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Bretton Woods Committee Annual Meetings – Wednesday, January 22, 1986

PRIORITY ISSUES ON THE WORLD BANK'S AGENDA

Remarks

By

A. W. Clausen, President

The World Bank

and

International Finance Corporation

to the

Bretton Woods Committee

Washington, D.C.

January 22, 1986

Good afternoon, ladies and gentlemen.

The first order of business is a word of congratulations. The Bretton Woods Committee has completed its first year, and already it is firmly established. You have seized opportunities to speak clearly and frankly about the international economic issues of the day. You have advanced public understanding of the Bretton Woods institutions through your diligent work with the media and the Congress. We are most grateful to you for these efforts, and we would urge you to build upon this impressive beginning, expanding the unique and important role which your organization has proved itself so capable of performing.

This is an exceptionally well informed audience. So today I'd like to concentrate on some of the key priorities that are at the top of The World Bank's agenda -- most notably our strategies to assist the highly indebted nations; our work with other middle-income nations; our support for urgently needed development progress among the poorest nations, which is to say the role of IDA; and our commitment to private sector development through the work of the International Finance Corporation and our new Multilateral Investment Guarantee Agency.

We are most grateful to Secretary Baker for stressing the importance of a resumption of growth in the highly indebted countries at our last Annual Meetings in Seoul, Korea, and for placing such confidence in The World Bank as a major participant in the international debt strategy. Our long experience in promoting growth throughout the developing world makes us very willing and, let me say, capable partners in this effort.

The new consensus on the debt issue that emerged at Seoul grew from a recognition that our efforts to ease the debt problem were being hindered by some unfavorable, unexpected developments. The robust U.S. recovery did not endure, commodity prices remained flat, and the expected flows of new money did not come forth from the commercial banks.

All of this has left the highly indebted nations turning in a vicious circle. Their heavy debt service obligations take away resources needed for domestic investment. The resulting shortfall of investment activity precludes a significant expansion of export capacity to generate additional foreign exchange. Debt payments remain an overwhelming burden, which in turn diminishes economic prospects and investor confidence. Commercial banks shy away and domestic capital flies off to more hospitable climes. And there is no economic growth.

Our discussions in Seoul have put the issue sharply in focus: without new sources of capital the heavily indebted countries will fall deeper into a low investment -- low growth trap. In order to escape that trap, the heavily-indebted countries will need cooperative, concerted action from all participants in an expanded international debt strategy. This means that the indebted countries themselves, the industrial economies, the commercial banks, and the multilateral development banks each have their respective responsibilities. The World Bank takes its role very seriously.

But I want to point out that our sense of urgency on the debt problem did not originate in Seoul. Well before that meeting we had put together creative lending programs for several of the highly indebted Latin American countries. In Colombia, for example, we supported the government's trade liberalization initiative with a $300 million quick disbursing loan, and our monitoring of Colombia's trade policy is associated with the provision of new money by commercial banks. We have forged similar cooperative lending arrangements with Costa Rica, Chile, and Uruguay.

Building on this firm base of recent experience, our work on the debt issue has accelerated sharply.

We are pressing ahead with extensive planning and analysis activities. We are redeploying staff to enhance our capabilities as our coordinating function in the debt strategy grows. We are more directly engaging commercial banks in the process and more dynamically entering into discussions with our borrowers. And let me assure you that our coordination with the IMF is being developed even further. The will to secure this on both sides of Nineteenth Street is very great -- as Jacque de Larosiere has just emphasized in his remarks.

Our special capability in this enhanced international strategy lies in our close relationship with the countries themselves. Through our knowledge of those countries and the mature quality of our policy dialogue, we have and we will continue to help them work out the necessary changes in economic policy. Three basic areas must be addressed -- first, an increase in the rate of growth of savings, both in the private and public sector. Without new domestic savings, productive new investment will be very difficult to attain. Second, there must be an improvement in economic efficiency, particularly the use of capital if a high growth strategy is to be affordable. And finally, exports must increase in order to win back the creditworthiness which has ebbed away in recent years.

To take one specific example from the many countries we are actively working with, Argentina faces some daunting problems. Interest payments on external debt now absorb some 40 percent of gross domestic savings compared to less than 5 percent in the early 1970s. While that external debt increased, domestic production declined. In 1985, real GDP per capita was 13 percent below the 1974 level, and investment fell off too, from 21 percent of GDP to 13 percent last year.

What can Argentina do to reverse this decline? First, a continuation of its policy of monetary and fiscal reform is a necessary precondition for any program. Second, positive economic growth must be restored. Third, per capita consumption must steadily improve in order to maintain the social and political consensus behind the program. And last, the ratio of debt to exports must be brought down to levels where foreign capital will be willing to play a more normal role in the economy.

We are engaged in a vigorous, uninterrupted dialogue with Argentina and we are fully confident that an enhanced financial relationship will ensue, perhaps similar to our evolving work with Ecuador.

Just last week we signed two significant growth oriented adjustment loans to Ecuador, with the President of that country in attendance. These are the first in a series of loans which will strengthen that nation's ability to secure growth, to enhance domestic economic efficiency and, over time, create a far greater capacity to manage external debt obligations.

In December, I visited Ecuador, Uruguay and Argentina. My discussions with Latin American leaders were fruitful, and the expressed willingness of their governments to take tough actions in order to secure better long-term growth prospects was most encouraging.

Our discussions with indebted country governments are progressing well, and I assure you that the results of our current activities will become increasingly, publicly evident over the coming months. But let me make two very important points here. The first concerns the mechanics of our negotiations -- they are country-by-country. Each indebted nation has its own distinctive situation which requires highly customized attention. Today's debt problems will not be erased with a single sweeping gesture, but resolved only step-by-step and case-by-case.

My second point on country negotiations is this. Adjustment lending on the scale we envision and in association with the thorough economic restructuring that will be required will not be embraced or arranged overnight. Our experience in this sort of operation is well developed, and we have found that sovereign nations negotiate such loans with extreme care. They face political and economic dilemmas just as sensitive and just as intractable as those which we face right here in our own country.

So let us not build up naive expectations. We do have the will of the leaders of most of these nations to act swiftly, but political realities demand time for the process of economic analysis, policy formulation, loan negotiation and program completion to unfold.

If we push for instant results and swift conclusions, we will risk an impasse that will be damaging for all: damaging to the hopes for recovery in the countries themselves and damaging to the high quality of our lending which our shareholders and investors have come to regard so highly. Let there be no question that our negotiations with borrowers will proceed on an urgent basis, but we insist that the pace be measured and the results be of the highest quality.

The World Bank's coordinating role has also involved us in frequent discussions with commercial bankers who, as you know, are very key players in this cooperative strategy. We feel that the willingness of the commercial banks to provide more financing to the indebted countries will rest very squarely on the progress of adjustment in the indebted countries -- as John Reed pointed out to us this morning -- the quality of that adjustment, and its orientation to growth. My discussions with both bankers and developing country leaders in recent weeks make me confident that the required cooperation will be obtained.

Thus, we are geared up to play three distinct roles, and the work has begun. First, we will be assisting in the formulation of country growth programs and will be helping in the monitoring of their progress. Second, we will be providing an expanded volume of loans necessary to support the programs. Third, we will be acting as a catalyst in the mobilizing of capital from other sources.

We are already making excellent progress given the complexity of this many-sided effort. And we want all of our friends in the Bretton Woods Committee to understand how determined we are to see this debt strategy work and how confident we are that we can build on the progress already made.

It might seem from all the recent attention paid to the problem of the highly indebted nations that The World Bank has given up its project lending in the rest of the middle-income countries. This, of course, is not the case. To sustain growth and balanced development in these relatively unburdened countries is another key priority on our agenda. From China to Turkey to Indonesia and Tunisia our lending activities are moving ahead. Indeed, overall we see IBRD commitments this year totalling between $12 to $13.5 billion, we believe in the upper half of that range, compared to $11.4 billion achieved last year. And our work in progress leaves little doubt that in our next fiscal year still higher levels of commitments will be reached.

This growth in IBRD lending will continue, and before long, we will face limitations on that growth imposed by the amount of our capital and reserves. I therefore want to reiterate to this influential audience, that the IBRD will need, in time, within the next several years, a general capital increase.

Let me turn now to our concessional financing affiliate, IDA. It is no secret to this audience that the replenishment of IDA's resources has not always been trouble-free. IDA's 33 donor nations agreed to a $9 billion total in 1984, a sum $3 billion less than the previous replenishment and frankly a disappointment, not only for IDA's borrowers in Africa and Asia, but for many donors as well. At the conclusion of those negotiations, there was a palpable sense among donors of a job not fully done.

Africa's relentless economic decline has been a grim reminder of the need for a strong IDA, and early last year donors established the Special Africa Facility as a response to the crisis. To date $1.4 billion has been pledged, and we are appreciative of the recent appropriation by the United States to this Facility in an appropriation made just in the last several weeks. Next Monday the IDA Deputies will meet in Paris to discuss the 8th replenishment. They will look at the terms and conditions of IDA's credits; they will look at the geographical distribution of IDA's assistance, and they will discuss the policy orientation of IDA lending.

We are hopeful that the IDA donors will recognize that the resources we now have, through IDA and the Africa Facility, fall seriously short of what is needed by these poorest countries. They must understand that in Africa the needs for adjustment finance are much longer term than the three-year life of the Facility. And in addition to the investments needed in human resource development, poverty alleviation and basic infrastructure, one of IDA's more urgent tasks will be to address the emerging debt problems of many poorer countries in the developing world.

Let us be candid here. We cannot rely in the future on ad hoc, one-shot special facilities to make up for funding shortfalls in the IDA replenishments. This is not a complaint, but an appeal for pragmatism. To meet the need of all of our poorer country members, including the growing volume of adjustment lending, it will be far more effective to rely on a long established, proven instrument, and provide it with sufficient resources to do the job well. And that means we will need to equip IDA with resources which exceed the total of IDA VII and the Special Africa Facility contributions.

Secretary Baker has outlined ideas for additional concessional flows in association with the IMF Trust Fund flows. We are working diligently to help develop this most constructive initiative.

So IDA's replenishment and the Bank's full response to the needs of our middle-income countries are two of our highest priorities, but they are closely followed by issues crucial to the future of private sector development and deeply deserving of your continuing support -- that is the future of MIGA and the IFC.

Last year, we were very gratified with the decision of our Board of Governors to approve the convention establishing the Multilateral Investment Guarantee Agency or MIGA. MIGA will promote private investment for development through its coverage against the risks of adverse currency situations, political violence, and expropriation. Through those coverages and an array of advisory and intermediary services, we expect MIGA to substantially improve the investment climate in participating developing countries.

To bring the MIGA convention into force, we will need the signatures of five industrialized countries and fifteen developing countries. Six developing countries have already signed the convention and more are expected shortly. They are Korea, Turkey, Ecuador, Senegal, Sierra Leone, and St. Lucia. The United States has announced its intention to seek Congressional authorization of U.S. participation in MIGA; and we expect the Administration to move in the near term. United States leadership will be emulated by others, thereby moving up MIGA's first day of operation to the nearest possible date. Your vigorous support on this issue is indispensable.

Our commitment to private sector development is also in evidence with the expanding activities of the International Finance Corporation. The IFC's Board has approved a doubling of its capital to $1.3 billion. And last year, the United States Congress appropriated $29 million as a first installment on the American allocation of $175 million.

We are very pleased with that outcome but we should not be complacent. The Graham-Rudman procedures recently enacted by Congress will certainly be a factor in further installments, and therefore we must make clear how important it is to maintain the commitment to contribute the full U.S. allocation of IFC's capital increase, even if it means stretching out payments somewhat to meet budgetary targets. As in the case of MIGA, the U.S. role must be one of unquestioned leadership in the expansion of IFC's capital, and we hope to see that leadership role sustained for the strengthening of the IFC.

Ladies and gentlemen, we have set before you today the priority issues on our agenda as we see them. Against a backdrop of an uncertain economic climate in the industrial countries no one in this room can underestimate the degree of difficulty we face in these challenges. But The World Bank is stronger now than ever before to confront its responsibilities. Our liquidity is high, the management of our investment portfolio is efficient, and during the last six months, our borrowings have enjoyed the finest spreads ever over the cost of government obligations.

So let there be no uncertainties concerning the financial strengths of The World Bank, and let me assure you that in close partnership with the International Monetary Fund we will play to the full the major roles we and our shareholders have set for ourselves. And with your support and encouragement, we are confident that we will succeed.

Thank you.

THE WORLD BANK

Office of the President

January 2, 1986

Susan:

With reference to our conversation concerning the Bretton Woods Committee Annual Meeting and luncheon, ~~I have~~ the following (rather sketchy) information. Jan. 22

The meeting will begin at 10 a.m. for the Committee members only. They will break at 10:50 at which time they would like to have Mr. Clausen arrive. He will speak at 11 a.m. followed by a question & answer session. Jacques de Larosiere & John Reed of Citicorp are also scheduled to speak, but I'm not sure of the timing of their remarks. Lunch will be at 1 p.m. with Secretary Baker speaking at 2 p.m.

Sonya Schuster of the Bretton Woods Committee has asked for the names of those interested in accompanying Mr. Clausen. If you can let me know who might be interested, I will get in touch with Sonya and find out how she wants to proceed.

Thanks.

Myra

Botafogo
Vogl
Stanton
Maguire

to be invited
relayed to Sonya Schuster
1/3

Wednesday

Nov. 26

I had a call yesterday from Amb. Henry Owen's office concerning the Friends of Bretton Woods meeting on January 22nd. Last year, both you and Mr. de Larosiere spoke at their luncheon. However, this year they have asked if you could come at 11:30 a.m., make some remarks, take some questions, and then stay on for lunch, at which Secretary Baker will speak. Frank Vogl thinks you should do this.

MH

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DRAFT
C.Chamberlin
01/21/86

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Remarks

As Prepared for Delivery

By

Delivery Copy

A. W. Clausen, President

The World Bank

and

International Finance Corporation

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to the

Bretton Woods Committee

Washington, D.C.

January 22, 1986

Good ~~morning~~ AFTERNOON ladies and gentlemen.

The first order of business is a word of congratulations. The Bretton Woods Committee has completed its first year, and already it is firmly established. You have seized opportunities to speak clearly and frankly about the international economic issues of the day. You have advanced public understanding of the Bretton Woods institutions through your diligent work with the media and the Congress. We are most grateful to you for these efforts, and we would urge you to build upon this impressive beginning, expanding the unique and important role which your organization has proved itself so capable of performing.

This is an exceptionally well informed audience. ~~and I feel it would be more productive today if we had an exchange of views, rather than a long monologue from me. [illegible] will be brief [illegible] remarks, concentrating~~ So today I'd like to concentrate on some of the key priorities that are at the top of The World Bank's agenda - most notably our strategies to assist the highly indebted nations; our work with other middle income nations; our support for urgently needed development progress among the poorest nations, which is to say the role of IDA; and our commitment to private sector development through the work of the International Finance Corporation and our new Multilateral Investment Guarantee Agency.

Exemption

[illegible]

Gunn 20% cut.

Equal cut

alter.

Permit me to begin with the highly indebted nations and The World Bank's response to their difficulties. The members of the Bretton Woods Committee need no introduction to this issue -- indeed, you have already produced an excellent policy statement on the subject.

So, you will recall that in Seoul, at our last annual meeting, the Bank's shareholders reached agreement that the Bank should play an enhanced role in assisting the highly indebted, middle-income nations to move forward on a development path that would secure growth and restore creditworthiness. Secretary Baker ~~played a leading part in forging that new consensus on the debt~~ problem, and we are most grateful to ~~the United States~~ for stressing the importance of a resumption of growth in the highly indebted countries at our last annual meeting in Seoul, Korea -- and for placing such confidence in The World Bank as a major participant in the international debt strategy. Our long experience in promoting growth throughout the developing world makes us very willing and, let me say, capable partners in this effort.

The new consensus on the debt issue that emerged at Seoul grew from a recognition that our efforts to ease the debt problem were being hindered by some unfavorable, unexpected developments. The robust U.S. recovery did not endure, commodity prices remained flat, and the expected flows of new money did not come forth from the commercial banks.

Long Bonds need less capital

asset quality

Fed Reserve ≠ Capital Ratios

All of this has left the highly indebted nations turning in a vicious circle. Their heavy debt service obligations take away resources needed for domestic investment. The resulting shortfall of investment activity precludes a significant expansion of export capacity to generate additional foreign exchange. Debt payments remain an overwhelming burden, which in turn diminishes economic prospects and investor confidence. Commercial banks shy away and domestic capital flies off to more hospitable climes. And there is no economic growth.

Our discussions in Seoul have put the issue sharply in focus: without new sources of capital the heavily indebted countries will fall deeper into a low investment -- low growth trap. In order to escape that trap, the heavily-indebted countries will need cooperative, concerted action from all participants in an expanded international debt strategy. This means that the indebted countries themselves, the industrial economies, the commercial banks, and the multilateral development banks each have their respective responsibilities. The World Bank takes its role very seriously.

But I want to point out that our sense of urgency on the debt problem did not originate in Seoul. Well before that meeting we HAD put together creative lending programs for several OF THE highly indebted Latin American countries. In Columbia, for example, we supported the government's trade liberalization initiative with a $300 million QUICK DISBURSING loan, and our monitoring of Columbia's trade policy is associated with the provision of new money by commercial banks. We have forged similar cooperative lending arrangements with Costa Rica, Chile, and Uruguay.

Building on this firm base of RECENT experience, our work on the debt issue has accelerated sharply.

We are pressing ahead with extensive planning and analysis activities. We are redeploying staff to enhance our capabilities as our coordinating function in the debt strategy grows. We are more directly engaging commercial banks in the process and more dynamically entering into discussions with our borrowers. And let me assure you that our coordination with the IMF is being developed even further. The will to secure this on both sides of Nineteenth Street is very great. (AS JACQUE DeLAROSIERE HAS JUST EMPHASIZED IN HIS REMARKS)

Our special capability in this enhanced international strategy lies in our close relationship with the countries themselves. Through our knowledge of those countries and the mature quality of our policy dialogue we have and we will continue to help them work out the necessary changes in economic policy. Three basic areas must be addressed -- first, an increase in the rate of growth of savings, both in the private and public sector. Without new domestic savings, productive new investment will be very difficult to attain. Second there must be an improvement in economic efficiency, particularly the use of capital if a high growth strategy is to be affordable. And finally, exports must increase in order to win back the creditworthiness which has ebbed away in recent years.

To take one specific example from the many countries we are actively working with, Argentina faces some daunting problems. Interest payments on external debt now absorb some 40 percent of gross domestic savings compared to less than 5 percent in the early 1970s. While that external debt increased, domestic production declined. In 1985, real GDP per capita was 13 percent below the 1974 ~~1984~~ level and investment fell off too, from 21 percent of GDP to 13 percent last year.

What can Argentina do to reverse this decline? First, a continuation of its policy of monetary and fiscal reform is a necessary precondition for any program. Second, positive economic growth must be restored. Third, per capita consumption must steadily improve in order to maintain the social and political consensus behind the program. And last, the ratio of debt to exports must be brought down to levels where foreign capital will be willing to play a more normal role in the economy.

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Our discussions with indebted country governments are progressing well, and I assure you that the results of our current activities will become increasingly, publicly evident over the ~~next twelve~~ coming months. But let me make two very important points here. The first concerns the mechanics of our negotiations -- they are country-by-country. Each indebted nation has its own distinctive situation which requires highly customized attention. Today's debt problems will not be erased with a single sweeping gesture, but resolved ONLY step-by-step and case-by-case.

My second point on country negotiations is this. Adjustment lending on the scale we envision and in association with the thorough economic restructuring that will be required will not be embraced or arranged overnight. Our experience in this sort of operation is well developed, and we have found that sovereign nations negotiate such loans with extreme care. They face political and economic dilemmas just as sensitive and just as intractable as those which we face right here in our own country.

So let us not build up naive expectations. We do have the will of the leaders of most of these nations to act swiftly, but political realities demand time for the process of economic analysis, policy formulation, loan negotiation and program completion, to unfold.

If we push for instant results and swift conclusions, we will risk an impasse that will be damaging for all: damaging to the hopes for recovery in the countries themselves and damaging to the high quality of our lending which our shareholders and investors have come to regard so highly. Let there be no question that our negotiations with borrowers will proceed on an urgent basis, but we insist that the pace be measured and the results be of the highest quality.

The World Bank's coordinating role has also involved us in frequent discussions with commercial bankers who, as you know, are very key players in this cooperative strategy. We feel that the willingness of the commercial banks to provide more financing to the indebted countries will rest very squarely on the progress of adjustment in the indebted countries, the quality of that adjustment, and its orientation to growth. My discussions with both bankers and developing country leaders in recent weeks make me confident that the required cooperation will be obtained.

as John Reed pointed out to us this morning

Thus, we are geared up to play three distinct roles, and the work has begun. First, we will be assisting in the formulation of country growth programs and will be helping in the monitoring of their progress. Second, we will be providing an expanded volume of LOANS ~~capital~~ necessary to support the programs. Third, we will be acting as a catalyst in the mobilizing of capital from other sources.

We are already making excellent progress given the complexity of this many-sided effort. And we want all of our friends in the Bretton Woods Committee to understand how determined we are to see this debt strategy work and how confident we are that we can build on the progress already made.

It might seem from all the recent attention paid to the problem of the highly indebted nations that The World Bank has given up its project lending in the rest of the middle income countries. This, of course, is not the case. To sustain growth and balanced development in these relatively unburdened countries is another key priority on our agenda. From China to Turkey to Indonesia and ~~Cameroon~~ TUNISIA our lending activities are moving ahead. ACHIEVED Indeed, overall we see IBRD commitments this year totalling between $12 to $13.5 billion, (WE BELIEVE IN THE UPPER HALF OF THAT RANGE) compared to $11.4 billion last year. And our work in progress, ~~the pipeline as we call it~~, leaves little doubt that in our next fiscal year still higher levels of commitments will be reached.

This growth in IBRD lending will continue, and before long, we will face limitations on that growth imposed by the amount of our capital and reserves. I therefore want to reiterate to this influential audience, that the IBRD will need, in time, (WITHIN THE NEXT SEVERAL YEARS) ~~a general~~ capital increase.

Pause

Let me turn now to our concessional financing affiliate, IDA. ~~and that is IDA, the International Development Association~~. It is no secret to this audience that the replenishment of IDA's resources has not always been trouble-free. IDA's 33 donor nations agreed to a $9 billion total in 1984, a sum $3 billion less than the previous replenishment and frankly a disappointment, not only for IDA's borrowers in Africa and Asia, but for many donors as well. At the conclusion of those negotiations, there was a palpable sense among donors of a job not fully done.

Africa's relentless economic decline has been a grim reminder of the need for a strong IDA, and early last year donors established the Special Africa Facility as a response to the crisis. To date $1.4 billion has been pledged. Next Monday the IDA Deputies will meet in Paris. They will look at the terms and the conditions of IDA's credits; they will look at the geographical distribution of IDA's assistance, and they will discuss the policy orientation of IDA lending.

To discuss the 8th replenishment.

and we are appreciative ~~the~~ of the appropriation by the U.S. today to this facility -- an appropriation made just in the last several weeks.

T Pres Fund

We are hopeful that the IDA donors will recognize that the resources we now have, through IDA and the Africa Facility, fall seriously short of what is needed by the poorest countries. They must understand that in Africa the needs for adjustment finance are much longer term than the three-year life of the Facility. And in addition to the investments needed in human resource development, poverty alleviation and basic infrastructure, one of IDA's more urgent tasks will be to address the emerging debt problems of many poorer countries in the developing world.

Let us be candid here. We cannot rely in the future on ad hoc, one-shot special facilities to make up for funding shortfalls in the IDA replenishments. This is not a complaint but an appeal for pragmatism. To meet the need of all of our poorer country members, (including the growing volume of adjustment lending) it will be far more effective to rely on a long established, proven instrument, and provide it with sufficient resources to do the job well. And that means we will need to equip IDA with resources which exceed the total of IDA VII and the Special Africa Facility contributions.

¶ So IDA's replenishment and the Bank's full response to the needs of our middle-income countries are two of our highest priorities, but they are closely followed by issues crucial to the future of private sector development and deeply deserving of your continuing support -- that is the future of MIGA and the IFC.

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So let there be no uncertainties concerning the financial strengths of The World Bank, and let me assure you that in close partnership with the International Monetary Fund we will play to the full the major roles we and our shareholders have set out for ourselves. And with your support and encouragement, we are confident that we will succeed.

Thank you. ~~And now I will be pleased to hear your comments and questions~~.

THE BRETTON WOODS COMMITTEE
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WASHINGTON, D.C. 20006
TELEPHONE (202) 783-7000
TELEX 248924 CIG

1-22-86
BAKER

The World Bank.
Streamline procedures
Increased loans + increased disbursements
Privatization
Investments + Savings. Equity
1986 Lending - 2 billion higher than 1985

Improving the Int'l Financial System

John Reed
Com'l Banks reaction to debt problem.
Major progress - current account deficits has dropped dramatically. Countries have adjusted.
① Believes Baker initiative will work!
② Initiative is needed! Net new capital flows are essential.
③ We are addressing the problem of debt differentally than before [illegible].
④ The initiative is a new one! Moved focus from IMF to the World Bank. Different form of coupling between IBRD + IMF + between IBRD + Com'l Banks.
Com'l Banks want to participate in the negotiations w/ the developing Countries.

THE BRETTON WOODS COMMITTEE

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JAN 9. 1986

Policy Statement on the Role of the Bretton Woods Institutions in Fostering Economic Growth and Managing the International Debt Problem

Summary

The Bretton Woods Committee supports Treasury Secretary Baker's new initiatives to deal with the continuing LDC debt problem by fostering conditions which would lead to higher levels of economic growth and trade in the world. Success in these initiatives will require continued U.S. leadership and support for capital increases at the World Bank and the regional development banks, a replenishment of IDA, and special measures to deal with the problems of sub-Saharan Africa.

Policy Statement

The Bretton Woods Committee* believes that the economic recovery currently underway in the world, even though modest, is threatened by several related problems: the massive debt crisis faced by the developing countries; the danger of protectionism; and the prevalence of high interest rates and inconsistent macro-economic policies among the major industrial countries.

Addressing these problems will require the coordinated action of all the major countries involved--industrial and developing, creditor and debtor, alike. It will also require that the major international financial institutions--the IMF, the

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* The Bretton Woods Committee is a non-profit, bipartisan group organized to increase public understanding of the World Bank and the International Monetary Fund. The Committee consists of several hundred leaders throughout the United States, including businessmen, educators and former public officials.

World Bank, and the regional development banks--play a more active and better-coordinated role.

The Committee strongly supports two recent U.S. initiatives to address these problems.

The first of these initiatives was taken in September 1985, when the five major industrial countries (the United States, Japan, Germany, France, and the United Kingdom) agreed to intervene more actively in exchange markets in an effort to cause exchange rates to respond more accurately to changes in economic fundamentals. More importantly, it was reported that these five countries had, at the same meeting, discussed coordinating domestic economic policies. This announcement and their subsequent actions contributed to the further decline of the dollar, which in turn should eventually help to reduce the U.S. trade deficit and the pressures for trade restrictionism.

Whether this healthy trend continues will depend on whether further action is taken to assure that the fiscal and monetary policies of the five countries are mutually consistent and reinforcing. It is particularly important that the major industrial countries achieve rates of economic growth more in line with their economic potential. Specifically, as the United States makes progress in reducing its budget and trade deficits, as it must, Japan and Western Europe should move more vigorously toward expansion. Without more sustained and satisfactory levels of industrial country economic growth, the prospects for achieving a more open world economy and strong economic advance in the developing countries will be greatly diminished.

The Committee's specific interests at this time focus more directly on the second U.S. initiative--advanced by Secretary Baker at the IMF-World Bank meeting at Seoul in October--to deal with the debt crisis by concentrating on the factors needed to support higher economic growth in the developing countries.

In the Committee's view, this approach is essential and timely. The debt problem has clearly reached a new phase. The IMF-sponsored austerity and adjustment programs succeeded in surmounting the immediate crisis that faced many large debtor countries and threatened the international financial system itself. By now, however, the social limits of adjustment in many countries have been reached, while at the same time the net flow of foreign capital has virtually come to a halt.

Progress in bringing the debt problem under control will now depend on achieving higher levels of sustained economic growth. Growth will be stimulated to the degree that resources are used more efficiently, domestic savings and investments are encouraged, capital is repatriated, market-oriented policies are adopted and new foreign investment is attracted. In turn this progress will require building on the policy reforms fostered by the IMF -- notably in bringing about more realistic interest and exchange rates, reducing budget deficits, promoting market-related pricing, removing subsidies and other distortions, and weeding out inefficient public sectors.

The World Bank and the regional development banks can foster these reforms by their technical expertise and by being prepared to reward policy reform with a substantial increase in quick-disbursing loans. To a greater degree than before, the World Bank and the IMF must work closely together in formulating policy advice and supporting new programs in developing countries. For example, as part of a growth policy the international financial institutions should condition lending of quick-disbursing loans on the adoption of measures by borrowing countries to improve the structure and function of their capital markets. Efficient capital markets are essential to channel domestic savings, repatriated capital and foreign investment in an effective manner to the private sector.

In response to these efforts on the part of the borrowing countries and the international financial institutions, the commercial banks should provide new loans -- perhaps $20 billion or more over three years -- to the fifteen major debtor countries identified in the Baker plan. This must be in addition to what is provided to the other creditworthy developing country borrowers not encompassed in the Baker initiative.

The U.S. initiative reflects a three-pronged, mutually reinforcing effort to stimulate economic growth. It will only succeed if all three elements -- debtor countries, international development institutions, and commercial banks -- cooperate closely. Each must be confident that the others will be carrying out their responsibilities.

The Committee believes that the industrial countries should make a purposeful effort to support this program when they provide trade credits and bilateral development assistance. Integrating these official credits more closely with those of the multilateral banks will enhance the effectiveness of both.

Eventually the proposed expansion in lending by the World Bank and the regional development banks will require an increase in their capital. The Committee supports such an increase and believes that it should be substantial. This is not a significant budgetary issue for donor countries, if it is one at all. In the case of the World Bank, at least, a new capital increase should not require a paid-in portion. The subscription of capital by member countries serves as a guarantee authority that enables the Bank to borrow funds by floating its bonds on world markets.

In addition, and more urgently, the Committee believes that the United States should support and share in a new, increased, replenishment for the International Development Association (IDA) which will have to be renegotiated in 1986. This cost-effective program is needed to ensure continued economic progress in poorer countries, such as those in the Indian subcontinent and even more critically to foster policy reforms, attract private capital and to build the foundation for sustained economic growth in Africa. The concept of shared responsibility underlying IDA makes it the best way of meeting this need.

The Committee believes that other new measures will also be needed to deal with difficult problems of countries in sub-Saharan Africa. In general, these countries are not large debtors simply because they are not sufficiently creditworthy. An effort is needed to couple concessional resources for them with structural reforms. They need these concessional resources to build a base to support economic growth -- indeed, in many countries, to reverse a precipitant decline in per capita income.

At Seoul, Secretary Baker outlined a new approach to these countries. He suggested the redirection of the IMF Trust Fund, reflows to Africa, a possible U.S. contribution to the Special Facility for sub-Saharan Africa and, tentatively, mounting new programs jointly formulated and supported by the IMF and the World Bank. These important initiatives deserve stronger international support than they have yet received.

THE BRETTON WOODS COMMITTEE

1616 H STREET, N.W., SUITE 400
WASHINGTON, D.C. 20006

TELEPHONE (202) 783-7000
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Annual Meeting

January 22, 1986

The Grand Hotel
24th and M Streets, N.W.
Washington, D.C.

A G E N D A

Members Only	9:30-10:00	Registration (Conference level)
	10:00-10:20	Business Meeting (Grand Ballroom)
	10:20-10:50	Discussion

Coffee (Arrival of Guests)

11:00	Mr. A. W. Clausen, President The World Bank
11:45	Mr. John Reed, Chairman CitiCorp

12:30	Reception
1:00	*** Luncheon *** (Promenade)
	Mr. Jacques de Larosiere, Managing Director, IMF

2:15	Hon. James A. Baker, III, Secretary U.S. Department of the Treasury
3:00	Discussion (Grand Ballroom)
4:00	Adjourn

* IMPORTANT

FORM NO. 75
(6–83)

THE WORLD BANK/IFC

ROUTING SLIP	DATE: Jan. 22,1986

NAME	ROOM NO.
Roy Southworth	

	APPROPRIATE DISPOSITION		NOTE AND RETURN
	APPROVAL		NOTE AND SEND ON
	CLEARANCE		PER OUR CONVERSATION
	COMMENT		PER YOUR REQUEST
	FOR ACTION		PREPARE REPLY
	INFORMATION		RECOMMENDATION
	INITIAL		SIGNATURE
	NOTE AND FILE		**URGENT**

REMARKS:

This final draft includes the two additional sentences on the U.S. contribution to the Facility and on the Trust Fund as well as the two corrections Mr. Clausen detected (Cameroon to Tunisia and 1984 to 1974).

FROM:	ROOM NO.:	EXTENSION:
Chris Chamberlin		

PRIORITY ISSUES ON THE WORLD BANK'S AGENDA

Remarks

As Prepared for Delivery

By

A. W. Clausen, President

The World Bank

and

International Finance Corporation

to the

Bretton Woods Committee

Washington, D.C.

January 22, 1986

Good morning ladies and gentlemen.

The first order of business is a word of congratulations. The Bretton Woods Committee has completed its first year, and already it is firmly established. You have seized opportunities to speak clearly and frankly about the international economic issues of the day. You have advanced public understanding of the Bretton Woods institutions through your diligent work with the media and the Congress. We are most grateful to you for these efforts, and we would urge you to build upon this impressive beginning, expanding the unique and important role which your organization has proved itself so capable of performing.

This is an exceptionally well informed audience and I feel it would be more productive today if we had an exchange of views, rather than a long monologue from me. So, I will be brief in these opening remarks, concentrating on some of the key priorities that are at the top of The World Bank's agenda -- most notably our strategies to assist the highly indebted nations; our work with other middle-income nations; our support for urgently needed development progress among the poorest nations, which is to say the role of IDA; and our commitment to private sector development through the work of the International Finance Corporation and our new Multilateral Investment Guarantee Agency.

Permit me to begin with the highly indebted nations and The World Bank's response to their difficulties. The members of the Bretton Woods Committee need no introduction to this issue -- indeed, you have already produced an excellent policy statement on the subject.

So, you will recall that in Seoul, at our last annual meeting, the Bank's shareholders reached agreement that the Bank should play an enhanced role in assisting the highly indebted, middle-income nations to move forward on a development path that would secure growth and restore creditworthiness. Secretary Baker played a leading part in forging that new consensus on the debt problem, and we are most grateful to the United States for stressing the importance of a resumption of growth in the highly indebted countries and for placing such confidence in The World Bank as a major participant in the international debt strategy. Our long experience in promoting growth throughout the developing world makes us very willing and, let me say, capable partners in this effort.

The new consensus on the debt issue that emerged at Seoul grew from a recognition that our efforts to ease the debt problem were being hindered by some unfavorable, unexpected developments. The robust U.S. recovery did not endure, commodity prices remained flat, and the expected flows of new money did not come forth from the commercial banks.

All of this has left the highly indebted nations turning in a vicious circle. Their heavy debt service obligations take away resources needed for domestic investment. The resulting shortfall of investment activity precludes a significant expansion of export capacity to generate additional foreign exchange. Debt payments remain an overwhelming burden, which in turn diminishes economic prospects and investor confidence. Commercial banks shy away and domestic capital flies off to more hospitable climes. And there is no economic growth.

Our discussions in Seoul have put the issue sharply in focus: without new sources of capital the heavily indebted countries will fall deeper into a low investment -- low growth trap. In order to escape that trap, the heavily-indebted countries will need cooperative, concerted action from all participants in an expanded international debt strategy. This means that the indebted countries themselves, the industrial economies, the commercial banks, and the multilateral development banks each have their respective responsibilities. The World Bank takes its role very seriously.

But I want to point out that our sense of urgency on the debt problem did not originate in Seoul. Well before that meeting we put together creative lending programs for several highly indebted Latin American countries. In Colombia, for example, we supported the government's trade liberalization initiative with a \$300 million loan, and our monitoring of Colombia's trade policy is associated with the provision of new money by commercial banks. We have forged similar cooperative lending arrangements with Costa Rica, Chile, and Uruguay.

Building on this firm base of experience, our work on the debt issue has accelerated sharply.

We are pressing ahead with extensive planning and analysis activities. We are redeploying staff to enhance our capabilities as our coordinating function in the debt strategy grows. We are more directly engaging commercial banks in the process and more dynamically entering into discussions with our borrowers. And let me assure you that our coordination with the IMF is being developed even further. The will to secure this on both sides of Nineteenth Street is very great.

Our special capability in this enhanced international strategy lies in our close relationship with the countries themselves. Through our knowledge of those countries and the mature quality of our policy dialogue, we have and we will continue to help them work out the necessary changes in economic policy. Three basic areas must be addressed -- first, an increase in the rate of growth of savings, both in the private and public sector. Without new domestic savings, productive new investment will be very difficult to attain. Second, there must be an improvement in economic efficiency, particularly the use of capital if a high growth strategy is to be affordable. And finally, exports must increase in order to win back the creditworthiness which has ebbed away in recent years.

To take one specific example from the many countries we are actively working with, Argentina faces some daunting problems. Interest payments on external debt now absorb some 40 percent of gross domestic savings compared to less than 5 percent in the early 1970s. While that external debt increased, domestic production declined. In 1985, real GDP per capita was 13 percent below the 1974 level, and investment fell off too, from 21 percent of GDP to 13 percent last year.

What can Argentina do to reverse this decline? First, a continuation of its policy of monetary and fiscal reform is a necessary precondition for any program. Second, positive economic growth must be restored. Third, per capita consumption must steadily improve in order to maintain the social and political consensus behind the program. And last, the ratio of debt to exports must be brought down to levels where foreign capital will be willing to play a more normal role in the economy.

We are engaged in a vigorous, uninterrupted dialogue with Argentina and we are fully confident that an enhanced financial relationship will ensue, perhaps similar to our evolving work with Ecuador.

Just last week we signed two significant growth oriented adjustment loans to Ecuador, with the President of that country in attendance. These are the first in a series of loans which will strengthen that nation's ability to secure growth, to enhance domestic economic efficiency and, over time, create a far greater capacity to manage external debt obligations.

In December, I visited Ecuador, Uruguay and Argentina. My discussions with Latin American leaders were fruitful, and the expressed willingness of their governments to take tough actions in order to secure better long-term growth prospects was most encouraging.

Our discussions with indebted country governments are progressing well, and I assure you that the results of our current activities will become increasingly, publicly evident over the next twelve months. But let me make two very important points here. The first concerns the mechanics of our negotiations -- they are country-by-country. Each indebted nation has its own distinctive situation which requires highly customized attention. Today's debt problems will not be erased with a single sweeping gesture, but resolved step-by-step and case-by-case.

My second point on country negotiations is this. Adjustment lending on the scale we envision and in association with the thorough economic restructuring that will be required will not be embraced or arranged overnight. Our experience in this sort of operation is well developed, and we have found that sovereign nations negotiate such loans with extreme care. They face political and economic dilemmas just as sensitive and just as intractable as those which we face right here in our own country.

So let us not build up naive expectations. We do have the will of the leaders of most of these nations to act swiftly, but political realities demand time for the process of economic analysis, policy formulation, loan negotiation and program completion to unfold.

If we push for instant results and swift conclusions, we will risk an impasse that will be damaging for all: damaging to the hopes for recovery in the countries themselves and damaging to the high quality of our lending which our shareholders and investors have come to regard so highly. Let there be no question that our negotiations with borrowers will proceed on an urgent basis, but we insist that the pace be measured and the results be of the highest quality.

The World Bank's coordinating role has also involved us in frequent discussions with commercial bankers who, as you know, are very key players in this cooperative strategy. We feel that the willingness of the commercial banks to provide more financing to the indebted countries will rest very squarely on the progress of adjustment in the indebted countries, the quality of that adjustment, and its orientation to growth. My discussions with both bankers and developing country leaders in recent weeks make me confident that the required cooperation will be obtained.

Thus, we are geared up to play three distinct roles, and the work has begun. First, we will be assisting in the formulation of country growth programs and will be helping in the monitoring of their progress. Second, we will be providing an expanded volume of capital necessary to support the programs. Third, we will be acting as a catalyst in the mobilizing of capital from other sources.

We are already making excellent progress given the complexity of this many-sided effort. And we want all of our friends in the Bretton Woods Committee to understand how determined we are to see this debt strategy work and how confident we are that we can build on the progress already made.

It might seem from all the recent attention paid to the problem of the highly indebted nations that The World Bank has given up its project lending in the rest of the middle-income countries. This, of course, is not the case. To sustain growth and balanced development in these relatively unburdened countries is another key priority on our agenda. From China to Turkey to Indonesia and Tunisia our lending activities are moving ahead. Indeed, overall we see IBRD commitments this year totalling between $12 to $13.5 billion, compared to $11.4 billion last year. And our work in progress, the pipeline as we call it, leaves little doubt that in our next fiscal year still higher levels of commitments will be reached.

This growth in IBRD lending will continue, and before long, we will face limitations on that growth imposed by the amount of our capital and reserves. I therefore want to reiterate to this influential audience, that the IBRD will need, in time, a general capital increase.

Let me turn now to our concessional financing affiliate, and that is IDA, the International Development Association. It is no secret to this audience that the replenishment of IDA's resources has not always been trouble-free. IDA's 33 donor nations agreed to a $9 billion total in 1984, a sum $3 billion less than the previous replenishment and frankly a disappointment, not only for IDA's borrowers in Africa and Asia, but for many donors as well. At the conclusion of those negotiations, there was a palpable sense among donors of a job not fully done.

Africa's relentless economic decline has been a grim reminder of the need for a strong IDA, and early last year donors established the Special Africa Facility as a response to the crisis. To date $1.4 billion has been pledged, and we are appreciative of the recent appropriation by the United States to this Facility. Next Monday the IDA Deputies will meet in Paris. They will look at the terms and conditions of IDA's credits; they will look at the geographical distribution of IDA's assistance, and they will discuss the policy orientation of IDA lending.

We are hopeful that the IDA donors will recognize that the resources we now have, through IDA and the Africa Facility, fall seriously short of what is needed by the poorest countries. They must understand that in Africa the needs for adjustment finance are much longer term than the three-year life of the Facility. And in addition to the investments needed in human resource development, poverty alleviation and basic infrastructure, one of IDA's more urgent tasks will be to address the emerging debt problems of many poorer countries in the developing world.

Let us be candid here. We cannot rely in the future on ad hoc, one-shot special facilities to make up for funding shortfalls in the IDA replenishments. This is not a complaint, but an appeal for pragmatism. To meet the need of all of our poorer country members, including the growing volume of adjustment lending, it will be far more effective to rely on a long established, proven instrument, and provide it with sufficient resources to do the job well. And that means we will need to equip IDA with resources which exceed the total of IDA VII and the Special Africa Facility contributions.

Let me add that Secretary Baker has outlined ideas for additional concessional flows in association with the IMF Trust Fund -- we are working to develop this most constructive initiative.

IDA's replenishment and the Bank's full response to the needs of our middle-income countries are two of our highest priorities, but they are closely followed by issues crucial to the future of private sector development and deeply deserving of your continuing support -- that is the future of MIGA and the IFC.

Last year, we were very gratified with the decision of our Board of Governors to approve the convention establishing the Multilateral Investment Guarantee Agency or MIGA. MIGA will promote private investment for development through its coverage against the risks of adverse currency situations, political violence, and expropriation. Through those coverages and an array of advisory and intermediary services, we expect MIGA to substantially improve the investment climate in participating developing countries.

To bring the MIGA convention into force, we will need the signatures of five industrialized countries and fifteen developing countries. Six developing countries have already signed the convention and more are expected shortly. They are Korea, Turkey, Ecuador, Senegal, Sierra Leone, and St. Lucia. The United States has announced its intention to seek Congressional authorization of U.S. participation in MIGA; and we expect the Administration to move in the near term. United States leadership will be emulated by others, thereby moving up MIGA's first day of operation to the nearest possible date. Your vigorous support on this issue is indispensable.

Our commitment to private sector development is also in evidence with the expanding activities of the International Finance Corporation. The IFC's Board has approved a doubling of its capital to $1.3 billion. And last year, the United States Congress appropriated $29 million as a first installment on the American allocation of $175 million.

We are very pleased with that outcome but we should not be complacent. The Graham-Rudman procedures recently enacted by Congress will certainly be a factor in further installments, and therefore we must make clear how important it is to maintain the commitment to contribute the full U.S. allocation of IFC's capital increase, even if it means stretching out payments somewhat to meet budgetary targets. As in the case of MIGA, the U.S. role must be one of unquestioned leadership in the expansion of IFC's capital, and we hope to see that leadership role sustained for the strengthening of the IFC.

Ladies and gentlemen, we have set before you today the priority issues on our agenda as we see them. Against a backdrop of an uncertain economic climate in the industrial countries no one in this room can underestimate the degree of difficulty we face in these challenges. But The World Bank is stronger now than ever before to confront its responsibilities. Our liquidity is high, the management of our investment portfolio is efficient, and we recently borrowed at the finest spreads ever over the cost of government obligations.

So let there be no uncertainties concerning the financial strengths of The World Bank, and let me assure you that in close partnership with the International Monetary Fund we will play to the full the major roles we and our shareholders have set for ourselves. And with your support and encouragement, we are confident that we will succeed.

Thank you. And now I will be pleased to hear your comments and questions.

WORLD BANK / INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE : January 17, 1986

TO : Messrs, Clausen, President, Stern (SVPOP), Qureshi (SVPFI), Botafogo VPE)

FROM : Frank Vogl, FV Director IPA

EXT : 72468

SUBJECT : Bretton Woods Committee Speech next Wednesday, January 22

Attached is a draft of a presentation by Mr. Clausen to the Bretton Woods Committee next Wednesday. Other speakers at that meeting will be Mr. Baker and Mr. de Larosiere. The press will be present and will be given copies of the speech after it is delivered. We decided, given the range of the other speakers at the meeting and the highly informed audience that it would be most effective if the speech was short and very closely focussed on the key topics that the Bretton Woods Committee has indicated are of the greatest interest to its members. We have tried to lay out in clear terms that the Bank is very active on the Baker plan but that there is a great need for realism with regard to expectations ... a message clearly needed in view of recent press reports on this subject. Comments made in the rest of the speech on IDA, MIGA and IFC are all directly in line with what we have said publicly already, but are tailored to be particularly effective with this audience.

Please give us your comments by first thing Tuesday morning so that we can provide Mr. Clausen with a final version on Tuesday afternoon.

FV:rgw

Attachment

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OFFICE OF THE PRESIDENT