loans. After more than 20 years of experience the Bank's ability to appraise and evaluate projects is more efficient than ever and we are constantly improving our techniques. The Bank limits its lending to any one country to amounts that are well within the creditworthiness of the country, i.e. its ability to service its obligations to the Bank. The Bank's loans are expected to be repaid when they are made. Moreover, the Bank maintains continuous relations with its borrowers be they public or private institutions. It advises, persuades and where necessary insists on the pursuit of sound policy designed to insure effective use of funds borrowed from the Bank and thus to insure repayment to the Bank.

out of place (The Bank has been setting aside a portion of its substantial net income, now amounting to a net of \$75 million a year to the building of additional reserves to meet contingencies.) Before the Bank enters new fields of investment such (as education or) new countries, a most careful examination is made to insure that the investment will increase the capacity of the country to produce and its capacity to repay debt. The Bank has had a

All financial data ought to be concentrated either in 1a or 1c

1.c

continuous history of expanding its scope of investments to new fields, as for example, entering into agriculture. However, such expansion will not jeopardize the reputation of the Bank any more than it did in the past, because the Bank does not intend to make loans for whatever the purpose may be, unless it has a sound basis to believe that the funds will be well used and the loans repaid.

~~resulting~~ ^{balanced} result in a diversified ^{part of the} and balanced portfolio and a satisfactory ^{and} ~~record~~ ^{records}

Answer to Question 1

1. Generally speaking I propose to raise the money needed to finance the World Bank over the next year by borrowing in capital markets of the developed countries and from other investors such as ^{throughout the world} central banks who find the holding of World Bank bonds attractive. Before entering into more detail aspects of the question, I would like to emphasize my conviction that the Bank's position in capital market is based essentially on its record ^{of} and well-conceived operations and its insistence on high standards from the borrowing countries, both in the preparation and execution of investment projects and in the pursuit of desirable economic and financial policy. The Bank makes its own careful appraisals of investments ^{opportunities} and ^{the conditions} of the national economies, including the creditworthiness of its borrowers. It does everything possible to insure that loans from the Bank are used for productive purposes which add to the economic strength of the borrowing countries and lay the basis not only of servicing ^{of} their debt to the Bank, but also to other public and private investors.

including close ^{scrutinizing} scrutiny of the execution of projects,

proper policies

Question 2

~~I am worried about~~ the increasing debts of some of the developing countries and believe this is becoming one of the most critical problems *for certain* ~~of the field of development finance.~~ ~~However~~ I believe that the problem

is manageable, if handled in time. At present the annual debt service on amortization and interest of developing countries accounts on average of about 8% of their earnings from exports of goods and services. In some countries however external debt service is 20% or even more of exports. In such cases, concern ^{over} the ability to repay is inevitable. Experience teaches us however that ^{other} such ratios are not conclusive. Mexico, for example, with a high debt service ratio has a very good credit standard. ~~Other~~ ^{and diversification} factors such as growth of exports, debt servicing record, ability to attract private capital, political stability, etc. all ^{should be} weigh in the judgement of creditworthiness. These factors, where unfavorable, ^{can frequently be} are subject to change.

We regard it as part of our job in the Bank to do all possible to assist countries to pursue those policies which strengthen their capacity, both at present and in the future, to service debt. Developing countries cannot hope to develop satisfactorily without increasing their external debt.

~~Our aim~~ ^{should be} ~~should not be to avoid increasing debt,~~ ^{on reasonable terms} but to insure that debt is incurred ^{that the} for productive purposes and ability of the country to repay debt is constantly strengthened.

For those countries which reach the limits of their debt servicing capacity, the World Bank is simply not in a position to make any new loans. It is for ^{urgent} this reason why we have attached considerable importance to the existence of the International Development Association, which provides funds from national budgets, ^{replacement of the resources} which enable credits to be made ^{very long maturity} with ~~very long maturity~~ and virtually ~~no~~ ^{interest free} interest.

However, some general debt has been incurred for poor reasons and a excessively onerous terms.

on a fifty year basis

over

Many developing countries are showing a much more responsible attitude in incurring more external debts; ~~and have so far~~ e.g. by severely limiting increases in short-term external debt.

1.b The persistence of balance of payments difficulties in some of the industrial countries, particularly the United States and the United Kingdom, have been an important factor in the fund raising activities of the Bank. The Bank is eager to do its utmost not to enhance such balance of payments difficulties, while at the same time fulfilling ^{the} responsibilities given to it in its Articles of Agreement, namely, assisting the development of the less developed countries of the world. In those cases where balance of payments difficulties have led to drastic restrictions of exports of capital such as the United Kingdom, the World Bank has not tried to borrow money in ^{the} capital markets in recent years. In the case of the United States, which is the largest capital market, there has fortunately been a recognition by the United States authorities that exports of capital to the developing countries should be maintained, although at a reduced level than might otherwise prevail.

STET
? This recognizes the basic principle that poor countries are not in a position to carry on development and to service the foreign investment already made in their countries, unless they receive new inflows of capital from abroad on a continuing basis. The United States in response to its balance of payments difficulties has "tied" its development assistance to purchases in the United States. In the case of the World Bank, however, such tying is incompatible with its multilateral character and the principle of international ^{competitive} ~~bidding~~ bidding which guides the Bank in its lending operations. Thus funds disbursed by the Bank to its borrowers ^{Can be used in any country} ~~are not tied~~, and the amount of exports which any industrial country receives as a result of Bank loans depends on its international competitiveness. ~~The World Bank is indeed grateful to the United States authorities that they have continued to allow the World Bank to have access to the United States capital market,~~ ^{The World Bank} ~~on the~~

Must

member country plus
sanctions

1.b

In this connection, it may
~~other hand it is to~~ be noted that the cumulative effect of all World Bank transactions has been to make a very large positive contribution to the United States balance of payments and it is expected that it will continue to do so. The World Bank is not only a borrower in the US capital market, but is also an investor. It holds a large portion of its current cash and securities in the United States. As of latest available date such cash and securities amounted to about \$1.5 billion (?).

~~I do hope that the new Administration will continue to allow~~
~~the World Bank to have access to US capital markets.~~ I ~~also~~ *trust* hope that, as recently in the case of Germany, the countries which experienced large balance of payments surpluses will permit the Bank to take advantage of these conditions by borrowing more heavily than otherwise in the markets of such countries.

Question 5

*Countries
have given the Bank*

I do not believe that regarding the World Bank as a development institution ~~in any way~~ diminishes confidence in its bonds. The World Bank is a special type of a bank whose characteristics are clearly set forth in the Articles of Agreement. These Articles have guided the institution for over 20 years. Under these Articles, the World Bank has a clear responsibility to help bring about the economic development of its member countries. It is for this reason that countries have subscribed over \$22 billion, of which over \$2 billion has already been paid in and the remainder still uncalled for becomes in effect a guarantee fund ~~against possible losses.~~ ~~It is also to~~ ~~help to~~ ~~pursue the objective of the Bank to gain access to capital markets and other~~ ~~ways to raise funds in the developed countries for use in productive investment in the developing countries.~~ ~~It is these~~ ~~special responsibilities which make the World Bank a development institution, while at the same time retaining its essential character as a bank operating on the principle of maintaining and strengthening its financial structure and insuring ~~the~~ liquidity ~~of the~~ institution in the short run and its financial soundness in the long run.~~

I am sure that if we adhere to the principles of sound financial management, as summarized above, the bank will continue

confidence of the world's capital markets as expressed by the high rating of World Bank's bonds and the success we have had in expanding our ~~lending~~ *money* operations. Perhaps it should be emphasized that even with our expanded program of lending operations, I do not believe that it will be necessary for the World Bank to borrow more in the foreseeable future than it has already succeeded in doing in the current fiscal year.

To enjoy the

*has enabled the
Bank*

Irving.

I've had need to work
with this within the shop
because more really
knows the answers.

S.A. has had a look,
but R. McN. would like
you to consider carefully.

I hope you may be
able to do this in the
next week in spite of
pressures. Let me know if
I can help.

12/19 To Mr. Clark

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: December 19, 1968

FROM: William Clark

SUBJECT: Dutch newspaper "Interview".

Mr. Aldewereld suggests the following points which, if you agree, we will work on in the next ten days:

1. That in the education piece (p.6) we take in the point (you made to Ed Dale) that our education loans are directed to economic growth, not, primarily, personal fulfillment.

DK

2. Add the points on our special creditworthiness studies (also made to Dale) (Question 2, p.8)

DK

3. On the soundness of our bonds stress ever more that their best guarantee is our careful appraisal of projects and of creditworthiness. The ultimate guarantee of Governments ~~lies only in background~~. Note that the guarantee of U.S. alone is bigger than our total funded debt. (p.14-15).

is the guarantee

Don't stress that the best guarantee is the careful appraisal but emphasize that there is a careful appraisal.

4. On page 11 he wonders if this is too much directed to L.D.C.'s and not enough to the "hard headed" Europeans. I am not sure.

[Handwritten arrow pointing to point 4]

*pg 10 is good -
pg 11 is redundant*

WDC:Clark:sf

*Please ask Irving to work with you.
Return time for review.
In the meantime, don't "commit" us.
WDC*

3.20

D R A F T
December 18, 1968

ALGEMEEN HANDELSBLAD, AMSTERDAM

QUESTIONS AND ANSWERS

1. How do you propose to raise the money you will need to double the Bank Group's financing over the next five years, in view of:

- A. The scarcity of funds in the capital markets;
- B. The balance of payments difficulties of many rich countries and the consequent reduction of their aid;
- C. The concern that expansion threatens the Bank's reputation as a sound and successful institution.

Answers:

1.A. There is no absolute shortage of financial resources in the rich countries. Their immense capacity for generating growth has, after all, enabled them to raise their combined annual real income by about \$400 billion during the 1960's; this addition to the annual income of the rich countries is far greater than the total annual income of all the developing countries taken together. So there is no problem as far as the availability of resources is concerned; the wealth,

a poor answer not directed to the question - ask Irving Friedman to read and answer

and the capacity to increase it, are there. The problem lies rather in the allocation of resources. Will the developed countries use their enormous accretions of wealth only to raise their own standards of living still further above those of the poorer nations, or will they invest more widely some of the extra resources they create each year? Will the base of the growth pyramid remain a narrow one as it is today, or will it broaden to include the many countries of the developing world as well as the few of the developed?

I believe that a broad based pyramid offers not only greater stability, but also the likelihood of a more sustained overall rate of advance. Just as a move towards income redistribution can prime the pump of growth within a country, so a wider spread of the world's wealth can stimulate the more rapid growth of the prosperity of the planet as a whole - with consequent advantages to all.

The real point, then, is that I do not accept the idea that there is a scarcity of funds. The money is there. What ~~must occur~~ *is needed* is a greater realization on the part of private investors and of governments that development

makes both economic and political sense. There is a very large job ahead in ^{creating} ~~forging~~ a greater will to participate more fully in the development effort.

1.B. As to balance of payments problems, it is perfectly true that these have led to the deterioration in the flow of resources from some of the rich countries to the poor, but I believe the rationale for these cut-backs is incorrect. Those responsible for them believe that there is no distinction between capital outflows to other developed countries on the one hand, and outflows to the developing world on the other. I think they are wrong. Money "spent" on development is not a once-and-for-all loss to the rich countries, for the simple reason that it does not stay in the developing nations' pockets. They cannot afford to hoard deutsch marks, or dollars, or gold. They must use the resources they receive to buy the products which only the developed world can supply. Funds invested in sound projects in the less developed countries therefore return very rapidly to the developed countries in the form of orders for goods and services.

A messy answer.
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+ "tighten"
up

Of course, some advanced countries may make greater gains than others from this return flow; those which can supply goods more competitively benefit more than their less competitive neighbors. But this only underlines the fundamental point about the balance of payments disequilibria of the advanced countries - that they reflect the relative strength in world markets of the developed countries vis-a-vis each other. The fundamental point which must be stressed is that the developed world as a whole loses nothing by aid disbursement; indeed it almost certainly gains, as a result of the greater world economic activity produced by a transfer of this kind.

1.C. The Bank's reputation rests on a number of factors.

The first of these is its skill as an investor.

Over the years ^{under my predecessors} we have worked out extraordinarily effective procedures for appraising and evaluating

the projects we finance, and for supervising

them once a loan is made. These techniques are

~~and are today~~ constantly being refined, and adapted to new

fields of lending as we move into them.

Today they are, in my experience, more efficient than ever before

It is of course true that we shall in the future be financing projects in some countries which are just beginning to develop, and whose level of

sophistication may be relatively low. But that is not a new situation for the Bank. To use one area of the world as an example, when we began lending in Latin America almost twenty years ago those countries knew very little about project or sectoral or national planning. But we worked with them, and others worked with them, and the results, while far from perfect, have really been very gratifying. Today most of the Latin American countries -- and many countries in other areas which started from the same low base -- have become very good at planning and carrying out development projects and programs. One of the Bank's great strengths both in its operations and its reputation for soundness is that it works with borrowers over the long term. When it makes a loan, it doesn't write a check and walk away. It lives with the country and the project for many years. It concerns itself with problems that may arise during construction, and later during operation. It advises, persuades, insists. The result is an evolving sophistication on the part of our borrowers. We have already seen many of them develop great capabilities; and I am certain that as we move more deeply into some of the newer countries where we have not yet been very active the same learning process will occur.

Another aspect of the Bank's expanded lending program which has caused a good deal of interest - ~~and a certain amount of concern~~ among investors is our commitment to involve ourselves more deeply in loans for education, and to enter into the new field of population control.

Concern has been voiced that these are areas in which it is less easy to quantify the return on investment than those in which the Bank has traditionally involved itself. This is only partly true. The return on an investment in education is measurable, but indirect - it takes the form of a more skilled new generation, with new capabilities to perform more complex tasks. But one can quantify this return by taking the output of a country which has received education loans, and comparing this to what the output would have been if those loans had not been made. The incremental value is often considerable. Over and above this, it is important to bear in mind the conceptual point that the Bank makes loans to countries in the belief that the projects it supports will contribute to the viability of entire national economies. Loans may similarly be thought of as being repaid out of the benefits accruing to the economy as a whole. I see no reason to reject in principle lending for education or population control; the benefits of loans

*not for investment
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reads*

for these purposes can be enormous. For example, in the field of population control, take two different developing countries with similar standards of living, each with a birth rate of 40 per 1,000. Now estimate what would happen if the birth rate in one of those countries, in a period of 25 years, were to be halved to 20 per 1,000. The country which lowered its population growth would raise its standard of living 40% above the other country in a single generation. This is some measure of the benefits obtainable from population control investment.

Finally, investors in our bonds have an ultimate ~~guarantee~~ safeguard in the Bank's uncalled capital, presently equal to more than \$20 billion equivalent. The Bank's Articles of Agreement provide that if the Bank is unable to meet its obligations to investors member countries can be called upon to make payments up to the amount of their capital stock subscriptions until such obligations are satisfied.

~~subscriptions to the bank's capital.~~ The possibility of this eventuality occurring is highly unlikely, but the protection to the investor is written into the Bank's constitution. This protection could only fail if one postulated the simultaneous and complete economic collapse of all the solvent countries in the world - in which case the relative security of one investment or another would become an academic question.

will be on basis of something like this

I have answered this particular question at some length, because I believe it to be of great importance to assure investors that expansion of the Bank's lending in no way endangers their investment. ~~The expansion we are undertaking cannot be entirely riskproof to the Bank, any more than any business institution's expansion can be entirely riskproof. However, I cannot stress too strongly that investors in Bank bonds are protected against any eventuality except the complete collapse of the whole world's economy. Holders of bonds of individual governments or corporations are a good deal less protected.~~

receive for greater protection

than the

individual business

Question 2. Are you worried about the increasing debts of some developing countries?

Answer 2. The Bank has always warned its member countries about the danger of running up too much debt, and we take the existing debt burden of a country into account in evaluating its economy prior to making a loan. Fundamentally, the problem of debt is a problem of trade; the acceptable amount of debt a country can carry is intimately associated with the health of its export business. For example, India can only carry a greater amount of debt if it can expand its exports to cover the cost of the payments it must make on the additional debt it wishes

and prospective

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to incur. An increase in debt without an increase in the debtor country's external earnings represents a dangerous trend.

We at the Bank watch the debt situation of our developing member countries with great care. In some cases the burden of debt becomes too great for the economy to stand, and the debt needs to be rescheduled. My own belief is that a liberalization of world trade and a determined effort at export diversification by the developing countries themselves are pre-requisites for the alleviation of the debt problem. We do our best to encourage these general remedies; we also try to make sure that our own loans to countries with debt problems are concentrated in sectors which either earn foreign exchange directly by boosting exports, or which save the expenditure of foreign exchange by helping economic import substitution.

The short term debt problem can best be alleviated by the provision of concessionary finance. This is essential if a number of developing countries which have particularly severe debt burdens are to keep up the momentum of their development programs. Many of these countries simply cannot afford to borrow the large sums they need at the interest rate the Bank must charge its borrowers

no loans are the made

today, 6-1/2%. The Bank's instrument for surmounting this difficulty is the International Development Association (IDA) which is financed largely by grants from the developed countries. The present delay in the second replenishment of IDA's resources is little short of disastrous for those countries with a serious debt problem.

Question 3. How do you think the efficiency of the Bank's aid might be increased?

Answer 3. The efficiency of the Bank's activities has been well proved over the last twenty years, and we are constantly working to increase it. Today, there are a number of kinds of development assistance which can have a particularly high payoff: one example is a sector of investment which the Bank considers extremely important -- agriculture. Recent breakthroughs in the development of high yielding strains of wheat and rice have made it possible to obtain yields per acre two or three times as high as could have been produced with normal types of seed. It has also been found that the new high yielding varieties are particularly responsive to irrigation and fertilizer inputs. An important way to increase the Bank's total impact on development, therefore, is to increase the proportion of

that total represented by investment in the new agriculture.

The "agricultural revolution" is a spectacular example: there are other less obvious but equally valuable kinds of development activity which can yield a disproportionately high return on the time and money invested in them. One such activity is the breaking of strangleholds on development. A development program can sometimes fail to produce the benefits it should because of some unforeseen problem -- perhaps quite small in itself -- which is holding up progress. The identification and removal of the obstruction may cost relatively little and yield enormous dividends.

We can increase the efficiency of the aid we give by identifying and concentrating our help on pivotal areas in the development process, where timely investment can yield a particularly high return in terms of economic progress. Massive aid to agriculture, which is now becoming a really profitable proposition, assistance in breaking strangleholds on development, providing member countries which have special problems with technical assistance -- these are three such areas.

Question 4. What are the prospects for the areas in which you have said the Bank wishes to make a particular effort, education, agriculture and population control? With regard to the latter, what criteria will you use in setting up programs, and how will you avoid adverse reactions on religious or ethnic grounds?

Answer 4. In my speech to the Bank's Governors, I outlined the prospects for our agricultural and educational lending by saying that we intended to quadruple the volume of the former and triple the volume of the latter over the next five years. As far as population control is concerned, I should stress that this is a new field of operation for the Bank, and we are still working our way into the subject. The process of deciding how best to assist population control is not made easier by the fact that far too little research has been done on this subject anywhere in the world.

But I must stress again that it is not the absolute size of a country's population which worries us, but its rate of population growth. We are, seriously concerned that the rate of growth of countries' populations should not be so high as to negate the rate of their economic development. For example, if a country's gross domestic product is rising at a level of 3% per annum and population

at a rate of 2.5% per annum, there is painfully little room for the improvement in the standard of living which we as a development agency want to see -- and which humane people all over the world hope for. Our aim is to give children in developing countries the possibility of growing up in a world where they can live with at least some ^{degree} minimum of human dignity. In some cases this can only be achieved by limiting the growth of population to levels with which countries' efforts to promote their economic development can keep pace.

population control?

We fully realize, of course, the religious and ethnic sensitivities in the area of population control. These pose thorny and difficult problems, but fundamental to our approach are respect for the dignity of man and for the right of nations to determine their own approaches to the population question. We are resolved however that the dangers of rapid population growth must be pointed out, and we are determined to extend help when asked.

Question 5. Do you believe that your announced view of the World Bank as being at least as much a development institution as a bank diminishes confidence in its bonds in the money markets, and thereby creates problems for the Bank when it makes bond issues?

91 certainly not.

Answer 5.

In the first half of the current fiscal year the Bank has raised \$804 million equivalent in capital markets. This is a large amount by any standards, and can hardly be taken as a sign of wavering investor confidence in the Bank. Frankly, I think ^{one underestimates the sophistication and} it is an insult ~~to the~~ intelligence of the international financial community to suggest that bankers and investors are unaware of the ^{Soundness of WB bonds, founded on} ~~fundamental im-~~ ^{Moreover these bankers + investors know the im-} ~~portance~~ to the world economy of righting the ^{generally} ~~existing~~ lopsided rate of growth of world prosperity.

The financial community knows very well the potentially catastrophic situation created by the present imbalance between the rich and the poor nations. Development is good business, ultimately the best business of all, because it gives the world a chance of averting economic disaster. Bankers know this; they also know that our members' backing for our obligations and our record as a successful investor make the World Bank's bonds an unimpeachably secure form of investment.

Of course there are problems of raising money in today's capital markets, but these are not unique to the World Bank. The two major elements of difficulty are the current exchange rate confusion, and the general prevalence of inflation. Both these adversely affect sales of fixed interest bonds

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denominated in national currencies. Like any other major borrower, we may occasionally bite on the bad tooth, but our fund-raising program has been very successful so far under this year's difficult conditions, and I have every confidence that it will continue to be so. It is precisely because I respect the intelligence and the ability of the international financial community that I assert my confidence in the viability of the Bank's program over the next five years -- a program which anyone concerned with the orderly growth of prosperity on this planet cannot possibly fail to support.

#

D R A F T

January 15, 1969

To: Mr. Robert S. McNamara

From: Irving S. Friedman

Subject: Creditworthiness Studies

You will recall on December 11 I sent a memorandum to you on creditworthiness studies, attaching a draft of "Creditworthiness Analysis" prepared by Mr. de Vries. You were promised at that time that as soon as we had finished one region, probably the Western Hemisphere, we would send a memo to you on how the work was shaping up. I am attaching a further memorandum from Mr. de Vries on this subject.

I am hoping that this work will serve a number of purposes, of which one is to provide a general analytical or ~~my~~ philosophical paper on creditworthiness as part of the new five-year program.

Needless to say much depends in the future on the performance of countries in determining their future creditworthiness. Mr. de Vries, however, has based himself on the best available knowledge about the country as we know it now and what we can foresee for the future on the basis of on-going ~~mak~~ policies. I find particularly interesting the attempt to establish a creditworthiness evaluation for each country since they do give us indications as to which countries we might reasonably be enabled to envisage which increase any Bank lending programs and still have due regard to the risks ^{that} ~~for~~ the Bank takes in expanding countries to this criteria.

Mr. Robert S. McNamara (through Mr. Friedman)

January 10, 1969

Barend A. de Vries

Creditworthiness Evaluation Table

The attached table summarizes key elements in creditworthiness evaluation of six Latin American countries. The material is based on last year's Five-Year Plan projections and subsequent economic reports and has been discussed with the Western Hemisphere Department.

The evaluation is based on ongoing policies. Changes in growth policies may take effect slowly. However, deterioration in balance of payments management or other financial policies may be more rapid and require substantial revision in the evaluation.

In the updating of the Five-Year Plan, now in a preparatory stage, we intend to include essentially the same statistical information which would subsequently be kept under review.

We should appreciate any comments on the form and content of the presentation which may be pertinent to our further work.

cc: Messrs. Friedman ✓
Adler
Valtz

CREDITWORTHINESS EVALUATION OF SELECTED COUNTRIES

1. The attached Table presents information relevant to the Bank's creditworthiness evaluation of major countries. The information included is intended to summarize key elements in the evaluation; it does not constitute a comprehensive survey of all relevant factors.
2. Section I of the Table contains information on the present position and projected trends over the coming five years in the country's official debt and official financing requirements. Section II contains information on the Bank's present and projected participation in the overall official financing. Section III gives a summary creditworthiness evaluation in terms of the estimated tolerable maximum debt service ratio in 1973 and a schematic classification of the main types of debt servicing problem which the country may encounter. The evaluation in Section III is based on an overall appreciation of a wide range of factors relevant to the country's position and prospects and is not derived solely from the factors specified in Sections I and II.
3. The projection data in Sections I and II have been taken from country statements for the last Five-Year Plan exercise or from subsequent economic reports. These statements and reports generally contain a Five-Year external financing flow which is considered appropriate for the country, given its present policies, economic position and prospects, its present and prospective debt burden and aid requirements. The creditworthiness evaluation in Section III is

based on a general review of information in these statements and reports and has been arrived at in consultation with Area specialists taking into account most recent developments.

4. Section I specifies the following selected indicators:

(i) Amount of public and publicly guaranteed debt outstanding as of December 1967 and the rate of amortization on this debt over the period to December 1972.

(ii) Export growth in the recent past and the projected growth to 1973 (columns 4 and 5). This is included as a basic indicator of the country's debt servicing capacity.

(iii) Dependence on net external capital 1969-73.

Increasing dependence on external finance for net capital requirements in conjunction with the country's existing debt service obligations will be indicative of increasing or diminishing future difficulty in coping with debt problems.

5. The present level and projected growth in the gross official inflow. A rapid growth in the gross inflow requirement may indicate difficulties in raising the necessary volume of finance on appropriate terms.

6. Dependence on concessionary finance (i.e. grants and loans with maturity over 30 years and interest rate 3% or below). The greater the dependence on concessionary finance, the greater may be the risk that the country experiences a setback in its projected external financing plan with possible consequences for its ability to service debt.

7. Liquidity. Debt crises are frequently caused or precipitated by the inadequacy of the country's freely available reserves (liquidity) to meet the contingency of temporary setbacks in its receipts of foreign exchange resources. These setbacks may arise from erratic movements in the country's export earnings or from the volatility of its capital account receipts. Continued servicing of debt in situations of temporary decline in current foreign exchange earnings will depend on the adequacy of reserves. Columns 13 to 16 of Section I are intended to provide some indication of the safeguard against a possible liquidity problem. In these columns the level of present reserves (including IMF facilities), an estimate of the maximum contingent decline in export earnings and the projected debt servicing burden are all expressed in relation to export earnings. Where the potential decline in export earnings is large in relation to debt service claim and the basic reserve position a possible liquidity problem is indicated. The actual measures used for the liquidity indicators are specified in the footnotes to Section I. The basic reserve position shown in the Table relates to 1968 reserves and exports. The indicator of export shortfall has been measured as the larger of the percentage downward deviations from trend in either a single year or in a consecutive two-year period over the years 1955-67. This measure has been chosen because it provides an indicator of the maximum shortfall on the basis of past experience and therefore an approximation to the upper limit of the contingency. A two-year limit to the export shortfall has been adopted since more continuous declines might indicate a structural rather than a liquidity problem.

8. Section II summarizes the present and projected Bank involvement in external financing. Columns 17 to 21 indicate the projected total amounts of gross official financing and projected Bank commitments and disbursements for the years 1969 through 1973. Columns 22 and 23 show the amount of net Bank loans outstanding at 1968 and the projected amounts outstanding in 1973, assuming that the Bank's Five-Year loan targets are met. Columns 24 through 27 show actual 1968 and projected 1973 service payments to the Bank in dollar amounts and as a proportion of total debt service on total official borrowing.

9. Section III identifies critical elements in creditworthiness evaluation:

(a) Column 28 shows an estimated maximum tolerable debt service ratio derived on the basis of a broad assessment of the country's present and prospective balance of payments problems. This column should be compared with the 1968 and 1973 ratios in order to gauge the leeway the country has in its debt management.

(b) The following main categories of debt servicing problems which the country may encounter:

(i) Control of medium-term credits critical. This covers situations in which the proportion of medium-term credits (particularly suppliers' and commercial credits) is such as to indicate that debt servicing may be jeopardized unless the country was able to acquire a larger proportion of its financing needs on relatively softer terms.

(ii) Liquidity crisis indicates situations in which the present reserve position and likely contingency in export shortfall in relation to debt servicing obligation may suggest difficulty in mobilizing foreign exchange resources.

(iii) Difficulty in obtaining project loans due to inadequate project preparation resulting in the country having to have recourse to external financing on less favorable terms.

(iv) Difficulty in obtaining program loans or loans on other concessionary terms. Where such difficulty is possible, the country's development plan may be jeopardized or it may have recourse to borrowing on terms which aggravate its debt servicing burden.

10. The final two columns summarize the various aspects of risk by indicating the likelihood of a need to a refinancing or rescheduling arrangement, either including or excluding IBRD debt. The risk is specified as low, medium or high. This represents an approximate judgment and does not indicate a precise probability.

SUMMARY TABLE - WESTERN HEMISPHERE

I. SELECTED INDICATORS

Countries	Outstanding Public Debt As at the End of 1967 /1 (\$ million)	Amortization Payments During 1968 to 1972 As of Outstanding Public Debt at the End of 1967 /2	Export Growth /3 (Average)		Dependence on Net External Capital 1969-73 (Average) /5		Gross Official Financing /6			Concessionary Aid 1969-73 (Average) /7		Liquidity			
			1962-66 /4	1969-73	Amount /5	% of Imports /6	1962-66 Average /6	1969-73 Average /6	% Increase 1969-73 /6	Amount /7	% of Gross Official Financing /7	Basic Reserve Position 1968 /8	Largest Consecutive Exp. Decline Since 1955 /9	Debt Service 1968 /10	1973 /10
			1962-66 /4	1969-73	(\$ mil.)	% of Imports	1962-66 Average /6	1969-73 Average /6	% Increase 1969-73 /6	(\$ mil.)	% of Gross Official Financing /7	Percentage of Exports	1968	1973	1968
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)
Argentina	2,407	60	5.7	5.8	-11.4 /16	-8 /16	129.8	163	26	-	-	60 to 84 /17	9.7	27.0 /18	15 /18
Brazil	3,669	43	5.8	5.1	60.4	23	488.4 /19	730	50	40	6	22 to 39	12.0	23.8 /20	22.8 /20
Chile	1,725	37	18.3 /21	9.6 /21	10.4	10 /22	234.4	205	-12	83	40	30 to 37 /21	13.5	31.2 /23	19.2 /23
Colombia	1,118	31	4.0	9.5	283 /25	27	123.7 /25	250	102	45	18	24 to 30	10.7	12.6	15.9
Mexico	2,648	57	7.6	9.0	385	13		580		-	-	31 to 42 /26	8.3	21.8 /27	17.3
Peru	968	44	8.3 /28	5.4 /28	198	18	68.4	177	159	55	31	17 to 25 /28	16.8	12.0 /29	10.8

II. BANK PARTICIPATION

III. CREDITWORTHINESS EVALUATION

	Gross Official Financing /11 Non-Concessional					Net Bank Position		Service Payments to Bank in				Estimated Tolerable Maximum Debt Service Ratio /10	Control of Med.-Term Credits /Critical	Liquidity Crisis	Risks Difficulty in Obtaining		Of Debt Refinancing During 5-Year Period	
	1969	1970	1971	1972	1973	1968 /12	1973 /12	1968		1973					Project Loans	Program Loans or Other Concessional Terms	Excluding IBRD /15	Including IBRD /15
	1969	1970	1971	1972	1973	1968 /12	1973 /12	Amount /13 (\$ mil.)	% of Total /14	Amount /13 (\$ mil.)	% of Total /14							
(17)	(18)	(19)	(20)	(21)	(22)	(23)	(24)	(25)	(26)	(27)	(28)	(29)	(30)	(31)	(32)	(33)	(34)	
Argentina	(Total	244	171	127	122	152	109.3	365.3	12	2	31	10	20	x	x	L	L	
	(Bank Commitments	90	90	120	50	75												
	(Bank Disbursements	24	48	63	72	79												
Brazil	(Total	554	565	733	778	821	167.9	685.9	22	5	65	11	25	x		M	L	
	(Bank Commitments	75	185	180	175	250												
	(Bank Disbursements	59	106	130	147	161												
Chile	(Total	119	114	113	120	141	92.1	200.1	12	5	20	10	20	/24	x	x	H	L
	(Bank Commitments	30	48	38	35	25												
	(Bank Disbursements	32	24	28	34	29												
Colombia	(Total	225	200	200	200	200	291.0	534.0	30	32.7	54	30.8	20	/24	x	L	L	
	(Bank Commitments	110	95	119	85	70												
	(Bank Disbursements	40	50	80	86	78												
Mexico	(Total	700	700	500	500	500	483.4	680.4	49	9.3	68	11.3	20	x		L	L	
	(Bank Commitments	105	35	90	100	100												
	(Bank Disbursements	43	64	68	69	81												
Peru	(Total	133	122	123	119	114	128.2	212.2	12	12.6 /30	19	17.3	11	x	x	x	H	L
	(Bank Commitments	17	40	40	60	50												
	(Bank Disbursements	19	18	20	26	32												

See Footnotes on page 2.

- /1 Including undisbursed loans.
- /2 Amortization payments during 1968 to 1972 against loans procured up to 1967, as a percentage of outstanding public debt at the end of 1967.
- /3 Of goods and non-factor services.
- /4 Based on 3-year moving averages for 1962-1966.
- /5 Public and private capital.
- /6 Imports of goods and non-factor services.
- /7 Grants and loans of over 30 years maturity.
- /8 The percentages are normally with reference to 1968 exports of goods and non-factor services. Reserves as of September 1968 for Colombia, August 1968 for Argentina, Brazil and Chile, and July 1968 for Mexico and Peru. Basic reserves include gold and gross foreign exchange holdings of Central Banks or Monetary Authorities and facilities available under IMF's Compensatory Financing Scheme; in addition for working out maxima and minima of the ranges indicated, "basic reserves" include "Gross Fund Position" and "Gold Tranche Position" respectively (source for basic reserves - IFS November 1968).
- /9 Of goods and services (including factor services); these percentages represent declines from trend values (established with reference to logarithmic trend equation). The maximum percentages normally relate to consecutive years of declines. Only in those cases where the year of maximum percentage decline is neither followed nor preceded by annual decline that the figures indicated in Col. 14 relate to one year. These years are 1961 for Argentina, 1962 to 1963 for Brazil and Chile, 1961 to 1962 for Colombia and Mexico and 1958 to 1959 for Peru.
- /10 The percentages in columns 15, 16 and 28 are normally with reference to exports of goods and non-factor services.
- /11 Bank commitment and disbursement figures in columns 17 to 21 are on financial year basis.
- /12 Net Bank loans outstanding (including undisbursed) as at the close of June 1968 or June 1973.
- /13 During July 1968 to June 1969 or July 1972 to June 1973.
- /14 Percentage of total public debt service in 1968 or 1973; for Argentina and Chile the percentages are with reference to total debt service changes (public and private).
- /15 In columns 33 and 34 "L" stands for 'low', "M" for 'medium' and "H" for 'high'.
- /16 Minus sign indicates net outflow of capital.
- /17 As a percentage of exports of goods.
- /18 Including service on private debt and with reference to exports of goods and services.
- /19 Includes some unguaranteed private capital which is not separately identifiable.
- /20 Excludes IMF payments and is with reference to exports of goods and non-factor services.
- /21 Refers to exports of goods less net factor payments.
- /22 Imports of goods and net factor services.
- /23 Including service on private debt and as a percentage of exports of goods less net factor payments (other than interest charges).
- /24 The problem of control of medium-term credits (including supplier credits of less than 8 years) is comparatively less critical.
- /25 Including net transfer receipts.
- /26 As a percentage of exports of goods and services.
- /27 Provisional and as a percentage of exports of goods and services.
- /28 With reference to exports of goods and services less factor payments.
- /29 Provisional for 1967; as a percentage of exports of goods and services net of factor payments (other than interest payments on public debt).
- /30 Provisional.

January 9, 1969

Spare

Mr. Robert S. McNamara

December 11, 1968

Irving S. Friedman

Creditworthiness Studies

You will recall that Mr. de Vries and myself discussed with you the program on creditworthiness studies on the basis of a memorandum of November 6, a copy of which is attached for reference.

At that time you requested that we give you a time schedule for the first two items in the attached memorandum, namely the drafting of a list of creditworthiness analysis "instructions" and a preliminary list of creditworthiness for Bank lending for countries included in the Five-year Program. Mr. de Vries has been at work on this and we are now able to report the following:

1. "Instructions": Mr. de Vries has prepared the attached draft set of creditworthiness analysis "instructions". He will be discussing this draft "instructions" with the Area Departments and on the basis of comments received will prepare a revised version. In the meantime, however, you may be interested to see the "instructions" as they stand at present.

2. Creditworthiness Table: the purpose of this table is to bring out critical elements in the Bank's evaluation of the creditworthiness of major countries. The table will be prepared region-by-region and discussed with the Area Department concerned before being transmitted to you. We expect that by February 1 most of this work will be completed, although of course there may be some delay in case the consultations with Area Departments take longer than we now anticipate. As soon as we have finished one region - probably the Western Hemisphere - we will send it to you to give you some idea how this is shaping up.

FORM NO. 75
(2-60)

-INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL FINANCE
CORPORATION

INTERNATIONAL DEVELOPMENT
ASSOCIATION

ROUTING SLIP

Date

December 31, 1968

NAME

ROOM NO.

Mr. Friedman

A. 1221

To Handle

Note and File

Appropriate Disposition

Note and Return

Approval

Prepare Reply

Comment

Per Our Conversation

Full Report

Recommendation

XX

Information

Signature

Initial

Send On

REMARKS

From

Baumbach

* Main problem is relating overall credit worthiness to Bank credit worthiness

DEC 31 1968

OFFICE MEMORANDUM

TO: Files DATE: December 30, 1968
FROM: Barend A. de Vries
SUBJECT: Discussions of Draft Paper "Creditworthiness Analysis"

1. This note summarizes some of the questions and issues that have come up in the course of discussions with Area Departments of the December 11 draft.

only Area Depts



(a) The paper states (para. 7) that the Bank cannot as a rule expect to be in a preferential position. In practice, of course, the Bank may seek to obtain preference and has succeeded in getting it. Many Part I member governments seem to assume that we have a preferential position. The Bank's dependence on the capital market may also require that it obtain preference. In creditworthiness analysis we should, however, assume that the Bank cannot count on being in a preferential position: this implies a more severe creditworthiness test. Furthermore, in situations where the Bank is no longer a marginal provider of capital it will also, in practice, be impossible to maintain a preferential position.

(b) Either the guideline paper or the internal discussion of this paper should clarify what risks the Bank should be prepared to undertake in its lending operations. Following are some relevant points and questions:

(i) The paper states (para. 8) that the Bank is able to assume the full risk of suspension of debt service caused by worldwide depression, widespread internal conflict and natural catastrophes.

(ii) Risks increase with dependence on external capital. All situations where dependence is high are potentially risky. Basically the question is whether it is worthwhile for the Bank to assume the risks involved in a situation. The memorandum (paras. 12, 13.b. and 15) assumes that the Bank's assessment be based on countries' present policies and a reasonable expectation of policies in the immediate future. This approach implies risking

risk related to
assess of Bank
① risk of not being
paid (as sum related
to flexibility of country in
responding to help program)
② risk of develop program
being devaluated

the consequences of policy reversals in the future. Specifically a reversal may quickly dissipate a country's reserve position, its access to secondary liquidity and may weaken its ability to cope with short-term fluctuations. The risk of future liquidity crises is particularly crucial since they were the immediate cause of most past debt crises. This risk is, of course, higher when debt burdens are high in relation to potential set backs, for example, in export earnings. If the Bank is willing to assume the risk of future policy reversals, its decisions are based on present policies and little use is served by speculating about the likelihood of future political changes. On the other hand, particularly as our position in potentially risky situations increases, we will do well to observe the Bank's "stake" over a 5-year period, based on present lending plans. Furthermore, we should stand ready to scale back our plans should policies deteriorate.

(iii) What should be the Bank's attitude toward the risk of revolution? Staff following developments in certain countries see clear danger signs ahead. In countries like Ethiopia and the Philippines they may even consider a revolution, including agrarian reform, desirable. But "revolution" and "reform" may bring to power forces which are hostile to external interests and external debt or may cause severe liquidity crises. In cases such as these the economic report would normally identify the key problems in the country's development and discuss whether the Government is taking sufficient action to cope with them. Where the Government is sufficiently deficient in this respect, the Bank may well be assuming an unjustifiable risk if it were to lend up to the amounts which would look safe on liquidity grounds alone. Creditworthiness considerations suggest limiting lending by linking it to basic reform in critical sectors. Again decisions would be based on ongoing policies.

(c) The long-term projections have been kept simple. But they are long-term and therefore speculative. Where we feel uncertain about our present parameters (e.g. savings trends) and data (e.g. national income accounts), the projections may have to be even simpler (e.g. limit them to the balance of payments). Where possible we would want to check the long-term trend in imports against GDP

measures to ensure good external debt management to prevent political changes?

not clear?

and components (investment, industrial production, etc.). I would imagine we want to undertake long-term projections only when a basic country assessment is made. And then perhaps only in cases where there is considerable risk, or where the present and/or prospective debt burden is high; these cases to be identified more precisely in the next draft. When there are high risks and we feel we know so little that we cannot state what the longer term trends are, perhaps the uncertainty reflects our doubt as to the country's creditworthiness.

(d) Thus far we have left open the question whether the paper will eventually become an operational memorandum. The purpose is a paper that will provide effective guidance to economists in analyzing creditworthiness. The paper should remain under review in light of experience gained.

(e) The assessment of a country's creditworthiness should bring out somewhat more explicitly the items suggested in Section III of the draft. Given the speed with which green cover economic reports must often be converted into grey cover, it may be desirable to include the more candid discussion of creditworthiness issue in an economic policy memorandum. The analytical support for the policy memorandum should, of course, come in the appropriate sections of the economic report.

1/ Any concept of "apparent" cost of
 interest - part in terms of
 creditworthiness
 2/ Partly attribute forward risk taking - (see
 P. 1.)

*Euro-Dollar
file*

Mr. Irving S. Friedman

October 23, 1968

Ugo Sacchetti

Euro-Dollar and Euro-Bonds Markets

This is in response to Mr. Aldewereld's request for background information on the subject.

The following publications or reproductions from other publications, which are attached, contain the essential elements for the knowledge of the structure and some historical background of the two markets. It is suggested that they be read in the order in which they are listed (the Monthly Bulletin of the First National City Bank of New York is referred to as "City Bank").

1. Federal Reserve Bank of New York--
Monthly Bulletin, August 1968,
Pages 169-174.
2. City Bank, May 1966, Pages 56-58.
3. City Bank, July 1966, Pages 81-83.
4. City Bank, August 1967, Pages 89-92.

The following photostats give the most recent developments in the Euro-Bond market and the Euro-Dollar interests rates.

1. A reproduction from the October 17,
1968, issue of World Financial Markets
published by the Morgan Guaranty Trust
Company.
2. A memorandum by Mr. David Williams of
the Treasury Department of the IMF,
dated October 22, 1968.

A very detailed description of the operations in the Euro-Dollar market in 1967 is contained in the latest annual report of the Bank For International Settlements, Pages 145-161. I mention this merely as a reference since I consider it too detailed for the purpose.

The publications are borrowed from the library and I would appreciate it if once used, they were returned to me.

Attachments: Photostat on Euro-Bonds
Monthly Economic Letters for May 1966, July 1966, August 1967
Photostat on The International Bond Market
Photostat of Office Memorandum dated October 22, 1968

USacchetti:rdd



Office Memorandum

TO : Mr. Hulley

FROM : David Williams *DW*

SUBJECT : Euro-dollar Interest Rate Series

DATE: October 22, 1968

As promised attached is a time series for end of week call deposit and three month euro-dollar deposit rates in London. The London 1 year U.S. dollar CD rates are published only since early October--apparently the market in this paper were unrepresentatively small before this time. However, the following two quotations give some idea of the close link between the euro-dollar deposit rates and the CD rates.

"London dollar CDs are issued to non-residents of the United States for 1 to 12 months, at rates generally 1/8 per cent point below comparable Euro-dollar deposit rates".
(p.417, The Banker, May 1967 issue).

"Certificates are issued with a comparatively low minimum denomination (\$25,000) and yield about 1/8 per cent less than the corresponding euro-dollar maturity."
(p.158, BOE Quarterly Bulletin, June 1968 issue).

We cannot find a representative series of 3 year euro-dollar deposit rates--these rates are apparently open to negotiation. One New York bank gave me a recent quotation that was being offered (not by that particular bank) in London in early October.

I hope these will be of some help to you.

Attachment

October 22, 1968

		<u>Euro-Dollar Deposits</u>		<u>1 Year Denominated in Dollars</u>	
		<u>Call Notice</u>	<u>Three months</u>	<u>1 Yr. CD</u>	<u>3 Years</u>
July	5	6 3/8 - 6 7/8	6 11/16 - 6 13/16		
	12	5 5/8 - 6 1/8	6 5/16 - 6 7/16		
	19	5 3/8 - 5 7/8 ^{a/}	6 3/8 - 6 5/8		
	26	5 3/4 - 6 1/4	6 3/16 - 6 5/16		
	31	6 1/8 - 6 5/8	6 1/4 - 6 3/8		
August	2	5 5/8 - 6 1/8	5 5/8 - 6 1/8		
	9	5 5/8 - 6 1/8 ^{a/}	5 15/16 - 6 1/16		
	16	5 1/2 - 6	6 - 6 1/8		
	23	5 5/8 - 6 1/8	6 - 6 1/8		
	30	6 - 6 1/8	6 1/8 - 6 1/4		
September	6	5 5/8 - 6 1/8	6 1/16 - 6 3/16		
	13	5 1/2 - 6	5 13/16 - 5 15/16		
	20	5 - 5 1/2	5 13/16 - 5 15/16		
	27	5 1/8 - 5 5/8	6 - 6 1/8		
	30	5 1/8 - 5 5/8	6 3/16 - 6 5/16		
October	4	5 5/8 - 6 1/8	6 5/16 - 6 7/16		
	11	5 3/4 - 6 1/4	6 - 6 1/2	6 9/16 - 6 11/16	6 3/8 - 6 5/8

a/ Previous day.



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	19	5 3/8 - 5 7/8 ^{a/}	6 3/8 - 6 5/8		
	26	5 3/4 - 6 1/4	6 3/16 - 6 5/16		
	31	6 1/8 - 6 5/8	6 1/4 - 6 3/8		
August	2	5 5/8 - 6 1/8	5 5/8 - 6 1/8		
	9	5 5/8 - 6 1/8 ^{a/}	5 15/16 - 6 1/16		
	16	5 1/2 - 6	6 - 6 1/8		
	23	5 5/8 - 6 1/8	6 - 6 1/8		
	30	6 - 6 1/8	6 1/8 - 6 1/4		
September	6	5 5/8 - 6 1/8	6 1/16 - 6 3/16		
	13	5 1/2 - 6	5 13/16 - 5 15/16		
	20	5 - 5 1/2	5 13/16 - 5 15/16		
	27	5 1/8 - 5 5/8	6 - 6 1/8		
	30	5 1/8 - 5 5/8	6 3/16 - 6 5/16		
October	4	5 5/8 - 6 1/8	6 5/16 - 6 7/16		
	11	5 3/4 - 6 1/4	6 - 6 1/2	6 9/16 - 6 11/16	6 3/8 - 6 5/8

a/ Previous day.

THE INTERNATIONAL BOND MARKET

The flood of DM-denominated issues continues. Preliminary figures indicate that at least \$168 million of DM issues will be offered by foreign borrowers during October. This follows an average of nearly \$270 million in each of the preceding three months. Since mid-year, DM-denominated bonds have accounted for over half of total new issue volume in the international bond market, compared with less than 20% in the first half of 1968. Despite this heavy activity, secondary market yields on these bonds have declined: for example, the average yield on 10- to 20-year, DM bonds of U.S. companies dropped 11 basis points - to 6.23% - between the end of August and mid-October. However, some market observers feel that German investors, who have been purchasing a large portion of these DM issues, may become increasingly selective.

Although new issue activity in U.S. dollar-denominated bonds has been fairly moderate since August, it now appears to be picking up. More U.S. dollar bonds will be floated in October - at least \$185 million - than in August or September. The market for straight-debt U.S. dollar issues, in particular, continues to show improvement. Average secondary market yields of U.S. companies' U.S. dollar-denominated five-year notes and 10- to 20-year bonds declined from their end-August levels - by 8 and 9 basis points respectively - to 6.67% and 7.07% on October 11. Earlier this month, a U.S. company offered a \$12.5 million, 7%, five-year note issue, priced to yield 7.24%. Two 12-year issues - one for \$20 million with a semiannual coupon and another for \$40 million with an annual coupon - are planned by U.S. companies for later this month. Both issues are expected to be offered with 7% coupons, priced at a discount.

International Bond Issues in 1968 - (in U.S. \$ millions)

	Quarters			Aug.	Sep.	Oct. ^P	Jan.-Oct. ^P
	I	II	III				
<i>Total New Issue Volume</i>	<u>876</u>	<u>1,276</u>	<u>1,411</u>	<u>413</u>	<u>404</u>	<u>438</u>	<u>4,001</u>
U.S. Dollar	643	854	540	140	100	185	2,222
German Mark	101	279	809	248	275	168	1,357
Other	132	143	62	25	29	85	422
U.S. Companies	561	819	380	90	90	217	1,977
Other	315	457	1,031	223	314	221	2,024
Straight Debt	415	513	956	318	304	380	2,264
Convertibles	461	763	455	95	100	58	1,737

TABLE III

COMPARATIVE LONG-TERM BOND YIELDS*

	<i>Government Bonds</i>				<i>Corporate Bonds</i>			
	<u>Sep.</u> <u>1967</u>	<u>June</u> <u>1968</u>	<u>Aug.</u> <u>1968</u>	<u>Sep.</u> <u>1968</u>	<u>Sep.</u> <u>1967</u>	<u>June</u> <u>1968</u>	<u>Aug.</u> <u>1968</u>	<u>Sep.</u> <u>1968</u>
DOMESTIC ISSUES								
Belgium	5.28	5.12	5.13	5.19	5.92	5.96	5.65	5.72
France	5.73	5.94	5.96	5.95	7.35	7.72	7.40	7.49
Germany	6.90	6.68	6.59	6.54	6.95	6.65	6.42	6.43
Italy	4.86	4.76	4.63	4.57	6.92	7.08	7.19	7.19
Netherlands	5.96	6.32	6.37	6.26	6.66	6.84	6.93	6.85
Denmark	9.34	8.79	8.82	8.82	-	-	-	-
Norway	4.97	4.95	4.99	4.89	5.83	5.75	5.76	5.75
Sweden	5.95	6.29	6.31	6.33	6.53	7.04	7.05	7.06
Switzerland	4.32	4.35	4.35	4.34	4.93	4.91	4.90	4.91
United Kingdom	6.85	7.75	7.46	7.46	7.61	8.39	8.35	8.36
Australia	5.25	5.22	5.25	5.25	7.50	7.75	7.75	7.75
South Africa	6.48	6.46	6.48	6.46	7.25	7.50	7.50	7.50
Japan	6.97	7.05	7.07	7.08	8.16	8.77	8.03	8.09
Canada	6.19	6.62	6.43	6.60	7.43	8.05	7.84	7.82
United States	5.14	5.33	5.18	5.24	5.90	6.47	6.21	6.25
INTERNATIONAL ISSUES								
<i>U.S. Companies</i>					<u>Sep.</u> <u>1967</u>	<u>June</u> <u>1968</u>	<u>Aug.</u> <u>1968</u>	<u>Sep.</u> <u>1968</u>
5-Year Dollar-Denominated Euro-Notes					6.06	7.56	6.75	6.61
10- to 20-Year Dollar-Denominated Euro-Bonds					6.47	7.57	7.16	7.07
10- to 20-Year DM-Denominated Euro-Bonds					6.34	6.39	6.34	6.22
10- to 20-Year SwF-Denominated Bonds					4.90	5.12	5.15	5.08
<i>European Companies</i>								
10- to 20-Year Dollar-Denominated Euro-Bonds					6.75	7.79	7.35	7.22
10- to 20-Year DM-Denominated Euro-Bonds					6.22	6.22	6.02	6.22
<i>Governments</i>								
10- to 20-Year Dollar-Denominated Euro-Bonds					6.59	7.61	7.11	7.01

* Explanation of rates and yields appears on pages viii and ix. Yields at or near the end of the month.

KEY TO INTEREST RATES AND BOND YIELDS
USED IN TABLES AND CHARTS

BELGIUM:

Day-to-Day Money Rate - call money.
3-Month Treasury Bills - 3-month Treasury certificates.
Other Money Market Rate - 4-month Fonds des Rentes certificates.
3-Month Bank Deposit Rates - special maximum rate for sizeable time deposits.
Bank Lending Rate to Prime Borrowers - prime overdraft rate.
Long-Term Government Bond Yields - Kredietbank 10-20 year government bond average yield net of withholding tax.
Corporate Bond Yields - Kredietbank 10-20 year private bond average yield net of withholding tax.
Stock Prices - Brussels Bourse Industrial Share Index.

FRANCE:

Day-to-Day Money Rate - call money against private paper.
3-Month Treasury Bills - 1-year Treasury bills.
Other Money Market Rate - rate for 3-month interbank money against private paper.
3-Month Bank Deposit Rates - 3-month time deposits.
Bank Lending Rate to Prime Borrowers - overdraft rate for prime borrowers, including a commission of 0.05% per month on highest debit balance during the month, which is equivalent to about 0.60% per annum.
Long-Term Government Bond Yields - INSEE tax-adjusted yield on 5% government perpetual bond.
Corporate Bond Yields - INSEE tax-adjusted average yield on outstanding private corporation bonds.
Stock Prices - Paris 52 Industrial Shares Index.

GERMANY:

Day-to-Day Money Rate - interbank call money.
3-Month Treasury Bills - effective yield on 60-90 day Treasury Bills applying to sales by German central bank.
Other Money Market Rate - 3-month interbank deposits.
3-Month Bank Deposit Rates - 3-month time deposits of large amounts.
Bank Lending Rate to Prime Borrowers - approximate effective approved overdraft rate for prime borrowers.
Long-Term Government Bond Yields - "FAZ" 7% public authority bond average.
Corporate Bond Yields - "FAZ" 6% industrial bond average.
Stock Prices - Herstatt Index.

ITALY:

Day-to-Day Money Rate - none available.
3-Month Treasury Bills - none available.
Other Money Market Rate - interbank deposits.
3-Month Bank Deposit Rates - 3-month time deposits of L.100 million or more. Higher rates may be negotiated for large deposits.
Bank Lending Rate to Prime Borrowers - unsecured overdraft rate, including a commission of 0.125% per quarter on the maximum amount outstanding for more than 10 days during the quarter, which is equivalent to about 0.50% per annum. Lower rates may be negotiated by prime borrowers.
Long-Term Government Bond Yields - 5% government perpetual bond.
Corporate Bond Yields - average yield on ten industrial bonds.
Stock Prices - "Il Sole" Industrial Index (Milan).

NETHERLANDS:

Day-to-Day Money Rate - open market call money in Amsterdam.
3-Month Treasury Bills - 3-month Treasury bill yields.
Other Money Market Rate - 3-month municipal loans.
3-Month Bank Deposit Rates - 3-month time deposits of large amounts.

NETHERLANDS (Continued):

Bank Lending Rate to Prime Borrowers - overdraft rate for prime borrowers.
Long-Term Government Bond Yields - C.B.S. average yield on nine 3% to 3 1/2% government bonds.
Corporate Bond Yields - C.B.S. average yield on three 4 1/2% to 4 3/4% private corporate bonds.
Stock Prices - A.N.P.-C.B.S. Industrial Index (Amsterdam).

DENMARK:

3-Month Bank Deposit Rates - time deposit of 3-month notice.
Bank Lending Rate to Prime Borrowers - lowest rate for commercial bank loans and advances.
Long-Term Government Bond Yields - 4 1/2% Government bond of 1997.
Long-Term Corporate Bond Yields - none available.

NORWAY:

3-Month Bank Deposit Rates - 3-month time deposits. Higher rates may be negotiated for 6-month or more time deposits of large amounts.
Bank Lending Rate to Prime Borrowers - overdraft rate, including a charge of 0.25% per quarter on the total line of credit.
Long-Term Government Bond Yields - 5% Government bond of 1996.
Long-Term Corporate Bond Yields - 5 3/4% Dalen Portland-Cement bond of 1969-84.

SWEDEN:

Day-to-Day Money Rate - none available.
3-Month Treasury Bills - yields on new issues of 3-month Treasury bills.
Other Money Market Rate - none available.
3-Month Bank Deposit Rates - deposits at 4-month notice.
Bank Lending Rate to Prime Borrowers - overdraft rate for prime borrowers, including a fee of 1% per annum on the total amount of credit authorized.
Long-Term Government Bond Yields - yields on 15-year government bonds.
Corporate Bond Yields - Central Statistical Bureau average yield on corporate industrial bonds.
Stock Prices - Stockholm Industrial Index.

SWITZERLAND:

Day-to-Day Money Rate - call money.
3-Month Treasury Bills - none available.
Other Money Market Rate - 3-month bank time deposit.
3-Month Bank Deposit Rates - 3-month time deposit.
Bank Lending Rate to Prime Borrowers - overdraft rate for prime borrowers, including a commission of 0.25% per quarter on the highest debit balance during the quarter, which is equivalent to about 1% per annum.
Long-Term Government Bond Yields - Swiss Confederation bond average.
Corporate Bond Yields - average of yields on outstanding bonds of four leading Swiss companies.
Stock Prices - Swiss Bank Corporation Index.

UNITED KINGDOM:

Day-to-Day Money Rate - day-to-day loans.
3-Month Treasury Bills - 91-day Treasury bills at tender.
Other Money Market Rate - 3-month local authority deposits.
3-Month Bank Deposit Rates - 3-month time deposits.
Bank Lending Rate to Prime Borrowers - unsecured overdraft rate for prime borrowers.
Medium-Term Government Bond Yields - 5% Exchequer Stock of 1976-78.

UNITED KINGDOM (Continued):

Long-Term Government Bond Yields - 2 1/2% Consols.
Corporate Bond Yields - "F.T."-Actuaries 20-year debentures and loans.
Stock Prices - "F.T."-Actuaries 500 Shares Index.

AUSTRALIA:

Day-to-Day Money Rate - approximate effective interest rate in the authorized short-term money market.
3-Month Treasury Bills - yields on new issues of Treasury notes.
Other Money Market Rate - 3-month prime finance company paper.
3-Month Bank Deposit Rates - 3-month time deposits.
Bank Lending Rate to Prime Borrowers - maximum overdraft rate. Rate for prime borrowers may be 0.25% to 0.75% lower.
Long-Term Government Bond Yields - 20-year government bonds.
Corporate Bond Yields - A.U.C. indicated long-term secured debentures.
Stock Prices - Sydney All Ordinaries Index.

SOUTH AFRICA:

Day-to-Day Money Rate - National Finance Corp. call money rate.
3-Month Treasury Bills - 3-month Treasury bills at tender.
Other Money Market Rate - 90-day bank acceptances.
3-Month Bank Deposit Rates - 3-month time deposits at merchant banks.
Bank Lending Rate to Prime Borrowers - minimum overdraft rate.
Long-Term Government Bond Yields - 6% Government bonds of 1985.
Corporate Bond Yields - an approximate yield based on average yields of long-term bonds of the semi-public ESCOM, plus 1/2%.
Stock Prices - Financial Mail Industrial Index (Johannesburg).

JAPAN:

Day-to-Day Money Rate - Tokyo call money, unconditional.
3-Month Treasury Bills - yield on 60- to 62-day non-interest bearing discount government bills.
Other Money Market Rate - average yield on 1-year discount bank debentures, computed by Bank of Japan.
3-Month Deposit Rates - 3-month time deposits.
Bank Lending Rate to Prime Borrowers - average rates on loans and discounts of city banks, computed by Bank of Japan. In addition, compensating balances may be required.
Long-Term Government Bond Yields - yield on 6 1/2% National Government Bond of February 1973.
Corporate Bond Yields - average of yields on outstanding NT&T interest-bearing debentures.
Stock Prices - Dow Jones Industrial Average (Tokyo).

CANADA:

Day-to-Day Money Rate - chartered banks' day-to-day loans.
3-Month Treasury Bills - 3-month Treasury bills at tender.
Other Money Market Rate - 3-month prime finance company paper.
3-Month Bank Deposit Rates - 3-month time deposits.
Bank Lending Rate to Prime Borrowers - prime rate. In addition, compensating balances are sometimes required.

CANADA (Continued):

Long-Term Government Bond Yields - Bank of Canada average, yield on all direct government bonds 10 years or over.
Corporate Bond Yields - McLeod, Young, Weir average yield on ten industrial bonds.
Stock Prices - Toronto Stock Exchange Industrials Index.

UNITED STATES:

Day-to-Day Money Rate - effective federal funds rate.
3-Month Treasury Bills - 3-month Treasury bills.
Other Money Market Rate - 3-month prime finance company paper.
3-Month Bank Deposit Rates - 3-month negotiable certificates of deposit issued by Morgan Guaranty Trust Company.
Bank Lending Rate to Prime Borrowers - minimum short-term commercial loan rate of Morgan Guaranty Trust Company. In addition, compensating balances are required.
Long-Term Government Bond Yields - Morgan Guaranty 20-year U.S. Government Bond Index.
Corporate Bond Yields - Moody's Aa Corporate Bond Index.
Stock Prices - Standard and Poor 425 Industrials Index.

EURO-DOLLARS (Short-Term):

Day-to-Day Money Rate - prime banks' bid rates for Euro-dollar call money in London.
Other Money Market Rate - prime banks' bid rates for 3-month Euro-dollar deposits in London.
3-Month Bank Deposit Rate - prime banks' bid rates for 3-month Euro-dollar deposits in London.
Bank Lending Rate to Prime Borrowers - representative average rate for short-term Euro-dollar loans to prime borrowers.

INTERNATIONAL BOND YIELDS:

Dollar-Denominated Euro-Notes of U.S. Companies - average of yields on the ten most recent, outstanding 5-year dollar-denominated Euro-notes of prime, well-known U.S. companies.
Dollar-Denominated Euro-Bonds of U.S. Companies - average of yields on the ten most recent, outstanding 10- to 20-year dollar-denominated Euro-bonds of prime, well-known U.S. companies.
Deutsche Mark-Denominated Euro-Bonds of U.S. Companies - average of yields on the ten most recent, outstanding 10- to 20-year DM-denominated Euro-bonds of prime, well-known U.S. companies.
Swiss Franc-Denominated Bonds of U.S. Companies - average of yields on ten outstanding SwF-denominated bonds of prime, well-known U.S. companies.
Dollar-Denominated Euro-Bonds of European Companies - average of yields on the ten most recent, outstanding 10- to 20-year dollar-denominated Euro-bonds of prime, well-known European companies.
Deutsche Mark-Denominated Euro-Bonds of European Companies - average of yields on the five most recent, outstanding 10- to 20-year DM-denominated Euro-bonds of prime, well-known European companies.
Dollar-Denominated Euro-Bonds of Governments - average of yields on the most recent, outstanding 10- to 20-year government or government-guaranteed dollar-denominated Euro-bonds of Australia, Denmark, Italy, New Zealand, Norway and Sweden.

NEW ISSUES OF INTERNATIONAL BONDS*
(in millions of U.S. dollars).

	1965	1966	1967	Jan. - Oct. 1967	1968 ^p
<i>EURO-BONDS: TOTAL</i>	956	1,140	1,934	1,678	2,977
<i>By Category of Borrower</i>					
U.S. Companies	358	454	527	405	1,801
Other Companies 1/	345	467	994	875	756
Governments 2/	189	118	293	278	395
International Institutions	64	101	120	120	25
<i>By Currency of Denomination</i>					
U.S. dollar	690	898	1,722	1,493	2,222
German mark	202	146	161	146	664
Other 3/	64	96	51	39	91
<i>By Type of Security</i>					
Long-Term Straight Debt	786	700	1,414	1,267	945
Five-Year Notes (or less)	60	243	260	248	295
Convertibles 4/	110	197	260	163	1,737
<i>FOREIGN BONDS: TOTAL</i>	379	339	370	278	1,024
<i>By Category of Borrower</i>					
U.S. Companies	10	24	48	48	176
Other Companies 1/	171	77	65	45	71
Governments 2/	65	56	143	101	318
International Institutions	133	182	114	84	459
<i>By Currency of Borrower</i>					
Belgian franc	12	10	21	15	15
French franc	25	41	41	41	-
German mark	123	-	10	10	693
Italian lira	24	139	24	-	48
Dutch guilder	77	-	-	-	30
Swedish kronor	-	-	20	20	20
Swiss franc	78	93	152	132	206
British pound	40	56	102	60	12
<i>By Type of Security</i>					
Long-Term Straight Debt	369	339	345	253	901
Five-Year Notes (or less)	-	-	25	25	123
Convertibles	10	-	-	-	-

* Data include all publicly announced issues, whether publicly or privately placed.

p Preliminary.

1/ Includes public agencies and state enterprises as well as private companies.

2/ Includes national and local governments.

3/ Includes Unit-of-Account and £/DM option issues, plus two French franc issues, one in 1967 and one in 1968.

4/ Includes issues with warrants.

Note: An international bond issue is underwritten and offered outside the country of the borrower. A foreign bond issue is underwritten and offered for a foreign borrower principally in a single national market and denominated in the currency of that market. A Euro-bond issue is underwritten and offered for a foreign borrower principally in markets other than the market of the currency in which the issue is denominated.

NEW INTERNATIONAL BOND ISSUES[§]

Issuer	Guarantor	Principal amount in millions (\$ equiv.)	Coupon rate*	Maturity (years)	Offering price (yield)*	Earliest call date (earliest call price)	Conversion date (premium)*
SEPTEMBER 1968							
<i>U.S. COMPANIES</i>							
Transocean Gulf Oil Company	Gulf Oil Corporation	DM 200 (\$50)	6 1/2%	1983 (15)	99 1/2 (6.56%)	1 Sep 75 (101)	
Utah International Finance Corporation	Utah Construction and Mining Company	\$30	5 3/4%*	1983 (15)	100 (5.67%)*	15 Sep 73 (105 3/4)	1 Apr 69 (8.8%)
GATX Overseas Finance Corporation#	General American Transportation Corporation	DM 40 (\$10)	7%	1978 (10)			
<i>OTHER COMPANIES</i>							
Outokumpu Oy (Finland)	Central Bank of Finland	DM 40 (\$10)	7%	1978 (10)	99 1/2 (7.07%)	Noncallable	
Tauernkraftwerke AG (Austria)	Republic of Austria	DM 60 (\$15)	6 1/2%	1983 (15)	99 1/4 (6.58%)	1 Sep 78 (101 1/2)	
Burmah Oil Company, Limited (United Kingdom)		\$70	5 1/2%	1988 (20)	100 (5.50%)	1 Oct 78** (102 1/2)	1 Apr 70† (0.7%)
Mortgage Bank of Denmark		DM 70 (\$17.5)	6 3/4%	1980 (12)	98 1/2 (6.94%)	Noncallable	
Charter Consolidated Overseas N.V. (United Kingdom)	Charter Consolidated Limited	DM 120 (\$30)	6 1/2%	1983 (15)	99 3/4 (6.54%)	1 Oct 72 (104)	
Oy Stockmann AB (Finland)	AB Nordiska Foreningsbanken	SwF 7 (\$1.6)	6%*	1978 (10)	100 (5.91%)*	10 Oct 76	
<i>GOVERNMENTS</i>							
Government of Japan		SwF 60 (\$13.7)	5 1/2%*	1983 (15)	99 (5.53%)*	10 Oct 78 (100)	
Argentine Republic		DM 100 (\$25)	7%	1978 (10)	97 1/4 (7.40%)	1 Oct 71 (101 1/2)	
Province of Quebec#		DM 120 (\$30)		1975 (7)	(6.93%)		

§ Publicly announced issues, whether publicly offered or privately placed, outside the United States.

* Coupon interest is payable semiannually unless followed by an asterisk (*) which indicates an annual coupon. Annual coupons are discounted semiannually for comparability.

+ Conversion price premium over closing price of common stock on day preceding offering.

Private placement.

** Noncallable until this date unless 75% or more of the principal amount has been converted.

† Convertible into common stock of Shell Transport and Trading Company Ltd. (U.K.).

Issuer	Guarantor	Principal amount in millions (\$ equiv.)	Coupon rate*	Maturity (years)	Offering price (yield)*	Earliest call date (earliest call price)	Conversion date (premium)+
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SEPTEMBER 1968 (Continued)

GOVERNMENTS (Continued)

Commonwealth of Australia #		DM 200 (\$50)	6 1/4%	1974 (6)	99 1/2 (6.35%)		
Kingdom of Denmark #		DM 150 (\$37.5)	6 1/2%*	1980 (12)	100 (6.40%)*		

INTERNATIONAL AND REGIONAL ORGANIZATIONS

Inter-American Development Bank		SwF 60 (\$13.7)	5 1/2%*	1983 (15)	99 (5.53%)*	30 Sep 78 (100)	
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OCTOBER - NOVEMBER 1968

U.S. COMPANIES

Teledyne International N.V.	Teledyne, Inc.	\$37.5	6 1/2%*	1983 (15)	100 (6.40%)*	1 Oct 73 (105)	Detachable Warrants
Teledyne International N.V.	Teledyne, Inc.	\$12.5	7%*	1973 (5)	98 1/2 (7.24%)*	1 Oct 68 (100 1/2)	
Marathon International Finance Company #	Marathon Oil Company	DM 140 (\$35)	6 1/2%*	1975 (7)	100 (6.40%)*		
General Electric Company		SwF 60 (\$13.7)	5 1/2%*	1983 (15)	100 (5.43%)*		
Occidental Overseas Capital Corporation	Occidental Petroleum Company	DM 150 (\$37.5)	6 1/2%	1983 (15)	98 1/2 (6.66%)	1 Oct 72 (104)	
General Mills Finance N.V.	General Mills, Inc.	\$20	7%	1980 (12)			
Iroquois Industries #		\$5.25	6 7/8%	1978 (10)			Convertible
Ward Foods Overseas Capital Corporation N.V.	Ward Foods Inc.	\$15	5 3/4%	1988 (20)	100 (5.75%)		1 Jun 69
Transocean Gulf Oil Company	Gulf Oil Corporation	\$40	7%*	1980 (12)			
Cassa per il Mezzogiorno (Italy)	Republic of Italy	\$25	6 3/4%	1983 (15)	98 1/4 (6.94%)		

* Coupon interest is payable semiannually unless followed by an asterisk (*) which indicates an annual coupon. Annual coupons are discounted semiannually for comparability.

+ Conversion price premium over closing price of common stock on day preceding offering.

Private placement.

<i>Issuer</i>	<i>Guarantor</i>	<i>Principal amount in millions (\$ equiv.)</i>	<i>Coupon rate*</i>	<i>Maturity (years)</i>	<i>Offering price (yield)*</i>	<i>Earliest call date (earliest call price)</i>	<i>Conversion date (premium)+</i>
OCTOBER - NOVEMBER 1968 (Continued)							
<i>OTHER COMPANIES (Continued)</i>							
Electricity Supply Commission - ESCOM (South Africa)		DM 100 (\$25)	6 1/2%*	1983 (15)			
The Reed Paper Group, Ltd. (United Kingdom)		EUA 12 (\$12)	6 3/4%	1983 (15)	98 1/2 (6.92%)		
Nippon Petrochemicals Company, Limited (Japan)	Mitsui Bank	\$10	7 1/2%	1973 (5)		15 Oct 71 (100 1/2)	
Societe Nationale des Chemins de Fer Francais - SNCF (France)	Republic of France	DM 120 (\$30)	6 1/2%*	1983 (15)	99 1/2 (6.46%)*	1 Oct 72 (100)	
Ente Nazionale Idrocarburi - ENI (Italy)		\$20	6 3/4%	1988 (20)			
Industrial Mortgage Bank of Finland, Limited	Republic of Finland	DM 60 (\$15)	6 3/4%	1980 (12)			
Mitsui and Company (Japan)		\$20		1981 (13)			Convertible
Honda Motor Corporation (Japan)		\$15-20					
Kansai Electric Power Company, Inc. (Japan)		DM 50-100 (\$12.5-\$25)					
<i>GOVERNMENTS</i>							
United Mexican States		SwF 50 (\$11.4)	6%*	1983 (15)	99 (6.01%)*	31 Oct 77 (103)	
Commonwealth of Australia		SwF 60 (\$13.7)					
Republic of Venezuela		DM 100 (\$25)	6 3/4%	1983 (15)		1973	
Kingdom of Denmark		SKr 55.6 (\$10.7)		1988 (20)			
<i>INTERNATIONAL AND REGIONAL ORGANIZATIONS</i>							
European Coal and Steel Community		LIT 15,000 (\$24)	6%	1988 (20)	97 1/2 (6.23%)		

* Coupon interest is payable semiannually unless followed by an asterisk (*) which indicates an annual coupon. Annual coupons are discounted semiannually for comparability.
+ Conversion price premium over closing price of common stock on day preceding offering.

U.S. \$ billion

U.S.	39.8
Germany	4.1
U.K.	3.0
France	1.7
Canada	2.9
Switzerland	0.9
Total	<u>52.4</u>
Others about	<u>12,-</u>
Total	64.4

Outline of a Memorandum on
The Bank's Position in Capital Markets

General

1. The Bank has an established 20-year record of sound and well-conceived operations. Although the Bank has always recognized its major responsibility as a development finance institution, it has not compromised on the high standards required by it from the borrowing countries.

2. The Bank would continue to insist on high standards of creditworthiness and performance of its creditor countries, as well as of the particular projects and programs it finances. The Bank's future lending program which indicates doubling of operations is based on a careful country-by-country evaluation which has taken into account the creditworthiness, economic and financial policies and project availability prospects of the major developing countries.

Financial Position and Strength

3. The Bank has a paid-in capital of \$2,300 million^{1/} at the end of 1968. In addition, it has a "special reserve" of \$291 million, which has been accumulated from commissions received ~~and set aside~~. According to the Articles of Agreement the Special Reserve is to be held in liquid form and to be used only for the purpose of meeting liabilities of the Bank on its borrowing (bonds sold) and guarantees.

^{1/} Following figures are an approximation for December 1968. Exact figures would have to be used when available.

4. In addition to the above, the Bank has a Supplemental Reserve of over \$900 million, accumulated from retained earnings against losses on loans and guarantees and from currency devaluations. Altogether the Bank has a paid-up capital and reserve position of about \$3,500 million.

5. Although the present financial strength of the Bank rests mainly on the above amount of paid-in capital and reserves, it has also Capital subscribed but not called of \$20.6 billion, which forms a guarantee of all major governments to holders of Bank bonds and obligations. This includes not only the guarantee of the U.S. Government, but also of several other governments, the financial position of which is considered very strong in international financial markets. The uncalled capital is considered by the Bank only as a guarantee to be used as a last resort. The prospective operations of the Bank do not indicate any need to call on this part of the subscribed capital.

Future Earnings

6. The Bank has a consistent record of high net earnings, as follows:

FY 1962	\$98 million
1963	113 "
1964	131 "
1965	138 "
1966	140 "
1967	170 "
1968	147 "

On the basis of conservative projections, net earnings are expected to amount on about an annual level of \$170 million in the next five years. The Bank expects to retain up to half (check) of such earnings, in order to strengthen its Supplemental Reserve.

7. The present Bank's lending rate is 6.5 percent, which is higher than the average rate of borrowing by the Bank (6.38 percent in the second half of 1968). The Bank keeps its lending rate under continuous review, and will continue to make it compatible with interest rate levels prevailing in capital markets. Should there be a need to raise the lending rate in view of trends in capital markets, the Bank will not hesitate to do so.

8. The following are some ratios frequently used to test the financial prudence of an institution:

- (1) Ratio of income available to pay Interest on Debt to Interest Requirements
- (2) Net Income as percentage of average available Capital and Reserves
- (3) Reserves as percentage of Receivables from Loans
- (4) Reserves as percentage of Funded Debt

Past data on above ratios are available, and some projections have been made, which of course depend on assumptions used. If these ratios are to be used, the projections would have to be updated.

Markets for Bank Bonds and Sale of Loan Participations

9. The Bank has been able to enter new sections of the capital markets, such as the mortgage banks in Germany. About central banks are investing in medium-term Bank bonds, as part of their relatively liquid holdings. Thus the market for Bank bonds has become more widely based and diversified.

*10. The Bank has made sales of loans out of portfolio, an important source of financing and will continue to do so, adjusting the yield to market conditions. (Data should be added).

Creditworthiness of Borrowers from the Bank

11. In addition to the Bank's own capital and reserve position, the Bank's financial position rests on the creditworthiness of its borrowers. The Bank continues to be selective and cautious with respect to their creditworthiness of its borrowers. The Bank continues to be selective and cautious with respect to their creditworthiness. Some member countries have been made ineligible for Bank or IDA lendings, on grounds of inadequate economic and financial policies. A number of countries whose performance is reasonably adequate but who face long-term balance of payments difficulties are eligible only for IDA credits, not for Bank lending. Only those countries which have adequate policies combined with creditworthiness and ability to prepare and execute good projects receive Bank loans.
12. The creditworthiness of the Bank-eligible countries has continuously increased, as shown by the growth of their exports. (Figures of export growth of above countries will be calculated.) The Bank has actively encouraged diversification of exports in countries depending upon a small number of commodities which face marketing problems. The Bank does not generally finance expansion of productive capacity of "surplus commodities" in international markets (e.g. coffee, sugar).
13. The use of suppliers' credits and other shorter term debt which caused debt crises in some developing countries has been curtailed, by mutual agreement of such countries with the IMF and the Bank (check if data are available for such credits in External Debt section).

Bank's Sectoral Lending Policies

14. The Bank's emphasis on expansion of lending for agriculture and even education (the latter will in fact be financed mostly by IDA credits not Bank loans) would not weaken the financial and economic strength of its investments. This policy is based upon the long-term experience of the Bank which clearly indicates the past weaknesses of LDC in provision of their food requirements. Agricultural credits are carefully scrutinized to secure adequate financial and economic returns. They will also help reduce the balance of payments gap of LDC, by savings on their large food import bill (altogether over \$4 billion annually). Loans for education help increase the skill potential of LDC, which has proven to be one of the major bottlenecks, and are therefore as "productive" as loans for equipment.

Subjects for Future Work

Credit Rating of Borrowing Countries

21. Methods might be sought for credit rating of countries borrowing from the Bank to indicate whether the composite credit rating of the Bank's portfolio is likely to be lowered, especially as remaining credits of European countries, Australia, Japan, and similar high-rated countries will be repaid. Such data must be strictly confidential, but might serve as an internal indicator.

Bank's Lending Rate

22. The effects of the present lending rate (6.5%) on the Bank's position in capital markets should be reviewed.

Bank Guarantees

23. Ways and means to convince U.S. bonds investors of the value of non-U.S. Government guarantees should be explored.

Image of the Bank

24. Further thought ought to be given as to proper means to strengthen the public "image" of the Bank. The main challenge would be to convince the financial community that imaginative and innovating lending policies (e.g., agricultural, education, and population control loans; program loans) can be consistent with financial strength.