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The World Bank
1818 H Street NW
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Telephone: 202-473-1000
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President G.D. Woods Briefs - 18th Annual Meeting
S. Asia & Middle East

1963

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Annual Meeting briefing papers, 1963 - South Asia and Middle East - Briefing papers

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT
ASSOCIATION

INTERNATIONAL FINANCE
CORPORATION

OFFICE OF THE PRESIDENT

SOUTH ASIA AND MIDDLE EAST

INDEX - G. D. WOODS'S MEETINGS

India	Sat., 9/28	- 3:00 pm	(ABC-IFC)	1 hour
Iran	Thurs., 10/3	- 9:20 am	(AB)	20 min
Israel	Tues., 10/1	- 4:40 pm	(AC)	20 min
Pakistan	Tues., 10/8	- 10:00 am	(ABC) (IFC)	Indef.
U.A.R.	Sat., 9/28	^{12:00} 12:00 noon	-(AB)	1 hour
		or 11:00 am(2)		

B. Schmitt
9/19/63

AFGHANISTAN

~~CONFIDENTIAL~~ **DECLASSIFIED**

MAY 16 2017

WBG ARCHIVES

AFGHANISTAN

BRIEFING PAPER

I. MEETING WITH DELEGATION

Thursday, October 3

3:00 p.m. for 20 minutes

Attended by: Mr. Wilson
Mr. Rosen

Mr. Reid
Mr. Brakel

II. MEMBERS OF DELEGATION

Abdul Hai Aziz

Deputy Minister of Planning

Foruk Achekzai

Director, Da Afghanistan Bank

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

(a) State of relations (irrigation and education credits in prospect; development bank studied)

Afghanistan joined the Bank in 1955 but has not been considered creditworthy for lending--a view which was never accepted by the Afghan authorities. Over the years two officials have completed the EDI course and another has just completed the trainee program. Afghanistan joined IDA in February 1961 as a Part II country. A mission which visited the country in November/December 1961 recommended that IDA should try to assist Afghanistan's economic development by investing in high priority sectors, such as agriculture and education. Accordingly, the Bank offered to help work out a project that would improve irrigation in the lower Kunduz-Khanabad river basin and to consider financing a project in education. Missions in connection with these proposals visited Afghanistan late in 1962.

Regarding Kunduz-Khanabad it was agreed that the Bank would consider paying the foreign exchange cost of a technical assistance study which would prepare a detailed project suitable for IDA financing. The terms of this contract for which the Bank selected SOGREAH as consultant, are still being discussed with the Government. (A separate memo is attached to summarize the current status of these discussions.)

In 1962 a UNESCO mission recommended an education program for IDA financing. Its recommendations were reviewed by the Bank mission which visited Afghanistan in November 1962. In August 1963 the Staff Loan Committee accepted the Area Department's recommendations that IDA seek to work out a project, of the order of \$4 million, consisting of (i) a regional education program for the lower Kunduz-Khanabad river basin, including the construction and equipping of a technical school, a teachers' training school, an agricultural school and possibly a commercial school, and (ii) a center in Kabul to train staff for teachers' training schools throughout the country. IDA would be willing to finance the foreign exchange costs, or up to 3/4 of the total cost, of such a project and to send a mission to work out details of the project. It is expected that this mission could be in the field after the Annual Meeting.

At the Government's request an IFC mission visited Kabul in July 1963 to appraise the prospects for an institution to finance private, industrial development. At present IFC has the mission's preliminary report under consideration. (A separate memo is attached regarding this proposal.)

(b) Topics likely to be raised by delegation

(i) Since the education project is proposed for a location close to the main area of Russian influence, the delegation may suggest an alternative site. Management should respond that this change would require a complete review of the project but will be considered if the Government insists. The delegation may also press for a larger project than IDA has proposed. The response should be that the proposed project is in line with the availability of IDA resources; furthermore, administrative

problems are likely to be so great that it seems prudent to begin with a modest first project and to expand later in other parts of the country on the basis of that experience.

(ii) The delegation will probably also wish to discuss Bank/IFC views on the proposed industrial financing institution and the Kunduz-Khanabad study. (See memos attached.)

(iii) In previous discussions the Government has proposed 100 percent financing of project costs. Management may wish to point out that IDA policy does not allow the full amount of project expenditures to be covered, and that the Afghan Government will be expected to contribute a reasonable share of the cost of any projects submitted to the Association. However, the Afghan Government should be commended for recent efforts to balance the budget, and we should show an awareness of the difficulty of raising local currency resources for investment purposes.

(c) Topics to be raised by Management

(i) Management will want to report on progress with the SOGREAH contract, the education project and/or the development bank if any one of these topics is not raised first by the delegation.

(ii) Management may wish to inquire how the new border agreement with Pakistan is working and to learn if there are still problems in connection with the flow of traffic across that border.

IV. BACKGROUND INFORMATION

(a) Bank loans

None.

(b) IDA credits

None.

(c) 18% capital subscription

No release. The Area Department will suggest that Afghanistan release its subscription by stages over a reasonable period of time.

(d) Holdings of World Bank bonds

None.

(e) I.F.C.

Member. Subscription \$111,000. An institution to finance private industrial development is under study.

(f) I.D.A.

Part II member.

V. POLITICAL SITUATION

A major change in the Government took place in spring 1963. The two leading political figures of the last ten years, both cousins of the King, Sardar M. Daud (Prime Minister) and Prince Naim (Minister of Foreign Affairs) retired. A new and younger cabinet, composed of people outside the royal family, is believed to represent a step towards a more liberal regime in the country, both in politics and in economic affairs. Diplomatic relations have been re-established with Pakistan, and an agreement was reached for reopening the Pakistani border, which had been closed for almost two years. After some initial difficulties, trade from Karachi through the Khyber Pass is said to be flowing again. The new Government is maintaining a lively interest in development, particularly in stimulating private industrial investment.

VI. ECONOMIC SITUATION

<u>Population</u> (1963 estimate)	8-10 million (some estimates are considerably higher), said to be growing very slowly
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Per capita GNP (approximate)	\$100
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A serious effort to develop the Afghan economy was started only in 1956 with the launching of the First Five-Year Plan. Although it was only a hastily put together aggregation of project-ideas, the plan has succeeded in building some of the infrastructure needed for economic development. Production of some basic industries like cement, power and coal, although still quite limited in absolute amount, has increased substantially. The capacity of the textile industry has more than doubled and production has increased by over one-third. Agricultural production has fluctuated over the years, and although no reliable estimate is available, it seems that cash crops (particularly cotton) have reacted favourably to price changes introduced during the last growing season. Fruit production, which is an important source of exports, has also grown substantially.

The Second Five-Year Plan was officially launched in 1962 but is undergoing a radical revision, due to the foreign exchange and fiscal reform undertaken early this year.

The main highlight of the Afghan economy in 1963 has been the reform of the foreign exchange and budgetary system, which took place in March. A new par value of the Afghani has been accepted by the IMF; the multiple exchange system has been reduced to a two rate system with the free market rate kept near the official exchange rate (for Government transactions) by means of open market operations. It is believed that the currency reform, and the new fiscal measures that were adopted in connection with it, will greatly benefit the export sector of the economy. Reports coming from Kabul indicate that some of these benefits are already materializing. Meanwhile,

the external free market value of the Afghani has been fairly stable in the first six months since the currency reform. The 1964 budget, approved by the parliament in July, is drafted according to principles of sound monetary management agreed upon between the IMF and the Government. Accordingly, the large deficit of the previous year's budget has been cut by two-thirds. This will have repercussions on the level of development expenditures over the next fiscal year and will make the shortage of local currency resources available for investment even more acute.

Attachments (to be added):

Memos on Kunduz-Khanabad irrigation study and the proposed industrial financing institution.

DWJeffries/WBrakel/GVotaw/wh
September 16, 1963

SEP 27

AFGHANISTAN: DEVELOPMENT FINANCE INSTITUTION

(To be attached to Briefing Paper on Afghanistan)

In May 1963, the Government of Afghanistan approached IBRD/IFC with a request for a mission to assist in the creation of a new industrial finance institution. The mission went to Kabul in July to appraise the need for industrial financing in the country and to recommend ways in which this need could be met.

The Government expects a report from us, with precise recommendations as to the way in which a new development corporation should be set up. Although no mention was ever made of an IFC investment, the Government obviously hopes to receive IFC assistance in raising the foreign component of the equity and quasi-equity and may also be interested in a Bank loan.

The first draft report contained a precise proposal for the creation of a development finance corporation with a mixture of Government and private capital, but under private control. This draft is now being revised to reflect the marginal character of this proposal and to add another alternative, in case the necessary amounts of equity and quasi-equity should prove impossible to raise. It can be put in final form very soon after next week's discussion with the Afghan delegation.

Mr. Aziz, the main driving force behind the proposal for a development corporation in Afghanistan, has recently resigned his post as Minister of Planning. In spite of his resignation, he will attend the Annual Meeting and will, in all likelihood, expect to know what our present thinking is. (See previous paragraph).

INDIA

INDIA

BRIEFING PAPER

I. MEETING WITH DELEGATION

Saturday, September 28

3:00 p.m. for one hour

Attended by:	Mr. Woods	Mr. Reid
	Mr. Knapp	Mr. Stevenson
	Mr. Wilson	Mr. Wright
	Mr. Rosen	Mr. Jeffries
		Mr. Pollan

II. MEMBERS OF DELEGATION

L.K. Jha	Alternate Governor (IBRD) Secretary, Ministry of Finance
P.C. Bhattacharyya	Alternate Governor (IMF) Governor, Reserve Bank of India
K.B. Lall	Temporary Alternate Governor (IBRD) Ambassador of India to Belgium
J.J. Anjaria	Adviser Executive Director, (IMF)
K.S. Sundara Rajan	Adviser Executive Director (IBRD)
S.L.N. Simha	Adviser Alternate Executive Director (IMF)
A.K. Ghosh	Adviser Alternate Executive Director (IBRD)
Miss P.S. Mirza	Adviser
A.U. Ratwani	Adviser

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

(a) State of relations

Since August 1949 thirty-one loans have been approved with a total value (net of cancellations) of nearly \$850 million, or 12 percent of the Bank total. In the course of the last two and a half years 13 IDA credits have been approved for India, totaling \$300 million or 55 percent of all IDA commitments. In 1958, responding to the Bank's initiative, countries interested in providing financial assistance to India's development program formed a consortium, which now includes ten member countries. At its most recent meeting, August 7, the consortium pledged \$1,052 million for the year ending March 31, 1964, bringing the three-year total to \$3,417 million. In the current year the Bank has pledged \$105 million and IDA \$140 million, bringing total Bank/IDA pledges for the three year period to \$695 million.

Relations between the Bank and India are close; because of the very large role which consortium financing plays in Indian development planning, the Bank has been obliged to study and offer detailed comments on many aspects of the economic situation in India. In some fields (e.g., price policy, export promotion, agricultural development, and the organization of planning) changes in policy are overdue but likely to come about only gradually.

Projects now under active consideration for Bank/IDA financing are listed below, roughly in the order that negotiations are expected and with very tentative estimates of the size of loan or credit:

	(\$ Million)	
Tata Iron and Steel Co.	25	Bank
Kothagudem fertilizer	16-18	Bank
Commercial vehicle production, equipment for capital producing industries, and construction equipment	Up to 90	IDA
Railways	50-60	Bank or IDA
Telecommunications	30-35	Bank or IDA
Indian Iron and Steel Co.	12.6	Bank
Tata coal project	20-25	Bank
Kothagudem power (stage II)	15	Bank or IDA
Calcutta water supply	8-10	IDA
Bangalore water supply	15	IDA
Parambikulam irrigation	25-30	IDA

Not all of these projects are expected to be ready for negotiation during the Indian fiscal year ending March 31, 1964, and the list therefore includes some to be carried forward toward next year's lending program.

In addition to the Bank's 1963/64 pledge of \$105 million there is a carry-over of \$25 million from sums pledged in previous years; it is proposed that new loan agreements with TISCO, Kothagudem Fertilizer, and for the Railway and the Post and Telegraphs Department would make up the required total. With respect to the \$140 million pledged from IDA, \$50 million has already been committed in railway and power agreements signed last spring; the \$90 million balance is expected to come mainly from the equipment credits for commercial vehicle production, industrial machinery and construction equipment.

In addition to these commitments within the framework of the consortium, the Bank expects to make a loan of \$23 million for the Beas irrigation and power project as part of the Indus settlement. This loan, to cover the cost of equipment, will be presented to the Board as soon as A.I.D. is ready to go ahead with its share of the project. A final decision is expected from A.I.D. by November, or as soon as the Agency receives a project analysis from the Bureau of Reclamation, which is reported to be very favorable.

The Bank has cooperated with the Government of India in a number of economic studies. A technical assistance grant of \$750,000 represents a major share of the cost of a Coal Transport Study, from which final recommendations are expected this winter. A more modest grant is assisting in the study of sites and the preparation of designs for a second crossing of the Hooghly River in Calcutta. In October the Bank's own staff will initiate a study of the potential for exports of iron ore, in order to help design an investment program to exploit that potential. The Bank's Delhi office is looking into pricing and marketing policies for oil seeds, cotton and other agricultural commodities. The idea of the Bank financing a technical assistance study of coastal shipping and minor ports has been discussed with the Government, and we are awaiting a request to proceed.

(b) Topics likely to be raised by delegation

(i) The next meeting of the consortium was discussed briefly in an exchange of letters between Management and the then Minister of Finance last June and July. (Copies are attached.) In the past the Government of India has usually favored an early (i.e. winter) meeting, so that foreign aid pledges would be known in advance of its budget presentation to Parliament in late February; in practice, however, aid pledges have never been finally settled before the summer. For next year (the fourth year of the Plan) it has been proposed that two meetings be held in December 1963 and January 1964. This was accepted by the former Finance Minister but we have subsequently had indications at the official level that the Indians may prefer somewhat later dates, e.g. January for the first meeting and February for the second. If postponement is suggested, Management

will want time to consider the suggestion in consultation with other principal consortium members. In proposing winter meetings this year the Bank stated two major conditions: (a) that there be significant progress to report with respect to some of the major concerns of consortium members (e.g. investment planning, export promotion, encouragement to private foreign investment, relaxation of controls, pricing policies, higher interest rates, etc.) and (b) that the Government of India accept primary responsibility for preparing documents reporting progress in these same problem areas, outlining the investment program proposed for the next four or five years and analyzing the probable balance of payments situation for at least two years ahead. In the past the Government of India has not been responsible for such presentations and the April 30, 1963 meeting was the first instance that a Government representative (namely, Mr. L. K. Jha) appeared before consortium members to summarize the case for aid and to answer questions.

The Bank's conditions were accepted in the Finance Minister's reply, and he undertook to report on these preparations at the Annual Meeting. However, as a result of recent changes in the Indian Cabinet, preparations seem to have been delayed, and we have been informed that the new Minister of Finance, Mr. T. T. Krishnamachari, hopes to visit Washington late in October or in the first weeks of November after the relevant policy decisions have been taken in Delhi, and that he may prefer that consortium preparations be discussed at that time.

If the delegation is prepared to discuss the consortium time table, Management should emphasize the consensus among consortium members that it is necessary to look at economic prospects several years ahead, even though pledging is for a single year. Furthermore, the Indian Government has repeatedly stated that projects which were not taken up for financing by mid-1963 would lose their character as Third Plan projects; it follows that the next meeting of the consortium will be looking, albeit preliminarily, at the most obvious and urgent projects of the "Fourth Plan". It should be emphasized that investment programming in major sectors such as power, transport and industry ought to go forward decisively, even though other details of the Plan document are not yet approved for publication.

(ii) The delegation may wish to discuss more distant prospects for the consortium. Management could reply that the Bank is prepared to continue to convene and chair these meetings as long as there is a reasonable prospect of healthy development in the Indian economy and a need for coordinated Western assistance. Specifically, with respect to the Fourth Plan, it should be made clear that the proposed winter meeting of the consortium will already be considering 1966/71 projects in a preliminary way, as noted above. The need to get away from a rigid system of planning by five-year periods might also be discussed.

(iii) Improving the terms of aid is a constant concern of the Bank, and there may be hope of some further progress this year through DAC. On the other hand, the proviso attached to the foreign aid bill by the U.S. House of Representatives, which would raise the rate of interest on AID loans, is an inauspicious development. If the delegation broaches this subject, Management should re-emphasize its concern over India's debt servicing problem and assure the Government of our support in pressing for easier terms of aid.

(iv) Bank financing for public sector industrial projects may be requested, particularly in the case of the Gujarat State Fertilizer Company. Because the State Government, which is sponsoring the project, proposes to distribute 51 percent of the stock widely among private individuals, insurance companies and others, the Company is nominally in the private sector; nevertheless, a controlling interest and management responsibility seem to rest with the government of Gujarat as the project is now formulated. The Bank has not had occasion to study the project in any detail. If the issue arises, Management should take the opportunity to clarify Bank policy in this regard, since there is a general problem involved which may become more and more important in planning new operations in India. Emphasis should be given to the autonomy of management, technical proficiency and the economic viability of individual projects rather than the exact form of ownership.

(v) The delegation may request Bank assistance in conducting commodity studies to help India in promoting exports. Mention should be made of the iron ore export study, which the Delhi office is just getting under way. The Bank would be happy to consider this matter and will cooperate in such studies to the best of its ability.

(c) Topics to be raised by Management

(i) Consortium arrangements must be discussed as a follow-up to the exchange of letters, which is attached, and the subject offers a good bridge into other topics. If consortium plans are not mentioned by the delegation, Management should initiate discussion along the lines of III (b) (i) above.

(ii) One of the major points mentioned in Mr. Woods' letter of June 20, 1963, was the need to take more effective steps to attract private foreign investment. Management should ask the delegation if there is anything the Bank might do to assist India in her efforts to attract private capital from abroad.

(iii) Disbursements on projects in India are generally somewhat behind the implementation schedules agreed to by the Government at the time of appraisals. Similarly, commitment of consortium assistance (including Bank/IDA funds) often lags many months behind the pledges. This summer the Government appointed a committee of economists to study measures for speeding up the utilization of aid. Management may wish to ask what the Government proposes specifically with respect to Bank/IDA disbursements and also more generally with respect to the more rapid commitment of consortium pledges.

(iv) A decision on steel pricing is due shortly. Management should ask about the proposed steel price policy. The consultation also represents a good opportunity for Management to confirm that in principle the Bank is prepared to assist in financing two further expansions proposed for the private sector and would like to proceed with the development of these projects as quickly as possible. The two companies together would have estimated foreign exchange requirements of \$300-\$370 million; both plan one million ton expansions, but IISCO's would be in two stages of 300,000 tons and 700,000 tons, respectively.

(v) There is growing concern in the consortium - and also in India - that the Indian economy is more and more overburdened with controls and that these controls lead to distortions, temptations toward corruption, and the danger of choking off reasonable economic initiative. Management will wish to reiterate its misgivings with respect to these trends and to learn what steps are being taken - or studied - toward gradual decontrol.

IV. BACKGROUND INFORMATION

(a) Bank loans as of August 31, 1963

	Amount (equivalent in \$ million)
Total (net of cancellations and refundings)	847.4 ^{1/}
of which has been repaid	135.7
Total now outstanding	711.7
Amount sold	76.3
of which has been repaid	56.2
Net amount now held by Bank	20.1
	691.6

^{1/} Includes \$49.5 million ^{which became} not yet effective. on September 17, 1963.
Includes \$101.3 million not yet disbursed.

Loans signed since July 1, 1961

Date	Borrower	Purpose	Amount
			(equivalent in \$ million)
Aug. 9/61	India	Private coal mining development	35.0
Aug. 17/61	Calcutta Port	Port improvements (II)	21.0
Oct. 13/61	India	Railway improvements (VI)	50.0
Dec. 22/61	IISCO	Coal development and expansion	19.5 <u>2/</u>
Feb. 28/62	ICICI	Expansion of private industry	20.0
Jan. 5/63	ICICI	Expansion of private industry	30.0 <u>2/</u>

2/ ^{Became} ~~Not yet~~ effective. *September 17, 1963.*

(b) IDA credits as of August 31, 1963

Date	Purpose	Amount	
		(equiv. in \$ million) Approved	Disbursed
Jun. 21/61	Highway construction and improvement	60.0	19.3
Sep. 6/61	Tubewell irrigation	6.0	3.0
Nov. 22/61	Shetrunji irrigation	4.5	1.3
Nov. 22/61	Salandi irrigation	8.0	.8
Nov. 22/61	Punjab flood protection and drainage	10.0	5.8
Feb. 14/62	Durgapur power extension	18.5	.1
Jun. 29/62	Sone irrigation	15.0	1.9
Jul. 18/62	Purna irrigation	13.0	2.9
Aug. 8/62	Koyna power (II)	17.5	-
Sep. 14/62	Bombay port	18.0	2.6
Sep. 14/62	Telecommunications	42.0	2.5
Mar. 22/63	Railway improvements (VII)	67.5	20.7
May 24/63	Kothagudem power	20.0	-
Total		300.0 <u>1/</u>	61.0

1/ Whole amount effective. \$239.0 million not yet disbursed.

(c) 18% Capital Subscription (\$72.0 million)

Entire 18 percent is released: \$21.6 million convertible into any currency is already on loan; \$50.4 million for purchases in India. The Area Department will suggest that the Government do its best to see that Indian suppliers bid on Bank/IDA projects as a means of utilizing the unreleased portion.

(d) Holdings of World Bank bonds

None. However, India does hold \$5 million of Borrower's obligations, i.e. portions of Bank loans to India.

(e) I.F.C.

Member. Capital subscription \$4.4 million. IFC has invested a total of \$2.5 million in three projects; three more investments (with a total value of \$6.0 million) are scheduled for consideration by the Board in September. Two projects are under study (viz., Coromandel Fertilizers and Modern Mills).

(f) I.D.A.

Part II member. In a recent conversation with Mr. Knapp India's Executive Director indicated that the Government would be prepared to release some of its 90 percent (i.e. rupee) subscription for purchases in India of goods required by IDA-financed projects in other countries. The Treasurer has been instructed to seek opportunities to utilize rupee funds and thereby to test the Government's intention in this regard.

V. POLITICAL SITUATION

The President announced Cabinet changes on August 24. The changes went beyond what most observers had expected. In the reorganization Chief Ministers of six states and six members of the national cabinet resigned. Politically, the change has been interpreted by some as a means of balancing the loss of left-wingers Menon and Malaviya by ousting right-wingers Desai and Patel. The ostensible purpose of the Kamaraj thesis is that senior leaders of the Government should now devote themselves to strengthening the Congress Party; but there are some indications that most of the resignees will have much less influence out of office than in. The Party has suffered some by-election reverses but has shown surprising strength in other, less publicized contests. In any case three of the most conservative former ministers have been added to an expanded, seven-man Parliamentary Board of the Congress Party. Nehru, although showing wear and tear, remains the single most important power. The recent shake-up, however, has given increased standing, and apparently more influence on party and economic policies, to Krishnamachari, Subramaniam (the Steel Minister), and Kamaraj, all from Madras. They are not operating as a unified force; in fact, their respective zones of influence are now being staked out. The real crisis in the Party will occur only after Nehru's departure from the political scene. Meanwhile, the Government rather than the Party is the focus of most popular dissatisfaction, and measures so far taken offer only the promise of new vigor, rather than the renewal of leadership for which the country is waiting.

VI. ECONOMIC SITUATION

<u>Population</u> (1963 estimate)	460 million, growing at 2.4 percent per year
<u>Per capita GNP</u> (1961/62)	\$70
<u>Average annual growth</u>	
National income (constant prices, 1955/56 - 1961/62)	3.7 percent
National income per capita (1955/56 - 1961/62)	1.4 percent
Industrial production (1955-62)	7.1 percent
Agricultural production (1953/56-1959/62)	2.7 percent
Wholesale price index (1956/57-1962/63)	3.3 percent
Consumer price index (1956/57-1962/63)	3.5 percent
Exports (current prices, 1955/56 - 1962/63)	2.5 percent

The vast agricultural sector has remained stagnant in recent years and, as a result, farm production is likely to fall far below Plan targets. Dependence on imports, especially of foodgrains and cotton, seems likely to continue; meanwhile, in the last few months prices have risen sharply and even the official index records wholesale food prices more than 5 percent above year-ago levels. Industrial production is held back by shortages of spare parts and other imported materials, and the construction of new capacity in such critical sectors as fertilizers is two or more years behind schedule. The transport bottleneck seems to have disappeared but only temporarily. The depressed condition of the securities market is attributed to uncertainties of all sorts: e.g., the Chinese military threat, rumored Cabinet changes, disappointing pledges of Western aid, and shortages of electric power. Organized labor is said to have become particularly restless as a result of the compulsory deposit scheme (a disguised withholding tax) and sharp increases in excise duties initiated this spring; this restlessness will increase if consumer prices continue to rise. Some exports (in particular oilcake, vegetable oils, jute manufacturers, iron ore and tea) have increased, but others declined and foreign exchange reserves remain constant at what is considered a minimum level. The economy continues to grow at a more rapid pace than population, but the margin is narrow, and there would seem to be significant opportunities for improvement.

GVotaw/EPWright/bj
September 18, 1963

1st July 1963

Dear Mr. Woods,

Thank you very much for your letter of June 20, 1963. First of all, I would like to express my appreciation and gratitude to you and to the officers of the Bank for all that you have done to make the meetings of the India Consortium a success. I would further assure you that, as L.K. Jha said at the consortium meeting in Washington, we shall give full consideration to the suggestions made in the excellent Economic Report of the Peter Wright Mission, and to the views expressed at the consortium meeting to which you have referred.

2. We ourselves have been concerned for some time about the low rate of growth during the first two years of the Third Plan. In general, the increase in industrial production has not been unsatisfactory and the poor performance of the economy is mainly due to the absence of any significant increase in agricultural production. While this has something to do with weather conditions, we are well aware that a great deal has to be done, and done quickly, on the agricultural front. Just at the moment, I feel that there is need also to provide a stimulus to industrial activity in the private sector. While I think it would be a mistake to read too much meaning into the figures of national income for the last two years, there cannot be any difference of opinion regarding the essential point that the performance of the economy needs to be improved.

3. I do not, however, at this stage, wish to dwell on the steps we are taking, or the particular points raised in the Washington meeting of the consortium to which you have drawn my attention. We are, at present, engaged on the mid-term assessment of the Third Five-Year Plan and also taking this opportunity to review our policies and procedures. The acceptance by the leading members of the consortium of our plea, which has also had the full support of the Bank, that credits should not be tied to projects, should be of great help. I shall be writing to you further on the subject at a somewhat later stage and shall anyhow take the opportunity of a personal discussion with you when I go to Washington for the annual meeting of the Bank.

4. Meanwhile, I feel I should immediately let you know that we agree with the main points which you have made about what needs to be done before the consortium meets again. We fully share your view that planning is and must be a continuous process. The Plan which we formulate every five years covers a multitude of things, education, health, social services, problems of resource mobilisation and the allocation of resources and responsibilities between the Centre and the States. At the same time, we recognise the importance of continuous forward planning in certain spheres where, having regard to the long period of gestation, it is always desirable to be looking well ahead into the future. In fact, for quite some time now, we have been engaged in forward planning of power, transport, steel and certain other basic facilities and industries and a good deal of preliminary but detailed work has already been done. You may be aware that we have been discussing with the Bank some power projects to be financed out of the current year's Bank/IDA programme which are really intended to augment power supply in the early years of the Fourth Plan. It is indeed our hope that project assistance to be committed during the next two years would relate essentially to what might be called Fourth Plan projects.

5. We were somewhat unhappy about the reference during the recent consortium meetings to the original estimates of the requirements of external assistance during the Third Plan period and the suggestion that only a modest balance remains to be assured in relation to these estimates. Quite clearly, if advance preparation for the Fourth Plan is to take place on an adequate scale and if there is to be no break in the continuity of development, we must seek, from now on, assistance which would be carried over into the Fourth Plan, and the quantum of such assistance would have to be larger than what was available as a carry-over when the Third Plan began. This is particularly necessary, because most countries allocate funds not on the basis of disbursements, but on the basis of commitments.

6. I entirely agree with you about the timing of the next round of consortium meetings. They should be well ahead of the beginning of our next fiscal year in April 1964 and I would assure you that we would be ready to present the kind of data that you have asked for. I think our primary concern during the next round of consortium meetings, apart from covering the immediate requirements of non-project assistance, should be to seek commitments for fresh development in the basic sectors to which I have referred earlier, with the full knowledge that they would be completed after the Third Plan is over.

7. I hope that the July meeting would produce the results which you and your associates are working for. I am looking forward to seeing you and Mrs. Woods in your new home in Washington at the time of the annual meeting.

With kindest regards and best wishes,

Yours sincerely,

/s/ Morarji Desai

Mr. George D. Woods,
President,
International Bank for
Reconstruction and Development,
WASHINGTON 25 D.C. (U.S.A.)

June 20, 1963

The Honorable
Morarji R. Desai
Minister of Finance
Government of India
New Delhi, India

Dear Mr. Minister:

Following the meeting of the Indian consortium in Paris on June 4/5, I am writing to you about some of the points that were raised during the discussion of aid pledges for 1963/64.

As you know, the pledges made at the Paris meeting came to a total of about \$915 million, and I am hopeful that this can be raised to at least \$1,000 million when the meeting is resumed in Washington next month. This would be a much larger figure than could have been expected on the basis of the original assessment of India's foreign exchange requirements for the Third Plan. The members of the consortium recognised the heavy additional strain imposed on the Indian economy as a result of the national emergency, and there has been general admiration for the courageous action which you took in the Budget to mobilise additional resources for defence and development. Consequently, your Government's statement of aid requirements for 1963/64 was on the whole sympathetically received. Nevertheless, there was also evident concern about the disappointing progress made by the Indian economy during the first two years of the Plan, and several members of the consortium indicated that they would have considerable difficulty in maintaining aid next year and the year after at this year's level.

I would like to draw your attention particularly to paragraph 5 of the report of proceedings of the earlier consortium meeting held in Washington on April 30-May 1. As the report stated,

"there was general agreement that, in the interests of economic development, more energetic efforts should be made to expand foreign exchange earnings and to create a more favorable environment for export promotion. Great importance was also attached by members of the consortium to measures that would encourage private foreign investment in India, to the relaxation of controls over industry, which would help to lighten the load on the administration, and to appropriate pricing policies. The meeting welcomed the statement of the Indian representative that his Government accepted the need for industry to enjoy greater freedom from detailed controls. Other matters on which the meeting laid stress were the desirability of a gradual increase in interest rates and the importance of not pressing considerations of balanced regional development to the point where they impeded the efficiency of industry. Concern was expressed at the heavy burden of external debt service on India's balance of payments. Action to curb the growth of population in India was acknowledged to be an indispensable condition of satisfactory economic progress."

These were the unanimous views of the ten countries represented at the meeting, and I am in full agreement with them.

It was pointed out at the Paris meeting that, when the consortium first considered the Third Plan, total requirements of external assistance for the five years, including non-consortium aid and private foreign investment, were placed at \$5,460 million (Rs. 2,600 crores), of which it was suggested that \$4,400 million might be provided through the consortium. Against this, the consortium has already pledged \$3,280 million (i.e. about 75 per cent) in the first three years. Yet in spite of the fact that aid pledges from the consortium have exceeded what was originally contemplated, the growth of the economy has fallen far short of Plan expectations, and there is no sign that India's dependence on external support is being reduced.

A further cause of concern for the future arises from the fact that the consortium does not have any clear idea of your Government's programs and policies for the continued development of the economy during the next three years and into the Fourth Plan. A year ago my predecessor, Mr. Black, wrote to you suggesting the need for a thorough-going reappraisal of the investment program as a basis for reassessing the balance of payments for the next few years. Without such a reassessment, there is no way in which the consortium can arrive at a reliable judgement on the amount of additional aid that will be required in the coming years or on the uses to which such aid can be best applied.

I realise that the task of economic planning in India has been greatly complicated by the national emergency, but I think it is essential that, before the consortium meets to consider aid requirements for the last two years of the Third Plan, your Government should provide some sort of outline plan for the development of the economy over the next four or five years - that is, well into the period of the Fourth Plan. This should include a review of economic policy and indicate the steps being taken to improve the organisation for the implementation of development programs sector by sector.

The need for continuous forward planning, as distinct from planning at five-year intervals, seems to me all the more urgent in India because much of the aid extended by the consortium, as well as most of the aid from non-consortium sources, is tied to specific investment programs and projects. As you know, the consortium has laid particular stress this year on the need for non-project assistance, but it is clear that many members of the consortium, including the Bank and IDA, must continue to relate a large part of their aid to projects - and as most of the projects in the Third Plan have now been committed, it is becoming increasingly difficult to find new projects suitable for external financing. This problem will be even more acute next year unless the present system of five-year planning in India is considerably modified, and unless many of the programs and projects due for completion during the period of the Fourth Plan are prepared (and approved by the Planning Commission) well in advance of the time when the Plan is due to start.

- 3 -

When the consortium resumes its meeting in July to consider aid pledges for the current year, it will also discuss the timing of the next round of meetings. In principle, I think we should aim for December 1963/January 1964 or January/February 1964, so that the pledges for 1964/65 can be indicated before the beginning of your next financial year. However, in view of the attitude taken by a number of delegates in Paris, I doubt whether such an early meeting would be fruitful unless your Government is able by then to provide a much clearer indication than we have at present of your plans for the future growth of the economy and of the implications of these plans for the balance of payments. I should be grateful therefore if you could let me have your reactions to this letter before the July meeting, which will probably be held about the middle of the month.

I very much look forward to seeing you here in Washington for the Annual Meeting at the end of September.

Sincerely yours,

George D. Woods

EPW:hvs

Cleared with and cc: Messrs. Reid, Wilson, King

cc: Messrs. Knapp, Krishna Moorthi, Stevenson, Jeffries

IRAM

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IRAN

BRIEFING PAPER

I. MEETING WITH DELEGATION

Thursday, October 3, 1963

9:20 a.m. for 20 minutes

Attended by: Mr. Woods
Mr. Knapp

Mr. Reid
Mr. McDiarmid
Mr. Brakel
Mr. Vloeberghs

II. MEMBERS OF DELEGATION

Abdol Hossein Behnia

Governor (IBRD)
Minister of Finance

Mehdi Samii

Governor (IMF)
Governor, Central Bank of Iran

Ata Salmanpour

Temporary Alternate Governor (IMF)
Chief, Exchange Control and Foreign
Department, Central Bank of Iran

Ali Akbar Khosropur

Adviser
Alternate Executive Director

Jahanghir Amouzeghar

Alternate Governor (IBRD)
Minister Plenipotentiary
for Economic Affairs
Embassy of Iran

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

(a) State of relations (prospects for lending will brighten when a new parliament is convened)

(i) In the past two years relations were less close than in the years 1955-60. An economic mission reviewed the Third Plan and the mission's report was distributed to the Board in April 1963. A grant of \$750,000 was made available for technical assistance to the Iranian Electricity Authority in July 1963. However, the Bank has been unwilling to consider lending, because the Iranian Constitution prohibits the Government from borrowing abroad without Parliamentary approval, and there had been no Parliament since May 1961. Furthermore, the Bank declined to organize the consortium which had been requested, so long as the Bank itself was not lending; the merits of a consortium were doubtful anyhow, since few projects were well enough prepared to be considered for financing and recent Governments have not been inclined toward a very vigorous development policy. The Bank's view, conveyed to the Prime Minister in Mr. Woods' letter of May 24, 1963, was accepted by the Iranian Government in July; copies of this exchange of letters are attached.

(ii) As soon as the Government set a firm date (September 17) for parliamentary elections, a technical mission was sent to Iran to appraise a second road loan. It is expected that this project will be ready for consideration by the Board in November. Iran enjoys a sufficient margin of creditworthiness so that further lending, in addition to the proposed new road loan, is possible if suitable projects can be found. In a recent discussion, Mr. Amouzeghar, Head of the Iranian Financial Mission in Washington, mentioned that a number of relatively small agricultural projects may be combined into one agricultural program with a foreign exchange component large enough to warrant consideration by the Bank. In future we might also become involved in the financing of power projects, but this will depend on the results of various technical studies which will only become available in a year or two. Last winter Iran asked the Bank's opinion on the financing of an oil loading terminal at Khor Moussa on the Persian Gulf; we gave no encouragement to this project.

(iii) In the past year, because general business conditions remained depressed, only three subloan requests were submitted by IMDBI. The Bank approved two; one has already been credited to the loan account, but the other borrower (a textile project in Yazd) is hesitating before making the final step. Thus far only \$1.3 million has been credited to the loan account, out of a total of \$5.2 million; therefore, the final date for receiving the proposals from IMDBI, originally set on November 1, 1962, ~~will have to be~~ postponed a second time, ~~probably~~ to November 1, 1964. *has been*

(b) Topics likely to be raised by delegation

(i) The delegation may inquire about the Bank's position on further lending now that elections are being held. The answer would be that we hope to go ahead with the new road loan and that in that connection we will have to update our knowledge of the economic situation. We would propose to send an economic mission (one or two persons) to Iran some time this autumn. The mission would also provide a good opportunity to discuss further lending possibilities with the new Government. Because of its urgency agricultural development would be an attractive field but it seems unlikely that a satisfactory program can be worked out quickly in view of serious administrative limitations; the mission would have to take them into account in its preliminary assessment of new project possibilities. In general, Management should emphasize that the Bank can lend only if Iran presents well thought out projects of high economic priority.

(ii) A request for technical assistance to help improve Iranian port administration has been received, and the delegation may wish to discuss it at the Annual Meeting. The question of port management has long been a subject of controversy between the Bank and Iran, and the Bank refused to go ahead with a port loan some years ago partly because Iran was not willing to separate the technical administration of ports from customs management as we had recommended. On July 12 we replied to Iran's most recent request that there seems to be no point in sending a staff member to Iran to see what type of assistance is required until after the Government reaches a decision on granting operational and financial autonomy to the agency in charge of port administration. The Government has also requested technical assistance in port administration from AID.

(c) Topics to be raised by Management

We should express the hope that the Bank will be able to increase its activity in Iran. The need for an economic mission should be mentioned in this connection, and also the need for well prepared projects. Release of \$2.1 million, representing the special increase in subscription taken up in February 1960, should be requested. The Area Department will discuss arrangements whereby oil revenues are set aside for amortization and interest payments on loans to Iran.

IV. BACKGROUND INFORMATION

(a) Bank loans as of August 31, 1963

Year of Loan	Borrower	Purpose	Amount (equivalent in \$ million)
Jan 22/57	Iran	Equipment for development	75.0
May 29/59	Iran	Roads	72.0
Feb 20/59	IMDBI	Industrial development financing	5.2
Nov 23/60	Iran	Dez multi-purpose project	42.0
Total (net of cancellations and refundings)			194.2
Of which has been repaid			83.6
Total now outstanding			110.6
Amount sold			17.6
Of which has been repaid			13.5
			4.1
Net amount now held by Bank			106.5

1/ Includes \$7.4 million not yet disbursed: \$1.2 million for roads, \$2.0 million for Dez and \$4.2 million for IMDBI. Whole amount effective.

(b) IDA credits

None.

(c) 18% Capital Subscription (\$8.1 million)

\$6.0 million, corresponding to the original 18 percent subscription has been released and is on loan; \$2.1 million, representing 9 percent of the special increase taken up in February 1960, has not been released. Release of this small remaining portion could be suggested during the meeting with Management; if the discussion does not lend itself to this, the matter will be taken up by the Area Department.

(d) Holdings of World Bank bonds

\$1 million subscribed to the new issue.

(e) I.F.C.

Member. Capital subscription: \$372,000. IFC has one investment in Iran: a loan of \$300,000 extended in 1958/59; the company subsequently

experienced financial difficulties and has been reconstituted. Repayment of principal and payment of interest are now guaranteed by the Bank Melli Iran.

(f) I.D.A.

Part II member.

V. POLITICAL SITUATION

Asadollah Alam succeeded Dr. Ali Amini in July 1962 as Prime Minister, but in fact the Shah himself has been in close control of the Government. The Minister of Finance, Behnia, has been the most influential figure in the Alam Cabinet with respect to economic affairs; his conservatism is considered partly responsible for the lack of energetic efforts to develop the economy. The Shah seems dedicated to reform; but Arsanjani, the strong man behind agricultural reform, was forced to resign and the long-promised civil service reform is bogged down in committees. In January a referendum endorsed the Agrarian Reform Law and certain other measures (a literacy campaign, profit-sharing in industry, voting rights for women, etc.). In June religious leaders incited mobs in Tehran and other major cities to riot against these reforms. In recent years the Shah has lost some support from powerful groups which previously were behind him (e.g., landowners and religious leaders); however, his position with the masses may be stronger than it was in the 1950's. The National Front (Mossadegh followers) remains the only voluntary political party but is opposed to everything the Shah does. The success or failure of land reform appears to be a key issue, and in this connection it is important that effective measures be taken to replace the services formerly provided by landlords and to improve agricultural productivity. On August 5 it was announced officially that Parliamentary elections would be held on September 17; a separate note on the elections is appended.

VI. ECONOMIC SITUATION

<u>Population</u>	20-21 million, growing at 2.5 percent per annum
<u>Per capita GNP</u>	\$180
<u>Gross National Product</u>	\$3.4 billion
<u>Oil royalties (1962)</u>	\$330 million

In 1959/60 the rise in public expenditure outpaced that in oil revenues, and the Government resorted to deficit financing; the booming private sector also resorted extensively to bank financing. Inflationary pressures resulted in a balance of payments crisis. In late 1960 a stabilization agreement was concluded with IMF: credits to both the

private and the public sectors were severely curtailed, and public development expenditures fell as a larger portion of the oil revenues was used for ordinary expenditures.

From the financial point of view the stabilization program was successful. The trade deficit (excluding oil) fell by \$35 million from 1960 to 1962, while oil royalties continued to increase (to \$330 million in 1962 from \$285 million in 1960). Net foreign exchange reserves increased by \$90 million between December 1960 and June 1963. However, the stabilization program also contributed to the collapse of the building boom, general business stagnation and unemployment. Although credit restrictions were eased during 1962, the land reform social legislation and general political uncertainty resulted in low business confidence and delayed recovery.

The lack of thrust in the public sector has contributed to the stagnation of the economy. The Plan Organization has insufficient political strength to give leadership to the development effort as it once did. The Third Plan, which nominally started in September 1962, lacks well-prepared projects. Financial allocations for the Third Plan will have to absorb larger expenditures for the land reform program than were contemplated when the Plan was drafted; for example, in 1963/64 the land reform program is expected to require \$90 million (including the cost of compensation) out of estimated public development expenditures of \$316 million. The Government, so far as we know, is allocating oil revenues to the Plan Organization in accordance with the Third Plan Law (i.e. 60 percent in the current year). However, this year actual development spending may be lower than planned, because of lags in project preparation. Meanwhile, the Government's non-development expenditures are budgeted to increase by about 20 percent, largely for the armed forces.

Attachments (3): Copy of letter dated May 24, 1963 from Mr. Woods to the
Prime Minister
Copy of letter dated July 28, 1963 from Prime Minister to
Mr. Woods
Copy of letter dated July 12, 1963 from Mr. Reid to Mr. Asfia.

JBaneth/Stolbert/hae

September 27, 1963

MEMORANDUM ON IRANIAN ELECTIONS

(To be added to Briefing Paper on Iran)

Elections were held on September 17. As was to be expected 171 of the 200 new members of the Majlis were elected by the "Congress of Free Women and Free Men", which was created with a view to supporting the Shah's program. Its leader is Mr. Hassan Ali Mansour, a young and quite able politician and former civil servant who has been a Minister in previous Governments. Most of the new members of Parliament had not been elected before. The landlords representing a vast majority in previous Majlis will no longer dominate the legislative branch. Among the Majlis members are labor representatives, women, teachers and a considerable number of younger college graduates.

The new Majlis will open on October 6 but at present it is not known whether a new Government will be formed by that time. Some indications are that Mr. Assadollah Alam, the present Prime Minister, may stay on as the head of a new Cabinet. Some think it likely that Behnia, the present Finance Minister and IBRD Governor will not remain.

C O P Y

Prime Minister of Iran
Teheran, Iran

Ref. No. 956 KKH

July 28, 1963

Mr. George B. Woods,
IBRD
Washington, D.C.

Dear President Woods:

This is to acknowledge the receipt of your letter of May 24 and to thank you for sending me the Bank's appraisal report on the Iranian Third Plan.

I have had a brief opportunity to review this report. I am pleased to see that the Plan's philosophy, emphasis and direction enjoy the appreciation and support of the Bank.

As far as the Plan's implementation is concerned, you can rest assured that my government will give appropriate attention to the suggestions made in your letter and that due care will be taken to execute the reform measures previously envisaged in the Plan.

I am also pleased to inform you that after deliberations with Mr. Asfia and Dr. Amuzegar we too have come to the conclusion that the formation of an aid-giving consortium is not essential, at least for the present, and that the foreign exchange requirements of the Third Plan can be met through other means.

I sincerely hope that the Bank under your leadership will cooperate with my government in the spirit of earlier times, and that our road construction projects now before the Bank will receive a more understanding and a more sympathetic consideration from the Bank.

It would be a pleasure to have you with us in Iran, and you can be sure that whenever you get a chance to visit our country you will be most welcome.

With personal best wishes.

Sincerely yours,

(Signed) ASSADOLLAH ALAM
Prime Minister

Dr. Saff Asfia
Managing Director
Plan Organization
Khatam Daneshkadeh
Tehran, Iran

July 12, 1963

Dear Dr. Asfia:

This is with reference to your letter of June 22, 1963 regarding the provision of expert advice relating to port operation in Iran.

We are glad to learn that the Government proposes an administrative reorganization which would separate the technical administration of the ports from that of customs management. This is a step which the Bank recommended in our earlier discussions of the problems of port administration in Iran, and we still consider it an essential measure. You will remember that in these discussions we consistently urged also that sound port management required the granting of a sufficient degree of operational and financial autonomy to the agency in charge of port administration - whether that be the present Ports and Navigation Authority or some other entity - to enable it to perform its tasks effectively. Only after a decision is taken on this point would expert advice on technical questions, such as mentioned in your letter, appear useful.

We would appreciate your informing us whether the Government has reached a decision to grant such autonomy to the port agency, and in what manner. In the event of a favorable reply, we should be happy to exert our best efforts to provide the requisite technical assistance. To this end we would propose initially to send one of our port engineers to Iran for a few days of discussion with you and your colleagues to enable the Bank to determine precisely what kind of assistance is needed and what should be the terms of reference for the experts.

I note in your letter a reference to a recent "long-run view" of port development in Iran. If this were in the form of a report which could be made available to us, it might be helpful to us in assessing the plans and needs in this field.

With kindest personal regards,

Sincerely yours,

Shared with and cc: Mr. Carmichael
Mr. Benjenk
Mr. Mubnig
cc: Mr. Cancio
Mr. Rigby

Escott Reid
Director
Department of Operations
South Asia and Middle East

STTolbert/fh

cc: Mr. J. Wheeler, A.I.D. 8/23

His Excellency
Asdollah Alam
Prime Minister of Iran
Tehran, Iran

May 24, 1963

Dear Mr. Prime Minister:

I take pleasure in sending you a copy of the appraisal report prepared by the Bank on the economic development program of Iran. As you know, the report was originally drafted by a mission which visited Iran a year ago. That draft was discussed with your Government last year and on March 20, 1963, Dr. Asfia sent to the Bank comprehensive comments from the Plan Organization. I was pleased to note from his letter that on major issues the Plan Organization is substantially in agreement with the Bank mission. These comments have been taken into account in preparing the final report which has now been circulated to the Executive Directors of the Bank.

I was glad to learn that efforts are being made to raise public revenues through increased taxation as well as to reduce the rate of increase in the current expenditures of the Government considerably below the annual rate of 7½% contemplated in the Third Plan Law. As the Bank mission pointed out in its report, if the Plan is to be successfully executed, there will have to be sizeable increases in receipts from taxation and a careful control of Government expenditures. On both counts there is, in our opinion, still considerable room for improvement. It is also essential that the decision to set aside an increasing proportion of the oil revenues each year for the "Plan Income Account", rising from 55% in the last half of 1962/63 to 80% in 1967/68, be strictly implemented and that the allocation of funds from the "Plan Income Account" be made only for development expenditures. All of this has become even more urgent now that the gross savings of Government industrial enterprises, of the National Iranian Oil Company, and of the railways, have been excluded from the resources available for the Plan without a corresponding reduction in the proposed level of expenditures.

In his letter to Mr. Wilson Dr. Asfia again raised the question of the Bank's organizing a consortium for Iran. We have given a great deal of thought to this problem and have concluded that, at least in present circumstances, this approach would not be the best way for the Bank to help Iran in coordinating foreign aid required for the Third Plan. There is only a limited number of major projects in the Plan which lend themselves

to external financing, and for most of these projects which are in a sufficiently advanced stage of preparation to be considered for early execution, offers or commitments of the necessary foreign exchange have already been obtained from abroad.

As Mr. Knapp said at his discussion with Mr. Amouzeghar on May 15, we hope that it will soon be possible for the Bank to assist Iran further in financing its development program. As soon as the path is opened to a resumption of Bank lending, we would be glad to initiate informal discussions with the United States Government as to how our lending might appropriately be coordinated with theirs. Other aid-giving countries could then gradually be brought into the picture in the same informal way as specific needs for foreign exchange financing appear.

I am confident, Mr. Prime Minister, that the cooperation between the Bank and Iran, which started under my predecessor Mr. Black, will bear further fruit in the future. I hope to have the pleasure of visiting your country as soon as time and opportunity permit. In the meantime may I extend my best wishes for a successful execution of the Third Plan.

Sincerely yours,

George D. Woods

WBrakel:jbt

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IRAQ

BRIEFING PAPER

I. MEETING WITH DELEGATION

Wednesday, October 2

9:00 a.m. for 20 minutes

Attended by: Mr. Knapp

Mr. Reid
Mr. McDiarmid
Mr. Brakel
Mr. Tolbert

II. MEMBERS OF DELEGATION

Abdul Karim Al-Ali

Governor (IBRD)
Minister of Planning

Khair El-Din Haseeb

Governor (IMF)
Alternate Governor (IBRD)
Governor, Central Bank of Iraq

Subhi Frankool

Alternate Governor (IMF)
Chief of Banking, Central Bank of Iraq

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

(a) State of relations

The new Government, which overthrew the Kassim regime in February, advised Mr. Woods on April 4 of its wish to renew relations with the Bank. Mr. Brakel visited Baghdad in the latter part of April, and a fact-finding mission of three Bank staff members was sent to Iraq for three weeks in May/June. The mission's report was to be reviewed by SLG on September 25; a separate note is appended giving the results.

(b) Topics likely to be raised by delegation

The delegation will probably inquire about Bank lending prospects and the mission's findings. The response should be as indicated in the attached report on the SLG meeting.

(c) Topics to be raised by Management:

Whether the delegation does so or not, the Management will wish to raise the question of lending prospects in the light of the SLG review. We should discuss the scope and timing of any further Bank missions to Iraq. We should inquire about the Government's progress in revising the development program and the status of plans for reorganization of the planning function.

IV. BACKGROUND INFORMATION

(a) Bank loans as of August 31, 1963

Year of Loan	Borrower	Purpose	Amount (equivalent in \$ million)
Jun 15/50	Iraq	Flood control	12.8
		Total (net of cancellations and refundings)	6.3
		of which has been repaid	6.3
		Total now outstanding	---
		Amount sold	---
		of which has been repaid	---
		Net amount now held by Bank	---

(b) IDA credits

None.

(c) 18% Capital Subscription (\$1.35 million)

\$1.1 million, equal to the full original 18 percent, has been released and is now outstanding on loan. A small quota increase was taken up in December 1959, but has not been released. Area will take the matter up with the delegation.

(d) Holdings of World Bank bonds

\$1.0 million.

(e) I.F.C.

Member. Capital subscription \$67,000. No operations and limited prospects.

(f) I.D.A.

Part II member.

V. POLITICAL SITUATION

The military coup which overthrew Kassim on February 8 was led by Baathists and non-party officers. The Baath is a minority party, but is backed by military leaders and has taken most government posts and power to itself. The new Government has carried out systematic and violent repression of Communist and Kassimite opposition. A brief truce with the Kurds lasted only until June, when hostilities were resumed on a large scale. Moves toward tripartite union with Egypt and Syria have been prevented by rivalry between Nasser and the Baath party. There is now some talk of Iraq-Syrian union, but no concrete steps have been taken; such union would probably be confined to broad political matters, since any move to share oil revenues would not be popular in Iraq.

VI. ECONOMIC SITUATION

<u>Population</u> (1963)	7.2 million, growing at 2 percent per year
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<u>Per capita GNP</u> (1961)	\$200
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Average annual growth (1953-1961)

Gross national product	7 percent
Per capita GNP	5 percent
Industrial production	10-12 percent
Agricultural production	Slight decline
(1959-61 as compared with 1953-55)	

After 1960 oil exports and revenues failed to expand because of the protracted dispute between Kassim and the oil company; the dispute culminated in 1961 with the cancellation by the Government of 99-1/2 percent of the company's concession area or all the area not already under active

exploitation. During 1960-62 petroleum exports were stable at about 45 million tons, and revenues to the Government were about \$260 million per year. The new Government has settled certain issues, including cargo dues on oil tankers, and exports have begun to rise again. Oil revenues may reach \$280-285 million this year.

On the central issue of concession areas, however, the new Government's position is not yet clear. The Government would find it politically difficult to give back a portion of the concession areas, but appears determined to find an acceptable compromise, so as to enable Iraq's exports at least to share in the general expansion of Middle East oil exports.

The price level has remained fairly stable as the inflationary effects of sizeable budget deficits and the expansion of private credit have been offset by drawings on foreign exchange reserves. During Kassim's regime the reserves fell from \$288 million at the end of 1958 to \$188 million at the end of 1962 (which is equal to 50 percent of annual imports). Budget deficits continue; the new Government has expressed its intention to eliminate the deficit projected in the 1963/64 budget, but this is rendered unlikely in view of the resumption of hostilities against the Kurds and by announcements of various new social welfare measures.

Despite substantial investment in water storage, irrigation and land reclamation, agricultural production has shown no rising trend. Industry, aided by protection and other incentives, has shown significant growth, though it still accounts for only 10 percent of national income.

Fifty percent of oil revenues are allocated to development and 50 percent to the ordinary budget. The new Government inherited from the Kassim regime a five-year plan (1961-66) proposing expenditures of roughly \$310 million per year. Actual expenditures were around \$190 million per year in the first two years of the plan; half of this went for public buildings and housing. The new Government is revising this plan; it has approved a program for the current year which provides for expenditures of \$182 million, which can be covered by oil revenues plus aid already committed under agreements with the U.S.S.R. and Czechoslovakia; additional projects would be taken up if additional external financing were obtained.

SMTolbert/wh
September 18, 1963

September 27, 1963

MEMORANDUM ON SLC MEETING ON IRAQ

(To be added to Briefing Paper on Iraq)

In the light of the SLC review of the economic mission's report, the Management should convey to the Iraq delegation the Bank's willingness to resume lending in Iraq. Management will probably wish to suggest that the Area Department take up with the delegation the selection of a priority field in which assistance is desired and in which a project could be prepared for reasonably prompt execution. (If the delegation inquires as to the amount, we should indicate it depends on the project: that it might be of the same order of magnitude as the 1950 Wadi Tharthar loan of \$ 12.8 million, or more or less as the project merits. The SLC approved a range of \$10-20 million.)

We should state that on the basis of present information road and bridge construction appears the most likely field, but if the Government strongly preferred, we would consider a project in one of the other fields which the Government had discussed with the economic mission - irrigation and drainage, power, including the natural gas pipeline, or telecommunications. The preparation of a project in any of the latter fields would, however, probably take longer. The Area Department would also discuss the possible timing of an appraisal mission.

We should make clear to the delegation that in Iraq's present circumstances, we consider only a moderate amount of foreign borrowing appropriate, in view both of questions of absorptive capacity and of the need to concentrate upon making the existing fairly high level of development expenditures most effective. We might wish also to commend Iraq's avoidance of reliance upon suppliers' credits, and express the hope that this will continue to be the case. (The Government has recently negotiated agreements with Sweden and Germany providing for such credits.)

We should tell the delegation that over the longer run, however, we consider this initial project to be only a first step. Provided sound projects are presented, and provided also that the Iraq Government pursues sound fiscal and development policies, we would expect to continue working with them. In this connection, we should inquire about the progress of negotiations with the oil company on the concession areas.

If the delegation shows genuine interest in obtaining technical assistance in development programming and financial coordination, we should state our willingness in principle to provide such assistance and suggest that determination of the exact needs would, of course, require further consultation.

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ISRAEL

BRIEFING PAPER

I. MEETING WITH DELEGATION

Tuesday, October 1

4:40 p.m. for 20 minutes

Attending: Mr. Woods
Mr. Wilson

Mr. Reid
Mr. McDiarmid
Mr. Pollan

II. MEMBERS OF DELEGATION

David Horowitz

Governor, (IBRD)
Governor, Bank of Israel

Pinhas Sapir

Governor (IMF)
Minister of Finance
Minister of Commerce and Industry

Jacob Arnon

Alternate Governor (IBRD)
Director General, Ministry of Finance

Y.J. Taub

Alternate Governor (IMF)
Acting Secretary General, Bank of
Israel

Aryeh Manor

Adviser
Economic Minister, Embassy of Israel

Adin Talbar

Adviser
Economic Counselor, Embassy of Israel

Miss Bella Rosenberg

Adviser and Secretary
Government of Israel, Economic
Offices, New York

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

- (a) State of relations (prospects for an additional loan to Ashdod Port in the spring of 1964 and a second road loan later).

(i) The Bank's first loan to Israel, approved three years ago, is financing the construction of a new deepwater port at Ashdod. An application is expected for an additional \$2.5 million loan to help construct a pier which would handle potash and other bulk chemicals at Ashdod. Pier designs cannot be completed until a decision is taken on whether rail or road transport should be used from the Negev to Ashdod--a subject which will be studied by consultants during the next six to nine months as part of the 1962 roads project. A third loan for the "second stage" of Ashdod port development is a more distant prospect.

(ii) The Bank's second loan was to the Dead Sea Works, a project that promises substantial new export earnings to Israel. A third loan was approved after the last annual meeting and is financing highway construction. As part of this project economic consultants are to be hired to survey transport needs throughout Israel; the selection of consultants should be made within the next few weeks. This survey may indicate future lending prospects in the transport sector.

- (b) Topics likely to be raised by delegation

(i) In a letter of May 24, Governor Horowitz stated that he would like to discuss the possibility of stretching out disbursements of Bank loans in view of the fact that foreign exchange reserves are (temporarily) quite high. He indicated that the stretch out would apply only to 1963, since Israel would "urgently need this currency in the year 1964." Management's position would follow the line taken in Mr. Reid's letter of June 12, which stated that we are concerned about the progress of work on the three bank projects in Israel as well as the rate at which funds are drawn, which is a related but secondary consideration. (Letters attached.) The Dead Sea Works expansion is progressing ahead of schedule, and although the Ashdod Port is at least a year delayed, this can be attributed mostly to unavoidable technical difficulties. However, the roads project has been threatened with serious delay by the Government's own failure to appropriate sufficient local funds. Management should again ask the delegation to use its influence to see that all the projects are carried forward with due speed and should insist on prompt withdrawals from the loan accounts. If Governor Horowitz offers some more specific proposal than was contained in his letter, it will have to be studied.

(ii) In the past the Israeli delegation has made various proposals for IDA financing; if this subject is raised again, the delegation should be told, as it was told very firmly a year ago, that less developed countries have a more urgent claim on the very limited resources of IDA.

(iii) The delegation may bring up the case of Mr. David Golan, who for a time was considered by the Bank for a six-month assignment as an industrial consultant in the Philippines. Later a reconsideration of Philippine requirements suggested the need for at least a 12-month assignment of somewhat different qualifications and a decision was taken not to employ Mr. Golan. The Israeli Government was reportedly more than a little put out by the fact that Mr. Golan was not appointed after three months consideration, and Management may wish to reiterate the Bank's concern over this misunderstanding. In expressing its continued interest in employing Israeli technicians for special missions, Management might note that the Bank is very pleased that the Director of the Division of National Accounts at the Central Bureau of Statistics, Mr. Levy, has recently been released, also for a mission to the Philippines. (If the issue is not raised by the delegation in consultations with Management, the Area Department will express appreciation for the Government's cooperation and our continuing interest in employing experienced specialists from Israel.)

(c) Topics to be raised by Management

(i) Management may wish to discuss with Governor Horowitz some of its proposals for changing the Bank's lending policies. In the past Governor Horowitz himself has offered proposals regarding Bank lending policy. For example, at the 1962 Annual Meeting he urged that the Bank lend funds at a very low rate of interest; the difference between that low rate and the Bank's normal charges would, under Horowitz' scheme, be covered out of an Equalization Fund subsidized by the participating governments. Under his proposal each \$50 million per year contributed to the Equalization Fund would make possible \$1 billion of Bank lending at one percent interest for one year. Capital would be raised by the Bank in the usual way, but the Equalization Fund would be supported by subscriptions from the cooperating governments. IDA funds would be used exclusively as a guarantee fund for these low interest Bank loans instead of extending direct credits. Alternatively, Governor Horowitz proposed that IDA follow a more flexible policy with immensely increased resources.

IV. BACKGROUND INFORMATION

(a) Bank Loans as of August 31, 1963

<u>Year of Loan</u>	<u>Borrower</u>	<u>Purpose</u>	<u>Amount (equivalent in \$ million)</u>
1960	Israel	Construction of new deep- water port at Ashdod	27.5
1961	Dead Sea Works Limited	Potash production	25.0
1962	Israel	Highway construction and improvement	22.0
Total (net of cancellations and refundings)			74.5 ^{1/}
of which has been repaid			--
Total now outstanding			74.5
Amount sold		3.3	
of which has been repaid		-	<u>3.3</u>
Net amount now held by Bank			<u>71.2</u>

^{1/} Includes \$50.8 million not yet disbursed.
Whole amount effective.

(b) IDA Credits

None.

(c) 18% Capital Subscription (\$3.0 million)

All but \$400,000 has been used for purchases in Israel.
This situation is considered satisfactory.

(d) Holdings of World Bank bonds

\$5.6 million known to the Treasurer.

(e) I.F.C.

Member. Subscription \$50,000. A household appliance project is under study.

(f) I.D.A.

Part II member but now considered to be too well developed to be eligible for IDA assistance.

V. POLITICAL SITUATION

Mr. Zalman Shazar (73), Israel's first Minister of Education, was elected the President of Israel by the Knesset in May 1963. He succeeded the late President Ben-Zvi, who died in April 1963.

The Knesset is elected for a term of four years. General elections were last held in August 1961 and Mapai (the Labor Party) again emerged as the dominant party, having won 42 of the 120 seats. After Ben-Gurion's resignation in June 1963, Mr. Levi Eshkol, formerly Minister of Finance, succeeded him as Prime Minister and Minister of Defence. The new government was based on the same coalition as its predecessor, including Mapai and five other parties controlling a total of 68 of the 120 seats in the Knesset.

VI. ECONOMIC SITUATION

<u>Population (1963)</u>	2.3 million, growing at 4 percent per annum
<u>Per capita GNP</u>	\$800
<u>Average annual growth (1951-61)</u>	
Gross national product	10 percent
Per capita GNP	5.3 percent
Industrial production	n.a.
Agricultural production	12.8 percent

The main objectives of the Government's fiscal policy have been to try to finance the large current account deficit associated with a high level of investment and rapidly rising consumption and, at the same time, to control inflation. In the past a substantial inflow of foreign capital has been available to meet the payments deficit, and changes in the exchange rate (especially in 1953, 1955 and 1957) removed the more serious discrepancies caused by inflation. In February 1962 the Israel pound was again devalued from £I 1.80 to

£1 3.00 to the dollar, and a New Economic Policy adopted, emphasizing measures to fight inflation. Since the inflow of foreign capital is expected to decline in the future, the Government is trying to reduce the current account deficit from the present annual level of about \$400 million to \$250 million by 1965 without inflation and without impairing economic growth. A major requirement of this strategy is to reduce the growth of per capita consumption from an annual rate of five or six percent to about two percent; although technically possible, it will be difficult to achieve this objective.

The economy continues to grow at a high rate. GNP in real terms rose by some 9 percent in 1961 and by 12 percent in 1962, continuing the trend of the previous twelve years. Per capita income is now about \$800 and compares favourably with some of the older industrial countries. The rate of investment is high (i.e., 26 percent of national product in 1961 and 30 percent in 1962); however, external assistance financed 65 percent of gross investment in 1961 and 80 percent in 1962. The continued heavy flow of capital into the country and the conversion of foreign exchange into local currency led to an unprecedented expansion of the money supply in 1962 and 1963. Nevertheless, price increases in 1962 were less than had been expected from devaluation and prices have also been fairly stable in the first half of 1963. Full employment continues despite the rapid increase in the labor force.

Attachments:

- (1) Letter of May 24, 1963 from Governor Horowitz to Mr. Escott Reid.
- (2) Letter of June 12, 1963 from Mr. Escott Reid to Governor Horowitz.

CW/DWJ/GBV:hvs
September 13, 1963

COPY

BANK OF ISRAEL

Office of the Governor

Jerusalem, May 24, 1963

Mr. Escott Reid
Director of Operations
South Asia and Middle East
International Bank for Reconstruction
and Development
Washington 25, D.C.
U.S.A.

Dear Mr. Reid

You are certainly well aware of the economic developments in Israel. We are at the moment amply provided with foreign currency and there is an idea to stretch out the drawings on our World Bank loan during a longer period of time than previously provided for.

Of course, we shall urgently need this currency in the year 1964.

I hope there will be no objection on the part of the World Bank to such a policy.

I am looking forward to meeting you in Washington on the occasion of the Annual Meeting of the Bank and the Fund and we may then discuss this problem in more detail.

Yours sincerely,

/s/ D. Horowitz

COPY

Mr. David Horowitz
Governor
Bank of Israel
Jerusalem, Israel

June 12, 1963

Dear Governor Horowitz:

I have just returned from Europe and found your letter of May 24 waiting for me. We are well aware of the temporary situation which has led to the accumulation of foreign exchange in recent months, and we look forward to discussing the implications of this situation with you at the time of the Annual Meeting.

In connection with the Bank's loans to Israel, we are more concerned about the progress of work on these three projects than the rate at which you draw funds from us, which under the standard loan regulations is a related but secondary consideration. It is therefore gratifying to know that the expansion of the Dead Sea Works is on schedule, or perhaps even a little ahead of schedule, but it is also alarming to learn that roads, vital to the potash export program, are threatened with very serious delay. The Port of Ashdod is reported 12-15 months behind schedule and will miss at least one of the citrus seasons for which it was expected. Therefore, I would ask you to use your influence to see that the projects themselves go forward with all due speed and that adequate funds are made available to them as quickly as required.

At the time of the Annual Meeting we shall take the opportunity to discuss these matters with you in more detail.

Sincerely,

Escott Reid
Director
Department of Operations
South Asia and Middle East

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MAY 16 2017

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JORDAN

BRIEFING PAPER

I. MEETING WITH DELEGATION

Wednesday, October 2

9:40 a.m. for 20 minutes

Attended by: Mr. Knapp
Mr. Rosen

Mr. Reid
Mr. Mason
Mr. Bart
Mr. Brakel

II. MEMBERS OF DELEGATION

Adeeb Sughayer

Governor (IBRD)
Undersecretary, Ministry of Finance

Mohamed Ali Rida

Governor (IMF)
Minister of Communications

Nijmeddin Dajani

Alternate Governor (IBRD)
Secretary, Development Board

A.K. Humud

Alternate Governor (IMF)
Deputy Controller of Currency

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

- (a) State of relations (prospects under consideration include water supply, agricultural credit, potash and industrial financing)

X (i) The processing of various projects under consideration by IDA is nearing completion. The progress on the four water supply projects (\$3.5 million) has been particularly slow, owing mainly to delays in the completion of feasibility reports by the Government's consultants and to the time required for appraisal. It is expected that these projects will be submitted to the Executive Directors after the annual meeting. In May 1963 a mission was in Jordan to complete the appraisal of the agricultural credit project (\$3million) for which negotiations are tentatively scheduled early in October. These projects, plus the Amman Water Supply project already approved for \$2 million, would bring IDA credits to Jordan to a total of \$8.5 million, which appears to be as much as is appropriate in view of the limited resources available to IDA.

(ii) In April 1963 another mission had preliminary discussions with the Government on the contemplated Bank loan to the Arab Potash Company. Although the Government showed reluctance to accept the principle of Bank rather than IDA financing, it was agreed that the consultants of the company (Western Knapp) would revise the projects with a view to reducing the initial estimates ~~before a final decision was made regarding the source of funds~~. We were recently informed by AID that revised estimates have now been completed and indicate a cost of \$23.5 million instead of \$31 million. However, no official notification has yet been received from the Government, which is reportedly negotiating about the financing of the project with the Banque de Paris et des Pays-Bas.

(iii) The only other project under consideration concerns an Industrial Development Corporation, for which only IFC participation has been requested so far.

- (b) Topics likely to be raised by delegation

There is a remote possibility that the delegation will raise the question of financing the Yarmouk scheme, which is given an urgent character by the contemplated pumping from Lake Tiberias by Israel, scheduled to start in February 1964. Some 12,000 acres of farmland might be seriously affected by increased salinity in the Jordan River resulting from pumping by Israel. It is, however, doubtful if Jordan will pursue this matter further if it is confirmed that additional IDA funds cannot be made available now.

(c) Topics to be raised by Management

(i) It is recommended that Management take the initiative in telling the Jordanian delegation that we cannot consider new proposals for IDA at this time. We should say that last winter we had hoped that IDA would have about \$500 million a year to commit but that new resources actually available from Part I countries will be only half that amount. Therefore, we cannot consider projects in addition to those already under study or approved for Jordan. If the delegation refers to the figure of \$12 million mentioned in the second paragraph of Mr. Woods' letter of January 29, 1963 (copy attached), Management should note that the emphasis of that letter was on projects already under consideration and on the overall prospects for IDA.

(ii) We should also inquire about the status of the Potash project in case it is not mentioned by the delegation.

IV. BACKGROUND INFORMATION

(a) Bank loans

None

(b) IDA credits as of August 31, 1963

Date	Borrower	Purpose	Amount (equivalent in \$ million)
Dec 22/61	Jordan	Amman water supply	2.0 <u>1/</u>

1/ Includes \$1.97 million not yet disbursed. Whole amount effective.

(c) 18% capital subscription (\$1.35 million)

No release. Area will urge release by stages.

(d) Holding of World Bank bonds

None

(e) I.F.C.

Member. Subscription \$33,000. The development corporation and Arab Potash Company projects are under study.

(f) IDA

Part II member

V. POLITICAL SITUATION

The new political orientation of Syria and Iraq in the spring of this year has again altered the interplay of forces to which Jordan is subject. The tripartite unity talks between the UAR, Syria and Iraq threatened to disturb the balance in Jordan; but due to the strong reaction of the royalist Government and the dissensions between Nasser and the Baath, she weathered the storm once more.

The vagaries of inter-Arab politics seem to matter less in Jordan than the fidelity of the Army and the threat of Israel. Most of the population continues to respond to the ideology of unity personified in Nasser (as was illustrated by the vote of the Parliament at the time of the tripartite talks); and those refugees who have not been integrated in the economy and for whom large-scale migration is now impossible still live in the expectation of revenge against Israel. On the other hand, there is an increased awareness, at least among the middle classes, that peace and prosperity are best served by Jordan's independence.

Comparatively free elections in November 1962 were followed by the traditional "managed" ones in July 1963, after Parliament had to be dissolved because of its stand in favor of Arab unity. True power continues to rest with King Hussein and the close group of former Trans-Jordanians and moderate Palestinians who control the Army and the Government. U.S. support, both political and financial, still provides most of the cement which keeps this precarious edifice together. Although the recent establishment of diplomatic relations with the USSR foreshadows a subtler international policy, Jordan is unlikely to be able to extricate itself from a position of economic dependency for many years to come.

VI. ECONOMIC SITUATION

<u>Population</u> (1963)	1.8 million, growing at 3 percent per year
<u>Per capita</u> GNP (1961)	\$150-200
<u>Average annual growth</u> (1954 - 1961)	
Gross national product	10-11 percent
Per capita GNP	7 percent

The rate of economic growth in 1962 was below the average of recent years, and there is a possibility that the national income in 1963 might decline as a result of poor cereal crops and smaller receipts from tourism. A deterioration in the balance of payments is expected owing to the continued increase in imports.

The main task facing the Government is the implementation of its development program, designed to reduce Jordan's dependency on external budget support. The initial 1962/67 plan is being extended to 1970, with a tentative level of public investments of JD 116 million (\$325 million). Most of the financial requirements of this plan are expected to come from abroad, although more domestic resources are being raised to meet increased current expenditures.

Attachment:

Letter from Mr. Woods to Mr. Wasfi Tell, President, Jordan Development Board, January 29, 1963

MBart/GVotaw/hae
September 16, 1963

C O P Y

January 29, 1963

Mr. Wasfi Tell
President
Jordan Development Board
Amman, Jordan

Dear Mr. President:

Thank you for your letter No. DB/161915922 of December 17, 1962, regarding your request for a credit of \$20.3 million to assist in financing the proposed project of the Arab Potash Company including the associated highway to Aqaba.

As you are aware we have financed one project in Jordan (Amman Water Supply) and have under consideration other projects (four new water supply projects and assistance to the Agricultural Credit Corporation) which may in due course bring the total of IDA credits to Jordan to an amount of \$12 million. I have reluctantly come to the conclusion that the resources available to IDA are too limited to permit the Association to make a credit of the amount requested in your letter over and above the projects we now have under consideration.

However, the project is potentially of great importance to Jordan and if it can be shown to be feasible, economic and profitable, it is possible that some way could be worked out to formulate it as a self-liquidating project suitable for financing by the World Bank on conventional terms. A Bank loan could still cover only part of the needs; whatever means of loan financing are employed the company should also raise further equity capital in order to put it on a sound financial basis. The Bank would want to consider with the company the possibility of raising further funds in the Arab countries, and possibly equity capital in the United States and Europe. The company would need to make arrangements to ensure both experienced management and an entry into the world potash market and some form of association with a foreign company would be an appropriate way of doing this.

If you are agreeable to the above approach, please let me know so that we may consider how to go about a thorough appraisal of the project's technical, financial and managerial aspects. In such case, I would suggest that the company not award any further contracts until they have been discussed with and agreed to by the Bank.

We have discussed this project with AID and have informed them that IDA funds would not be available to finance the project. I have also informed AID that the suggestion made in your letter of November 29, 1962,

to Mr. Russell S. McLure, Director of AID in Amman, that IDA should finance the road alone, does not seem practical in my view. The road appears to depend entirely on the potash plant for its economic justification and it would be far better for one institution to arrange for financing the project as a whole. I am sending Mr. Gaud of AID a copy of this letter for his information.

Sincerely yours,

(Signed)
George D. Woods

Copy to: Mr. William S. Gaud

JBurke Knapp:pd
GSM:avc

KOMAIT

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KUWAIT

BRIEFING PAPER

I. MEETING WITH DELEGATION

Tuesday, October 1, 1963

4 p.m. for 20 minutes

Attended by: Mr. Wilson

Mr. Reid
Mr. McDiarmid
Mr. Brakel

II. MEMBERS OF DELEGATION

Abdlatif Y. Al-Hamad

Alternate Governor (IBRD)
Director General,
Kuwait Fund for Arab Economic Development

Hamzeh Abbas Hussein

Alternate Governor (IMF)
Secretary, Kuwait Currency Board

Abdul Hamad Mazidi

Chairman, KIC

Talib Tawfik Al-Nakib

Adviser
Director, Banking Department
Central Bank of Kuwait

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

(a) State of relations (close cooperation but no lending prospects)

The Bank has made various organizational recommendations to Kuwait, and some of these--such as the setting up of a Planning Board--have already been carried out.

The major specific fields of mutual interest have been:

(i) The Bank assisted the Kuwait Fund for Arab Economic Development by seconding a staff member, Mr. Svoboda, to advise the Fund on matters of organization and operations. More recently, Mr. El Fishawy, a lawyer from the Bank, joined the Fund's staff.

(ii) Mr. McDiarmid visited Kuwait for a week in May and discussed Kuwait's industrial program and the revision of the Bank's economic report of 1961. It was agreed that the Bank would send a small mission in October to up-date the Bank report for distribution to the Executive Directors.

(iii) In July at the request of the Government the Bank made available a list of consulting firms capable of advising on industrial projects. The Bank has also recommended Mr. Aftab Khan of Pakistan to serve as senior adviser to the Planning Board; Mr. Khan plans to visit Kuwait in October.

(b) Topics likely to be raised by delegation

(i) Delegation may wish to discuss further cooperation between the Bank and Kuwait Fund, including the possibility of a replacement for Mr. Svoboda after 1964.

(ii) The Fund has, through Svoboda, requested the technical help of the Bank in reviewing investment projects in the financing of which it was interested. We have not considered it advisable for the Bank to make desk studies of projects but have furnished the Fund with economic and technical reports whenever possible. We should be receptive to suggestions for further assistance but must avoid assuming any general responsibility for advising on the merits of particular projects.

(c) Topics to be raised by Management

(i) Management should state its intention to send a Bank mission in October to up-date the economic report. The mission will be headed by Mr. McDiarmid and will probably include two other staff members; its report would be distributed to the Board towards the end of the year.

(ii) Management may wish to thank the Delegation for Kuwait's prompt positive response to our request for the release of the 18% subscription.

(iii) On July 2, 1963 Mr. Woods wrote to the Minister of Finance and Economy concerning Kuwait participation in the proposed replenishment, noting that each of the other Part I countries had already agreed to new contributions representing an average increase of two-thirds over the present level. A copy of that letter was sent to Mr. Black. Mr. Woods' letter referred to Secretary Dillon's request of May 14, 1963 that Kuwait subscribe to the replenishment "in the amount of \$3,360,000 million a year for the three-year period;" apparently, there are typographical errors in this letter, since \$3.36 million is the full amount of Kuwait's initial subscription. Mr. Woods also referred to the Minister's June 12 reply to Dillon, which reported a decision of the Council of Ministers to "keep in line with other Arab states" and therefore to decline from participation in the replenishment. There has been no reply to Mr. Woods' July letter and reconsideration should be urged at the annual meeting. In his July 2 letter to Mr. Black, the President noted that two-thirds of Kuwait's initial subscription would be \$1,125,000 per year for three years and suggested that this be considered the minimum Kuwait should do.

IV. BACKGROUND INFORMATION

(a) Bank loans

None.

(b) IDA credits

None.

(c) 18% Capital Subscription (\$6.0 million)

In a letter dated September 8, 1963, the Government agreed to release fully the 18% capital subscription in four semi-annual installments.

(d) Holdings of World Bank bonds

In a letter dated June 8, 1963 the Finance Minister reported the Government's decision to purchase £ 1 million worth of 5% Deutschmark bonds due 1974 and £ 1 million worth of 5% Italian Lire bonds due 1976. Kuwait has also subscribed \$1 million to the new bond issue.

(e) I.F.C.

Member. Capital subscription \$369,000. No operation and IFC considers its assistance unnecessary.

(f) I.D.A.

Part I member. Participation in the replenishment should be discussed in the meeting with Management and will be followed by Area. (See III - c - ii above.)

V. POLITICAL SITUATION

The internal situation is stable, and international tensions have eased with the advent of the new regime in Iraq. Kuwait now has an elected parliament, which is assuming considerable importance in financial matters. Some important changes have occurred in the administration, such as the appointment of a Prime Minister (son and heir of the Ruler), the broadening of the Cabinet to include merchants, and the setting up of a Planning Board.

VI. ECONOMIC SITUATION

Population (1961)

321,000, of whom half are citizens. The population appears to have grown substantially in the last two years, mainly as a result of immigration, and may now be approximately 400,000.

Per capita GNP
(1959 estimate)

\$2,700. Since 1959 the increase in income seems to have been balanced by the rapid rise in population.

Oil revenues for the current year are estimated at \$514 million. Production amounted to 92 million tons in 1962 (not including the Neutral Zone), an increase of more than 10 percent over the 1961 figure. At least this rate of increase will be maintained in 1963 as new off-shore concessions come into production. The Government is issuing tenders for a petrochemical plant to produce ammonia. There is talk of reaching agreement with Iraq to obtain water from Shatt-al-Arab for irrigation; this would make some agriculture possible in Kuwait. Public and private construction is booming.

In the past the most important means of sharing oil revenues with the indigenous population has been the Government's policy of purchasing land; such purchases have absorbed about one-third of oil revenues, but now, due to the pressure of public works expenditures, the Government is considering reducing this to roughly one-sixth of oil revenues. Similarly, mounting domestic expenditures, both current and capital, are likely to reduce overseas investment to 10 percent of oil revenues in 1963/64, compared to the 15 percent originally planned.

Attachments:

Copies of letters dated June 11 and August 21, 1963 from Mr. Knapp to the Finance Minister.

JBaneth/OJMcDiarmid/jbt
September 16, 1963

August 21, 1963

His Excellency
Sheikh Jabar Ahmed Al-Jabar Al-Sabah
Minister of Finance and Industry
Government of Kuwait
Kuwait

Excellency:

I just learned from Mr. Svoboda that my letter of
June 11, 1963 about the release of Kuwait's 18% sub-
scription to the Bank's capital has not reached you. I
am therefore attaching herewith a copy of that letter.

Sincerely yours,

J. Burke Knapp

J. Burke Knapp
Vice President

Encl.

JBaneth:pm

cc: Messrs. Wilson
Fligler
Victor C. Chang

C O P Y

June 11, 1963

His Excellency
Sheikh Jabar Ahmed Al-Jabar Al-Sabah
Minister of Finance and Industry
Government of Kuwait
Kuwait

Excellency,

We were extremely gratified upon hearing that during your recent conversations with Mr. McDiarmid, from the Bank's staff, you indicated your country's willingness to release on a fully convertible basis its 18% paid-in capital subscription to the Bank for use (and subsequent re-use) in the Bank's operations. This release will be of great assistance to the Bank and will enhance its international character.

We are fully aware of the many demands falling upon Kuwait's financial resources at present. The Bank would therefore deem it acceptable if the release of Kuwait's 18% subscription were effected gradually in, say, four semi-annual installments. We would appreciate it if you would let us know if this proposal is agreeable to your Government.

Sincerely yours,

(signed)

J. Burke Knapp
Vice President

cc: Mr. Wilson
Cleared with and cc: Messrs. Fligler, Victor C. Chang

LEBANON

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LEBANON

BRIEFING PAPER

I. MEETING WITH DELEGATION

Friday, October 4

9:40 a.m. for 20 minutes

Attended by: Mr. Knapp
Mr. Rosen

Mr. Reid
Mr. Mason
Mr. Bart

II. MEMBERS OF DELEGATION

Andre Tueni

Governor (IMF)
Director General of Finance,
Ministry of Finance

Raja Himadeh

Deputy Governor (IBRD)
Government Commissioner to
Banque de Credit Agricole,
Industriel et Foncier,
Ministry of Finance

Farid Solh

Deputy Governor (IMF)
Deputy Undersecretary of Finance
Ministry of Finance

Elias Sarkis

Governor (IBRD)
Director General of the Civil
Cabinet in the Presidency of
the Republic

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

- (a) State of relations (prospects include reactivation of the Litani River project and development banks for agriculture and industry)

(i) After two years of relative inactivity, the Bank's relations with Lebanon have become somewhat more active. Difficulties with the Litani River project appear to be on the way to solution. Early this year the Bank agreed with the Litani River Authority on the documents to be exchanged, a revised amortization schedule, and the other steps that must be taken before disbursements can be resumed. The first and most important step--namely, the appropriation by Government of funds required to complete the Litani project--was accomplished in May; it is expected that subsequent steps will follow without much further delay and that full disbursements can be resumed before the end of the year.

(ii) A recent development, which might pave the way for future lending, was the Bank/IFC mission, headed by Mr. Kuiper, which went to Lebanon in May, at the Government's request, to advise about a proposed national development bank. The mission recommended that separate credit institutions be established for industry and agriculture. Mr. Woods wrote to the President of the Republic in July, indicating that the Bank was prepared to assist in the establishment of the proposed agricultural bank and that IFC would be willing to consider participating in a private industrial bank (letter attached). No reply has yet been received.

(iii) In January 1963 the Government requested an IDA credit of \$50 million to assist in the scheme for land reclamation and afforestation known as the "Plan Vert". In reply we pointed out that the project seems to require further feasibility studies and that the available economic data indicate that Lebanon's creditworthiness would warrant Bank rather than IDA financing.

- (b) Topics likely to be raised by delegation

(i) Lebanon's eligibility for IDA credits: The development program which is being formulated by the Government for the five-year period 1964/68 is expected to require \$400 million of public investments, which would be financed from increased taxes and/or external borrowing. Therefore, it is possible that the delegation will inquire about Lebanon's eligibility for IDA financing. There has been no Bank economic mission to Lebanon since 1955, and the economic data currently available are incomplete; nevertheless, Lebanon is clearly too wealthy and too creditworthy to receive IDA assistance as long as IDA resources are as limited as they now are. There is no apparent bar to Bank lending, but if Lebanon intends to apply for assistance for new projects, a small economic mission should be sent to explore the situation more thoroughly.

(ii) IBRD and IFC assistance to the proposed agricultural and industrial banks: Management would repeat what Mr. Woods wrote in July: namely, that the Bank is prepared to consider assistance to an agricultural bank and IFC could help an industrial bank; the delegation would be asked for the Government's reaction to the idea of two specialized institutions and to the kind of assistance we propose. (See III (a) (ii) above and letter attached)

(c) Topics to be raised by Management

(i) The Guarantee Agreement for the Litani project stipulates that the Government will cause its Electricity Agency and other public distributors to purchase all power generated by the Litani. To date it seems that no steps have been taken by the Government, and we should ask what steps are proposed to fulfill this stipulation in the agreement.

(ii) Since the loan was made in 1955, changes in the scope of the Litani project have shifted the emphasis somewhat from power generation to irrigation. The Litani River Authority has been authorized to prepare an irrigation program for the entire southern half of the country, but steps taken so far are inadequate to ensure a prompt and efficient utilization of the water already available, let alone the much more abundant supply that is now being stored behind the barrage. The delegation's attention might be drawn to the possibility and indeed the necessity of having irrigation studies conducted by internationally recognized consultants rather than by the small staff that is at present available within IRA.

IV. BACKGROUND INFORMATION

(a) Bank loans as of August 31, 1963

Date	Borrower	Purpose	Amount (equivalent in \$ million)
Aug 25/55	Litani River Authority	Power and Irrigation	27.0 ^{1/}
	Total (net of cancellations and refunding)		27.0
	of which has been repaid		2.2
	Total now outstanding		24.8
	Amount sold -	-	
	of which has been repaid -	-	
	Net amount now held by the Bank		24.8

^{1/} Includes \$9.8 million not yet disbursed.
The whole amount is effective but disbursements on part of the project have been temporarily suspended, as explained in III (a) (i).

(b) IDA credits

None.

(c) 18% Capital Subscription (\$0.8 million)

Entire 18% paid and lent in U.S. dollars.

(d) Holdings of World Bank bonds

None.

(e) I.F.C.

Member. Subscription \$50,000. A development finance corporation and two other industrial projects are under study.

(f) I.D.A.

Part II member.

V. POLITICAL SITUATION

The prevailing impression is that both the factions of the bitter civil war of 1958 are increasingly willing to resolve their differences--though at the least common denominator--and to maintain Lebanon's independence vis-a-vis the UAR and Syria. The country has been unusually calm during recent months when talk of unity between Egypt, Syria and Iraq was common; even Arab nationalist circles refrained from taking a stand which would endanger the modus vivendi reached after 1958.

The internal scene continues to be dominated by the personality of President Chehab. The main issue during the coming year is likely to be whether he will accept or reject an amendment to the Constitution, which would permit his re-election. Public opinion is unusually unanimous in requesting him to accept a second mandate when his present term expires in September 1964.

VI. ECONOMIC SITUATION

<u>Population</u> (1963 estimate)	1.8-2 million, growing at 2.5 percent per annum
<u>Per capita GNP</u> (1961)	\$345
<u>Average annual growth</u> (1954-1961)	
Gross national product	6 percent
Per capita GNP	4 percent
Industrial production	4 percent
Agricultural production	5.5 percent

There are no reliable data regarding recent trends in national income or in the balance of payments. Such data as are available for external trade, banking and building indicate that the economy has continued to progress over the last year. Increased Government spending for development purposes, although depleting official reserves somewhat, has put an end to the liquidity crisis of the preceding two years. The currency, fully backed by gold, remains strong, even though total money supply increased by 14 percent in 1962. The main problem in the coming year will be the financing of a new development program, for which an annual average of \$80 million in public investments is expected during the period 1964/68. The balance of payments has so far showed a surplus, owing mainly to the continuing inflow of flight capital from neighboring countries. At the same time, however, trade with these countries through Lebanese middlemen has decreased, although the level of activity in other service industries remains high and in the case of tourism may have grown slightly. Manufacturing continues to expand, albeit slowly, except for the textile sector which is facing a severe crisis. The citrus and apple crops have continued to command sizeable markets abroad.

Attachments:

Letter of July 26, 1963 from Mr. Woods to President Chehab.

MPBart/wh
September 17, 1963

His Excellency
General Fouad Chehab
President of the Republic
Beirut, Lebanon

July 26, 1963

Dear Mr. President:

Because of the interest which you have taken personally in the creation of a National Development Bank, I am writing to you to inform you of the findings of the mission, consisting of Messrs. Kuiper and Bart, which at the request of your Government was sent to Lebanon in May to advise on this subject. Permit me first to express my appreciation for the cordial reception accorded to Messrs. Kuiper and Bart by your Government and for the privilege given to them of acquainting themselves with your thinking on this subject.

I am pleased to transmit to you the enclosed report of the Bank's consultant, Mr. E.T. Kuiper, on the proposal for a national development finance institution. Mr. Kuiper has reported on the discussions which he had with you and with members of your Government on the kinds of institutions required by Lebanon to promote its economic development.

We have also studied the IRFED mission's proposals and are impressed with the work which has been done. We have given careful consideration to the question raised by IRFED as to whether it would be more advantageous to have one institution to deal with the financing of development or to have more than one institution, each of which would specialize in certain fields.

Our experience in many countries has shown that it is usually of great advantage to have two institutions, one which looks after industrial development and one which looks after agricultural development. We therefore thoroughly endorse the recommendation in the Kuiper Report that Lebanon should consider having two institutions.

Mr. Kuiper suggests, and I agree, that the industrial finance corporation should be established under private control with as large a participation as possible from the Lebanese and foreign commercial banks. The purpose of the corporation would be to cater for the medium and long-term credit requirements of self-liquidating projects in the industrial field. Under these circumstances I would be prepared to consider a participation of the International Finance Corporation in the capital of this institution, subject to working out to our mutual satisfaction the capital structure, operating policies and arrangements for experienced management.

If this were done there would still remain the need to continue and to expand assistance in the agricultural field. The Bank has taken a great interest in this field in many countries and I am convinced that we should be able to find the means of assisting Lebanon. If you so desire, therefore, I would be prepared to send members of the staff to Lebanon to consult with your Government on the ways and means by which the Bank might assist in the establishment and financing of a development institution for agriculture.

We should also be glad to discuss both with your Government and with suitable representatives of the private sector how an industrial development finance corporation could best be established.

In these circumstances I think it would be appropriate for a mission to come to Lebanon some time in August or September for about a week for further discussions on the establishment of the two institutions which Mr. Kuiper recommends.

I can make arrangements for such a mission as soon as I hear from you that you are in agreement with this proposal and that August or September would be a convenient time for the arrival of such a mission.

Yours sincerely,

George D. Woods

Enclosure

Cleared with Messrs. Beevor and Escott Reid

cc: Mr. Beevor
Mr. Diamond
Mr. Escott Reid
Mr. Mason
Mr. Bart
Mr. Peter Reid

GSMason/uz Bank LH

NEPAT

NEPAL

BRIEFING PAPER

I. MEETING WITH DELEGATION

NO MEETING SCHEDULED

II. MEMBERS OF DELEGATION

Tulsi Giri	Governor (IBRD) Chairman, Council of Ministers and Foreign Minister
Lakshmi Nath Gautam	Governor (IMF) Governor, Nepal Rastra Bank
Yadav Prasad Pant	Alternate Governor (IBRD) Secretary Ministry of Finance
Naresh Man Singh	Alternate Governor (IMF) Professor, Tri-Chandra College
Pushkar N. Pant	Adviser Joint Secretary, Ministry of Economic Planning
Jagdish Shunsher Rana	Adviser Second Secretary, Royal Nepalese Embassy

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

- (a) State of relations (an exploratory mission preliminary to IDA operations is scheduled for October)

Messrs. Mason and Wright visited Nepal in February 1962. Mr. Suzuki visited Nepal in March 1963. A number of Nepalese officials have visited the Bank, including Mr. Shaha, Finance Minister (in October 1961) and Mr. Bahekh Thapa, Secretary of Ministry of Economic Affairs (in March 1962). Mr. Shrestha, Coordinator of Planning and Economic Research, Ministry of Economic Affairs, attended the 1962/63 EDI course, and Mr. Pant, Joint Secretary, Ministry of Economic Planning, will attend the 1963/64 EDI course. The 1963 General Training Program had a Nepalese participant, Udhir Thapa.

Nepal is not considered creditworthy for the Bank, but it is hoped that suitable projects can be found for IDA financing. Nepal became a member of IDA on March 6, 1963, and we have written to the Finance Minister proposing an exploratory mission for the second half of October 1963; this two or three man mission would assess development prospects and seek a suitable project or projects. The Government has replied that its delegation to the Annual Meeting will discuss this matter with us. (Letters attached.) It is likely that IDA will have to assist in the preparation of projects if they are to be developed to the point where they can be appraised.

- (b) Topics likely to be raised by delegation

The delegation may inquire about the prospects for IDA financing of some specific projects. In reply we would seek to ascertain the extent to which suitable projects are prepared from the engineering and organizational point of view; we will indicate that the type of projects they propose will be taken into account in staffing our mission and that, although the primary purpose of the mission will be to assess general economic conditions, it will also want to investigate specific project possibilities.

- (c) Topics to be raised by Management

(i) The character and timing of the proposed exploratory mission (note III-b above).

IV. BACKGROUND INFORMATION

- (a) Bank loans

None.

- (b) IDA credits

None.

(c) 18% Capital Subscription (\$0.9 Million)

No release, The Area Department will mention this problem and suggest the possibility of a release by stages over a reasonable period of time.

(d) Holdings of World Bank bonds

None.

(e) I.F.C.

Nepal applied for membership in August 1963. IFC is awaiting acceptance and payment of subscription before Nepal becomes a member.

(f) I.D.A.

Part II member.

V. POLITICAL SITUATION

The King dismissed Parliament and banned all political parties in December 1961. Later, opposition leaders living as exiles in India were alleged to have incited border incidents as well as several outbreaks of violence within the country; Nepal blamed India for not preventing these hostile activities, and relations were strained. However, more recently, in the wake of the recent India-China conflict, relations between India and Nepal have improved. The Nepalese Government formally maintains a policy of "non-alignment" with respect to India and China, but general sentiment seems to favor India.

In December 1962 the King promulgated a new Constitution which substituted a "partyless panchayat democracy" for the parliamentary system of the 1959 Constitution. Panchayat democracy is organized in tiers with village, city, district and zonal councils (panchayats). The top of this pyramid, a unicameral legislature called the National Panchayat, was inaugurated in April 1963. All executive authority remains with the King, who is advised by a Council of Ministers appointed by the King from among the members of the National Panchayat. A State Council to advise on constitutional problems is also nominated by the King.

VI. ECONOMIC SITUATION

<u>Population (1963)</u>	9.8 million, growing at 1.5 percent per annum
<u>Per capita GNP</u> (1963 rough estimate)	\$50

There are no reliable estimates of national income in previous years nor are production data available.

After completion of the First Five Year Plan in 1961, a Three-Year Plan (1962-65) was undertaken calling for a public outlay of N.R. 670 million (\$88 million). About 84 percent of the outlay would be financed by foreign grants (already pledged from the U.S., India, U.S.S.R. and Mainland China) and external loans, but the Fund reports that Nepalese authorities are also aware of the need to step up efforts to mobilize domestic resources. The Plan concentrates on transport (roads), irrigation and power, but the largest single allocation (23 percent) is for industry, mainly aimed at import substitution. The government-owned Nepal Industrial Development Corporation was set up in 1959 with U.S. assistance and has financed a number of small investments in the private sector, i.e. three hotels, two brick and tile factories, a sawmill, a sugar mill and a rice mill, as well as a small industrial estate at Kathmandu. The Corporation has lines of credit in U.S. dollars, India rupees and German marks and has requested similar assistance from the U.K. and Japan.

Attachments:

- (1) Letter of August 4, 1963 from Finance Secretary to Mr. Escott Reid.
- (2) Letter of July 12, 1963 from Mr. Escott Reid to Minister of Finance.

CWWang/DWJeffries/wh
September 16, 1963

COPY

HIS MAJESTY'S GOVERNMENT

Ref. No: 4/25

Ministry of Finance
Singha Durbar
Kathmandu, Nepal

Date: - August 4, 1963.

Dear Mr. Reid,

This is to thank you for your letter of July 12, addressed to the Hon'ble Finance Minister.

His Majesty's Government appreciates your idea of sending one IDA study-mission to Nepal. I shall discuss this matter in detail, while I will be in Washington during the next Annual Meeting in September.

I am sending herewith two booklets on First Five Year Plan and Second Three year Plan which, I hope, will be useful for you to have some ideas about Nepal's economic development. Please acknowledge the same, and oblige.

With regards,

Sincerely yours,

(signed)

(Y. P. Pant)
Finance Secretary
His Majesty's Government
Finance Ministry.

Mr. Escott Reid,
Director,
Department of Operations
South Asia and Middle East
International Bank for
Reconstruction and Development
Washington 25, D. C.

COPY

July 12, 1963

The Honorable
Surya Bahadur Thapa
Minister of Finance
Katmandu, Nepal

Dear Mr. Minister:

At the last Annual Meeting of the Bank in Washington in September 1962 we agreed that, when Nepal became a member of the International Development Association, the Bank would be ready to send a mission to Nepal to study the economy, to review the programs of economic development included in your present Three-Year Plan and to see if there are any projects which might be suitable for possible IDA financing.

I am very pleased that Nepal has now joined IDA and I would like to propose that a mission visit your country during the coming autumn, probably in the second part of October. I would be grateful if you would let me know as soon as possible if this proposal would be acceptable to your Government, so that we can make the necessary arrangements in good time. It would be most helpful if at the same time you could send us a copy of the final version of your Three-Year Plan and any other documents that the mission might usefully study in advance of its visit.

I hope that you yourself will be visiting Washington at the end of September on the occasion of the Annual Meeting and I look forward to meeting you then.

Sincerely yours,

cc: Mr. J. Burke Knapp
Mr. Geoffrey Wilson
Mr. D. W. Jeffries

Escott Reid
Director
Department of Operations
South Asia and Middle East

EPW:hvs

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PAKISTAN

BRIEFING PAPER

I. MEETING WITH DELEGATION

Tuesday, October 8

10.00 a.m. for 1 hour

Attended by: Mr. Woods
Mr. Knapp
Mr. Wilson
~~Sir William Tiff~~
Mr. Rosen

Mr. Reid
Mr. Mason
Mr. Hartwich
Sir Ernest Vasey

II. MEMBERS OF DELEGATION

* Mohamed Shoaib

Governor, IBRD
Minister of Finance

S. A. Hasnie

Governor, IMF
Governor, State Bank of Pakistan

S.A.F.M.A. Sobhan

Alternate Governor, IBRD
Secretary, Planning Division of
the President's Secretariat

Mumtaz Mirza

Temporary Alternate Governor, IBRD
Executive Director, IBRD

S.M. Sulaiman

Alternate Governor, IMF
Joint Secretary, Ministry of Finance

~~Osman Ali~~

Adviser
Secretary of Economic Affairs
Division

A.G.N. Kazi

Adviser
Economic Minister, Embassy of Pakistan

* Said Hasan

Adviser
Deputy Chairman of the Planning Commission

Munir Husain

Adviser
Economic Counselor
Embassy of Pakistan

* WILL ATTEND,

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

(a) State of Relations (lending slowed down by the Government's slowness in preparing suitable projects)

Consortium countries pledged \$945 million for the second and third years of the Second Plan. On June 30, 1963, the uncommitted portion of these pledges amounted to \$230 million, of which the Bank and IDA accounted for \$119 million. For the fourth year of the Second Plan, Consortium countries pledged \$425 million, of which the Bank accounted for \$30 million and IDA \$50 million. The \$119 million Bank/IDA back-log from the previous two years has now been reduced to \$60 million so that with the \$80 million pledged for the current year we have \$140 million to commit by June 30, 1964. The rate of lending in the past has been held down by the slowness of the Pakistan authorities in formulating and preparing projects. Many of the projects in the list published by the Planning Commission turn out to be vague and nebulous, and many months are required to translate them into practical schemes suitable for financing.

A mission will be in Pakistan in November (1) to discuss the decisions which need to be taken in Pakistan so that we can process two projects already appraised (viz., the Gaja drainage project and extensions to Karachi Port), (2) to appraise three projects already submitted to us (viz., the West Pakistan railways, the East Pakistan railways and roads in West Pakistan) and (3) to try to work out new projects for appraisal at a later date (such as irrigation schemes in East Pakistan, foodgrain storage, roads in East Pakistan, rural development (Comilla) and projects in the private sector larger than PICIC can handle).

An economic mission is planned for early January, whose task is primarily to assess aid requirements for the fifth year of the Plan (1964-65).

(b) Topics likely to be raised by the delegation

(i) Date of next consortium meeting: At present we are planning to hold the first consortium meeting to consider 1964/65 aid requirements in Paris in April and the pledging meeting in Washington in June. However, this depends to some extent on the rate at which Pakistan can commit existing pledges for suitable projects.

(ii) Necessity of softer terms of aid: The Bank has put pressure on consortium countries to furnish aid on terms which would minimize Pakistan's obligations in foreign exchange. A chart circulated at the time of the Indian Consortium meeting

in Paris showed that in order to keep Pakistan's debt ratio reasonably close to its present level, it would be necessary that over 80 percent of future borrowings be on soft terms. Some consortium members (i.e., the United Kingdom and France) have softened their terms. We might ask the delegation what further progress has been made in Pakistan's bilateral approaches.

(iii) Pakistan's Third Five-Year Plan: Mr. Said Hasan, the Chairman of the Planning Commission, ~~who may be at this meeting,~~ will be in Washington during and possibly after the Annual Meeting to discuss the preliminary outline of the third Five-Year Plan (July 1, 1965 to June 30, 1970); the staff welcomed this opportunity for an early discussion.

(iv) Industrial Development Bank of Pakistan: Mr. Shoaib has taken a personal interest in our financing this project. We have asked Sir Ernest Vasey to find out whether the Government would be prepared to take steps which would permit us to finance IDBP: e.g., by making IDBP basically a private bank which could be operated profitably. If Shoaib is prepared to take this approach, we would send someone to take a preliminary look at the IDBP. We have also suggested that an alternative method of providing foreign exchange financing for medium-sized industrial projects would be to lower PICIC's lending limits; IDBP could then concentrate on smaller industrial loans and loans for social purposes.

(v) Banning of imports: The usual manner in which a developing country limits imports (in order to reduce the pressure on its foreign exchange position) is either by a protective tariff or quantitative restrictions. In the fairly recent past Pakistan has resorted to another more extreme method, i.e., complete banning of a growing list of items. These items are not luxury goods but such articles as electric motors, paints, fans, lamps, explosives, pumps, galvanized iron pipe, etc. We do not know whether the intention is to protect industry or to preserve foreign exchange, but banning imports seems less easily acceptable than a tariff or quota since it removes any pressure on the indigenous manufacturer (who in many cases has little or no competition within Pakistan itself to maintain competitive prices and acceptable quality). We have run into difficulties because of the banning of imports in both the Indus Basin Settlement and the Khairpur Irrigation Project (for ground water and salinity control). In the case of the Indus Basin Settlement the banning of items came after contractors had made arrangements for importation; fearing delay in the completion of the works procedures have been arranged whereby

contractors could make an ad hoc case for the importation of banned items, but this is not working very well, particularly since the banned list seems to grow constantly. The Khairpur project depends largely on pumping saline water from the water table. The pumps required for this need to be protected by special metals against saline conditions. Pumps are among the banned items, and we have been concerned more with the question of quality than the price of the Pakistani substitute. We consider it essential that the contractors be able to choose freely the equipment which they would install on their own responsibility and whose performance they would have to guarantee. As a compromise we have proposed to the Pakistan Government that the tender documents require any bidder who offers goods manufactured outside Pakistan and presently banned from importation to submit an alternative bid using Pakistan pumps.

~~(vi) Indus: A meeting of the Indus Club is planned for September 25. After that meeting a separate brief on Indus will be prepared.~~

(c) Topics to be raised by Management

(i) Plans for the next consortium meeting if not raised by the delegation (see III-b-i above).

(ii) Pakistan's slow rate of commitment and disbursement of funds pledged: For 1961/63 Pakistan predicted a disbursement of over \$900 million. Actually only about half this amount was disbursed, and only \$715 million committed. Pakistan has consistently overestimated its rate of disbursement. This will have a decisive bearing on how much can be asked and obtained at the next consortium meeting. Pakistan should start preparing projects much earlier than is now the practice and policy decision making should be accelerated. A mission will be in Pakistan in November to appraise projects which Pakistan has submitted to the Bank and IDA for financial assistance, and the Pakistan Government should see that such projects have been thoroughly prepared. Also, the two Provincial Governments should strengthen their administrations, so that once the funds are committed the project can be carried out according to schedule and without the delays we have experienced recently in some Bank and IDA projects.

~~(iii) Indus: A separate brief, prepared after the Indus Club meeting of September 25, is attached.~~

(iv) Outstanding operational issues: Lack of good organization and management slow the work of many agencies, particularly in East Pakistan. The political situation in East Pakistan is such that only Bengalis can hold key positions, and it is among them that managerial and organizational talent is apparently scarcest. We should stress the importance of improving organization and management, since this is one of the main impediments to economic progress.

IV. BACKGROUND INFORMATION

(a) Bank Loans as of August 31, 1963

	Amount (equivalent in \$ million)
Total (net of cancellations and refundings)	299.2 ^{1/}
of which has been repaid	<u>41.6</u>
Total now outstanding	257.6
Amount sold	12.7
of which has been repaid	<u>8.3</u> <u>4.4</u>
Net amount now held by Bank	253.2

^{1/} Includes \$137.2 million not yet disbursed.
Whole amount effective.

Loans made from July 1, 1961 to August 31, 1963

Date	Borrower	Purpose	Amount (equivalent in \$ million)
Sep.14/62	Pakistan	Railways, West Pakistan	18.25
Sep.14/62	Pakistan	Railways, East Pakistan	4.75
Feb.13/63	PICIC	Industry	<u>20.00</u>
		Total	43.00 ^{1/}

^{1/} Includes \$36.6 million not yet disbursed: \$12.0 million for West Pakistan railways, \$4.3 million for East Pakistan railways and the full \$20.0 million for PICIC.
Whole amount effective.

(b) IDA Credits as of August 31, 1963

Date	Borrower	Purpose	Amount (equivalent in \$ million)
Oct.19/61	Pakistan	Dacca-Demra irrigation	1.0
Nov.22/61	Pakistan	Inland ports	2.0
Jun.29/62	Pakistan	Khairpur irrigation	18.0
Nov. 2/62	Pakistan	Industrial estates	6.5
Jun.26/63	Pakistan	Brahmaputra flood embankment	5.0
Jul.26/63	Pakistan	Chandpur irrigation	9.0
Aug.16/63	Pakistan	Dacca/Chittagong water supply and sewerage	<u>50.0</u>
Total:			91.5 <u>1/</u>

1/ Includes \$90.7 million not yet disbursed.
Includes \$64.0 million not yet effective.

(c) 18% Capital Subscription (\$18.0 million)

Due to balance of payments difficulties, Pakistan has released only \$0.2 million on a convertible basis; the rest of its subscription is only available for purchases in Pakistan.

(d) Holdings of World Bank bonds

None.

(e) I.F.C.

Member. Subscription \$1.1 million. Four investments totalling \$5.8 million have been made. Projects under study include Sui gas extension, pulp and paper, and National Steel.

(f) I.D.A.

Part II member.

V. POLITICAL SITUATION

The Government seems under less pressure from old line politicians than late in 1962. This may be because the heightened controversy with India has taken people's minds off local politics. Last spring an emergency session of the National Assembly was called as a result of

the supply of arms to India by Western countries. Later the Government of Pakistan said that it would not hesitate to call upon "the largest power in Asia" -- meaning Red China -- for protection, if needed. A "Political Parties Act" was passed by the Legislature, forbidding any political party prejudicial to Islamic principles or to the security of the country. The transfer of executive responsibilities from the Center to the two Provinces has continued. Since the Provincial Administrations are not well equipped to handle these new responsibilities, the public sector development program has been slowed down.

VI. ECONOMIC SITUATION

<u>Population</u> (1963 Bank estimate)	98 million, growing at
East Pakistan: 53 million	2.2 percent per year
West Pakistan: 45 million	

<u>Real income per capita</u> (1961/62)	\$75
---	------

<u>Average annual growth</u> (1951/52 to 1961/62)	
---	--

Net national product	2.6 percent
Per capita NNP	0.4 percent
Industrial production	14.8 percent
Agricultural production	2.3 percent

The most important recent economic developments in Pakistan are the adoption of new tax measures in the Government's budget for 1963/64, measures by the State Bank to restrict private bank credit and climatic conditions which adversely affected agriculture in 1962/63. The new tax measures are expected to increase revenues by about 13 per cent as compared with 1962/63. These tax measures will apply primarily to accumulated wealth, to the large profit margins now being earned by Pakistan's industrial enterprises and to some less essential consumer goods. Industrial production is maintaining its rate of increase of 6 to 7 percent per annum. However, agricultural production has suffered considerably from both storms and drought; except for cotton, the setback is general for all major crops. Consequently, overall growth in GNP in 1962/63 has been about 1 percent ~~above the previous year's level~~ compared with the 5 or 6 per cent growth rate enjoyed in the first two years of the Plan.

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SAUDI ARABIA

BRIEFING PAPER

I. MEETING WITH DELEGATION

NO MEETING SCHEDULED

II. MEMBERS OF DELEGATION

Ahmad Zaki Saad

Governor (IERD/IMF)

Executive Director (IMF)

Counselor to His Majesty King Saud

Abid M.S. Sheikh

Alternate Governor (IMF)

Minister of Commerce and Industry

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

(a) State of relations

There has been no operational contact with Saudi Arabia during the past year, and there are no lending prospects for the immediate future.

(b) Topics likely to be raised by delegation

None.

(c) Topics to be raised by Management

None. Area will ask Anwar Ali to give a general report on the development effort.

IV. BACKGROUND INFORMATION

(a) Bank loans

None.

(b) IDA credits

None.

(c) 18% Capital Subscription (\$6.6 million)

No release. Area will discuss this matter with the delegation.

(d) Holdings of World Bank bonds

None at present but an \$8 million subscription to the new issue is expected by the Treasurer.

(e) I.F.C.

Member. Capital subscription \$111,000. No operation.

(f) I.D.A.

Part II member. Capital subscription \$3.7 million.

V. POLITICAL SITUATION

Under the impact of the Yemeni revolution in September 1962, Prince Faisal, brother of the King, was reinstated as Prime Minister in order to strengthen the regime and to give guidance to gradual reforms, including the total abolition of slavery, a movement toward more representative government and increased emphasis on development.

Relations with the rest of the Arab world, especially with Egypt and other "liberated" countries, are bad because of the Yemeni conflict in which Egypt supports the republican regime and Saudi Arabia the royalists. However relations are good with Jordan, which has supported Saudi Arabia on the Yemen issue.

VI. ECONOMIC SITUATION

Population (1960 estimate) 5 million

No statistics are available on GNP or on industrial and agricultural production.

Oil production (1962) 7 1/4 million metric tons

Oil royalties (1962) \$39 1/4 million

Saudi Arabia's economic position continues to improve. Oil production and oil revenues were respectively 7 percent and 9 percent higher in 1962 than they were in 1961, and they continued their increase in the first part of 1963.

Recently an agreement was reached with Aramco and TAPline on various outstanding issues. This will increase future oil revenues per ton on the basis of present prices. The agreements also provide for substantial back payments, which will be allocated to a special fund for economic development.

Saudi Arabia's budget for 1963 balances at Riyals 2,452 million (\$545 million), an increase of 16 percent over 1962. Allocations for development projects now amount to Riyals 550 million (\$122 million), an increase of 37 percent over the previous year. One quarter of development expenditures is allocated to transport and communications; other large allocations are for municipal development, education, irrigation and agriculture, and the construction of mosques. Last year Saudi Arabia finished repaying the public debt, both internal and external, which had accumulated during the period of crisis around 1956/57.

Financially, the situation is extremely sound. Official gold and foreign exchange reserves continue to rise and in May 1963 stood at Riyals 1.5 billion (\$334 million), an increase of almost 50 percent since May 1961. However, reports from IBERD-alumnus Harold Folk, who was in Washington early this year, indicate that administrative limitations still severely restrict meaningful development activities in Saudi Arabia.

SYRIAN ARAB REPUBLIC

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SYRIAN ARAB REPUBLIC

BRIEFING PAPER

I. MEETING WITH DELEGATION

Wednesday, October 2, 1963 9:20 a.m. for 20 minutes

Attended by: Mr. Knapp Mr. Reid
 Mr. Brakel
 Mr. Baneth

II. MEMBERS OF DELEGATION

George Tomeh	Governor, (IBRD/IMF) Minister of Economy
Adnan Farra	Alternate Governor (IMF) Governor, Banque Centrale de Syrie

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

(a) State of relations (\$8 million road credit imminent)

(i) In January, after much deliberation, Syria decided to apply to IDA for a road credit. Economic and technical missions visited Syria in April. On August 21 the Government was invited to send a delegation to negotiate an agreement for a \$8 million road credit; by mid-September no reply to this invitation had been received. No other operations are contemplated for the time being.

(ii) At various times the Bank has been approached informally by Germany in connection with the building of a High Dam on the Euphrates, but the Bank was not involved in the German-Syrian agreement concluded in February 1963. However, a side letter to that agreement obligated the Syrians to a macro-economic study conducted by consultants agreeable to IBRD. The Syrians asked the Bank's opinion about their selection (The Netherlands Economic Institute); Mr. Knapp replied on March 29 that this seemed satisfactory, but he expressed some misgivings about the vagueness of their proposed terms of reference. Subsequently, the economic mission discussed these misgivings with the Chairman of the Euphrates Project Board who agreed to review our comments with Professor Tinbergen.

(iii) As a result of discussions and agreement with the previous regime, Sir Leslie Melville and Mr. Steuber were in Syria from April to June 1963. Most of their recommendations relative to the organization of the planning machinery seem to have been adopted. Nevertheless, it seems unlikely that the planning effort can become very effective in the near future because of the political preoccupations of the Government and the lack of sufficient data about large projects.

(b) Topics likely to be raised by delegation

(i) Future lending: If the question of future loans should be raised, the reply should be that the road project should first be put in hand. Reference should also be made to the need for Government action to avoid a serious economic crisis in the short run and to coordinate long-range plans for public investment and savings (See Section VI).

(ii) Planning: If the delegation asks for a planning adviser the reply should be, as in Mr. Knapp's letter of July 29: namely, that the Bank would be prepared to discuss further planning assistance when the NEI study has been completed and more is known about the Euphrates project. (A copy of the letter is attached.)

(c) Topics to be raised by Management

None.

IV. BACKGROUND INFORMATION

(a) Bank loans

None.

(b) IDA credits

None.

(c) 18% Capital Subscription (\$1.8 million)

No release, and balance of payments difficulties preclude release at this time. Syria has requested that its capital subscription be increased by two-thirds; subject to approval of a similar request by the Executive Board of the IMF, this application will be considered by the Governors during the annual meeting.

(d) Holdings of World Bank bonds

No bonds but \$350,000 of Borrowers' obligations reported by *the* Treasury.

(e) I.F.C.

Member. Capital subscription \$72,000. No operation and limited prospects.

(f) I.D.A.

Part II member.

V. POLITICAL SITUATION

Syria has not had a stable government for many years, and instability increased after Syria's ties with Egypt were severed in September 1961. On March 8 the latest coup resulted in the establishment of a regime headed by a "National Council of the Revolutionary Command", in which the Baath party is dominant. The desire for union with Egypt and Iraq is a basic tenet of the regime; tripartite talks held in Cairo resulted in the proclamation of a new UAR, the constitution of which was to be presented to a referendum in September. However, within Syria the Baathists have eliminated all other factions from power. Iraq is also dominated by the Baath, and President Nasser refuses to join in a federation where the Baath would have a controlling majority. The outlook for Syria is one of continued instability, as the division of the country into numerous political factions is compounded by personal rivalries and ambitions.

Syrian coups d'Etat have generally been bloodless. However, a number of participants in an attempted coup against the present regime have been executed in July. Also, while previous revolutions have left the civil service, even in its upper strata, largely unaffected, the present regime did remove several top career officials, including the Governor of the Central Bank, Mr. Husni Sawwaf, who has been our main point of contact with Syria, and the Secretaries General of most major ministries. Sawwaf was replaced on May 3 by Nouralla, the Director of the Agricultural Bank; the latter was in turn removed in mid-August and replaced by Mr. Farra, a director in the Central Bank under Sawwaf, and general regarded as competent.

VI. ECONOMIC SITUATION

Population (1962) ^{5.0}
~~4.8~~ million, growing at 2-1/2 percent
per year

Per capita GNP (1962) \$150

Average annual growth (1953-1962)

Gross national product	4.4 percent
Agricultural production	3.5 percent
Industrial production	5.5 percent

Until 1957 Syria's economy made very good progress, thanks largely to private initiative. From 1958 through 1961 under the UAR, a drought of unprecedented severity, aggravated by inflationary fiscal and monetary policies and in 1961 by control and nationalization measures, caused a foreign exchange crisis. After the break up of the UAR in September 1961, a stabilization program worked out in cooperation with the IMF ended the Government's reliance on bank credit. In mid-1962 the nationalization and exchange control measures were rescinded. Good rainfall and a record crop in 1962 resulted in high exports. However, the relaxation of restrictions and greater business confidence also stimulated imports. The return of private confidence was only partial, and, despite some improvement, the country's foreign exchange position remained quite weak.

A new coup occurred in March 1963; the present regime has reinstated exchange control and renationalized all banks. Private confidence is again low and industry is likely to stagnate. Disappointing earlier expectations, this year's crop turned out to be just average. As there has been a substantial flight of capital, serious balance of payments difficulties can be expected.

Over the next few years several medium sized agricultural schemes now under way should be completed; therefore, both production and exports (notably of cotton) should increase substantially. In the longer run Syria is committed to heavy public investment, but it is impossible to say at what pace projects will actually go ahead. Foreign exchange for these schemes has already been secured through bilateral agreements, but it will be very difficult to raise the necessary local funds. Inflationary pressures and/or an undue lengthening of project completion time may result; in either case, the country's economic growth would be slowed down.

Attachment: Copy of Mr. Knapp's letter of July 29, 1963 to Planning Minister.

JBaneth/GV/wh
September 16, 1963

July 29, 1963

Minister of Planning
Damascus, Syria

Your Excellency:

We were very pleased to learn on the return of Sir Leslie Melville and Mr. Steuber from Damascus about your decision to reorganize Syria's planning machinery. We hope that you have now found it possible to give full effect to your decision. As will be evident from our previous correspondence, we believe that the type of organization now proposed will provide a firm basis for effective planning in your country, especially in conjunction with the important changes you have made in your own ministry and the proposals to strengthen the planning units in other ministries and agencies responsible for development.

All of this is of particular importance in view of the fact that for nearly ten years two large development projects, the Euphrates dam and the new railway line, will absorb a large part of the funds which are likely to be available for public investment from domestic and foreign sources. Even with a drastic change in fiscal policies aimed at raising the level of public savings substantially, it may well prove difficult to finance both of these enterprises at the same time and carry them to completion at a reasonable pace without curtailing other essential public investment. A good planning organization will be needed to assemble the facts and the considerations that the Government will have to take into account in reaching decisions on the major problems that are bound to arise.

The visit of Sir Leslie Melville and Mr. Steuber and their report on the organization and management of economic and social planning in Syria, which you have used in making your own decisions, were in accordance with the arrangement made in correspondence between us. The arrangement was set out in my letter of March 1, 1963. I referred also to the possibility that this initial visit of from three to four months might be followed by a longer assignment. I understand from Sir Leslie that the Government would like to defer consideration of possible further Bank assistance for a few months until you have more complete data needed for effective development planning.

We shall be glad to review our arrangement with the Syrian Government whenever you find it convenient to do so. Would you agree with our view that before arranging for an advisor from the Bank to visit Syria we should

wait until the results of the study of the Netherlands Economic Institute on the macroeconomic aspects of the Euphrates dam project become available?

The road project about which Mr. Stevenson cabled you on June 17 is still under review. Because of the vacation season we are not likely to be able to send you our decision until next month. The Minister of Communications has also been inquiring about the project and I should appreciate it if you would inform him of the delay.

Sincerely yours,

J. Burke Knapp
Vice President

Sir Leslie Melville/SM Tolbert/JBaneth:pm

cc: Mr. Wilson
Sir Leslie Melville

UNITED ARAB REPUBLIC

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UNITED ARAB REPUBLIC

BRIEFING PAPER

I. MEETING WITH DELEGATION

Saturday, September 28, 1963

12 noon for one hour

Attended by: Mr. Woods
Mr. Knapp

Mr. Reid
Mr. Wright
Mr. Brakel
Mr. Tolbert

II. MEMBERS OF DELEGATION

A.M. El Kaissouni

Governor (IBRD)
Minister of Treasury and Planning

Abdel Hakim El Rifai

Governor (IMF)
Governor, Central Bank of Egypt

Hamed El Sayeh

Alternate Governor (IBRD)
Undersecretary, Ministry of
Economy

Hussein Khallaf

Alternate Governor (IMF)
Chairman, Banking Organization

Abdel Rahman Hamoud

Adviser
Ministry of Economy

A. Guerguis Marzouk

Adviser
Central Bank of Egypt

Ahmed Kishty

Adviser
Secretary to Dr. Kaissouni

III. STATE OF RELATIONS AND TOPICS FOR DISCUSSION

- (a) State of relations (progress toward settlement of nationalization claims and improved economic policies have been stated as preconditions of further operations)

An economic mission from the Bank visited the UAR last autumn. Its report was sent to the Government on February 1 with a letter from Mr. Woods to Dr. Kaissouni, stressing the need for measures to bring the Egyptian economy back into balance and stating that no operation could be contemplated until satisfactory steps have been taken towards settlement of claims arising from the nationalization of foreign property. (Copy attached.) The letter also stated that a consortium of aid-giving agencies, in which the Egyptian Government had expressed interest, could only be discussed when Bank/IDA are also in position to lend.

After considerable discussion and correspondence as well as adjustments in the report to take account of the Government's comments, the UAR authorities still held that the report was unduly influenced by the bad crop in 1961 and therefore was too pessimistic. In early June it was therefore decided that the report would not be circulated and that if and when present obstacles to Bank/IDA lending have been removed, a small mission would be sent to Egypt to up-date the report. It was also agreed that the annual meeting would be a suitable occasion to discuss further the points raised in Mr. Woods' February letter. (Mr. Woods' letter dated June 6, 1963 also attached.)

If the Bank was satisfied on the points raised in Mr. Woods' letters, we would envisage a \$25 million Bank loan for the Suez Canal and given suitable projects, \$30-40 million in IDA credits, mainly for the agricultural sector.

- (b) Topics likely to be raised by delegation

Dr. Kaissouni is known to be seeking substantial amounts of additional foreign aid to tide the country over another year in the face of continued acute balance of payments difficulties. The delegation will therefore almost certainly inquire about Bank/IDA lending prospects and may propose a loan for the Suez Canal as a special case to be considered separately from the issues of compensation and general economic performance. If so, we should repeat the points made in Mr. Woods' June letter, including the need for another look at the economic situation. The arrangements whereby Suez Canal revenues are set aside to meet amortization and interest payments on the Bank's loans do not in any way affect the fact that Canal projects cannot be considered for Bank financing until there is real progress on the other major issues.

(c) Topics to be raised by Management

We should inquire about progress on the compensation question and about the measures taken in order to reduce economic disequilibria. It seems advisable to take the initiative in raising these issues, since Mr. Woods' letters asked that the Bank be kept informed; furthermore, the issues will have to be mentioned if, as is almost certain, the delegation proposes projects for lending, and it would seem wise to discuss these questions as intrinsically important rather than as the Bank's "excuse" for not lending.

IV. BACKGROUND INFORMATION

(a) Bank loans as of August 31, 1963

<u>Year of Loan</u>	<u>Borrower</u>	<u>Purpose</u>	<u>Amount (equivalent in \$ million)</u>
1959	Suez Canal Authority	Suez Canal development	<u>56.5</u>
	Total (net of cancellations and refundings)		56.5
	of which has been repaid		<u>4.0</u>
	Total now outstanding		52.5
	Amount sold	5.5	
	of which has been repaid	4.0	<u>1.5</u>
	Net amount now held by Bank		51.0

(b) IDA credits

None.

(c) 18% Capital Subscription (\$19.6 million)

No release. In view of Egypt's very tight reserve position, no convertible release would be conceivable; there seems to be no point in raising the issue.

(d) Holdings of World Bank bonds

None.

(e) I.F.C.

Member. Capital subscription \$590,000. No current operation and very limited prospects.

(f) I.D.A.

Part II member. Capital subscription \$6.03 million.

V. POLITICAL SITUATION

Internally, President Nasser's Government seems assured of continued stability. The President himself is popular, and has retained the Army's full support. Moreover, the opposition has been financially weakened by nationalization measures and is suppressed by totalitarian methods. Authority is still very much concentrated in the President's hands, and under him it appears to be the Prime Minister Ali Sabry, who is mainly responsible for running the Government.

Relations with the West and especially the United States are fairly good, as are those with the U.S.S.R. No change in "positive neutrality" is to be expected, for that line has enabled Egypt to retain its independence and to obtain valuable aid from both East and West.

The tripartite federation announced in April will not materialize in the near future, mainly because the Baath leadership in Iraq and Syria is unwilling to submerge itself in a single party dominated by President Nasser, and conversely, Nasser does not want a federation which could possibly be dominated by the Baath. Arab unity is still an important preoccupation, and Nasser's appeal to a wide section of Arab nationalists everywhere is considerable. While recent press reports have announced the acceleration of troop withdrawals, the UAR continues to be heavily involved militarily in the Yemen; the weight of this burden on the budget and on foreign exchange resources is uncertain, but no doubt heavy.

VI. ECONOMIC SITUATION

<u>Population</u> (1963)	²⁸ 27 million, growing at 2.7 percent per annum
<u>Per capita GNP</u>	About \$150
<u>Average annual growth</u> (last five years)	
Gross national product:	5 percent
Agricultural production:	2.5 - 3 percent
Industrial production:	10 percent

Quite rapid economic growth has occurred in the UAR in recent years, especially in the field of industrial production. However, because voluntary savings were insufficient to finance the levels of investment contemplated by the Government, there was heavy reliance on foreign borrowing (often suppliers' credits) and on domestic credit expansion. Inflation was repressed by strict price controls and subsidies on basic commodities, but these subsidies further reduced the volume of public savings. As a result, despite the receipt of more than \$400 million of P.L. 480 assistance in less than four years, a large foreign debt has been accumulating. As of

June 30, 1962 debts repayable in foreign exchange were estimated at \$960 million, excluding military credits; it has been estimated that, if military credits are included, external debt service will absorb something like 20-25 percent of foreign exchange earnings on current account during the next few years. Exchange reserves have been sharply reduced (from the equivalent of \$260 million at the end of 1958 to \$80 million at the end of 1961). At the end of 1962, following a bad crop year, monetary liabilities (including net drawings on IMF) exceeded assets by approximately \$90 million.

Last year the multiple exchange rate system was simplified and the pound devalued. However, these steps were partially offset by changes in taxes and subsidies. Price controls and consumption subsidies have been maintained, and steps sufficient to reduce the inflationary impact of government spending have not been taken. This view is shared by the IMF mission, which visited the UAR in March 1963 and found that in spite of the stabilization program to which the Government had agreed at the time of the 1962 stand-by arrangement serious disequilibria still persisted.

According to the 1963/64 budget estimates, public expenditures continue to increase, although at a lower rate than in past budgets. Increases in the prices of some consumption goods--sugar, liquor, tobacco--have been announced, to be achieved through higher taxes or lower subsidies. The budgetary impact of these measures has not been estimated but is probably not very large.

In August the press reported a tendency towards unintended price increases; statistical data are not yet available to show their extent. Also in August most remaining private or semi-private industrial, mining and transportation enterprises of some size were nationalized. Very few of these were foreign.

Attachments:

- (1) Copy of letter dated February 1, 1963 from Mr. Woods to Mr. Kaissouni.
- (2) Copy of letter dated June 6, 1963 from Mr. Woods to Mr. Zando.

JBaneth/EPWright/wh
September 16, 1963

June 6, 1963

Dear Mr. Minister:

Thank you for your letter of May 13, 1963 about the draft economic report on the United Arab Republic. I note that you still believe that the general tone of the report is influenced by the crop failure of the 1961 season and therefore does not reflect the normal growth of the economy. I note further your feeling that 1961/62 data are now practically out of date, and your willingness to make all current information available in whatever way is most convenient to us.

In the circumstances, however, I would suggest that rather than proceeding now with further discussions of a draft which we think made due allowance for the temporary effects of the bad harvest of 1961 but may by now be rather out of date, we should set the matter aside until the occasion of the Annual Meeting. By then the budget for the coming year (1963/64) will be available and more will be known about the steps which your Government is taking to bring the economy into balance. At that time, too, we could discuss the disposition of claims arising from the nationalization of foreign property, about which subject I should appreciate being kept currently informed. As I said in my letter of February 1, 1963 to Dr. Kaissouni, it would be impossible for the Bank or IDA to extend further loans or credits to the United Arab Republic before this matter is resolved. Once this is done we would expect again to send members of the Bank's staff to Cairo to review the country's economic and financial position and to prepare an up-to-date report for circulation to our Executive Directors.

I am very grateful for your gracious invitation to Mrs. Woods and myself to visit Cairo. I would like to take advantage of this as soon as time and opportunity permit and I hope that Mrs. Woods will be able to accompany me.

Sincerely yours,

(Signed) George D. Woods

George D. Woods

His Excellency
Ahmed Zando
Minister of Economy
Cairo, United Arab Republic

WBrakel:jbt

cc: Messrs. Wright
Gord

His Excellency
Dr. Abdel Monem El Kaissouni
Minister of Treasury and Planning
Cairo, United Arab Republic

February 1, 1963

Dear Mr. Minister:

I enclose a copy of the report of the Bank's economic mission which visited the United Arab Republic in October and November last. The report has been reviewed within the Bank, and I find myself in general agreement with its analysis and conclusions. It brings out the impressive progress which your Government has made during the past ten years in developing production and investment, but it also stresses the severe internal and external financial problems arising out of the rapid expansion of demand for both investment and consumption. The increase in the external liabilities of the United Arab Republic is particularly disturbing.

You will, of course, be fully aware of these problems and of the urgent need for your Government to take action to deal with them. When you have decided on the appropriate lines of action, I should be glad to discuss with you, in the light of your Government's decisions, what the Bank or the International Development Association might be able to do to assist your Government in the difficult task of bringing the economy back into balance, while maintaining the momentum of development.

As Mr. Black made clear in his talks with you last year, it would be impossible for the Bank or the International Development Association to extend further loans or credits to the United Arab Republic until the question of claims arising out of the nationalization of foreign property has been settled. I would appreciate it if you would let me know how your negotiations with the countries concerned are progressing.

In your talks with Mr. Black in April 1962 you suggested that the Bank might help in organizing a group of countries interested in assisting the economic development of the United Arab Republic. As Mr. Black said then, this would be possible only if the Bank or the International Development Association were themselves in a position to extend assistance. Once this position is reached, I would be glad to discuss the matter further with you. As suggested in the economic report, it seems desirable that some method should be found for other governments to cooperate in working out with you a more satisfactory pattern of external financing in place of the present heavy reliance on short-term bank credit and medium-term suppliers' credits.

As indicated in Mr. Escott Reid's letter to you of December 13, we are not proposing to circulate the economic report to the Executive Directors until you and your colleagues have had an opportunity to comment on it. Mr. Wright will

His Excellency
Dr. Abdel Meneim El Kaissouni

- 2 -

be visiting India towards the end of February, and I am arranging for him to stop in Cairo for a few days to discuss the report with you. He could arrive in Cairo on Sunday, February 17, if that would be convenient. Additional copies of the report are being sent under separate cover, and the annexes will be forwarded by air freight next week.

I very much look forward to meeting you again, and I hope that we shall soon have an opportunity of renewing our acquaintance.

Yours sincerely,

(Signed) George D. Woods

George D. Woods

Enclosure

EPWright:lk

OFFICE MEMORANDUM

TO: Mr. George D. Woods (through Mr. *Eschott Reid*)

DATE: September 27, 1963

FROM: Hans Pollan *Hans Pollan*SUBJECT: INDIA - Steel

In connection with our recent appraisal of the TISCO balancing scheme I investigated certain aspects affecting India's steel industry as a whole. Specifically, I concentrated on the prospective demand for steel products, the related planning process for new steel-making capacity, and on the moves now afoot towards a relaxation of the present steel control system. The situation and outlook is briefly as follows:

Demand and Planning for New Capacity

Consumption of finished steel mill products is currently (summer of 1963) running at an annual rate of slightly over five million metric tons. This level, attained at the mid-point of the Third Five-Year Plan, compares with a consumption of about 3.5 million tons in the last year of the Second Plan (April 1, 1960 - March 31, 1961). The relative weight of the sources of supply for current consumption is best illustrated by the actual 1962/63 figures:

	(thousand tons)	Rated Ingot Capacity	Production		Finished Steel
			Ingots	Semis for Sale to Re-Rollers	
A. <u>Indian contribution</u>					
TISCO		2,000	1,798	427	986
IISCO		1,000	1,002	159	636
Hindustan Steel:					
Bhilai		1,000	1,060	254	555
Durgapur		1,000	731	265	234
Rourkela		1,000	702	-	497
Total "Big Five"		6,000	5,293	1,105	2,908
Mysore Steel Works		60	55	-	36
Re-Rollers		-	-	-	949
B. <u>Imports</u> of finished steel		-	-	-	916
C. <u>Total Consumption</u> of finished steel					4,809 *

* About 30 percent in the form of flat products (plates, sheets, etc.). Steel exports are insignificant. Data on inventories are not available.

The available Indian steel demand forecasts are all based on the assumption that the Third Plan targets will be fulfilled. Accordingly, requirements for finished steel in 1965/66, the last year of the Plan, were estimated in the range of 7-7½ million tons, with flat products taking a share of 37-39%. Against these requirements, the Indian planners had hoped that domestic production of finished steel would reach 6.8 million tons in 1965/66. This was to be achieved by adding another 4 million tons of ingot capacity, including one million tons at the proposed Bokaro plant, in the public sector, thus bringing total Indian ingot capacity to slightly over 10 million tons. In terms of finished steel, this capacity would be about 7 million tons.

Progress during the Third Plan, as is well known, has not been according to expectations. Actual developments during the first half and the prospects for the remainder of the Plan indicate that the demand for finished steel will only be of the order of 6.6 million tons, with over three-fourths of the short-fall vis-a-vis Plan demand estimates falling on structurals and merchant sections such as bars and rounds. (Flats account for about 2.45 million tons or 38-39% of total demand.) This reflects slower progress in organized industry, though partly offset by a stepped-up railway wagon program and higher defense requirements, and especially in construction and agriculture.

The short-fall in meeting Plan targets affects steel production itself. There is a carry-over effect of the delay in getting production from the 3 million ton ingot capacity built up in the public sector under the Second Plan program. There have been further delays in starting the public sector's Third Plan steel expansion with the Bokaro part shrouded in uncertainty. As a result, production of finished steel in 1965/66 is expected to amount to only 5.4 million with only 1.48 million tons being in the form of flat products. This throws the bulk of the import requirements at that time into this type of products. (It should be noted here that about two years later, when production on a substantial scale is likely to start from the public sector plants' Third Plan expansion, domestic production is estimated to come to 6.7 million tons including nearly 2 million tons of flats.)

The Indian authorities are now thinking about the steel capacity to be built up during the Fourth Plan (1966/67 - 1970/71). They have in their hands three Indian forecasts putting demand for finished steel by 1970/71 between 13-14 million tons, practically double the now apparent 1965/66 requirements. Again, these forecasts are based on growth models assuming fulfillment of the Third Plan and maintenance of a growth rate of 5-6 percent annually already postulated in the Third Plan document. These forecasts, especially the one issued last July by the National Council of Applied Economic Research (NCAER), serve however as planning tools for determining new steel capacity. The capacity planning now going forward is centered on the hope of attaining in 1970/71 a production of about 18 million tons of ingots and of a corresponding output of about 13 million tons of finished steel.

Some of the Indian planners, but not all of them, realize the consequences of the flagging Third Plan performance for steel demand in the Fourth Plan. Broadly speaking their strategy for an eventual pick-up of the overall growth rate from the present 3½% is focused on at least maintaining, if not expanding, the investments tentatively foreseen for the Fourth Plan in growth-oriented industry, especially capital equipment production, power and transport, even if this should happen at the expense of agriculture and social services. This strategy has several implications, such as a possible lower level of consumption in the next 5-10 years, which I am not discussing here. This approach is yet subject to a political decision on the highest level which will not be made before November, if not later, when the National Development Council reviews the mid-Plan appraisal and is expected to determine development policies for the next five years or more. Even if it were adopted, demand for finished steel in 1970/71 is expected to be only near 12 million tons, instead of the 13-14 million forecast, with requirements of flats of about 4.5-4.7 million tons. In practice, steel demand may well be one-half to one million tons lower.

In aiming at a production of about 18 million tons of ingots by 1970/71, the Indian steel planners have the following capacity additions in mind:

(million ingot tons)

<u>Capacity after Completion of Third Plan Program</u>	<u>Fourth Plan Addition</u>	<u>Total</u>
TISCO 2.0	1.0	3.0
IISCO 1.3	.7	2.0
Bhilai 2.5	.8	3.3
Durgapur 1.6	1.4	3.0
Rourkela 1.8	.7	2.5
9.2	4.6	13.8 Total Existing Plants

New plants: Bokaro (acceleration of U.S. Steel proposal)	4.0
Visakhapatnam-Bailadilla	1.5
Goa-Hospet	1.5
	20.8

The investment cost of adding another 11.6 million tons of ingot capacity has been very roughly estimated at \$3.5 billion equivalent with a foreign exchange component of about \$1.7 billion. This works out at an average of slightly over \$300 per ingot ton which appears low considering that per-ingot ton investment in new flat capacity may range between \$330-\$350 and the likelihood that the corresponding investment in new non-flat capacity may not be far below \$300.

There are evident physical reasons why a production of 18 million tons of ingots cannot be attained by 1970/71. First of all, Bokaro as envisaged is out. The Steel Ministry is still hoping that a 1.5 million ingot ton plant may emerge at Bokaro by 1968. It proposes to invite tenders for parts of the needed equipment and obtain financing through those of our Consortium countries from where the successful bidders come. (The Steel Minister told me that, unless hard pressed, he would not like to pursue possible USSR assistance.) I don't know whether this approach will be successful, but at best I would expect a 1.5 million ingot ton plant at Bokaro to come into existence by 1970/71. Secondly Indian experience has shown that the gestation period is at least $7\frac{1}{2}$ years between a decision of building a specific plant and obtaining substantial production after construction. Judging from the way steel planning is currently being handled, i.e. by a Steering Group involving the Government agencies concerned, scientists and the present producers, which meets for a week at about six-month intervals but without the support of a continuing secretariate or staff, the point of coming to a decision could optimally be reached only by spring of 1964 provided planning work is hereafter put on a continuous basis. Steel planning for the Fourth Plan so far has only concentrated on physical aspects (capacity, raw material and manpower requirements) without regard yet to the relative cost of investing in, and operating, specific types of rolling capacities in the various plants, and the phasing of construction and the availability of products. These are essential elements in determining the nature of capacity and product mix for each plant. Mr. Subramanian, the Steel Minister, well aware of the shortcomings in the planning process, now intends to establish a continuing planning group but it may take some time to make it operational. When Mr. King and I saw him most recently, $2\frac{1}{2}$ weeks ago, in Delhi he requested that the Bank send him a steel economist from our staff, but not a consultant, to help the group "in formation" in reviewing and formulating the basis for determining the product mix for new steel capacity, the phasing and relative cost of production, and in reviewing the steel use norms underlying the demand estimates in the light of trends in other countries. This should happen about late November-December after the decision on further growth rate targets in specific sectors has been made, and a better view regarding availabilities of financial and other resources been hopefully arrived at, by the Government. Mr. King and I said we would pass on the request, indicating that we did not know about the availability at that time of a suitable staff member. If the Bank can do it, we see great merit in accommodating the Minister.

Responsible people in the Steel Ministry and Planning Commission admit privately that India can hope for a production of only about 15 million tons of ingots by 1970/71. I think, and I am not alone, India will be doing well in achieving about 13 million tons by that time, or even one year or so later. I think this could be achieved by pressing ahead with the proposed expansion of the existing plants to what is now considered their maximum possible capacity of 13.8 million ingot tons and obtaining production from at least one new 1.5 million ton plant, possibly Bokaro. Measured against the estimated demand the resulting production of 9.5-10 million tons of finished steel would still leave import requirements at the end of the Fourth Plan of at least one million tons, about the present volume for which India spent about \$200 million in 1962/63. Import requirements in the middle of the Plan may even be higher.

It is already reasonably clear that the expansion of Bhilai and Durgapur will not make them producers of flats. Rourkela will remain one and Bokaro is planned to be one. After Rourkela's further expansion, and if Bokaro should emerge as a 1.5 million ton plant in 1970/71, there would still be a gap of about one million tons in the supply of flats, which are generally the more expensive steel products in India and abroad. Since putting further flat capacity at other new plants would probably take more time, the informal intentions of our present and prospective clients, TISCO and IISCO, to install a major portion of their proposed Fourth Plan additions as flat capacity deserve in my view favorable consideration. Anyway both of them are already producers of flats. From what I could gather at the end of my Delhi stay, the Steel Ministry seemed not averse to TISCO's and IISCO's ideas.

IISCO's and TISCO's Fourth Plan expansions have been approved in principle, but only in ingot terms. How to achieve the additional capacity and the product mix is still subject to approval which is not likely to be forthcoming until early next year. It is already evident that the two companies and the Government are looking to the Bank to meet these expansions' foreign exchange requirements.

If the Bank were to meet these foreign exchange requirements, further lending to TISCO and IISCO, on top of the \$60-\$70 million to be lent within the next six-eight months for both companies' balancing schemes, could be of the order of \$150-\$200 million and \$130-\$150 million, respectively, or a total of \$280-\$350 million. (The more flat capacity is installed, the more it is likely that the upper part of the range will be reached.) Assuming the Government approves the specific schemes of the two companies early next year, it would take most of 1964 to work out detailed project reports by consultants. IISCO has already consultants, the International Construction Company, Ltd. (London), and TISCO is prepared to engage consultants. Our appraisal could therefore take place at the earliest late in 1964 with possible loans following in the first half of 1965.

Modifications in Steel Control and Pricing System

In essence, the recent trend toward a relaxation of the control system is motivated by the growing recognition that

- (a) the effectiveness of the allocation functions (assignment of production programs and determination of steel customers) of the Iron and Steel Controller, established at a time when India was producing about one million tons of steel, has been eroded by the sheer rise of the problem, i.e. current steel production at about 4 million tons and imports of one million tons. The result, among others, is the sometimes "effective" prevailing of the producers' bias towards rolling easier sections, and the existence of a thriving black market for steel products, affecting about 15-20 percent of availabilities, mainly those routed through controlled and registered stockists.

- (b) the present level of retention prices to the producers for various categories do not reflect the relative costs of these categories' production; nor does it give adequate scope, viewing the producers in the aggregate, to generate funds to meet replacement costs or part of further expansion costs.

Two panels have been asked to present proposals for a modification of the control system: One, the Raj Committee composed of three economists (only one associated with Government and, incidentally, a former EDI instructor) the other composed of representatives, including the Chairman, of the principal producers, namely TISCO, IISCO and Hindustan Steel. Although both panels have yet to submit their final proposals, their tentative conclusions are already known.

As to the assignment of production programs, both want to see this function removed from an outside agency, such as the Iron and Steel Controller, and to be vested in a steel industry body. Although there is still scope for argument among the producers as to who rolls what and when, such a body would certainly have a better view of the utilization of the respective production facilities and the relative cost of producing specific categories in each plant.

Regarding distribution, both panels favor, after providing for narrowly defined priority demands mainly of Government, the abandonment of the present system of determining clients and licensing stockists. Distribution should, for the most part, be free and subject to market forces. Reservations of the producers (especially the private ones) are that certain categories of tested steel should still go to licensed stockists. The Raj Committee wants the Government to be responsible for all imports and use part of them in "open-market" operations to offset temporary or regional scarcities and attendant upward price movements.

On prices, both panels agree that the retention price should reflect production costs and take into account replacement and expansion costs. Both foresee that retention prices will move up and that the difference from the still higher prices for imported steel would be considerably narrowed. The Raj Committee still favors the setting of retention prices by Government. The producers want to set the prices for specific categories themselves, as a body, however, within a framework of an average price agreed with the Government from time to time. (Subramaniam told us he favors the latter approach). Both panels foresee continuation of equalized steel prices at all major railheads in the country, a feature which we do not welcome since it detracts from the force of the market and promotes uneconomic utilization of steel in parts of the country where steel costs should really be higher. The industry wants to administer its own freight equalization fund. The Raj Committee wants the Government to be responsible for it. The first step on prices will probably be, according to latest report, an increase in the average price to the producers by about 50-60 rupees per ton over the present average level of 555.5 rupees. This is expected to happen later this year. Sometime early next year, when the size and investment cost of the additional steel expansion will be better known, a further increase is expected - and the amount is not yet known - to defray part of the expansion costs. It is not expected that these price movements will significantly affect the aggregate or pattern of steel demand in the coming years.

The movement towards a relaxed steel control system cannot be viewed in isolation. The Minister, one of its spearheads, told us that his principal problem is the saleability of a relaxed control vis-a-vis his colleagues in the Cabinet and Congress Party and his ability to demonstrate that a distribution system, not saddled by the present cumbersome allocation procedures, and prices reflecting relative costs would result in the short run in the optimum output of the sections needed at a given time, and by including an element for replacement and expansion give the industry a better base to undertake the sorely needed capacity additions. The proposals of the two panels may still be modified, but unlikely in their essential outline. They are now expected to be presented early in October and be the subject of a Government decision about October or November.


The foregoing subjects together with others will be elaborated in a more detailed report on the Indian steel industry to be presented in conjunction with the TISCO balancing scheme.

cc: Messrs. Aldewereld, Fuchs, de Alba/Kreuter

fm
OCT 7 REC'D

OFFICE MEMORANDUM

TO: Mr. Woods

FROM: Escott Reid 

SUBJECT: Industrial Development Bank of Pakistan

DATE: October 7, 1963

I attach a memorandum of today's date by Vasey on IDBP. Mohamad Shoaib will be raising this question tomorrow (Tuesday) morning.

cc: Mr. Knapp
Mr. Wilson
Mr. Rosen
Sir Ernest Vasey
Mr. Mason

ER/uz

We should study the possibility of splitting internally the work of I.D.B.P. into two sections, dealing with medium and small size loans respectively with the Government of Pakistan underwriting any losses on the small loans section.

We should I think make certain that the Committee to coordinate the activities of P.I.C.I.C. and I.D.B.P. should have a majority of members representing the private sector. I understand that the G.O.P. would be prepared to accept a suggestion that a representative of the Bank should attend meetings of that Committee; if this is done it should be in the role of observer only.

Participation by the Bank would, as it has done in the case of P.I.C.I.C., strengthen the position of the management vis-a-vis the governmental pressures, Central and particularly Provincial, which occur from time to time in circumstances such as those existing in Pakistan.

We might suggest as a condition of assistance that there should be discussions between the Bank and the G.O.P. at a later date to review the position with a view to the Government placing on the market a portion of its shareholdings, putting the private shareholders in the majority as a beginning of steps designed to lead in time to the disappearance of Government investment and control.

My letters, No. 220 of July 19th to Mr. Wilson and No. 120 of May 30th to Mr. Stewart Mason covered general aspects of this matter.

I am sure that we need to play a large part in the development of the small and medium size commercial and industrial structure so as to assist in its direction along the proper lines, adjusting ourselves however to the existing conditions, but making certain that everything we do moves towards the objective of creating and maintaining the defence in depth so essential if the system we believe in is to endure in the developing countries.

I would strongly recommend that at least we send an investigating mission to Pakistan to look at the position of the I.D.B.P. and to outline the conditions on which we could move towards a position of influence in its operations.

Ernest Vasey

cc: Messrs. Woods
Knapp
Wilson
Rosen

We are trying to encourage a free economy or Western system in the developing countries. We must see that what is established can be maintained in the years ahead. In developed countries the "defence in depth" of the Western system has lain in the opportunities for ownership or participation in enterprise open to a large proportion of the people and in the benefits derived therefrom. Thus, in the Western democracies a large number of people feel that they have a direct interest in the preservation of the system and the maintenance of a free enterprise basis. In countries where this condition has not existed and, in consequence, the defence of the system has been left to a small number of people as beneficiaries the movement has inevitably been in the direction of increasing state ownership as a means of participation by the people.

The stock exchange, unit investment trusts, building societies and the spread of credit institutions have played a great part in the creation of this sense of participation in our countries but this has been a long history of growth and experience which has steadily brought more and more people into this field of participation in ownership. In countries like Pakistan these channels of participation, if in existence, have but recently been established - and if we are to create the necessary defence in depth of those things which we believe are of value in the Western system we must help in their development and direction. We must also have regard to our starting point - the conditions existing in any particular country and recognise that in moving towards our objective we should be ready to depart from the orthodox provided we feel sure that each move takes us towards our aim.

In many countries the field of local private enterprise is only just opening up and there is a limitation of resources, personnel and experience. In many cases therefore the Government of the country is the only force available to act as the creative or catalytic power and our task seems to me to be able to influence the direction of that force so that such institutions as I.D.B.P. do not become entrenched as a permanent Government controlled or bureaucratically directed area of operation. If we do not assist but abandon it to the bureaucrat this could well happen, whereas our participation should enable us to wield sufficient influence as to make sure that the sloughing off of governmental interference is a basic policy of the institution or institutions concerned - and this should be our objective in the agricultural, commercial and industrial fields, coupled with the increasing spread of participation and ownership to as large a number of people as possible.

I feel therefore that, provided we can make certain that the operations of the I.D.B.P. are directed along the correct path, we would be wise as a matter of long-term policy to assist that institution.

At the present moment the Central Government owns 51% of the shares but 49% are held by private institutions, banks, firms and shareholders, (in almost every case without Government participation). Politically it would be a matter of great embarrassment to the Government of Pakistan to alter the basis of the I.D.B.P. at present for it would mean legislative action in the National Assembly with consequential debate and the probability of hostility to the change.

The I.D.B.P. has not insisted on equity participation in any of the enterprises to which it has lent money and this policy should be maintained for it means that repayment of the debt ensures for the borrower an exit from any direct pressure or Government interference in the business concerned.

We should insist on the Board having a majority of men with actual business or banking experience and the same conditions should be applied to the advisory committees which have been set up in connection with the regional offices at Dacca, Karachi and Lahore.

To strengthen the position of I.D.B.P. we should consider pressing for the upper limit of I.D.B.P. loans to be raised so that more of the medium-sized loans could be dealt with by that institution and the profitability increased. I understand that Uquaili of P.I.C.I.C. would not oppose a proposal of that kind and feels it would have little effect on his own position. He is anxious for obvious reasons that the Bank should have influence with the I.D.B.P.