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VPD Senior Adviser

McNamara file

Development Policy
July - Nov. 1972

Folder 2

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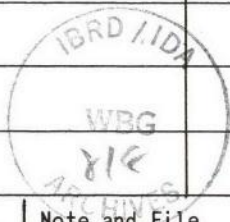
OFFICE OF THE PRESIDENT

Name

Room No.

Mr. Stern

A 1210



To Handle

Note and File

Appropriate Disposition

Note and Return

Approval

Prepare Reply

Comment

Per Our Conversation

Full Report

Recommendation

Information

Signature

Initial

Send On

Remarks

Returned with thanks from
Mr. McNamara. He has read it with
interest, and has obtained a copy
for his own retention.

From

B.
B. Moore

8/18/2/11
File

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: November 27, 1972

FROM: Ernest Stern *ES*SUBJECT: Reassessing North-South Economic Relations

11/27

The attached document was prepared by a private tripartite (US/European/Japanese) group. Ed Fried and Phil Trezise participated from Brookings.

Since I spent a considerable amount of time with Ed before he left for the Brussels symposium, I received this preliminary draft, which you will find of interest. It is to be published shortly.

I am pleased with the emphasis put on integrating the developing countries into the world economy. This is a theme I pushed hard with Fried and Trezise, who had come to similar conclusions themselves. While not of immediate relevance to the poorer countries, it is high time that the development community begin to think more actively and imaginatively about needs "beyond aid". Integrating LDC's into the world economy as partners - weak but equal in some senses - is a major task with broad implications. The draft report is a useful step in including these issues in the development dialogue.

An integral part of integrating LDC's better into the world economic and commercial framework is increased use by LDC's of the private portfolio market. This is discussed on pp. 35-36, including a suggestion for Bank action.

Would you return the document to me when you have finished with it.

Attachment

EStern/lm



Tripartite Report on Reassessing
North-South Economic Relations

Brussels,
November 15, 1972.

Participants in the Tripartite Meeting
on Reassessing North-South Economic Relations, organized by the
European Community Institute for University Studies, Brussels, the
Brookings Institution, Washington and the Japan Economic Research
Centre, Tokyo, held at the Brussels Europa Hotel on
November 13-15, 1972.

North American participants:

Mr. Edward R. Fried	: Senior Fellow, Brookings Institution
Mr. Philip Trezise	: Senior Fellow, Brookings Institution
Mr. Paul Wonnacott	: Professor at the University of Maryland, former senior staff economist Council of Economic Advisers
Mr. A. F. W. Plumptre	: Special Adviser to the President of the International Development Research Center (Ottawa)

Japanese participants:

Mr. Yusuke Kashiwagi	: Former Vice-Minister of Finance for International Affairs
Dr. Saburo Okita	: President of the Japan Economic Research Center, Tokyo
Dr. Akira Onishi	: Chief Economist, International Development Center of Japan
Prof. Tsunehiko Watanabe	: Professor at the Osaka University

European participants:

Prof. Theodor Dams	: Director of the Institute for Development Policy of the University of Freiburg
Mr. Sidney Golt	: Economic consultant; former Deputy Secretary, Department of Trade and Industry, London
Prof. François Luchaire	: President of the University of Paris (Fanthéon-Sorbonne)
Mr. Franco-Maria Malfatti	: Former President, Commission of the European Communities
Mr. Auguste Vanistendael	: President of International Foundation "Humanum"
Chairman	: Mr. Max Kohnstamm, President of the European Community Institute for University Studies
Staff members of the Institute	: Mr. Diarmid McLaughlin Secretary General : Mr. Wolfgang Hager, Director of Studies : Mr. Henri Ferroy, Rapporteur

REASSESSING NORTH-SOUTH ECONOMIC RELATIONS.

Chapter I:

Introduction

".... Earlier the problems of East-West tension were dominant: now we have a North-South problem of equal importance. ... If twelve years ago the balance of the world turned on the recovery of Western Europe, now it turns on a right relationship of the industrial North of the globe to the developing South"

... Sir Oliver Franks in 1959.

For more than a decade, the industrial countries - the North in Sir Oliver Franks' durable phrase - have been formally pledged to the assistance of the South, specifically: - "the economically more advanced nations should cooperate in assisting to the best of their ability the countries in process of economic development"¹

In this report, we propose to assess developments since the OECD countries thus committed themselves to help the developing countries and to consider what policies and actions by the industrial North are appropriate to the evolving relationship with the South.

¹ The citation is from the OECD Convention of 1960. Subscribers to it are the United States, Canada, Japan, Australia, and all of the countries of Western Europe.

In so doing, we shall examine whether we can achieve a more dynamic international division of labour and an adequate participation by the developing nations in the world economy. It is worth pointing out ^{parenthetically} ~~in parenthesis~~ that this will depend on an international monetary system that will ensure realistic exchange rates - a subject now under active negotiation. ^{1/}

The accomplishments of the past decade have ~~not~~ ^{been} ~~inconsiderable,~~ ^{when measured against the problems of development, how-} ~~although leaving much to be desired.~~ ^{ever, they} ~~leave~~

In the field of development assistance, all the industrialized countries have accepted, some with qualifications, United Nations targets for development assistance. Virtually all of these countries have by now established official agencies responsible for planning and providing development aid. Over the twelve years, 1960-71, net loans and grants financed by public funds ("official development assistance" in the term used by the OECD Development Assistance Committee) came to \$ 72 billion. Finally, as evidenced by the "Green Revolution", a promising start has been made in the development of technologies specifically related to the economic and social conditions of the South.

In the field of international trade arrangements, the industrialized countries in 1965 undertook special obligations in the GATT to assure the low income countries of greater access to their markets. More recently most of them have adopted tariff procedures intended to provide for enlarged imports of goods from developing countries.

^{1/} This subject was examined in a tripartite report on "Reshaping the International Monetary Order," Washington, D.C., January 1972.

Although progress has been uneven, a number of developing countries have had very substantial economic growth, with GNP expanding annually in double figures. We have seen some low income, agricultural societies become high growth, industrializing economies in astonishingly short periods, and others may well follow. Trade in primary products, except for petroleum, has stagnated in relative terms, but exports of manufactures seem to have crossed a threshold. The South, considered as a whole, has been increasing its sales of manufactured products to the point where they now account for 23 percent of all the exports of the poorer countries.

If we look at the averages the developing countries as a group have in recent years shared at an accelerating rate in the remarkable economic expansion of the postwar era. During the first half of the 1960's the GNP of the developing countries taken together rose by an average of less than 5 % per year. For the balance of the decade, the average was well over 6 percent.

The difficulty is that the averages obscure some stubborn facts. Many are by now familiar, but we must not blind ourselves to them on that account.

First of all, it has become clear that the capacities and the needs of the developing countries differ widely.

Some have neither resources nor "modern" experience in the arts of production or administration; others have administrative skills and experience, but are vastly overpopulated in relation to their natural resources; still others seem to be much nearer to a situation in which they need but little outside help, particularly if they can look forward to enlarging markets for products which then can produce efficiently; and then, of course, some have reserves of petroleum or other primary materials which provide the basis for general economic expansion.

Second, most of the millions of people living in the developing countries are desperately poor. Their average standard of "well-being" is less than one-tenth of the level in the industrial countries. There are more people below than above that average. Unemployment and underemployment exist in massive proportions and present an over-riding issue for most of the governments concerned. Under-nourishment and disease still impair the mentality and vitality of masses of human beings. And even the improvement in production and availability of food tends to be eaten up by the addition of millions of mouths, a trend which has scarcely begun to yield to the various and varied approaches to better family planning. Finally a debt burden has developed which, if it continues to accumulate, will become insupportable.

Furthermore, we cannot ignore the real obstacles to economic advance in the developing countries.

One of these is the difficulty of dialogue between the South and the North, a constraint on effective interaction that has become increasingly evident in recent years.

It appears in relations with newly independent countries as well as in longer established nations. In some international institutions, dialogue has tended to deteriorate into ^{unrelieved} confrontation.

A further one relates to technology. The advances of modern technology are primarily suited to the needs of the industrialized countries. But the mass of the population in the developing countries needs more food, a more balanced diet, better health measures, and better family planning - all within the context of cultures far removed from the jet and the computer.

A third constraint arises from ^{shortcomings in} ~~the differing attitudes~~ toward administration, organization, and innovation. These familiar attributes of our societies are only acquired very slowly where they are not indigenous.

And insofar as the unique responsibilities of the North are concerned, the fact is that most ~~developed~~ developed countries have not met their aid commitments, nor opened their markets in the spirit of their pledges in GATT.

Despite these obstacles, we remain convinced that economic progress in the developing countries is an objective that is both feasible and right. The ability to open our markets and to provide for an increased flow of resources to the poor countries is beyond reasonable question. ~~XX~~ ~~this connection, the task for the world would be still~~ ~~more manageable.~~ If the Soviet Union and Eastern Europe could mount an effort comparable to that of the other developed countries, the task would be easier still.

We may note, and not merely in passing, that official development assistance of about \$ 7 billion per year represents only ^{one twenty-fifth of the military budgets} ~~and~~ ~~of the~~ ~~industrial~~ ~~countries.~~ Surely an improvement in the international environment ^{should in itself be an} [assures an] opportunity to spend less on armaments and more on assistance.

✓ The broad political case for encouraging economic development in the South still rests basically, as it always has, on the belief that gross inequalities in the international distribution of wealth are morally unacceptable and incompatible with world peace and prosperity. The same motivation that leads the more advanced regions within a country to alleviate poverty in the less advanced may well be extended to the far deeper disparities that exist between different regions of the world. Development, in the words of the Pearson Report, is not a guarantee that the poorer nations will choose any particular ideology or value system. Nor can it assure in any part of the world, either stability or responsible behaviour. But it may well be indispensable to providing leeway for and giving ✓ constructive direction to social change.

Beyond these general considerations, there are compelling particular reasons, at this time, for a positive Northern policy towards the South. The industrialized countries have recently begun the process of re-ordering their own economic relationships, in the aftermath of the 1971 crisis of the Bretton Woods system. Monetary reform negotiations have begun. A new round of trade talks is scheduled to begin in 1973. Direct investment and the multinational corporation are potential items for the international agenda, and so may be the question of energy supplies.

These matters cannot be debated and resolved without the participation of the developing countries. Monetary reform, which is arguably the centrepiece of the enterprise, will in practice require the concurrence and the cooperation of non-industrial members of the International Monetary Fund. In other things as well, the views and interests of the South will impinge on the concerns of the industrial world, and accommodations will have to be made.

✓ Thus the management of the natural environment and the conservation of the world's resources will require more and more communication and cooperation between North and South. We do not accept the apocalyptic arguments which call for an end to economic expansion because of the alleged impending exhaustion of the earth's physical endowments; we believe, on the contrary, that only through well-directed economic growth can many of the world's problems be controlled successfully. But we do not set aside the warnings of potentially grave damage to the environment to be seen in the destruction of animal species, in the deterioration of the quality of the air, in polluted waterways and even seas.

It is clear that these ecological threats cannot all be dealt with by one country or any selected group of countries; collaboration on a global scale is also necessary. As was learned at the Stockholm Conference, however, the North and South have somewhat differing perceptions of their interests; to many people in the South poverty is the primary pollution to be eliminated. These differences will have to be reconciled not simply through discussion and negotiation, but by building habits of collaboration into the economic relations between the widely differing countries of the world.

✓ All of this is only to restate the reality that the developing nations are part of an increasingly interdependent world system. We in the advanced countries can better provide for our own prosperity and for the preservation of the global environment only by collaboration and cooperation with the developing world.

Thus a "right relationship" between the industrial North and the developing South is as relevant and even more necessary than it seemed to Sir Oliver Franks thirteen years ago. Even if we were to ignore the great moral questions raised by extremes of wealth and poverty in the world - which we cannot - there would be pressing economic, political and practical reasons why development in the South should be an objective of the governments and peoples of the more fortunate countries. The central question is not whether or why, but rather how - how can the development objective be pursued effectively in the changed circumstances of the 1970's?

Chapter II:

Alternative approaches

Steady growth and high employment in the industrial countries are essential conditions for, although not in themselves a guarantee of, economic progress in the non-industrial nations. In our highly interdependent world, a well functioning international monetary system is important for all countries, not just the principal financial powers. If the United States, Canada, Japan and the European Community are to try to resolve the trade problems that exist among them, the result will be critically important for the developing countries. So, although we focus our attention on three subjects - trade, private investment, and official development assistance - we are conscious of the interrelationship of these matters with other policies, especially with domestic employment policies and with the international monetary arrangements.

We need first to consider the general approaches of the North to their relations with the South. We have two inter-related issues in mind. One relates to 'zones of influence', the other relates to independence and membership in the family of nations.

Most developing countries in the South have special ties, of one sort or another, with particular countries or groups of countries in the North. In many cases the relationship stems from a colonial one, sometimes extending up to a relatively few years ago. In other cases it stems from a politico-military situation such as that epitomized in the Monroe Doctrine. In another case, that of Japan, the relationship that has been emerging with Asian countries is based on the economic dynamism exhibited by that country in the post-war period.

The question that now arises is whether that type of relationship should, as far as development policy is concerned, be continued and crystallized into accepted "zones of influence"?

It is our view that such a regionalization of world development policies would be a grave mistake. Of course traditional ties of many sorts will continue and geography will not change. Nevertheless, we believe that the thrust of the future should be in the direction of common rather than competitive development policies amongst the industrialized countries of the North.

A future world divided formally into "zones of influence" is not out of the question. The European Community has established preferential arrangements with a sizeable number of African and Mediterranean states. Under the terms of British entry, these arrangements may be extended into a preferential system covering most of Africa and the Mediterranean area. Japan's natural economic ties with Asia might provide a basis for a regional system there. And the concept of a US-Latin American preferential trading area will always have its political attractions for some.

Quite apart from the economic consequences of regionalization, all political experience argues that economic blocs are likely to acquire a neo-colonial stigma. Instances are all too available - the United States and Latin America, Britain and parts of the sterling area, France and post-independence Algeria may be mentioned - which suggest that close and extensive economic ties do not assure smooth bilateral relations. Expectations that special economic arrangements will provide preferred access to markets and raw materials or give security to investments are likely to be disappointed. It is the global competitive

market rather than the preferential regional market that works out as having the stronger potentiality and ultimately the stronger attraction.

We are convinced of the advantages of concerted efforts among the industrial countries in their development policies. A basic requirement is improved market access for the manufactured goods of the developing countries. In practice, this can be achieved in satisfactory measure only if the rich countries act together to open their markets and to circumscribe the use of safeguards against market disruption. In the same way, the depoliticizing of development assistance can best be achieved through increasing reliance on multilateral coordination and provision of aid. The debt problems of the developing countries obviously call for agreements among all creditors on how to manage their separate and joint interests; and an agreed doctrine and practice on export credits is urgently needed if more acute debt situations are to be avoided. We think that the best prospect for reducing the political objections to private investment probably lies in multi-laterally agreed and monitored policies.

In the second place we have the related issue of the independence, sovereignty, or self-determination of the developing countries. The North-South relationship will be most satisfactory, least open to misunderstandings and misrepresentation, if the developing countries are considered as full members of the family of nations.

To this principle we would add a point of elaboration. Just as the law and practice of most countries recognizes the need to ensure that bargains are not unbalanced and that the strong do not oppress or exploit the weak, so in the international community is it necessary for the

industrialized countries to recognize and try to avoid the misunderstandings that are possible in dealing with countries whose cultural backgrounds and administrative experience differ widely.

If, subject to this elaboration, country to country dealings are on the basis of equals, this implies that trade, the private capital markets, and direct investment should have expanding roles in the development process, and developing countries should have access to commodity and capital markets in any part of the world; they should not feel constricted to any particular zone. Official assistance, which will be a necessary and substantial supplement for some countries for longer or shorter periods, ought increasingly to be directed through the international institutions to points of need, for requirements that could not otherwise be met, and on non-political bases.

A North-South development relationship based on equality implies shared responsibilities and obligations. Thus we believe the poorer countries should allow investment disputes to be placed before international bodies for adjudication, assuming those bodies include representatives from South and North alike. We think that applicable GATT rules ought to be accepted by all contracting parties. We consider that the poor as well as the rich ^{countries} should submit their exchange rate policies to greater international surveillance in the future. The evolving international economic order surely is going to require further limitations on "sovereign rights" and the developing countries should expect to take their place in this process.

At the same time, we believe the developing countries must have equal opportunity to advance their interests in the evolution of the international order. This principle

should apply to negotiations on trade, on monetary arrangements, on environmental safeguards - indeed, wherever the steady trend towards interdependence will require the re-working of economic arrangements.

✓ There is finally to be considered ^{how} ~~the~~ questions of social justice ^{should affect the North-South relationship.} ~~in the developing countries.~~ In many of the poor countries today, we see extreme disparities of income, inhuman conditions of life, or unrepresentative governments. In reaction to these conditions, a body of opinion has grown up which believes that the priority given to economic growth itself may be wrong. The argument is advanced that a radically more equal distribution of income, accompanied by priority measures to maximize employment, provide the proper model for many of the developing countries.

We believe that these matters in the main must be left to those directly concerned. It would be unfair to assume that peoples have disavowed an interest in achieving greater material well-being before they have been given the chance to exercise a choice. We do not think that the issue of social justice can be determined from the outside. Economic growth will, of course, make little sense if its benefits are not spread generally. But while we may be able to concentrate development aid on labour intensive projects and otherwise to integrate social with economic aims, ~~we are not confident that~~ our development policies ~~can be~~ ^{cannot be} decisive in achieving social goals, ^{for others.} ~~In the end,~~ ^{These} judgments must be made by the developing countries themselves, ^{and the outcome will} This is consistent with our general proposition that the North-South relationship must be increasingly between independent partners.

depend principally on their actions

We are persuaded, in summary, that the "right" North-South relationship, properly understood, is an integral part of the "right" relationship that must be built among all countries in the world. The direction of Northern policy towards economic development should be founded on economic principles and directed towards multilateral action. It must de-emphasize tutelage and emphasize shared responsibilities and obligations. These propositions will be expressed in more concrete terms in the pages to follow.

Chapter III:

Trade Policy

Trade policy may well be the primary test of North-South relations, just as it will be for relations among industrial countries. The objective in both cases is the same: can we achieve a more productive and dynamic world-wide division of labour? This is not a question of rich countries giving assistance to poor ones, but of assuring greater mutual gains. As far as the developing countries are concerned, it is a question of providing the greatest possible opportunity for them to achieve the gains which their export potential can make available for them.

The world stands now at the outset of a major negotiation on the shape of the monetary and trade relations. The possible content and its desirable outcome of these forthcoming negotiations were discussed in detail in a Report¹ in which some of us collaborated, and the general conclusions of which we endorse. Briefly, these were as follows:

1. It is the first essential to get the basic international monetary structure right.

In our view, if this is achieved a large first step will have been taken towards removing some of the more evident causes of disequilibrium, and it will be possible to move forward again in the civilising of trade relations, the momentum of which is currently interrupted.

2. There should be a renewed attack by the advanced industrial countries on remaining barriers to international

¹ A tripartite report on "Reshaping the international economic order" Washington, January 1972.

trade, and in particular, their tariffs and quotas on manufactured goods and raw materials should be eliminated in stages, over a ten year period. There should also be a systematic reduction of agricultural protection; agreement on rules governing other non-tariff restrictions; and an agreed regime to limit any relief required for particular industries.

It is within a framework of this kind that we see the greatest hope for expanding the trade of the developing countries. Export expansion was a major stimulus to the remarkable growth of output in the world during the 1960s. It can play an even more substantial role during the 1970s as a contribution to continuing growth of the developing countries.

This is not to embrace the rhetoric of "trade not aid" - a slogan which, like so many others which have become fashionable in the development field, obscures rather than clarifies the issue. The relationship between trade and aid as engines of progress is complex, but certainly they should be complementary. For some of the countries which have been successful as exporters, the industrial and commercial infrastructure which aid has helped to provide has been a necessary ingredient. We think it inevitable that exports must continue to finance the bulk of imports required for development, quite apart from the influence of active export industries in promoting productive internal change.

Trade in manufactures

It is, however, necessary to qualify the traditional picture of what is involved in this situation. Certainly, much of the export activity of the developing countries will continue to be in traditional products. But an increasing number of them are building up an efficient basis for substantial new exports. As a group, they have been increasing

A growing number of primary product exporters--e.g. Malaysia,¹⁷ Thailand, Colombia, El Salvador, the Ivory Coast and Ghana--are increasing their exports of manufactured products at a rapid rate, although the total amount of these exports are still small.

their industrial exports at about 15% a year in money terms for almost 10 years, and are progressively adopting the policies on exchange and interest rates which are needed for success in export policy. Countries like Brazil, Iran, Mexico have joined the earlier exponents of export-led growth - Korea, Taiwan, Hong Kong and Singapore. Machinery and transport equipment were the two fastestgrowing export groups of the 1960s. A continuing rapid growth of these countries through the 1970s will make them major participants in world trade by the end of the decade. For some others, the prospects are less bright for an early development of manufactured exports. Where the developing countries make substantial progress in export markets, a significant contribution will be made to their growth; and the developed countries will likewise gain from the increased efficiency of world production and the higher overall level of welfare.

We therefore welcome the statements which have already been made at the session of the Contracting Parties to the GATT which began on November 10, 1972 and which foreshadow negotiations on this pattern. We look forward to the creation of conditions in which there will be continuing growth of exports of manufactures from an increasing number of developing countries.

If, however, the fullest possibilities of this kind are to be realised, the developing countries must be brought fully into the negotiations from the beginning, and there must be a specific effort to ensure that the interests and problems of the developing countries are seen as an integral part of the whole. No doubt the main dynamic in the trade negotiations will be the desire of the US, the European Community and Japan to overcome the problems that arise between them. But there is much to be put right in the relations between the developing and developed countries and in the operation of policies which

have borne adversely on the developing.

All industrial countries have applied quantitative restrictions on a wide range of manufactured products, sometimes with meagre justification. Textile quotas, sanctified by international agreement under the GATT, are only the best known example. The United States uses or has used the technique of voluntary export restraint agreements to restrict imports of such commodities as wood screws, thermometer blanks, umbrella frames, and stainless steel flatware, as well as a major item like steel. Western European countries continue to have a large number of import quotas in contravention of the GATT, and applied in a discriminatory way against Japan and the low-wage countries. Japan, until recently maintained many import quotas, even in the face of a balance-of-payments surplus that assumed embarrassing proportions. We see the negotiations as the opportunity to make a determined effort to deal with these impediments.

Again, the negotiations will no doubt be based on the principle of reciprocity of bargaining between the major countries - and in the last resort this means striking a bargain acceptable to the United States and the European Community, Japan and Canada. We do not believe that the industrial countries should expect any sizeable reciprocal contribution, in conventional trade negotiation terms, such as substantial reduction in tariff protection of domestic industry, from the developing. On the other hand, for those developing countries who are playing a significant part in international trade, and hope to become full partners in it, it will be in their own long term interests to accept progressively the same international discipline - in regard, say, to such matters as export subsidies, non-tariff barriers and other distortions of trade, avoidance of discrimination and the gradual elimination of excessive protection - as their developed partners. The ultimate objective is a sharing of

rights and obligations; the sooner that there is a concerted move towards this the better.

We believe that progress of this kind would enable new productive centres in the world, with widespread benefits for all. But this is not to say that these benefits do not bring in their train problems for existing industries in the older developed countries. They can cause adjustment problems.

Still, it would be wrong to exaggerate the adjustment difficulties in the developed countries associated with an increase of developing countries exports. We are certainly nowhere near a general deluge of goods from the developing countries. To put the magnitudes into perspective: if manufactured exports from developing to developed countries expanded by 15% per year, they would still reach only \$ 28 billion by 1980 - or approximately 7% of the total imports of manufactures in the more affluent countries. Adjustment to the growth of imports from the developing countries will represent only a small change compared to the adjustments continuously taking place in the face of changes in technology and everyday shifts in demand.

For particular industries, and for particular localities, the economic impact and social consequences could, of course, be considerably greater than the aggregate data suggest. Cases involving substantial job losses in uncompetitive industries may call for remedial government actions, of which the most important are measures to promote economic expansion and full employment. In most industrial countries, the potential job displacement effects of imports might well be swamped by the job requirements of full employment. But it will not be possible to escape the need to include in the negotiations some provision for specific safeguards against market disruption; to do so would be to fly in the face of realities.

Nor need this be deplored. With lowered barriers to trade and greatly increased international commodity flows, occasions will arise when a sudden heavy increase in imports will prove too much for the normal processes of economic adjustment to absorb. In these circumstances some kind of safeguards to restrict imports will be politically and socially necessary. Dangers arise from the fact that safeguards mean different things to different people. To some, they are a means to facilitate trade liberalisation in the sense described above. To others they are exactly the opposite: a means of restricting trade wherever the competition becomes significant. To others again they are a device to postpone painful adjustment decisions or to pass the burden of adjustment to others.

In examining this question, the OECD Group on Trade and Related Problems emphasised that when safeguards are permitted they must be limited in time, decreasing in incidence, and internationally agreed and monitored; and they placed the responsibility where it belongs - on the obligations to be undertaken by the country applying safeguard restrictions. They specified these obligations as follows:

- a. In the first place, the temporary nature of the protection measures should be emphasised by setting a relatively short time limit on their application.
- b. Second, the applicant country should undertake in any case not to reduce its imports below their level at the time the restrictive measures are applied and to allow imports to increase at a reasonable rate.
- c. Finally - and this is a fundamental point - application of the safeguard measures should be accompanied by action to bring about domestic adjustment so that use of the safeguard mechanism will in fact be temporary.

Adjustment to trade liberalisation need not create a great burden. The safeguard and adjustment provisions in the Rome Treaty have barely been used. Nor have the safeguard provisions of the EFTA Convention. No significant difficulties seem to have been experienced in accomodating to the full removal of tariffs despite a manifold increase in trade in both cases.

Japan's future growth, indeed, is partly predicated on its plans for structural adjustment. If, as projected by the Japan Economic Research Center, the growth of Japanese real GNP averages 9.5% during the rest of the decade, the average wage of Japanese workers will reach 80% of the expected US wage in 1980. In preparation for this, the Japanese Government is encouraging a shift in production away from labour-intensive products with the deliberate intention of replacing them by imported manufactures. The share of manufactures in imports is projected to rise from 30% in 1971 to at least 50% in 1980. This will amount to \$ 40 billion, of which no doubt a sizeable proportion will come from developing countries.

We have tried in the foregoing to sketch the ways in which the developing countries might share in the benefits to be gained from the forthcoming international negotiations, and the actions the developed countries should take to this end. Meanwhile, many developed countries (but not yet the US or Canada) have introduced the so-called "Generalised Preference Schemes" and much has been hoped for from these schemes as the answer to the developing countries' problems on exports.

The objectives of the original proposals on special treatment for developing countries were not, in fact, "preference" in the form in which it has emerged. It was rather access to the industrial countries markets, unimpeded by tariffs or

quotas and without any reciprocal concessions by the beneficiary countries; it was an attempt to apply for the developing countries, faster and more completely than the developed countries were ready to do for their supposedly more competitive industrial trading partners, the possibility of duty-free entry, without quota restriction. This was (and remains) the logical outcome and ultimate vision of the process of trade and tariff negotiation of which the Kennedy Round, at that time, was the concrete manifestation.

In the event, the generalised preference schemes are a pale shadow of these objectives. By all means, efforts should be made to improve them - to get rid of exceptions, to extend their application to other products, including especially processed raw materials and processed agricultural products, and to eliminate their restrictive aspects. Because of these limitations, the existing preference schemes now stand in some danger of worsening rather than improving the real opportunities available in the developed countries markets.

✓ In our view, it would be misleading to regard these schemes as a substitute for ensuring the full participation of the developing countries in a successful major trade negotiation. We believe that the best prospect for the developing countries is real and irreversible progress in the improvement of their opportunities in all markets by movement towards elimination of tariffs and real, not sham, removal of quantitative restrictions. They will be the more secure in the achievement of these benefits if all the major trading countries act jointly in this regard, and action for each of them is made easier by the knowledge that the others are doing the same.

Primary products and agriculture

Primary materials and agricultural goods still account

for the majority of the exports of the less advanced regions. Nevertheless, allowing for certain exceptions, the outlook for these products does not indicate rapid expansion of exports on anything like the scale which seems possible for manufactured goods.

For the countries which have sizeable reserves of petroleum and certain minerals, of course, export prospects are strong. Demand is rising sharply, the volume of trade is immense, and the major producing countries are able, within limits, to exert upward pressure on prices. ~~In some cases, the oil countries may be expected to be donors of assistance to their poorer neighbours.~~

Most other primary products will have expanding markets, as the world economy grows, but none of them are remotely to be compared to petroleum as potential export earners. The primary materials present questions about ownership and control and about the proper location of processing facilities. Each case of this kind is likely to be special, however, and we do not see the basis for policies of general application, beyond the benefits that would accrue from the removal of tariffs.

Agriculture is overwhelmingly the principal activity of the developing countries. Improvements in the conditions of agricultural production and increases in farm income will remain priority problems in the poorer countries for the foreseeable future. They will also have to meet an increasing demand for food in rural and urban areas ^{while relying less on} ~~that~~ international food aid. ^{These requirements suggest that} ~~with the necessary~~ / Agricultural products, ~~however,~~ - with some few exceptions - do not offer major prospects for export growth to developed countries. It is worth noting market prospects in each of the major agriculture export categories.

Market opportunities for tropical products ~~have~~ have in some ways improved in recent years as trade barriers have been removed. Further improvements might be achieved if special excise tax burdens were reduced and if the Soviet

Union and East European countries were to change their buying and internal price policies for these products. But in general, demand is rather inelastic, and the room for expansion limited.

There are ^{agricultural} ~~other~~ raw materials, like jute, hard fibres, rubber, and ^{many} ~~many~~ others, where there is considerable room for increased processing in the developing countries of their origin. The inclusion of processed products in the arrangements we have discussed above for manufactured goods would significantly improve the developing countries' prospects. General tariff reductions would similarly help exports of processed foodstuffs. This is one of the areas of trade where developed countries have been most resistant to liberalisation; this has manifested itself even in the restrictions within the generalised preference schemes. There have been many efforts - including most recently for cocoa - to create international commodity agreements for tropical agricultural products, as well as for raw materials. So far, there exist for tin and for coffee more or less world-wide agreements, which ^{have been successful in preventing sharp declines in} ~~have among their objectives stabilisation~~ of prices. There are a variety of other more limited arrangements, some of them affecting only part of the producing countries, others built around special price or supply arrangements for the benefit of particular suppliers.

There may be ^{other} ~~some~~ cases in which the international community can organise markets so as to prevent wide price fluctuations and provide benefits for producers in developing countries. These would be all to the good. We are doubtful, however, that commodity agreements can be an effective means for a substantial increase in export earnings for primary goods on a world scale.

There remain those agriculture products which compete with temperate zone production. We believe that in their own

interests, the developed countries need to begin to dismantle the formidable structure of obstacles to trade in those products, and that reduction in agricultural protection are an essential element in the forthcoming negotiations. There will no doubt be benefits to the developing countries from this process, and there may be particularly encouraging prospects for some commodities, such as animal feed grains, beef, fish and perhaps fruit.

There are also some products where there is room for expansion of trade among developing countries themselves. But it remains true that, in the general run of products of this kind, developing countries are on the whole less efficient producers than most developed exporting countries, and that in many cases they cannot meet their own needs from domestic production. We do not, therefore, see the likelihood of substantial export gains in these areas. Nevertheless, the policy prescription for developed countries is clear: to provide technical assistance, wherever feasible, to improve efficiency and to provide access to their markets if export surpluses do arise.

Sugar is a special case which is produced in both the tropical and the temperate zones. Sugar ranks third among internationally traded agricultural goods, and it is of special importance to the export trade of some of the poorest countries. Trade in sugar is now subject to a number of special arrangements: the International Sugar Agreement (relevant mainly to the small free markets); the Commonwealth Sugar Agreement between the United Kingdom and its associates; the US sugar legislation (which holds part of the American market open to imports, normally at premium prices); and the European Community's internal system of guaranteed price which has made the Community of Six a sugar exporter on a substantial scale.

The American sugar law, the Commonwealth Agreement, and the International Sugar Agreement all are up for renewal or revision in 1974. Commonwealth arrangements in any case must be fitted into the Community's agricultural policy. The occasion arises therefore to agree on changes in domestic price and production policies, ^{in the industrial countries,} so as to open markets for lower cost and low income suppliers.

* * * * *

We believe therefore that ^{for both manufactures and primary products} the interests of the developing as of the developed countries will best be served by determined resolution to bring about the success of the trade negotiations on the lines that have been suggested. Increasing freedom of the international market in manufactures over the past twenty years has been the engine of vastly increased prosperity for the developed countries. In the last ten years, an increasing number of developing countries have demonstrated that even with existing limitations, they can benefit substantially from access to that market. On all counts, including their own self interests, the duty of the developed countries now is to refrain from actively distorting the freedom of the market against the developing countries.

It would be reasonable, and will no doubt be necessary, to find ways of moderating the effects of change, especially of rapid change concentrated in particular narrow sectors. But the developed countries should make all possible effort to refrain from restrictionist interventions ^{to remove current} and distortion. As far as agriculture is concerned, the attainable ^{for the developing countries} prices are perhaps smaller; but the goal is the same. Over the whole field, it will be of the utmost importance to ensure that the problems of the South are fully considered in the process of negotiation, and that the countries of the South participate effectively in that process.

Chapter IV:

Private investment and development

Flows of private direct investment to the developing countries have been rising steadily and in 1971 were more than \$ 4 billion. These flows of course are separate and distinct from official development assistance. Their volume and character are determined in largest part by the decisions of private firms.

Of the total stock of private direct investment in developing countries, which comes to about \$ 40 billion, one third is in manufacturing industry, about equal to investment in petroleum. In spite of its expansion and diversification, however, private direct investment has come under criticism in some developing countries and on the part of observers elsewhere as having only a limited or even a negative impact on economic development.

The critique of private investment (and the multinational corporation) includes several points:

- It may be costly in balance-of-payments terms.
- It may lead to the creation of foreign enclaves which discourage the growth of local entrepreneurship.
- It may be anti-competitive, either because it is based on overwhelmingly superior market organisation or because the multinational corporation is powerful enough to assign market shares to its subsidiaries; it may thus inhibit rather than stimulate the growth of exports of manufactures.
- When host governments offer investment incentives in the form of subsidies or import protection - in some cases at the demand of the foreign firms - it may bring about and perpetuate uneconomic

production.

- In the bargaining between a large multinational corporation and the government of a developing country, the former may have overriding advantages in its access to legal and other skills and in its sheer market power.
- It may take up local savings which might otherwise go to local investment.
- It may interfere with or distort host government development planning by causing an allocation of resources different from that of the plan.

We recognise that the misgivings about the role of private direct investment are a factor in the North-South relationship. The affirmative case, however, also must be recognised. In the first place, the transfer of resources, skills, and knowledge through the vehicle of private investment is a standard, tested procedure, which comes naturally out of the manner in which the advanced market economies are organised. As a practical matter, the private corporation in these economies is a unique possessor of certain skills, especially of an organisational and managerial kind, and of technological processes as well. In some cases, these can be provided only through direct investment. (In others, the alternatives - licensing of technology or contracting for managerial help - may be feasible for countries in an early stage of industrial growth). The package of capital, technique, and technology that a multinational firm can provide may not be available in any other form. Second, private investment is likely to allocate resources efficiently. (It is nevertheless true that distortions may be introduced, either by host governments which are willing to subsidise investment in various ways or by private firms with market power.) And third, foreign direct investment will be essential to

enable the developing countries to take optimum advantage of greater access to export markets. In the countries where manufacturing export industries already have had strong growth, foreign private investment has been an important factor, and it can play an important role in the development of other countries.

Whatever the weight of the different arguments, one thing seems to be clear: it is not to the developed nations to decide for the others whether they should avail themselves of the opportunities offered by foreign direct investment. This decision is and must remain theirs.

Undoubtedly there will be problems, as when a country seeks assistance from an international institution to finance an investment which could be made, in other circumstances, by a foreign private firm. The argument will then be raised that the use of concessional funds for this purpose is unwarranted since these funds would then not be available for purposes that could not otherwise be financed. We have no general solution for such problems, and we doubt that there is one. Each instance is bound to differ from the last.

In recognizing the right of each country to decide its own policy toward foreign investment, we believe that an obligation exists to assure fair treatment of investments already in place and to accept impartial mediation of disputes, for example through the International Centre for Settlement of Investment Disputes.

So far as the advanced countries are concerned, official policy has a rather limited direct role in determining the volume of private investment abroad. A few countries offer tax or other incentives to investors

in developing countries and the United States has exempted these countries from the application of its official restraints on foreign direct investment. In the main, however, the principal means of encouraging investment flows has been to offer governmental insurance against political and exchange risks.

The official insurance schemes evidently do contribute to increasing the flows of investment. In major investing countries - the United States, Germany and Japan - the insurance facilities are used for a substantial portion of total investment in the developing countries and many investment decisions no doubt rest on the ability of firms to insure against the special risk believed to exist in certain developing nations.

On the other hand, investment insurance may bring governments into the investment process in a greater measure than intended. Official risk-bearing implies some official voice in deciding which investments will be safe, and in what degree, and therefore which should be made. Moreover, if insured investments are nationalised, the insuring government is likely to become more involved than would normally be the case; we foresee the possibility of political confrontations arising out of investment disputes.

We consider that the proposed World Bank multilateral insurance plan (the International Investment Insurance Agency) would be a desirable addition and alternative to the national schemes. While offering the same incentive to investors as do the bilateral insurance plans, it would be at greater remove from national concerns; its participation in the process would give the developing countries a neutral source of advice. And even if the developing

countries did not participate in its financing - as now seems probable - it would still represent the World Bank community and would help to diffuse and reduce emotional and political factors.

We note with great interest the considerable innovation in the forms which private foreign investment has taken in recent years - all designed to provide for increased local participation in ownership and management. The Development Assistance Committee of the OECD mentions, for example, joint ventures with local, private, or public interests; participation by regional investment companies and the International Finance Corporation (IFC); consortia in which no single investing country has a controlling interest; minority investments coupled with management contracts; and production sharing agreements. The private business section of our countries seem to be quite flexible in adapting to attitudes in the developing countries.

New modes of overseas private investment are being discussed in Japan. They include technology transfer separate from equity and management participation, gradual transfer of ownership to local entrepreneurs (divestment), production-sharing arrangements to recover investment in the form of products, and transfer of know-how of medium and small scale industries by providing government funds to private enterprises.

These non-traditional methods of investment must be tailored to individual situations. We believe that the IFC may be able to have an increasing role in the adaptation of private investment to the changing political climate. We have in mind in particular that the IFC can take a minority equity position in particular instances. This

equity can later be sold to local investors, as the enterprise becomes settled in and as local funds become available. The direct participation of the IFC ~~may be~~ is helpful, moreover, in assuring that direct investments do not include features unfair to the host countries. An extensive role for the IFC in equity participation in direct investment, however, will require an increase in its paid-in capital.

Finally, we have considered whether a code, or codes, of conduct for private investors and for host governments would be feasible or useful. Foreign direct investment has been the subject of a considerable amount of study in our several countries, but we do not feel able to make specific recommendations regarding codes of conduct without more exploration ~~and study~~ than was possible on this occasion.

Chapter V:

Export credits and portfolio investment

A. Export credit:

The subject of export credit flows to the developing countries is both important and complicated.

In the first place the amount of export or supplier credit is large. The net flow to developing countries rose from an average of \$ 668 million in 1960-1965 to \$ 2.7 billion in 1971. The 1971 level was almost identical with the total of bilateral development loans to the developing nations.

Second, export credits apply to virtually the entire range of commercial transactions between the developed and the less developed countries. Also, it is now normal procedure almost everywhere for governments to guarantee export transactions of all sorts, ranging from sales of heavy equipment to sales of consumer goods. The ready availability of these government guarantees unquestionably has helped to swell the volume of export transactions.

Third, it appears that the increase in export credits - or borrowing to finance imports - has been in most countries a factor contributing to economic expansion. The assumption must be that the goods so financed in the main are being used effectively to sustain and foster economic activity.

Where the export credit phenomenon becomes troubling is in the context of the debt service problem of the developing countries. Out-payments on foreign debt threaten to increase at an average of 15 per cent or more during the 1970's and to be an extremely heavy burden for

some countries. The Development Assistance Committee has warned that debt will continue to be a priority problem in the course of this decade. Three quarters of all present debt service is traceable to export credits.

To the extent that debt service cannot be managed out of foreign exchange reserves and earnings, it must be financed by other loans or grants, renegotiated, or defaulted. When the form of financing is official development assistance used indirectly to pay for debts incurred through the export credit mechanism, an obvious question of fairness arises. A very divisive issue appears when some advanced countries find themselves regularly paying for other advanced countries' exports. Furthermore, to allocate development assistance financing to countries having the most severe debt problems is not necessarily the most useful distribution of scarce resources.

It is difficult, therefore, to avoid the judgment that if the international community is going to finance exports to the developing world on an excessive scale, the end result must be to convert some of the export credits, through the process of debt rescheduling, into long-term lending. Thus, we may see the export credits becoming in part another form of official development assistance. And, while the export credits originate in a competitive scramble for exports, debt rescheduling needs to be done collectively, so that all lending countries are assigned fair shares of the costs of revising the terms of debts.

Debt rescheduling, however necessary it may be, is likely to be costly to the developing countries, since in many cases they will find that their credit worthiness and ability to borrow will have been damaged.

We find no simple answer to these problems, however. Export credits do contribute to the economic development of the poor countries as well as to day-to-day economic activity. But they may also, as we have seen, make more difficult the debt servicing problem. In some cases, moreover, easily available export credits have led to unwise and wasteful imports by developing countries.

What is warranted, we believe, is that the international community should monitor its practices and policies in the export credit field much more strictly than has been the case up until now. The best way to do this, we think, would be for the International Monetary Fund to take responsibility for reviewing flows of export credits to particular countries, evaluating them in relation to domestic economic growth and against the background of the volume of debt being assumed. This would be a kind of early warning system through which borrowers and lenders alike could be advised of potential problems ahead. The IMF could discuss its findings with both lending and borrowing countries in the course of its regular annual consultations. In especially threatening situations, the Fund could recommend more rigorous controls over export credits or even the imposition of temporary ceilings.

B. Portfolio investment

A growing number of developing countries have been turning to the private capital markets in the industrial countries, and for increasing amounts of funds. The volume of borrowing, through bond issues and bank credits of seven to ten years in duration, may have been as large as \$ 3 billion in 1971.

The borrowings differ from guaranteed export credits in an important way. The developing country - or rather its government - is normally the borrower and thus the guarantor of the loans. The commercial market, rather than the government in the lending country, judges the credit worthiness of the borrower, and decides on the risk to be taken.

We see in this growing recourse to private capital market a highly desirable trend. It represents a return to a traditional method of financing economic expansion. It leaves the borrowing country free to make its own decisions and it puts on the private market the responsibility for evaluating the merits of each bond issue or loan. As more developing countries acquire the capacity to borrow on private markets, official development assistance should correspondingly be concentrated in areas of greatest need.

In our opinion the World Bank might provide technical advice on request to developing countries wishing to go on their own to the private markets. The Bank's long experience with the world capital markets makes it a repository of knowledge and skill which could be made available to the developing countries.

Borrowing on the private market could, of course, be overdone, and the management of debt burdens made more difficult thereby. We would not wish to see pressures arising for official assistance for the purpose of paying off private lenders in the advanced countries. We would expect that an IMF review procedure, as suggested above, would examine the entire structure of obligations in individual cases and would be prepared to comment and advise on potential problems associated with all forms of debt.

Chapter VI:

Official assistance

We have left to last the discussion of official development assistance, the element of North/South relations that usually receives the most attention. Flows of capital on grant or highly concessional terms have helped to build basic facilities in a large number of developing countries and have been a key factor enabling some to reach a path of strong growth. They continue to be large and relatively important, accounting in 1971 for about \$ 7 billion out of a total flow of \$ 18 billion in financial resources moving from industrial to developing countries. Without them, the debt service problem would long since have become unmanageable.

We must recognise, however, that official assistance has been relatively stagnant over the past ten years particularly if allowance is made for price increases, despite the various commitments undertaken by the industrial countries to have their assistance reach a special proportion of their GNP. In general, very little progress has been made in untying bilateral development assistance. This failure not only reduces its flexibility but also its value since only untied assistance can be used effectively for programme as well as project purposes. It seems evident to us that a reversal of this trend is required.

The principle reason for this lacklustre record is the lagging performance of the US, which has only in part been made up by increased assistance from other countries. In so far as long-term, untied development assistance is concerned, none of the industrial countries has an outstanding record. Nor has the trend in development assistance from

the USSR and Eastern Europe helped matters; it has not increased and remains a very small percentage of GNP.

Bilateral programmes have been the principal means of providing development assistance and continue to account for four-fifths of the total. These funds, whether for technical assistance or development grants and loans, are provided mainly on the basis of special historic, cultural or political links between donor and recipient countries. Assistance through multilateral institutions, principally the World Bank, the regional financial institutions, the European Development Fund and the United Nations Development Programme is growing fastest but still accounts for only one-fifth of the total.

A number of countries have a diminishing need for official assistance because they can tap private capital markets. They do this on their own or through what amounts to the intermediation of the World Bank and the regional financial institutions. These countries have come a long distance towards being full participants in the international trading and investment system and they continue to expand at home at a rapid pace. Notable examples are Brazil, Taiwan, Korea and Mexico. Many others with records of high and consistent growth are diversifying their economies and are on the way towards becoming exporters of manufactured goods on a significant scale. It seems probable that additional countries are likely to join this group over the balance of the decade.

The principal oil producing countries form a second category. Some like Iran are able through oil revenues to finance rapid economic expansion on their own. Others like Kuwait and Saudi Arabia are themselves a source of assistance to other countries in their region. Still

others like Nigeria and Indonesia are benefitting from oil revenues, but not yet sufficiently to achieve on their own the necessary turnaround in their economies.

There are two additional categories of countries that clearly will continue to require a means of obtaining external resources on a concessional basis.

The first comprises the least developed countries - perhaps 25 to 30 in number having a total population of approximately 150 million. They are overwhelmingly non-industrial, and they are lacking in public facilities and services, such as education, transportation and communications, and financial institutions. These countries have still to develop the basic, social and economic structure that will permit sustained economic expansion. There is little prospect of their being able to do this without receiving concessional assistance from abroad for a long time to come.

The second category comprises a smaller number of countries with a much larger total population. India, Pakistan, Bangladesh and perhaps Indonesia and Nigeria are the largest countries in this group. Unlike the first category, these countries in the main have the basic public and technical facilities to support economic expansion and to become substantial members of the world trading community. They are burdened, however, by low per capita income and heavy pressure of population on resources. In this situation, great difficulty in effectively employing available manpower is virtually endemic. These countries will need large-scale assistance for at least a decade, not to bring about economic expansion but to accelerate its pace and to broaden its impact. Their prospects will primarily be decided by their own policies, which for example will determine how greatly they can benefit from

increasing trade. Nevertheless, left to their own, their development effort will be vulnerable to great risk of failure and they will have little margin for coping with their enormous problem of poverty and unemployment.

If these are likely to be the principal purposes for which official development assistance is needed over the balance of the decade how can they best be met?

A substantial contribution will no doubt continue to come from bilateral programmes for the special reasons noted above. The key condition, however, will be to raise the volume and improve the quality of assistance. That implies providing assistance that is highly concessional in character so as to minimise the debt service burden, untied so as to maximise its usefulness, and non-political so as to insure that it will go to countries where it is most needed and can be most effectively used.

improving the quality of technical assistance so as to develop
 A similar need exists for ~~the development of~~ new technology, or the adaptation of existing technology, to ~~meet~~ the special needs of the developing countries. ~~The~~ Its basic purpose is to increase productivity, enhance employment opportunities, and improve the quality of life in those sectors unlikely to be touched for many years by either foreign investment or foreign trade. Much of this effort will necessarily have to be focused on rural development. To an increasing degree the development and improvement of the necessary technology should be within the poor countries, rather than through institutes in the industrial countries.

This kind of assistance - both capital and technical - can be said to be the special concern of the international community as a whole, to be shared on an agreed basis.

Its characteristics argue for much greater emphasis on assistance supplied through the multilateral institutions. In the case of financial assistance, this would mean the World Bank Group and the regional financial institutions; they now account for the largest share of current official development lending (including loans made on near commercial terms) and they are rapidly expanding their capabilities to assume greater responsibility and leadership in this field. In the case of technical assistance, a larger role could be played by the UN Agencies and in the bilateral programs greater emphasis could be placed on financing joint international projects and independent experimental institutes with governing boards, including experts from developing and

We have no strong views as to how much, ~~with~~ with industrialized countries. of an increase in official assistance will be required, beyond the belief that the IDA and the soft loan facilities of the regional institutions in particular will have to be financed on a substantially larger scale than at present. It seems to us that a guide to answering this question could be accomplished by a tentative estimate drawn up for a three to five year period by the World Bank in collaboration with a group of experts drawn from the regional lending institutions and the UNDP, and perhaps from a few lending and borrowing countries.

An estimate drawn up on this basis would not of course be binding on the governments of the industrial countries. Nevertheless it would give them a basis for seeking appropriations, a method of facilitating agreement on sharing requirements among each other, an indication of how much progress had been made, and a sense of future trends.

It is in furtherance with such a system that a connection between monetary reform and development finance could be useful. Negotiating a new monetary structure for the world affords an opportunity for further internationalising of development-aid. One way to do this would be through use of the following procedure.

As new allocations of Special Drawing Rights occur, the industrial countries could assign a portion of their total allocation to the International Development Association (IDA), for low interest, long term lending. Additional funds could be made available to IDA if the monetary reform negotiations include arrangements to consolidate reserves held in US Dollars and Sterlings by exchanging them for SDRs. The IMF could then turn over to IDA any net earnings it realises from such arrangements. The amounts that might result will necessarily be uncertain since they will depend on the need for international liquidity which will be determined on entirely independent grounds. Hence we would consider these sources for financing multilateral assistance as supplementing rather than substituting current methods.

We see the above procedures as part of a process for coordinating all forms of development assistance, bilateral and multilateral, governmental and private. Our objectives should be to improve the degree to which all of these resources are responsive to the needs and priorities of the developing countries. We see this happening not only through greater resort to multilateral assistance but also through wider use of consortia and the formulation of bilateral programmes in a multilateral context.

Chapter VII:

Concluding remarks

In this report we have assessed separately the major elements in North-South economic relations insofar as they apply to the policies of the industrial countries. We have emphasized the possibilities for actions by the industrial countries in the fields of trade, private capital flows, and development assistance--actions that would advance the objective of economic development. It is useful now to see how our suggestions may fit within a more general perspective.

Let us suppose that in the 1970's the economies of the United States, Canada, the European Community and Japan grow at rates more or less the same as in the 1960's. By 1980, the combined Gross National Product of this grouping, in today's dollars, will be \$4 trillion.

Let us further suppose that our imports grow at an average rate of 8 per cent per year for the rest of the decade, and that their composition does not change very much. In 1980, total imports, valued in today's dollars, will be in the neighborhood of \$400 billion, of which perhaps \$250 billion will be in manufactures.

We think it is a fair question to ask whether, against these conservatively stated magnitudes, there should be any doubt about our ability to buy the goods that the developing countries can produce efficiently? Or whether there should be any doubt about our ability to transfer a growing volume of development resources through public as well as private channels? The conclusion must be that we can

afford to cooperate with the poorer countries abroad even as we do more to deal with our problems at home.

If, further, the hopeful signs of a lessening of East-West tensions are borne out, then we can begin -- with the Soviet Union -- to direct resources on a very large scale from military uses to the pressing needs of the poorer countries, as well as to our problems at home.

The truth is that we have the wealth, the productive capacity, the skills and the knowledge, not to make over the world but assuredly to provide in a decade the basis for genuine hope for the future. Our potential is immensely greater than the difficulties that seem so large when we look at the matters separately and narrowly.

To set its relations with the South on a new and hopeful course, the North needs only to widen its vision.

McN

ROUTING SLIP

Date

Dec. 28, 1972

OFFICE OF THE PRESIDENT

Name

Room No.

Copy to Mr. Stern



To Handle	Note and File
Appropriate Disposition	Note and Return
Approval	Prepare Reply
Comment	Per Our Conversation
Full Report	Recommendation
Information	Signature
Initial	Send On

Remarks

11/24 To Messrs. Knapp, Chenery. (1) Do we not need a written statement of Bank policy and guidelines in regard to the financing of urban transportation? (2) If so, who should prepare such a statement and by what date?

RMcN "
(McNamara)

From

Doris

11/24 to Messrs: *Kaplan* 11/21/72
11/27 1972
Country

OFFICE MEMORANDUM

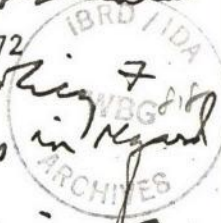
*Do we not need
a written statement*

TO: Mr. R. McNamara (through Mr. W. C. Baum)

DATE: November 21, 1972

FROM: R. Sadove *R. Sadove*

*of Bank policy &
guidelines in regard
to the financing of
urban transportation*



SUBJECT: The Private Automobile - Consideration for Urban Transport Project and Study Preparation

I understand that Mr. Baum has mentioned to you that the attached paper would be shortly available. As the paper deals with issues concerning the private automobile and makes suggestions regarding Bank policy -- topics on which I know you feel strongly -- I am taking the liberty of sending it to you.

*Should
prepare such
a statement &
by what date.
L. New*

Attachment.

RSadove:eta

2488

1/24

818/2/10

November 13, 1972



Dear Mr. Bloom:

As Mr. McNamara already indicated in his response to Mr. Benjamin, we do not have the figures in the form you want them. The idea is interesting and would dramatize the tremendous real income disparities in the world. However, data on the distribution of income, nutritional intake, public services, shelter, etc., are so inadequate that it would not be possible to construct your world scale with any degree of accuracy. Even to develop a very rough approximation would take a substantial research effort.

I have discussed this with Mr. Haq, who shares my disappointment at not being able to be of more help.

Sincerely,

Ernest Stern
Senior Adviser
Development Policy

Mr. Murray T. Bloom
The Reader's Digest
200 Park Avenue
New York, New York 10017

EStern/lm

808/2/9

2416

OFFICE MEMORANDUM



TO: Mr. Robert S. McNamara

DATE: November 2, 1972

FROM: Ernest Stern *ES*.

SUBJECT: Development Cooperation in the Eighties

113
At the recent consultation sponsored by the Canadian government on the future of their aid program, they circulated the attached paper which was prepared by Ben King who, as you know, is on detail from the Bank to the Canadian government. It was very well received by the participants, and I think you will find it of interest.

Attachment

EStern/lm

President has seen

818/218

OFFICE MEMORANDUM



TO: Mr. Robert S. McNamara

DATE: October 24, 1972

FROM: Hollis B. Chenery *ABC*

SUBJECT: Committee for Economic Development

1. Attached is the draft reply to Dave Sommers. The CED publications are useful and the institution is worth supporting.
2. If you approve, by signing the letter, I will initiate the necessary request. Since the cost is modest - \$250 - no special action will be necessary.

Attachment

EStern/lm

President has seen

October , 1972



Dear Dave,

Much of the work of the CED is indeed of interest to us, and the staff regularly utilizes the CED publications. We shall, therefore, be pleased to enter an institutional subscription to CED's publications.

Sincerely,

(Signed) Robert S. McNamara

Robert S. McNamara

Mr. Davidson Sommers
Chairman of the Board
The Equitable Life Assurance Society
of the United States
1285 Avenue of the Americas
New York, New York 10019

EStern/lm
October 24, 1972

1071 To Dr. ⁽²⁾ ~~Henry~~
Please draft
a brief
reply
WBG 88
ARCHIVES
① J. J. Jones - Clark
Clark + three draft
(PR funds?)

OCT 12 1972

THE EQUITABLE LIFE ASSURANCE SOCIETY
OF THE UNITED STATES

1285 AVENUE OF THE AMERICAS, NEW YORK, N. Y. 10019

DAVIDSON SOMMERS
Chairman of the Board

October 5, 1972

Mr. Robert S. McNamara
President
International Bank
1818 H Street, N. W.
Washington, D. C. 20433

Dear Bob:

I am National Finance Chairman this year of the Committee for Economic Development. I am writing to you at this time because the current agenda of important policy research being conducted by CED may be of immediate interest to you, particularly its research in International Economic Studies.

The CED Trustees, an outstanding group of American corporate leaders, are currently studying in depth a number of the nation's most urgent economic problems on the effective solution of which rests the health of the economy in general and of the business community in particular, and which also have important international implications. These problems include: Reform of the International Monetary System, Revenue Needs and the Tax System, The United States and Japan in a New World Economy, Financing the Nation's Housing Needs, and Improving the Quality of the Environment.

I enclose a copy of CED's Annual Report entitled "New Directions for Economic Policy," which will give you a rounded picture of the scope and significance of its activities. I commend it to your personal attention.

For almost 30 years CED has presented the carefully reasoned judgments of American business leaders on how to tackle our most pressing economic and social problems. The unbiased objectivity and practicality of its recommendations, arrived at after careful study by active business executives, assures that U. S. decision-makers, public and private, will give them serious attention. As we examine the current state of both domestic and international economies, the role of CED takes on additional importance, since it affords a unique outlet for this informed business opinion on key issues of broad economic and social policy.

Supplementing corporate contributions which constitute CED's main support, additional financing is obtained from \$250 subscriptions to CED's publications from a substantial number of Federal Reserve Banks and United States branches of foreign banks, as well as contributions from the private banking community throughout the United States. In view of the immediate relevance to the World Bank of CED's current analyses of international and domestic economic problems, it occurred to us that a subscription from the Bank would be appropriate, and it would certainly be most welcome. I suggest that you give this your consideration, and hope that your decision will be affirmative. Your check, which could be forwarded to me at your convenience, should be made payable to the Committee for Economic Development.

Yours sincerely,



Davidson Sommers

McN

ROUTING SLIP		Date 9/14/72	
NAME		ROOM NO.	
Mr. Hoffman		D1123	
<div style="font-size: 2em; font-weight: bold; transform: rotate(-45deg);"> W 37th Ave NY </div>			
To Handle		Note and File	
Appropriate Disposition		Note and Return	
Approval		Prepare Reply	
Comment		Per Our Conversation	
Full Report		Recommendation	
Information		Signature	
Initial		Send On	
REMARKS			
Mike - <i>Many thanks</i> <i>MSH</i> Take a look at this material. It is all Bank oriented. Activities in cooperation with other agencies ave been limited to some discussions with ILO on data improvement, and not much more.			
From E. Stern			

818/2/7

OFFICE MEMORANDUM



TO: Mr. Ernest Stern

DATE: September 13, 1972

FROM: J. H. Duloy

SUBJECT: ECOSOC Speech

Measures initiated this year to improve our knowledge of the problems of income distribution and employment, associated with the DRC are:

(a) Research Projects

- i) Short-Run and Long-Run Influences upon the Income Distribution.
- ii) Size Distribution of Income Study.
- iii) Some research projects are now addressing some aspects of these problems as part of a larger study. These are: the impact of the fiscal system upon regional incomes (Brazil), and programs to alleviate rural poverty (Mexico).

(b) Other Activities

- i) Creation of Income Distribution and Demand Studies Division in DRC.
- ii) Arrangements for seminar on "state of the arts" early 1973.

JHDuloy:ke

OFFICE MEMORANDUM



TO: Mr. Ernest Stern

DATE: September 14, 1972

FROM: P. D. Henderson *P.D.H.*SUBJECT: Improving Our Knowledge Concerning Employment and Income Distribution in LDC's

1. In response to your memorandum of yesterday, I am attaching two short papers by Mr. Hawkins and Mr. Tiemann. These summarize the work that is going on in our Department with the object of improving the information that we have about the distribution of income and the discussion of the employment problem in developing countries.

2. The studies referred to by Mr. Hawkins are those described on pages 68, 71, 73 and 75 of the booklet recently issued on the World Bank Group Research Program. The study referred to by Mr. Tiemann, in which we and the DRC are collaborating, is described on page 13 of the booklet.

3. Mr. Hume recently sent you a memorandum on the North-East Brazil project, and you received a copy of the latest back-to-office report on the Costa Rica study, prepared by Mr. Turnham. I am enclosing for your information a copy of a back-to-office report which Mr. Thias has prepared, in connection with the study of labor markets, following his recent visit to Malaysia.

cc (with attachments): Messrs. Duloy, Ahluwalia; Ray

cc: Messrs. Hawkins, Tiemann

OFFICE MEMORANDUM

TO: Mr. P.D. Henderson

DATE: September 14, 1972

FROM: E.K. Hawkins *EKH*SUBJECT: ECOSOC Speech

The following are the Research Projects initiated or approved from this Division this year which bear directly on lack of knowledge about employment and income distribution in LDC's:

Labor Markets in Developing Countries and Their Response to Education Expansion

The study investigates the structure and functioning of labor markets for educated manpower in developing countries. It seeks to identify the economic and institutional factors which determine the employment of secondary school graduates.

Labor Force Participation, Unemployment and Income

This study proposes to establish a framework for empirical investigation of labor market conditions in developing countries and to evaluate the utility of existing procedures and their results.

Costa Rica Unemployment Survey

This project is intended to obtain reliable statistics on the level of unemployment in Costa Rica. The information gathered is expected to provide an improved statistical base for framing policies for Costa Rica's socio-economic development as well as illustrating a methodological approach to employment surveys which may be applicable to other Central American economies.

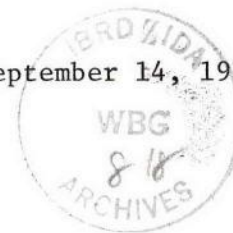
Study of Underutilization of Urban Manpower in Northeast Brazil

This study investigates the sociological and economic aspects of underemployment in Northeast Brazil. The study provides an opportunity not only to gather important information of direct policy relevance but also to fill a general need for data on marginal groups in the work force, on the nature of underemployment and on the operation of the urban labor market.

OFFICE MEMORANDUM

TO: Mr. P. D. Henderson

DATE: September 14, 1972

FROM: Arthur E. Tiemann *AET*SUBJECT: Material for McNamara ECOSOC Speech

In recognition of the crudity of statistics on income distribution and lack of information on this subject, the Bank has approved a research project on income size distribution and several steps have been taken to get the project moving. In particular,

- (1) The UN Statistical Office, the ILO and other interested international organizations have been informed of the Bank's interest. I was invited to participate, as the Bank's representative, in the Working Group which has developed a proposed system of statistics of income, consumption and accumulation.
- (2) The Bank is cooperating with ECLA and ILPES in exchanging information on research in income distribution and has been invited to meet with experts on this topic in Santiago.
- (3) I represented the Bank at the Conference of Asian Statisticians, sponsored by ECAFE and the UN Statistical Office, and the Bank was requested to assist financially in supporting an ECAFE Working Group on Income, Consumption and Wealth.
- (4) A French consultant, under my research project, has completed a study to develop a methodology for improving the quality of income distribution statistics through the use of national accounts and socio-economic data. The method has been applied successfully to five countries, and a report will be published after the translation from the French is completed.
- (5) A cooperative effort with the Bank's regional offices, Economics Department staff and me is currently working with the chief statisticians of Malaysia and the Philippines to make the best use of the statistics collected in the household income surveys in those countries. Data on income distribution in Thailand has been promised to the Bank.
- (6) As part of the income size distribution study, statistics on several additional countries have been collected and are now being classified in order to permit more valid cross country comparisons and better evaluation of the quality of the data.

The demands by developing countries for consultant assistance generated in the implementation of the research project have resulted in an increase in the estimated costs. These additional costs were spelled out in my memorandum showing consultant requirements for the balance of the fiscal year.

OFFICE MEMORANDUM

TO: Mr. Alexander Stevenson

DATE: September 12, 1972

FROM: H.H. Thias *HTC*SUBJECT: Mission to Malaysia: Back-to-Office Report

On my way to Kuala Lumpur I stopped in London to contact a number of British agencies and to discuss with their staff various aspects of the planned labor market study in Malaysia. In particular, I talked to officials in the Commonwealth Secretariat and ODA about their most recent work in Malaysia, and with the London City and Guilds Institute about vocational education programs in that country.

Upon my arrival in Kuala Lumpur on July 12, I called on Mr. Pathmanaban, Head of the Manpower Division of the Economic Planning Unit (EPU) in the Prime Minister's Department, who was our main contact during the mission. He arranged for a series of initial meetings with representatives from the various relevant Government departments, succeeded by numerous detailed follow-up discussions.

The first two weeks in the country were used:

- (i) to find out what labor market information was already available in a usable form;
- (ii) to determine to what extent existing "raw" information could be processed and used for the study;
- (iii) to decide what additional data collection would be required.

In very broad terms, and following for the sake of convenience our study outline of March 23, the data situation can be summarized as follows:

1. Data concerning the "requirements matrix" : in 1967/68, the Ministry of Labor undertook the compilation of a Dictionary of Occupational Categories. Among the unpublished background material is a detailed description of several hundred occupations including specifics of "necessary" formal education, vocational training and practical experience. No attempt has yet been made to use this material, e.g. for comparisons with the qualifications actually demanded by employers.

2. Data concerning the "demand matrix" : two main sources of information exist, neither of them, it is suspected, being free from major bias. The first is the register of job openings that are handled through the country's employment offices (between 2500 and 3000 each month). By the Ministry's of Labor own estimate, they cover only 20 - 25% of all job openings (taking other available information into account, this estimate appears low), presumably biased towards urban areas and medium-sized and larger firms. The relevant information (including details about education and experience required as well as salaries offered) is collected

on special forms (the so-called PP9 forms) but only used for the recruitment process itself. A systematic analysis of a sample of job openings should provide valuable insights into demand patterns for qualified manpower. The second source of information - newspaper advertisements - is likely to show the above-mentioned bias in an accentuated form. The reason for including this source of information in the data base is that it is the only source permitting longitudinal comparisons: we intend to analyse the job openings occurring during a certain reference period in 1968 and 1972, respectively.

3. Data concerning the "supply matrix" : the employment offices have files of about 170,000 job seekers who have to re-register every six months if they want to be eligible for jobs processed by the employment offices. This covers a high percentage of the actively unemployed, and probably an even higher one of the medium-level manpower the study will be concentrating on. The registers (the so-called PP1 forms) are aggregated in a national file which is updated monthly and used to produce a limited amount of monthly and quarterly statistics. It is hoped that a copy of the tape containing the national file can be obtained from the Ministry of Labor.

4. Data concerning the "recruitment matrix" : the only available information seems to be the PP9 forms, which also identify the names of the - successful and unsuccessful - job applicants referred by the employment offices. One might try to combine the information contained in the PP9 forms with that in the respective PP1 forms of the referrals. However, the fact that the tape with the national file contains only part of the original PP1 information would in all likelihood thwart this attempt to indirectly analyze the recruitment policy of employers.

When reviewing the available data we soon become aware of three important data weaknesses: one being the incomplete coverage and presumed bias of the demand data, the second the great practical difficulties of linking information on job openings and on job applicants, and the third the absence of some specific information on job-seekers (in particular their salary expectations).

This suggested that any additional data collecting efforts should concentrate on filling those gaps. Two separate surveys appear to be required: one addressed to a sample of employers (establishments) enquiring about their recruitment, promotion, and training policies, and the other to a sample of school leavers asking details of their unemployment/job histories (a "tracer study").

The Malaysian officials concurring with this view, I worked henceforth on the assumption that the subsequent field work would follow the course just outlined, and suggested that Mrs. Asher should participate in the preparatory work. She arrived in Kuala Lumpur on July 29. Apart from completing the collection of available data, we then worked on the preparations for the two planned surveys for the remainder of the mission.

On the side of the tracer study, the survey population had to be determined, and the addresses of the prospective interviewees to be found. This information, together with data on ethnic and social background were available in the school registers; the schools had also separate information on the school performance of their former pupils. In accordance with the study outline of March 23,

eight schools representing the general, technical, and vocational branches of secondary education, were selected, and the 1970 and 1971 cohorts of Form V^{1/} leavers taken as reference groups, i.e. those school leavers who at the moment of the survey will have been two (one) years in the job market. For practical reasons as well as for the sake of geographic homogeneity of the subsamples, it was decided to limit the survey to the cities of Kuala Lumpur, Penang, and Kuantan^{2/} (which represents a fairly satisfactory regional spread).

On the side of the establishment survey, we undertook similar preparatory work. From the frames of establishments available in the Statistics Department, we selected stratified random samples and prepared lists with addresses of establishments. We encountered two difficulties: one was the obsolescence of some of the sectoral frames, the other incomplete coverage: only for the manufacturing, mining, construction and hotel sectors are there suitable frames. In the case of rubber plantations (the country's largest employer), the frame is stratified differently, requiring some rearranging and in the case of commerce, it is just being compiled (and might be ready by the time the survey gets under way). The other sectors will have to remain uncovered for lack of a suitable sampling basis^{3/}.

Furthermore, we designed (and to a limited extent tested) the questionnaire for the establishment survey. Despite the small number of firms contacted we got some useful results which will be taken into account when we prepare the final version of the questionnaire.

After a series of final discussions with staff of the Ministry of Labor and the Economic Planning Unit I returned to the Bank on August 21. Mrs. Asher remained in Kuala Lumpur for another week to complete the data collection and to undertake the coding of the 1968 sample of job advertisements.

To sum up, Malaysia appears to be a very promising country for a case study on labor markets. The officials contacted were both knowledgeable and very cooperative. There is a great deal of unexplored data of comparatively good quality; it seems that the main bottleneck is on the data processing and "digestion" side rather than with data collection. The fact that the Government is at present

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- 1/ Form V is, in terms of academic selection, the most important "watershed" during the secondary education cycle.
 - 2/ These were the only three cities with technical secondary schools.
 - 3/ For the government sector the case is somewhat different, the (federal and state) Public Service Commissions/Departments being assigned the role of recruitment agent; they will be treated separately in the study.

September 12, 1972

preparing a Manpower Survey^{1/} may have both its advantages and drawbacks for our study: while it may supply us with additional recent information, it could add to the "survey fatigue" of firms which we noticed in a few instances. On balance, however, the latter should not affect the outcome of the study.

1/ We have consulted with EPU to make sure that duplication of questions is kept to an absolute minimum.

HHThias:ed

Cleared with and cc: Mr. E.K. Hawkins
Mrs. S. Asher

cc: Messrs. P.D. Henderson
B. Sandberg (EAP)
N. Erder (EDP)

Messrs. Henderson & Duloy

Ernest Stern

ECOSOC Speech

818/2/6
September 13, 1972



Mr. McNamara will address the upcoming ECOSOC meeting. He will probably extend his comments on the problems of income distribution and employment made at Santiago and planned for the Annual Meeting address. In both cases he emphasized the crudity of the statistics and our lack of knowledge about the subjects. In preparation for ECOSOC, we would like to know what measures have been initiated to improve our knowledge.

Would you let me have by noon, Thursday, a list of research projects or other activities (undertaken unilaterally or in concert with others) which were initiated by the Bank this year which deal with these issues. (The short deadline is no doubt compensated for by the fact that the list will be quite short.)

cc: Messrs. Ahluwalia
Hawkins
Ray

EStern/lm

Mr. Philip Hayes

September 13, 1972

Ernest Stern

ECOSOC Speech



Attached are the paragraphs proposed for McNamara's speech dealing with the Bank economic reporting system. Would you please look these over and return an annotated copy and all comments to Hollis in the next day or so.

Attachment

EStern/lm

SEP 15 1972 ✓
McK.

OFFICE MEMORANDUM

TO: Mr. Hollis B. Chenery

DATE: September 13, 1972

FROM: Ernest Stern *ES.*SUBJECT: ECOSOC Speech*Stern*

Chuck Weiss has already reviewed the paragraphs on technological research and submitted his comments to Demuth. A copy of his comments is attached.

I have forwarded the section on the Bank economic reporting system to Hayes for comments.

In regard to the suggestion for an occasional State of Development report, I would strongly urge that we delete the detail on pages 4 and 5 which indicate where such reports might be prepared. Given the nature of the forum in which the speech will be made, and the past history on this subject, the inevitable conclusion will be that the responsibility for such a report will be assigned to the Committee on Development Planning. Indeed, if I remember correctly, the terms of reference of that Committee envisaged a periodic global review. If such a report is to serve any purpose at all, it cannot be allowed to become bogged down in the United Nations system. Moreover it appears to me to misunderstand the purpose of such a report to suggest that it can be discussed in the General Assembly, in ECOSOC and in other political bodies. The representation at the United Nations is predominantly in the hands of foreign ministries, and their representatives have little concept of development problems. The discussions will be entirely around the political minutiae which constitutes UN politics, and the report will not achieve the educational value of the domestic decision makers which presumably ought to be its principal purpose. My personal view is that if we think such a report is desirable, the Bank needs to take the initiative from time to time to set up independent special commissions. We need not foot the bill alone, as we did for the Pearson Report, but we must insist on the independence of the commission and its capacity to function outside any of the existing bureaucracies. To keep this option open, I suggest that McNamara limit himself to a description of the problem (which ends in the middle of paragraph 4) and to conclude that one solution to the problem would be an occasional review

I think this has been done

Mr. Chenery

- 2 -

September 13, 1972

by a wholly independent body sponsored by all interested international agencies and governments. This point is reasonably well made in the first five lines at the top of page 5. The rest of the material on page 5 should be deleted.

(What United Nations reports, even on important current subjects, inevitably look like can be seen in the annual economic reviews and the 1970 Report on the World Social Situation. A copy of the latter is attached.)

Attachment

OFFICE MEMORANDUM

TO: Richard Demuth
FROM: Charles Weiss
SUBJECT: ECOSOC Speech

DATE: September 12, 1972



1. Thank you for letting me see the paragraphs on need for internationally supported research for the proposed draft of Mr. McNamara's speech to ECOSOC. I think the speech will, if delivered, be a fine contribution to the discussion of science for development.

2. Regarding the sentence at the top of Page 3, there exist "esoteric problems that delight the scientists" and at the same time are clearly directed to solving immediate and important problems of the LDC's (e.g., the sex life of the tick and tse-tse fly!).

3. The world scientific community is our natural ally, and it would be best to placate it by referring to mission-oriented research and not prejudice whether this will turn out to be basic, applied or adaptive in particular cases. To do otherwise will bring a storm of unnecessary criticism.

4. A minor point: It is probably too optimistic to say that we "ought" to have an agreed agenda of research needs soon, at least in the sense that it is likely that the OECD inventories will be ready soon. There are signs that the British and French may be dragging their feet. In the sense that it is essential that the inventories be prepared, the text is entirely correct. (Eventually, the text should be checked with Ed Martin.)

cc: Mr. Stern
Mr. Hoffman

Stem

OFFICE MEMORANDUM

SEP 11 1972
September 11, 1972

TO: Messrs. Knapp, Chenery, J.H. Adler, W. Clark. DATE:
FROM: Richard H. Demuth *RHD*
SUBJECT: Suggested Themes for ECOSOC Speech



Attached, as requested at the President's Council meeting this morning, is a memorandum which I sent to Mr. McNamara on September 8, suggesting certain subjects for discussion in his ECOSOC speech.

Ernie
The speech will include items 1 & 2 & omit 3. Weiss should go over 1 & make suggestions to Demuth.
Stem
ARZ

Ernie -

The speech will include items 1 and 2 and omit 3.
Weiss should go over 1 and make suggestions to Demuth.

HBC

Mr. McNamara

September 8, 1972

Richard H. Demuth

ECOSOC Speech

Attached, as requested, are first drafts of paragraphs on three subjects that you might want to consider for inclusion in your speech to ECOSOC, tentatively scheduled for October 18. The subjects are (1) the need for a great deal more internationally supported technological research directed specifically to the problems of the LDCs; (2) the contribution of the Bank's ~~new economic reporting system to the measurement of economic and social developments in the LDCs and to the identification and analysis of problems requiring action at the country level;~~ and (3) the need for periodic Pearson-type State of Development reports to perform somewhat the same functions at the global level. These paragraphs are designed for use as a wind-up section of the ECOSOC speech, following a condensed version of your Annual Meeting speech. The technological research piece needs some beefing up, I believe, and all the pieces need to be woven together and given an appropriate introduction. Before doing further work on these drafts, however, I would like to get your reaction to the ideas themselves as components of the ECOSOC speech.

If you decide to use the paragraphs on the need for periodic State of Development reports, I think we should give Philippa de Saynes a chance to comment before printing the speech.

MLHofman/RHDemuth/pnn

cc Mr. Weiss & Tech. Research paragraphs

Paragraphs on need for internationally supported technological research

Use
World
Report

Probably no contribution to development has been so universally acclaimed as that made by the agricultural research institutions that were responsible for creating and introducing new high yield grains. Nor has any other outlay of funds motivated by the desire to help improve life in the third world had anything like as large a payoff over the years. But the payoff was neither prompt or predictable. And the research during the critical years was not planned or supported by governments but by private foundations. It was only with the formation in 1971 of the Consultative Group for International Agricultural Research, of which the World Bank is proud to be a sponsor in collaboration with the FAO and UNDP, that a significant number of governments accepted responsibility for arranging long-range support of agricultural research for the benefit of the world as a whole, rather than just for particular countries.

It seems clear to me that there are other areas where research on technologies desperately needed by the developing countries is going to have to be approached on a similar international basis if anything effective is to get done. I have in mind the need for such things as radically cheaper methods of providing housing, water supply, sanitation facilities, basic education and urban transport. The whole area of industrial technology appropriate for developing countries must be much more systematically examined with a view to making really substantial increases in industrial production possible at competitive prices, thus providing employment for much larger proportions of the labor force. I have also in mind research designed to improve the competitive position of natural products produced and exported by developing countries, a matter whose importance has recently been underlined in a resolution of UNCTAD III. Many of these technical

bottlenecks have been identified by the Secretary General's "Advisory Committee on the Applications of Science and Technology to Development" (ACAST). A further pinpointing of key research needs is being carried out under the auspices of the OECD Research Planning Group on Science and Technology.

We ought shortly to be in a position of having a generally agreed agenda for priority technical research needed to enhance the effectiveness of the whole development effort.

General resolutions recommending more resources for research and development of benefit to less developed countries will not get us very far. The job is too vast for the private foundations to handle by themselves, important though their contributions are and will continue to be. Private industry will continue to do some research on adaptive technologies but the record of the past few decades suggests that the impact of new or adapted technologies introduced into the poorer countries by private industry seldom extends beyond a limited modern sector of the economy and provides much more limited benefits than many of us had hoped ten or twenty years ago.

And yet it is clearly illogical to continue to press for larger development investment programs, whether financed by increased savings from the people of the developing countries themselves, or by increased external assistance, without insuring that the appropriate research base is established. It is not only illogical, it is imprudent. A private corporation operating, as are all development agencies, in areas of changing technology where competition for resources is keen, would soon find itself in trouble if it did not allocate a significant percentage of its investment outlays to research and development. There is just as great a need for research support for the national and global investment programs we are all trying to carry out. What we are talking about, of course, is not research on

esoteric problems that delights the scientists, but mission-oriented and largely adaptive research clearly directed to solving immediate and important problems of the developing countries.

The costs of technological research of the nature and scale required are too great, and the benefits too unpredictable and too diffuse, to warrant the necessary outlays by the governments of individual developing countries, except perhaps some of the very largest. But a well organized combined effort to mount international and regional research programs, manned by the best available scientists, and working exclusively on the adaptation or development of technologies appropriate for the developing countries, might, I believe attract the necessary political and financial support, particularly now that we have the analogy of the CGIAR. The Bank would be prepared to cooperate actively with governments, the UN, the UNDP and other agencies in developing the plans for this major but badly needed new initiative.

Paragraphs on (1) the Bank's economic reporting system; and (2) the need for new machinery to produce periodic Pearson-type State of Development reports.

Hayes / Stern

Current debate in this Council, and elsewhere, indicates to me that governments are much concerned about how to record and measure economic and social developments. It is right that they should be so concerned. How can a government that cares seriously about the welfare of its people, and the difficult, often staggering problems that they face, find out without an exorbitant expenditure of money and skilled manpower what really is happening in the various sectors of its economy? Are people in the different regions and occupational groups, in the towns and on the farms, becoming better or worse off as the years go by? And how can this be done so that information becomes available quickly enough for timely action to be taken and the people to be told where their true interest lies? And how can the people of the world know whether the international development effort as a whole is succeeding or failing in this part of the world or that, in education or in health; whether things are better or worse, and in what sense?

The Bank has long considered it to be one of its major functions to help its member countries in recording and measuring various aspects of social and economic development and in identifying and analyzing problems that require action, particularly, but not exclusively, on the part of public agencies and the political leadership of the country. We are continuing to examine how we can be more useful in this field. Last year we established a new system for Bank economic reports to consist of three general types of country reports:

1. Basic Reports: These ^{will} ~~would~~ examine the long-term development of the economy in perspective. They would endeavor to deal with all matters vital to the understanding of options open to the government and with the need for

external assistance. They would evaluate the institutions responsible for managing the economic and social sectors. As problems of a long-term nature do not change significantly from year to year, such reports can be usefully written only every 4 or 5 years. We hope that in many cases, the timing of such reports can be made to fit the planning or programming cycle of the country in question. For FY 1973 we plan to produce basic reports on [14] member countries.

2. Current Reports: These would have two distinct purposes. On the one hand, they would deal with any developments that would necessitate changing the analysis in the last basic report. On the other, they would appraise the short-term problems of the economy, stressing such matters as fiscal performance, foreign trade, and the volume and terms of external assistance, which are of concern both to the government and to the Executive Directors of the Bank in connection with their reviews of Bank and IDA operations in such countries. For larger countries and countries in which the Bank Group is particularly active, current reports will normally be written annually. Our program calls for current reports on [52] countries in FY 1973.

3. Special Reports (of various kinds): These would include detailed surveys of particular economic or social sectors and studies of problems such as taxation that cut across all sectors. [58] special reports are programmed for FY 1973.

In connection with all this work the Bank is endeavoring to develop a standard set of statistical tables common to all countries in coverage and format. This is a very long-range endeavor which can never be more than partially achieved as it is necessary to work with established series of national statistics and these can only be conformed to common definitions in the broadest sense.

This program of economic reporting can be briefly described, but it is in fact a sizeable undertaking. In carrying it out, we are trying to avoid multiple calls on governments and agencies for information. It is often the case that a recent report of a mission of the IMF covers much of the ground which needs to be covered by a Bank current economic report. In such cases we rely on the Fund report and do not repeat the analysis, though the Bank report may have to add material on matters outside of the concern of the Fund.

The schedules of forthcoming Bank missions are sent regularly to other interested UN agencies and Bank reports are regularly distributed to the other agencies in the UN system, as well, of course, as to all member governments of the Bank Group. We have clear evidence that our reports are being used extensively and are highly regarded by the professional staffs of both international agencies and member governments. We are now planning to publish as many as possible of both country economic reports and sector reports, with the agreement, of course, of the governments concerned. Many governments have made it clear that they would like to have the facts, figures and analyses contained in the standard Bank reports available not only to public officials, but to scholars, businessmen and the news media in their own countries.

But country reports, no matter how expertly prepared and readable, are not enough. Moreover, adding up figures from a lot of national reports will not tell us the full story as to whether or in what sense real progress is being made in the developing world as a whole. In my address to the recent meeting of the Boards of Governors of the Bank Group institutions, and here today, I have engaged in a form of review and appraisal of what seem to me to be some key problems facing the developing nations. My colleagues, the Directors General of the other Specialized Agencies, the Chairman of DAC, and of course the Secretary General, regularly address the international

community with reports and evaluations of major world trends as they comprehend them. The Committee Development Planning, the Regional Economic Commissions and this Council all hold reviews.

But the eyes and ears of the world, governors and governed alike, are assailed by a medley of tracts and voices, many, I fear, more sensational or louder than anything international agencies produce. Some glory in small failures, making mountains of disaster out of mole hills of transient difficulties. Others thrive and prosper on periodic prophesies of general doom. Still others seek to assure this or that constituency that everything is rosy and that the management of the people's affairs is in the best possible hands. What is the listening world to make of all this? Where can the people turn?

Despite all the reporting, evaluating and reviewing now going on throughout the UN system, I do not believe that we yet have what seems to me to be needed at this juncture in the international development effort -- a periodic, objective and impartial review of development progress and prospects by a body of wise and experienced persons not under the control of any government or group of governments, or of any international agency, and with its own high-level independent professional staff. Such a review would encompass the progress of development; the economic and social problems facing the developing countries and their successes, or failures, in coping with them; the aid and trade policies of the developed countries; and, not least, the policies and performance of the multilateral agencies. Such a body could identify policy issues calling for attention by governments and international organizations and could make recommendations for an improvement in development and development assistance efforts, both national and international. It could relate progress to the various norms and policy prescriptions adopted by political bodies such as this Council, the General Assembly and UNCTAD. But

it should, beyond that, subject the norms themselves to critical review. It should be a wholly independent body looking at the whole development effort. I believe that the voice of such a body would be heard above the cacophony and that its judgment and advice could become a powerful coordination force to the benefit of all of us, in governments and international organizations alike.

4-5
A comprehensive report on the State of Development is needed only every two or three years; special reports on specific problems of major significance might be produced in other years. The reports of the review group would be transmitted to, and debated in the General Assembly, this Council, the Trade and Development Board and other political bodies, as well as in the governing bodies of the Specialized Agencies and of the regional financial institutions. They would provide a focus for the review and appraisal of D.D. II.

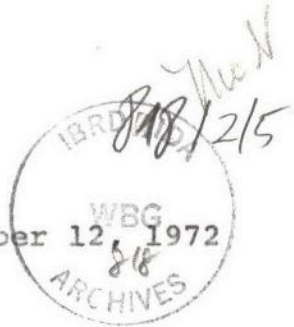
It is the objective that needs to be agreed; I have no preconceived ideas about the machinery required to achieve it. Perhaps the Committee for Development Planning, given a full-time Chairman and a strong and independent staff of its own, could do the job. But I think it would be preferable to establish a smaller group that would include, in addition to economists, leading personalities with experience in public affairs, business, labor and agriculture -- somewhat along the lines of the commission assembled by Mr. Lester Pearson in 1968, but with the participation of nationals from the Eastern European countries and greater participation of nationals from the developing countries. There are many feasible ways to accomplish the objective I have outlined, none of which needs to be elaborate or very expensive, but it is not my purpose to go into such details today. If the objective itself is agreed to be desirable, the Bank would be happy to discuss with the Secretary General and others concerned ways and means to organize and finance the necessary machinery.

Mr. Robert S. McNamara

Ernest Stern

Social Justice Programs in Rural India

September 12, 1972



This is the report I was thinking of at lunch yesterday. If you have not read it yet, I commend it to your attention. The problem of credit to small farmers is discussed in Paragraphs 51-58 and in the recommendations (Paragraph 72).

Attachment

EStern/lm

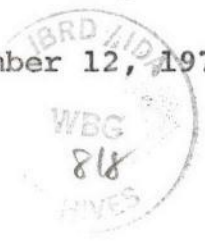
818/2/4

Messrs. McNamara and Chenery

September 12, 1972

Ernest Stern

Attached Report



The attached paper was written by the staff of the Harvard Advisory Group in Ghana. It is a fascinating post-mortem of the decision-making process that led to the devaluation. The report is exceptionally frank about the roles of individuals and is therefore highly sensitive. The DAS agreed to this limited circulation, but I promised to stress that no further distribution of any kind would occur without their express consent.

Attachment

EStern/lm

Mr. R. H. Demuth

September 5, 1972

Ernest Stern

Visit of Mr. Paul-Marc Henry



As you know, Mr. Paul-Marc Henry will be in Washington September 30 to attend the SID Council Meeting. He told me in Belgrade that he should like to meet with Mr. McNamara and, subsequently, some other Bank officials. He will be available October 2 and 3.

Depending on Mr. McNamara's interest and schedule, either a luncheon or a meeting during the day would be suitable. Paul-Marc is, as you know, an interesting person with broad experience, and Mr. McNamara might enjoy the more leisurely setting of a luncheon.

Could you consider whether a meeting could be arranged and advise Giulio Fossi in Paris, who is in charge of the schedule.

EStern/lm

OFFICE MEMORANDUM

818 / 2/2

2743

TO: Mr. Robert S. McNamara

DATE: August 4, 1972

FROM: Ernest Stern *ES*



SUBJECT: Appropriate and Inappropriate Technologies

8/4

If you haven't seen this, it is worth reading. The case study illustrations provide several good examples of the strong drive (intellectual and financial) in the developing countries to choose the wrong technology and the alternatives that would have been available in each case.

The "future policy measures" are a grab-bag of old and new ideas, good and bad ones.

Attachment

President has seen

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RESEARCH
FILES

Appropriate & Inappropriate Technologies



SOME CASE HISTORIES . . . BRIDGED FROM A PAPER
BY KEITH MARSDEN
Small Industries Adviser to International Labour Organisation.

Everybody would agree that aid for developing countries should bring the maximum improvement in living standards to the maximum number of people. But how is its effectiveness to be judged? To arrive at a realistic assessment there are four questions which can and should be asked of any aid programme:-

1. Does it make the optimum use of resources already available?
2. Does it make for social progress by bringing benefits to the mass of the population and not merely to a privileged few?
3. Does it represent technical progress in terms of improvements over existing methods rather than by measurement against arbitrary and possibly irrelevant standards?
4. Is it flexible enough to allow for change and growth in subsequent years?

It is clear that many schemes are not satisfactory when judged by these criteria.

1. Many planners seem unaware that a machine which would be economic in a situation where capital is plentiful and labour scarce becomes uneconomic when the situation is the reverse.

Case Study Illustration

The total costs of alternative methods of making wooden window frames have been compared in the two situations referred to above. It was found that in the labour-expensive country two special purpose machines, one performing foursided planing and moulding, and the other a double ended tenoner, were the cheapest combination for output capacities in excess of 50,000 units per annum. In the cheap-labour-dear-capital country, however, they would be uneconomic unless the capacity

exceeded 450,000 units per annum. Up to an output of 64,000, which encompasses the great majority of carpentry workshops, the lowest units costs would be achieved by using single-purpose planing and thickening machines and single-ended tenoners, with a considerably lower investment per worker.

2. It is not always realised that large-scale, capital-intensive schemes will only achieve good results if markets are substantial, distribution channels are well organised, workers are used to factory discipline and those in charge are trained in management techniques. If these conditions do not apply, results are bound to be disappointing, as these examples show:-

- A large public sector shoe factory operating at 20 per cent of capacity because it had no means of reaching the small private shoe retailers who handled 90 per cent of the shoe trade.
- The battery plant satisfying a month's demand in five days.
- The woollen textile factory with a 10 per cent material wastage figure (costing precious foreign exchange) because the management did not know how to set and control material usage standards.
- The \$2 million date processing plant out of action for more than two years because no one knew how to repair a blow out in the cleaning and de-stoning unit.
- The confectionery plant inactive for most of the year because 80 per cent of sales were made during the month of a religious festival.
- The ceramics factory whose quality was poor because it had to use up two years' stocks of the wrong glaze, imported in error, because the general manager had too much work to attend to all details satisfactorily. Prevailing social attitudes accounted for a lack of middle management and responsible supervisory personnel and the management's reluctance to delegate authority.
- The radio assembly factory whose production line broke down repeatedly because of the high rate of absenteeism among key workers - to attend weddings, etc.

3. Even when run below capacity, advanced machinery can produce products more cheaply than traditional methods. But this may also mean that indigenous craftsmen are put out of work and only a small number can be reemployed in the new automated factories. The result is rising unemployment and depression of real income, so that the blessing of cheaper production never become available to the mass of people. In many instances, the main beneficiaries are the exporters of machinery, materials and components.

Case Study Illustration

One country imported two plastic injection moulding machines costing \$100,000

with moulds. Working three shifts and with a total labour force of 40 workers they produced one-and-half million pairs of plastic sandals and shoes a year. At \$2 a pair they were better value (longer life) than cheap leather footwear at the same price. Thus 5,000 artisan shoemakers lost their livelihood which in turn reduced the markets for the suppliers and makers of leather, hand tools, cotton thread, tacks, glues, wax and polish, eyelets, fabric linings, laces, wooden lasts and carton boxes, none of which was required for plastic footwear. As all the machinery and the material (PVC) for the plastic footwear had to be imported, while the leather footwear was based largely on indigenous materials and industries, the net results was a decline in both employment and real income within the country.

POLICY GUIDELINES

Recent history in the developing countries has shown that, when investment decisions are left solely to the industrialist, results for the country as a whole are not always happy. Private profit may be given pride of place over social welfare. Technical efficiency may be confused with economic efficiency. Furthermore, the individual entrepreneur is often unaware of the full range of technical alternatives that may be available.

In view of this, it is important for government policy makers and national economic planners to have certain considerations clearly in mind.

1. Investment policy must raise the productivity of all those in the traditional and subsistence sectors by substantial injections of capital into these. What is needed is not a few isolated "model" schemes which the mass of people have neither the capital nor the training to emulate. Rather, the ideal to be aimed at is a continuing process of step-by-step modernisation through which the discrepancies between the modern and traditional sectors of the economy are steadily reduced.

Case Study Illustrations

An automatic plant bakery, with pneumatic flour handling, continuous mixing, kneading, dividing and proving, a travelling oven and conveyer fed wrapping machine, costing \$4 million and employing 100 men could supply all the bread for a town of 100,000 people. But if the average income were only \$100 per head per annum and savings \$10 per head, the whole of the town's savings would go into the new bakery and the mass of the workers in other trades and industries would have to make do with less equipment than they had before (because of depreciation). Demand would fall too because of the reduced incomes of the redundant bakery workers. Thus total output and employment in the town would decline.

If, on the other hand, the existing small bakers were supplied with simple dough kneaders to replace hand mixing, at a total capital for the town of \$10,000, the

average labour productivity in the bakery industry could be raised by 10 per cent and there would be plenty of savings left over in the community to finance further investment in the other sectors where marginal increases in productivity could be achieved too. And there could be improvements in the social amenities of the town, e.g. hospitals, schools, etc. Thus growth would be balanced and mutually self-supporting.

2. The technologies chosen must suit the widely varying social and economic environments which may be encountered. For subsistence economies, only simple artisan workshops are likely to be suitable. In more advanced societies, it may be possible to establish small factories, though these should always be of a size and nature to ensure that personal relationships, hours of work, etc. are kept flexible and informal.

Case Study Illustrations

In Japan, which has achieved the most rapid sustained economic growth of any country in this century, small and medium firms (under 300 employees) have taken the lead in many industries and as late as 1954 employed 59 per cent of the total labour force in industry. In Japan small firms make 100 per cent of the toys, 87 per cent of household utensils, 81 per cent of leather shoes, 78 per cent of printing ink, 71 per cent of farm utensils, 70 per cent of cotton textiles, for example. Much of their technology would be classed as obsolete in the U.S.A.

In the U.A.R. small firms (less than 100 workers) achieved a higher productivity of capital than did large firms in 15 out of the 20 major industrial classifications in the 1960 census. Yet their capital intensity was generally much lower. A similar picture is found in Indian and Ecuadorian data.

3. New technologies must stimulate output in indigenous industries, processing indigenous raw materials, thus saving scarce foreign currency and providing work for a wider range of people.

Case Study Illustrations

A ceramic factory making floor and wall tiles formerly imported its hand-operated presses. In co-operation with small engineering workshops in its locality it was able to have replacement presses made locally, using castings, moulded from scrap metal in small foundries and machined on general purpose lathes and drilling machines. The tiles themselves were made from indigenous clay deposits, and fired in kilns composed mostly of local refractory bricks. Thus output, income and employment were stimulated in a number of other industries and trades, e.g. scrap metal, foundry, carbon, refractory, engineering, mining.

This multiplier effect was just beginning to make itself felt when it was decided to build a modern large-scale ceramic plant in place of the existing one, with high-speed fully automatic presses, continuous tunnel kilns, etc. This equipment required special steels and engineering skills, refractories with a high aluminium oxide content and technical know-how which were not available

locally (and were not likely to be for many years). Therefore, they had to be imported. Also because of the high speed of operation, very malleable clays were required and these too had to be imported. In the end the consumer got a poorer quality, dearer product because the breakage rate was higher due to: a) inadequate temperature control in the tunnel kilns (technological inexperience); b) clumsy handling during glazing operations (inadequate supervision in the new factory). Employment and net output declined in the ceramic and allied industries listed above and the country's trading deficit widened.

The second case study illustration is more encouraging. An Asian country which had formerly imported its sewing machines decided to promote its own machine building industry. A nucleus already existed in the small workshops manufacturing replacement parts for imported models. Profiting from the temporary protection afforded by import restrictions local entrepreneurial initiative quickly appeared to co-ordinate and expand the activities of these specialised workshops and set up assembly units. In a few years the sewing machine industry, equipped with general purpose lathes and drills (rather than multi-spindle boring machines and special jigs) was turning out models at 60% of the price of previous imports. The local sewing machines had a more limited range of operations, and were less accurate, but because of their lower price, they had opened up a new market among small scale clothing and footwear establishments, thus increasing their efficiency. By 1966, import restrictions could be relaxed and the industry was strong enough to have established a thriving export trade to neighbouring countries.

4. The productivity of capital should be maximised and the real social cost of making a product should be minimised. This is true, even when it means ignoring the considerations that normally apply when making private investment decisions - for it has to be remembered that money costs do not always reflect the real costs to society when using the factors of production.

Case Study Illustrations

A tanning industry project in one country envisaged building a small model tannery to act as a training centre and to demonstrate new techniques, together with a number of new buildings to rehouse existing tanneries, thus improving working conditions and separating the industry (with its obnoxious smells) from the living quarters. The total capital costs were projected as \$2½ million for an output of \$15 million per annum (a high capital productivity). The buildings and some of the machinery could be made locally so the import content was small. Demand for leather was growing at 5 per cent per annum and labour productivity was expected to rise at this rate due to improved methods and conditions, thus the total labour force in the industry of 3,000 would remain the same.

This project was rejected, however, on the grounds of not being modern enough. In its place was sustained a scheme for a large government-owned tannery estate, costing \$15 million, equipped with the latest imported machinery and with a total capacity 50 per cent in excess of the existing firms. Labour productivity would

be doubled but the savings in wages would be more than offset by higher capital (interest and depreciation) costs if a shadow interest rate were used. The productivity of the capital employed would only be 25 per cent of the anticipated level in the first project proposed.

Employment in the industry would be halved, the existing equipment made obsolete and the import bill increased by more than \$8 million. The present firms would be broken up and experienced owners made redundant. Little improvement in quality could be expected because further foreign exchange to buy better hides and tanning materials (which together with technical know-how were the primary determinants of quality) could not be afforded. And in international terms they would not end up with an expensive "white elephant", because heavy sole leather and even some upper leathers were being replaced rapidly in world markets by synthetic materials (e.g. resin rubber and vulcanised rubber compounds for soles, Dupon Forfam, polymeric material and PVC for uppers).

Thus the more modest scheme was not only more appropriate for the particular internal circumstances of this developing country but also gave it greater flexibility to take advantage of world-technological developments when it had the necessary resources (a petro-chemical industry).

On the other hand, there are undoubtedly examples of advanced capital intensive technology satisfying these criteria best. A case in point is a fibre board plant in an African country. This cost \$2 million and employed only 120 workers directly, because the higher pressures and great bulk involved required very heavy machinery. However, it processed the residue of sugarcane and maize stalks which would otherwise have gone to waste. Thus the value added during the process was high and it provided additional incomes to the farmers. The finished product was a good, cheap substitute for certain kinds of wood for furniture and housing. The wood had previously been imported, so foreign currency was also saved. This project therefore served the national interest in several respects.

SOURCES OF PROGRESSIVE TECHNOLOGY

Often in developing countries, unsuitable techniques are applied because nothing else on the market is known. There is an urgent need for the full resources of scientific and technical knowledge to be brought to bear on this problem. If this is done, it will be found that there are many resources which can be tapped.

New Designs

There is a great need for brand new designs which incorporate recent inventions but, at the same time, take account of the scarcity both of capital and of managerial and operative skills. Innovation is required also in the use of local raw materials. Research on this subject is already being carried out by United Nations agencies and by specialist bodies. But much remains to be done. It would be well if advanced countries were to set aside a certain percentage of their aid funds for work of this kind.

Case Study Illustrations

Capturing the heat of the sun by means of reflecting mirrors to distil fresh water from salt water, and as an energy source for industrial purposes.

"Hover" (air cushioned) tractors for small-scale cultivators.

Self-maintaining machinery.

The processing of date palm fibres to replace wool and hair in upholstery stuffing.

The extraction of creosote and charcoal from the husks and shells of coconuts and biological insecticides from coconut oil.

Modern Technologies

Modern technologies may often have an important part to play in developing countries. Four main groups in particular are worthy of consideration.

- i) Technical know-how with little or no capital element, e.g. methods of making or growing a product based on research into its chemical, biological or physical properties.
- ii) Technologies in which a particular process can be carried out mechanically without prejudice to the overall employment picture.
- iii) Machines to take the place of human skills which are not at present available and which cannot be cheaply cultivated.
- iv) Modern technologies which may be the only effective means of exploiting a country's physical resources.

Case Study Illustrations

Colour charts, penetrometers and triaxial compression testing machine for measuring the properties of soil and clays - leading to improved crop selection and rotation, higher land yields, cheaper more durable roads and improved ceramic products.

A modern gas or oil fired fuel system for a bread oven would give more precise temperature control, resulting in even quality and reduce wastage.

Diagnostic machines for locating and identifying defects in automobiles.

Tape-controlled, transfer machine tools which economise on skilled labour.

Infra red scanners and tungsten tipped drills for discovering and tapping hidden water and oil resources.

Long Established Designs

Classic designs which may have been superseded in more advanced countries can still prove useful at intermediate technology level. Much more could be done in this field by trade associations and by major international companies with subsidiaries in the developing countries.

Case Study Illustrations

Bakery Industry. Perkins steam pipe ovens which ensure an even dispersion of heat by means of coiled steam pipes; drawplate ovens in which the loading and unloading is speeded up by putting the plate of the oven on wheels and rollers; Viennar, T'arm kneaders in which a single reciprocating arm kneads the dough in a rotating mixing bowl. This equipment is more advanced and efficient than bricklined, open flame ovens and hand mixing, but is much less capital-intensive than turbo-radiant travelling ovens or continuous mixers.

Ceramic Industry. Oil or coal fired Bottle or Hoffman kilns; hand operated jiggers for forming plates, semi-automatic presses for tiles, gravity-fed extruders for pipes. These are all superior to traditional methods but less expensive than tunnel kilns and fully automatic equipment.

Shoe Industry. Simple Blake sewing machines (first introduced in 1859) for stitching the sole to the upper and insole. This is quicker than hand stitching but may be more appropriate than vulcanising or injection moulding equipment for soling in these countries.

Second Hand Machinery

Second hand machinery is frequently both cheaper and simpler to use than ultra-modern plant and can often be readily adapted by indigenous engineering industries. Such machinery, if rigorously inspected before use, can give many years satisfactory service and produce important financial savings.

Case Study Illustration

Table 1: Costs and Output of Alternative Sole Stitching Machines

	<u>Second-hand model</u>	<u>New model</u>
	\$	\$
Price	1,000	5,000
Depreciation period	5 years	10 years
Interest rate on loans	15 per cent	15 per cent
Yearly output	50,000 pairs	70,000 pairs
Number of operatives	1	1
Annual wage cost	500	500
Fuel and power costs	50	50
Light and floor space and insurance	50	50
Repairs and maintenance	75	100

Note: Servicing costs are higher for the new model because foreign engineers and spare parts are required, whereas the older, simple machine can be replaced by local personnel.

Table 2: Analysis of Direct Labour, Fuel and Capital Costs

	<u>Second-hand model</u>	<u>New model</u>
	\$	\$
Depreciation and interest	275	857
Fuel	50	50
Light, floor space, etc.	50	50
Servicing	75	100
Labour costs	<u>500</u>	<u>500</u>
Total	<u>950</u>	<u>1,575</u>
Cost per pair	\$0.0190	\$0.0225

This example is based upon actual costs which have been rounded off for simplicity.

Despite the fact that the new sole-stitching machine has 40 per cent greater productivity and double the anticipated working life of the older model, its costs per pair are 18 per cent higher. This is because capital costs are high and wages low. If the annual wages costs were around \$2,500 per worker, as in the U.K. shoe industry, this second hand machine can be bought so cheaply on the used equipment market. In this exercise materials costs are assumed to be constant. If anything, there would tend to be a greater percentage of material wastage on the new machine because of the higher speeds and the inexperience of the operative.

FUTURE POLICY MEASURES

It is unrealistic to think of providing each potential investor with a check list of do's and don'ts, together with a full inventory of alternative techniques, and then to wait until common sense and social justice prevail. The only practical approach is for governments to create a legislative framework and a general economic climate in which individual investment decisions, both public and private, tend to coincide rather than conflict with the national interest. Some possible steps are suggested below:-

- a) The formation of customs unions with other states at a similar stage of development and with complimentary resources. These would encourage a new international division of labour and a competitive stimulus for efficiency, while avoiding head on, heavily one-sided encounters between rich and poor nations in the international trade and technology fields.
- b) Higher official interest rates to raise the price of capital vis-a-vis labour costs. This would tend to bring more labour into productive employment as well as increase the propensity to save.

- c) Providing indigenous industries with ample scope to expand, develop and diversify over time without bumping their heads against competing industries which are technically more advanced because greater resources (uneconomically priced) have been placed at their disposal. Giving a clear run ahead to indigenous entrepreneurs is likely to be more conducive to growth and development than protective subsidies and quotas in an attempt to have the best of both worlds.
- d) Tax concessions and political guarantees to attract foreign capital and know-how, accompanied by legislation requiring all companies to buy a certain proportion of raw materials, components and replacement machinery locally within a fixed time period (as in Mexico).
- e) The setting up of documentation and information centres to keep track of past and current technological developments throughout the world. These would establish close liaison with international and other national advisory services for the selection of equipment.
- f) The provision of widespread primary and technical education facilities at the apprentice level, combined with night school tuition and upgrading courses for practising operatives, supervisors and managers. ILO sponsored vocational, instructor and management training institutes already function in many countries; while UNESCO programmes cover school, college and university education.
- g) Training courses for managers and planners in feasibility study and cost/benefit analysis techniques to increase the 'rationality' of investment decisions and in the use of other management tools (e.g. work study) which will increase the efficiency of existing manufacturing methods. The ILO and UNIDO are operating here.
- h) The encouragement, by state subsidies, grants, etc., of trade and research associations for each industry, sponsored and run by the members themselves. Special budgets could be allocated for importing standard machines to be stripped down, adapted and eventually reproduced locally.
- i) The institution of incentive rewards schemes for inventions, plus patent protection for local adaptations of foreign designs.
- j) The formation of common facility co-operatives and joint production workshops to raise the productivity of artisan and handicraft industries. The ILO Co-operative and Related Institutions Branch provides technical assistance in this field.
- k) The provision of extension services for small scale-entrepreneurs, providing advice on product and process development, technical skill information and the selection and use of appropriate technologies. Again the ILO is active in this work through Small Industry Institutes and experts on individual assignment.
- l) Long-term planning of manpower and skill requirements in the various sectors of the economy, closely related to the foreseen rate and character of technical change. The Manpower Planning Branch of the Human Resources Department of the ILO is advising several governments in this field.
- m) The adoption of factory legislative and safety regulations which provide adequate working conditions and safeguards for all groups of workers and do not create dual standards (i.e. for those within and those outside the practical jurisdiction of the laws) or act as barriers to expansion for the smaller enterprises.

- n) The creation of central quality control and inspection schemes to ensure that products destined for export meet external quality standards, but without imposing unrealistically high standards on total production within the country.
- o) Priority in the allocation of import licences for machinery and materials given to those organisations which have already demonstrated the aptitudes, skills and motivations required for success in the export markets.
- p) Conducting systematic market research surveys abroad to identify precise consumer needs (and appropriate distribution channels) which might be satisfied by the use of relatively labour intensive techniques. UNCTAD and GATT have already sponsored and carried out such investigation on behalf of member governments.
- q) The establishment of special Small Business Development Banks to reduce the differentials in capital accessibility between the traditional and the modern sectors. The IBTD is giving technical and financial assistance in this area.
- r) The planned distribution of industry to backward areas to provide more employment opportunities outside the major cities and to reduce income inequalities between regions. Processing of agricultural and other land based products are obvious choices (the FAO has substantial interest in this field). Valuable planning techniques have been devised in the socialist countries for this purpose.
- s) Financial incentives (e.g. tax rebates on training costs) to international companies to set up apprentice training schools, management development programmes and planned succession to management position for indigenous staff. This would reduce the foreign exchange costs of expatriate staff, while ensuring that their essential expertise in operating, servicing and managing more advanced technology is passed onto local personnel.
- t) Revaluation of currencies to ensure that the importer has to pay the real cost of foreign machinery and materials, and a proper evaluation is made in initial feasibility studies.
- u) State financed hire purchase and rental schemes with lower interest rates for imported secondhand machinery and locally made equipment.
- v) Subsidised factory premises in provincial towns and villages to slow down the population drift to the cities. The subsidies could be equivalent to the cost of housing and other facilities which would otherwise have to be provided in the cities.
- w) Tax holidays to foreign machinery and component manufacturers to set up local design and production plants to develop indigenous technologies.

Whether action along the above lines will be taken depends in the final analysis on how convincing a case can be established for the arguments which have been advanced in this paper. A great deal of further research is required to test the various hypotheses and to establish a firmer theoretical basis for them. Where they have been applied in the field the results are promising. They appear to open up new avenues for a dynamic attack on poverty in the developing countries, in which the progressive and wide-spread introduction of new methods (new compared with their traditional ones) could lead to a better use of their current resources and achieve a rapid sustained growth shared by the whole people.

2018

OFFICE MEMORANDUM



TO: Mr. Robert S. McNamara

FROM: Ernest Stern *ES*

SUBJECT: Study on U.S. Overseas Investment

DATE: July 11, 1972

8/18/2/1

I talked to Fred Bergsten, as you requested. The study on U.S. overseas investment, described in the attached, is still in the design stage. Work is scheduled to start after Bergsten returns from his vacation, in August.

Tentatively, he is planning a book with a chapter each dealing with the major economic and foreign policy aspects of U.S. foreign investment. There will be chapters on the impact on U.S. employment, the balance of payments, trade, political relations as well as the impact on development. The book is not limited to U.S. investment in developing countries and, given the distribution of U.S. foreign investment and Fred's interests, the emphasis will be on a) Europe, b) the effects on the U.S. of capital outflow. The book's objective is to propose a U.S. policy on foreign investment - something that is lacking at the moment.

I will stay in touch with Bergsten and keep informed on his work. However, the overlap with our direct interests is likely to be small.

President has seen

In view of these possibilities, it is expected that up to \$300,000 annually will be made available from this appropriation for each of the first two years and \$150,000 for the third year.

Funding with a matching requirement for a select number of projects as proposed here would be a halfway step between the broad program support approved in the 1969 appropriation and individual project support which might be considered after 1975. Brookings does not now have any matching funds clearly in sight for the eleven projects listed beyond July 1, 1972. However, Messrs. Gordon and Owen are optimistic about the opportunities for continued outside support and are satisfied that the proposed terms offer a realistic challenge to them.

In addition to the two-thirds support for the listed projects which is to be provided by Brookings or other sources, it should be noted that there will be other projects in the foreign policy studies program which will be financed entirely from non-Ford Foundation sources. Thus in relation to the complete foreign policy studies program three-year \$5,000,000 budget, the proposed contribution toward the eleven selected projects should mean that Foundation funding for the full program will remain significantly below one-third.

Brief comments summarizing those projects for which support is recommended follow:

Defense Policy Studies (\$400,000 over three years). This is in our view perhaps the single most important segment in the program and at the same time the one for which it is most difficult for Brookings to find outside support. More effectively than perhaps any other private domestic body Brookings through the defense analysis project contributes to the public understanding of "the main problems which give rise to U.S. military activity, the policies and capabilities of potential adversaries and the implications of alternative defense postures and budget levels." The problems faced by any private organization which attempts to understand and interpret defense policies are very great. Brookings has assembled a skilled staff and gained sufficient experience to accomplish this task with distinction. Alton Quanbeck, a retired Air Force colonel and systems analyst, has replaced Professor William Kaufmann of MIT as head of the project. The two additional senior fellows are Martin Binkin, another retired colonel, and Arnold Kuzmack. Over the next three years this part of the program would again produce the defense sections for the annual volumes analyzing the Federal budget entitled Setting National Priorities and 12 to 15 staff papers upon which these more general analyses would be based. The defense analysis section of the "budget book" has grown from 75 to 125 pages over the past three years, and consideration is now being given to its publication as a separate volume. The topical areas for staff papers which are projected include: tactical air issues, considerations of nuclear strategy, the future of naval force levels, the all-volunteer army, and related

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Please ask Emil Stern to
discuss with Fred Bergsten his
study on private investment + report

manpower questions. On the recommendation of a special visiting committee (consisting of James Killian, Paul Nitze, Charles Rossotti, Matthew B. Ridgway, and Henry Rowen), the program will attempt in the next three years to expand the focus of the defense studies well beyond technical strategic questions which were the main concern of the early research to include matters of broad foreign policy. To this end staff members from other parts of the program heretofore concerned primarily with foreign policy issues will be assigned to and integrated within each defense policy study project.

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As in the past, Brookings will emphasize a variety of means to maximize the impact of their defense studies. In addition to producing books and papers the staff will deliver lectures, testify before Congress on request, and, in particular, conduct a seminar on national security policy for Congressional staff personnel. Typically this seminar contains twelve Congressional aides of differing viewpoints and both political parties. It meets for dinner eight times per year.

As evidence of the respect in which the defense policy studies are held inside and out of government, it may be noted that the Senate Armed Services Committee has entered into a relationship with Brookings wherein staff members serve for brief periods with the committee while on leave. There is some possibility of a formal contract with the Committee in future.

Foreign Economic Policy Studies (\$215,000 over three years).

This segment of the program has been significantly strengthened in recent months by the appointment of Philip Trezise, formerly Assistant Secretary of State for Economic Affairs, and C. Fred Bergsten, formerly on the staff of the National Security Council. It is proposed that five projects in this area be supported from the recommended appropriation. The first of these is for American participation in a series of trilateral conferences among economists from North America, Western Europe and Japan. The initial conference was held at Brookings in December, 1971 on the broad topic of reshaping the international economic order and the second will be held in Belgium in November, 1972 on economic relations between the developed and less-developed nations. The third, on the renegotiation of textile and sugar agreements, and the fourth, on energy problems, will be held respectively in the spring and fall of 1973. It is expected that two conferences of this type per year, with background studies prepared carefully in advance, will be held during the three-year period.

The two studies of overseas private investment and of adjustment assistance would be carried out by Fred Bergsten and Charles Frank respectively. The first would attempt to cast light on the significance for donor and recipient countries of international capital flows and it would discuss the policy implications of this phenomenon. The second would explore means of alleviating