ESSAYS IN INTERNATIONAL FINANCE

No. 33, March 1959

THE INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

ALEC CAIRNCROSS

INTERNATIONAL FINANCE SECTION

DEPARTMENT OF ECONOMICS AND SOCIOLOGY

PRINCETON UNIVERSITY

Princeton, New Jersey

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The author, Alec Cairncross, is Professor of Applied Economics at the University of Glasgow and Editor of the SCOTTISH JOURNAL OF POLITICAL ECONOMY. *He has served in many other positions; among them are Economic Adviser to the Board of Trade, Economic Adviser to the Organization for European Economic Cooperation, Director of the Economic Development Institute and member of the Radcliffe Committee. The views expressed in this essay are, of course, his own and do not purport to reflect those of any institution with which he is or has been associated.*

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LESTER V. CHANDLER, *Acting Director*
International Finance Section

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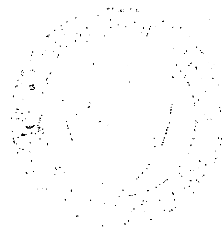

THF INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

I. THE BANK AND THE FUND

OF THE twins of Bretton Woods, the International Bank for Reconstruction and Development enjoyed far less of the limelight at its inception than the International Monetary Fund. At the preliminary conference at Atlantic City in June 1944, attention was concentrated on the Fund and at Bretton Woods the main source of controversy was the Articles of Agreement of the Fund, even when it was intended that similar provisions should apply to the Bank. The quotas on which so much of the discussion centred were worked out first for the Fund and later became the basis for subscriptions to the Bank—to the consternation of members who had sought high quotas in the Fund in order to establish drawing rights but were less anxious to make equal capital subscriptions to the Bank. At Savannah it was again the Fund that was the principal subject of debate; it seems to have been assumed that the same relations between management and executive directors would govern both institutions. The site chosen for the Fund automatically became the site of the Bank, which until 1958 shared the same building in Washington and continues to share the same library.

Yet in the first ten years of its existence it was the Bank rather than the Fund which most readily found a place for itself. The scope of its activities steadily expanded; it was never subject to the frustrations that inevitably beset the Fund when the burden of international reconstruction fell on the United States; its policies took increasingly firm shape; and its influence on world economic development grew progressively.

The membership of the Bank has throughout been identical with that of the Fund; Bank membership is, in fact, open only to members of the Fund. All the 44 countries represented at Bretton Woods subsequently joined the two institutions except the Soviet Union, New Zealand and Liberia. Nearly all other countries of any economic importance outside the Communist bloc (except Switzerland) have been added to the list of members, which now totals 68. Poland withdrew

in 1950 and Czechoslovakia was expelled in 1953 for non-fulfilment of its obligations, leaving Yugoslavia the only Communist member. China's membership was continued in favour of Taiwan on an undertaking from the emigré government that it would pay the remaining (and major) part of its subscription as soon as possible, and the Chinese Executive Director retained his position as an appointed member of the Board.

Although the two institutions have led a more separate existence than was perhaps originally intended, they supplement one another and the future of the one is closely tied up with the future of the other. The Bank is concerned primarily with the flow of capital into long-term investment across national boundaries, the Fund with problems of international liquidity and short-term credit. But both institutions share a common interest in helping their members to reconcile economic balance and economic growth, in promoting economic and financial policies that pay regard not only to national but also to international interests, and in maintaining an international framework within which countries can make necessary adjustments in their economies without excessive strain.

II. THE FUNCTIONS OF THE BANK

The purpose of the Bank is implicit in its title. This emphasises an immediate and temporary function: that of assisting the restoration and reconstruction of productive capacity destroyed during the war. It also underlines a continuing and longer-range function: that of contributing to the development of economic resources and the growth of productive power and standards of living, particularly in backward or under-developed countries.

These functions were regarded at Bretton Woods as competitive; so long as the capital at the disposal of the Bank was limited and the claims of reconstruction were pressing, and indeed paramount, there could be no assurance that the Bank would have enough funds to discharge its obligations towards the less-developed countries. In the early years of the Bank there did in fact appear to be some antithesis between its functions. The first loans were made exclusively for the reconstruction of countries in Western Europe and it was only after a large proportion of the Bank's freely usable, paid-in capital had already been committed that any loan agreements were concluded with under-developed countries. But even at that stage the limiting factor in loans to those countries was not the inadequate resources of the Bank so much as the greater care that was needed in examining the projects submitted for financial support, and the delays that prolonged examination entailed. In any event, it was obvious that, sooner or later, reconstruction would

come to an end and the needs of economic development would become the enduring preoccupation of the Bank. Marshall Aid hastened the transition and for many years the word "Reconstruction" in the Bank's title has been an anachronism.

The functions of the Bank can be not inadequately summarised by describing it as an international development bank. It is in the first place an *international* institution: a specialized agency of the United Nations operating as a co-operative venture in long-term foreign lending. It is, secondly, a *development* bank: not perhaps the exact counterpart at the international level of those development banks which it has done so much to encourage at the national level, since these have been devoted exclusively to industrial financing and have been privately owned; but, like them, engaged in promoting development by supplying long-term capital, and following an older tradition of development banks in financing a variety of large projects of special importance to the economies of member countries. Moreover, just as many development banks found themselves obliged to enter other fields of activity as they took a more comprehensive view of all that development implied, so the Bank, starting out as a lender on long-term, has been forced to take an increasingly wide view of its responsibilities.

As an international institution, the prime task of the Bank is to stimulate and support foreign investment. So far as this involves the use of the Bank's own resources, it must be able to mobilize capital from a variety of capital-exporting countries and lend the capital so mobilized to a variety of capital-importing countries. The wider the range of borrowers and lenders, the more truly international will the Bank become. It has in fact relied heavily on the United States for its funds and has found employment for those funds chiefly in the under-developed countries. But it is by no means simply a vehicle for channelling American investment towards the under-developed countries. It has raised a growing proportion of its funds outside the United States and it has always been willing to make loans to countries that would not normally be regarded as backward, or even under-developed. Every country aspires to economic development and nearly every country has a pressing need for extra capital. Developed countries, though generally lenders, particularly on long-term, very often import capital and may have good reasons for trying to borrow through an international institution. Similarly, under-developed countries, although normally importers of capital, at least on long-term, may at times be in a position to lend to the Bank or accelerate repayment of their loans from it. The Bank's international role, therefore, need not consist in raising capital in developed countries in order to lend it to under-developed countries.

It may borrow from either group and lend to either group. It may even finance projects in countries from which it is currently borrowing; and it has in fact done so. For example, in a recent issue by private placement, the Bank found buyers for its bonds in no less than nine countries to which it had made loans during the year 1957-58. In May 1957 the Dutch Herstelbank borrowed $15 million from the Bank, although public issues of guilder bonds had been made in 1954, and again in 1955, by the Bank, and the Netherlands is a steady buyer of the Bank's dollar bonds.

As a development bank, the Bank is first and foremost a lender on long-term. From its standing as a lender, it has acquired authority in the exercise of other functions. It has built up a special expertise in the peculiar blend of engineering, economics and administrative skill necessary for the appraisal and supervision of large projects of construction. It has also a unique experience in the formulation of comprehensive programmes of economic development. This experience leads member countries to turn to the Bank not only for finance, but also for advice and guidance; while the Bank, in devising techniques by which it could put its experience at the service of member countries has come to think of itself as a consultant quite as much as a financial institution.

The functions of the Bank extend, therefore, well beyond the series of loan transactions in which it engages. Not only does it, like other development banks, maintain a continuing relationship with borrowers throughout the life of each loan. It insists that the loans cannot be treated as isolated transactions and that the projects which they finance must be examined in relation to the rest of the development effort of the borrower. It constantly emphasises the value of a development programme into which the major projects are fitted. It aims also at identifying the economic and financial policies most conducive to development and the strategic factors upon which governments should be encouraged to operate. Thus the Bank has found itself involved in working out, if not a theory, at least a philosophy of development. This is not a philosophy which the Bank has ever articulated in any detail. But there are passages in its Annual Reports that recur to the same general themes: the limited value of additional finance if other, institutional factors are not propitious; the importance of good management both in the planning of individual projects and in the conduct of a nation's affairs; the need to encourage initiative, enterprise and the will to develop, and to avoid policies which, through weakness, vacillation or impatience, prevent the emergence of attitudes and institutions favourable to development.

III. THE BANK AS BORROWER

At Bretton Woods it was envisaged that the Bank would operate mainly by guaranteeing loans by private investors rather than through direct loans from its own capital. It was thought that the immediate needs of post-war reconstruction would be met by UNRRA, and that thereafter an adequate amount of long-term capital might be raised with the Bank's guarantee, the Bank pledging the collective credit of its members in security. The Articles of Agreement call upon the Bank "to promote private foreign investment by means of guarantees or participations in loans and other investments made by private investors." It is only when private capital is not available on reasonable terms that it is required "to supplement private investment by providing on suitable conditions finance for productive purposes out of its own capital, funds raised by it and its other resources."

This explains why the bulk of the Bank's subscribed capital—four-fifths—takes the form of a guaranty fund, to be drawn upon when necessary to meet obligations arising out of loans and guarantees. Only the remaining fifth of the subscriptions from member countries is payable in cash; and of this fifth only one-tenth, or 2 per cent of the total capital, must be paid in gold and dollars. Even this 2 per cent was at first subject to a concession—to meet Russian objections at Bretton Woods—in favour of countries occupied during the war; it was the failure of Czechoslovakia to pay the balance of her 2 per cent dollar subscription that led to her expulsion.

The expectation that the Bank would operate by guaranteeing loans raised by its members from private investors came to nothing. From the Bank's point of view there would have been serious inconvenience if loans issued by different countries, all bearing its guarantee, had been sold in the market at different rates. This not unlikely contingency would have been damaging to the Bank's credit; and it was largely in an effort to establish that credit on a firm basis that it was decided to issue Bank obligations rather than guarantee those of member governments.

The decision to follow the path of direct lending involved the Bank in a long struggle to extend the market for its bonds, to gain access not only to the American but to other capital markets as well, and to obtain fuller and more unrestricted use of member countries' subscriptions. It took some years before the Bank could claim with assurance that its lending would not be limited by the funds at its command and that it could undertake to lend to any country as much as that country, in its judgment, could hope to repay.

By the middle of 1948, for example, the Bank had lent almost $500

million in United States dollars, for periods ranging up to thirty years, to France, the Netherlands, Luxembourg and Denmark. On the other hand, the member countries other than the United States had paid in less than $100 million in gold and United States dollars so that the Bank had to find the whole of the balance out of the United States subscription of $635 million or from loans floated in the United States market, largely against the security of the uncalled portion of the United States subscription. The marketing of Bank loans in the United States, however, presented difficulties since there were initially only a few states where institutional investors could legally invest in the Bank's securities and it required a prolonged campaign, first to obtain legislative approval for such investment and then to interest the leading institutions in the Bank's offerings of bonds.

The first bond issues, one for $100 million and one for $150 million, were made in order to test the market in July 1947, and were heavily over-subscribed. Apart from a re-financing issue in 1950, no further issues were made in America until 1951, but there has been at least one issue in every subsequent financial year except 1954-55 and 1955-56. The chief buyers have been pension and trust funds, which hold nearly half the total in the United States, and insurance companies and savings banks which together hold most of the other half. As one might suppose, these have proved firm holders, and the price of Bank bonds has been well maintained in relation to the price of United States government obligations.

TABLE I

BORROWING OPERATIONS OF THE WORLD BANK, 1946-58
($ MILLION)

United States	*Funded debt outstanding*	*Net increase in funded debt*	*Funded debt held outside the United States*	*Net increase in funded debt held outside the United States*
June 30 1948	254	—	—	—
1949	254	—	—	—
1950	261	7	—	—
1951	325	64	64[1]	—
1952	500	175	100	36
1953	556	56	155	55
1954	777	221	279	124
1955	852	75	374	95
1956	850	−2	380	6
1957	1034	183	480	100
1958	1658	625	730	250

Source: *Annual Reports* of I.B.R.D.

[1] Cumulative to June 30, 1951.

In seeking to broaden the market for its bonds, the Bank did not look exclusively to action in the United States. It obtained listings on various stock exchanges and found buyers for some of its dollar obligations outside the United States, chiefly among the central banks of member countries. By the middle of 1957, about $280 million of United States dollar bonds, or one-third of the outstanding total, was held outside the United States and in the ensuing year three dollar issues totalling $250 million were placed privately with the Deutsche Bundesbank. The Bank made its first issue of bonds denominated in other currencies when it placed a small issue of Swiss franc bonds in 1948 with the Bank for International Settlements, an issue which the B.I.S. readily disposed of to Swiss banks. This was followed in 1951 and later years with public issues made in succession in the United Kingdom, Switzerland and the Netherlands. The Bank also floated two issues in Canada and brought Canadian and European participants into one of the early syndicates through which its bonds were offered to the public.

The record has been one of diminishing dependence on the United States as a source of finance and of increasing dependence on Western Europe. Although it was not until 1951 that the Bank was able to make public offerings of its bonds outside the United States, bonds to the value of nearly $700 million (including dollar bonds) were purchased by non-American holders over the next seven years, and by the middle of 1958 they held about half the total funded debt of the Bank. The experience of recent years suggests that this proportion is likely to be maintained.

It remains true, however, that the Bank is heavily dependent on United States finance. The need to have recourse to the United States for half its current borrowings may do no more than reflect the concentration of industrial and financial potential in that country but must at the same time take from the international character of the Bank's operations. Moreover, apart from the United States there are still very few other capital markets to which it is possible to turn: European holders of Bank bonds are largely confined to Germany, a comparatively recent supplier of funds, Switzerland, a non-member of the Bank, and, to a much smaller extent, the United Kingdom, the Netherlands and Belgium.

How successful the Bank will be in the future in broadening the sources of its funds must depend not only on the success of capital-rich countries in generating a favourable balance of payments but also on their willingness to open their capital markets to foreign borrowers, on their desire to direct the flow of capital to suit their own national interests or colonial and commonwealth responsibilities, and on the rates

of interest at which bond issues can be made. The establishment of the Common Market in Europe, for example, may operate to reduce the access of the Bank to European capital; and the pressures on the British capital market may also rule out a revival of British investment through the Bank.

Almost from the beginning, the Bank found it possible to arrange for participation in its loans by institutional investors and to make sales to them from its own portfolio, with or without its guarantee. When sales are made without the Bank's guarantee, as has been the invariable practice in recent years, the Bank passes on to the borrower all savings in interest up to 1 per cent, the commission payable to the Bank; but the rise in interest rates has made it impossible to sell maturities appreciably, if at all, below the full rate (including commission) already payable. The Bank is under no obligation to seek authority from the borrower before selling a portion of his loan—a circumstance that was cited by the Colonial Development Corporation in 1950 as an obstacle to the conclusion of a loan agreement with the Bank.

Participations and sales have been by no means confined to American investors and a growing proportion of the funds—in recent years well over half—has come from Europe. The total amount realized to the middle of 1958 came to $420 million or about one-ninth of the loans made by the Bank up to that time. Sometimes participations are arranged simultaneously with the loan agreement, at other times they represent subsequent sales from the Bank's portfolio: in 1957-58 the two were roughly equal. The Bank normally takes the longer maturities, leaving it to the participating institutions to take the short- and medium-term tranches. This is apparent from the fact that of the $420 million, no less than $173 million had already been repaid, whereas only $219 million had been repaid directly to the Bank on its much larger portfolio.

These sales from the Bank's portfolio economize the call on its own resources and extend the total market for loans raised by the borrowing countries. A similar effect is obtained by joint operations with the investment market in the United States. On a number of occasions, the Bank has made a loan to a member government to finance a programme of development while the government concerned made a public offering (or placement) of its bonds concurrently through investment banking firms in order to obtain supplementary finance for the same programme. These joint operations, which have enabled countries like South Africa and Belgium to offer their bonds in the United States market, usually involve the Bank in taking the longer maturities, just as in the case of

direct participations. The total raised from the market in this way up to June 30, 1958, was $140 million.

In view of the limited access that the Bank had to the nominally very large capital subscriptions by its members, it was natural that it should lay increasing stress on the desirability of removing restrictions on the use of the 18 per cent payable in members' own currencies. This 18 per cent may be lent by the Bank only with the consent of the member country concerned. In the early years the Bank recognised that few of its members had capital to spare for foreign lending and that, even if they had, they would have difficulty in lending convertible currencies. At the same time, since it was one of the main purposes of the Bank to internationalize foreign lending, it could not rest content with a situation in which nearly all its funds came from a single member.

Progress was made gradually and in a variety of ways. Some countries have been persuaded to announce that their 18 per cent can be used to finance purchases made from them; one important member, Great Britain, agreed in 1953 to the use of £60 million for loans to the sterling countries of the Commonwealth and has since agreed to release the remaining £20 million over a series of years; others have agreed to partial convertibility (for example, to the use of their 18 per cent within the area of the European Payments Union) or to release, step by step, over a period of years; only a few have accepted complete convertibility, releasing their 18 per cent for purchases in any part of the world.

The position in 1958 is that, out of the 18 per cent subscriptions of its members, the Bank has been able to make use of only $1176 million, half of which is made up of the United States subscription. As recently as 1954, other member countries had released less than $150 million, but this total has grown to some $600 million in the past four years. Even now, a sum equivalent to about $500 million has not yet been made available for lending, although part of this total could be used, subject to conditions laid down by the members concerned.

The funds available to the Bank at June 30, 1958, and the increase in those funds over the preceding three years are shown in Table II.

Thus the principal sources of funds have been, in roughly equal measure, members' subscriptions and bond issues. The contribution made by net income from loans is small but growing and has doubled in the past five years. Participations and sales have averaged about $75 million in the past few years, and have furnished a rising proportion of total funds. Repayment of loans, although extremely small, must eventually become a much more important source of funds; a situation in which repayments are under $30 million a year while loans over the

TABLE II

FUNDS AVAILABLE FOR LOANS, JUNE 30, 1958
($ MILLION)

	Cumulative to June 30, 1958	*Net increase June 30, 1955–June 30, 1958*	*Column 1 Excluding the United States*	*Column 2 Excluding the United States*
Members' subscriptions				
2 per cent	186	8	122	8
18 per cent	1176	412	605	412
Funded debt	1658	806	730	356
Participations & sales	420	216		
Net income (put to reserve)	236	107		
Repayments to Bank	219	78		
Total available funds	3895	1627		

past ten years have averaged over $300 million a year is clearly transitory.

From the Bank's point of view, however, the only really elastic source of funds is the issue of fresh bonds. It may cajole the members to respect their obligations; it may plough back all it earns; it may sell from its own portfolio to a widening circle of clients. But if lending spurts as it did from 1956 onwards, the Bank is forced to borrow in the market. Even this elasticity is limited so long as investors regard the uncalled liability of the United States as their prime security. By the middle of 1958 the outstanding debt of the Bank, nearly all of it payable in dollars, was over half the United States' total subscription and was rapidly approaching the 80 per cent that represents the United States contribution to the Bank's guaranty fund.

It was obviously desirable that action should be taken in good time to increase members' subscriptions, and the proposal to double them, put forward at the New Delhi meeting of the Bank in October 1958, has since been accepted. This increase will not, however, result in any additional payments to the Bank. No doubt it is difficult to persuade countries that have met their obligations in full to subscribe additional cash so long as many other countries have still to release unconditionally their full 18 per cent; but it is also unwise to set a precedent for making the Bank entirely dependent on the issue of more bonds, without some simultaneous levy on its members.

On the whole, the Bank has made good progress towards making itself a vehicle for the international mobilisation of long-term capital. It is likely to continue to depend mainly on the United States for its funds, but there should also be a large flow of capital from Western Europe, even if the Common Market leads to the emergence of new financial institutions that make substantial calls on European capital markets. These institutions may channel more capital to Italy and to Western Europe's under-developed territories overseas, and so meet requirements that might otherwise be served by the Bank. But some at least of the Six—Germany and Holland, for example—can hardly avoid remaining net exporters of capital and the Bank can hardly fail to be one of the beneficiaries of their lending.

IV. THE BANK AS LENDER

By the summer of 1958 the Bank had made over 200 loans totalling nearly $4 billion. Its rate of lending, after a first burst of reconstruction loans in 1947-48, and a second, minor boom in 1950-52, remained relatively steady in the middle fifties at around $400 million but shot up in 1957-58 to a record total of $711 million. Most of the later loans have been made to countries which, on any normal definition, would be classed as under-developed. Thus, European countries, to which all the first loans were made, have not been large borrowers in recent years, with the important exception of Italy, itself in many ways under-developed. On the other hand, South-east Asia has come increasingly to the front as a borrower. India has emerged as the largest of the Bank's debtors and over the past two years has borrowed $240 million, or 20 per cent of the total sum lent by the Bank during that period. Asia and the Middle East, which at one time occupied a relatively modest place in the Bank's lending operations, accounted for over half the value of the loans made in 1957-58 and showed every sign of continuing to absorb a high proportion of total loans. Four countries—India, Pakistan, Thailand and Japan—borrowed between them over $350 million during the year and by June 30, 1958 had received loans totalling $772 million out of the aggregate for Asia and the Middle East of $948 million. Loans to Latin America totalled $798 million, Mexico, Brazil and Colombia being the largest borrowers; but this total has mounted at a relatively slow pace in comparison with that for South-east Asia. Among the African countries, the main borrowers have been South Africa and the Federation of Rhodesia and Nyasaland, which borrowed $301 million by mid-1958 out of a total of $479 million for the continent.

Australia, with loans totalling $318 million took second place only to India as a borrowing country. European countries, in addition to the reconstruction loans amounting to $497 million, had borrowed a total of $689 million. In all, loans had been made to 47 member countries and territories by the Bank; but of these, 10 countries accounted for 60 per cent by value of the total loans.

TABLE III

LENDING OPERATIONS OF THE WORLD BANK, 1946-58
($ MILLION)

	Loans (Gross of cancellations and repayments)	*Disbursements*	*Sales of Loans*	*Repayments to Bank*
1946-48	497	470	—	—
1948-49	153	56	28	—
1949-50	166	88	—	1
1950-51	297	78	5	5
1951-52	299	185	23	4
1952-53	179	227	14	2
1953-54	324	302	32	4
1954-55	410	274	102	124
1955-56	396	284	72	24
1956-57	388	332	57	26
1957-58	711	499	87	28
Cumulative to June 30, 1958	3820	2795	420	218

Has the Bank in its lending fulfilled the expectations that might reasonably be entertained in view of its origins and membership? Or, if not, wherein has the Bank failed in making loans to its members?

No critic of the Bank thinks that it should have done less, but a great many think that it should have done more. The scale on which it has lent may seem quite inadequate, for example, in relation to the needs of the under-developed countries. If the calculations of the United Nations experts who in 1951 estimated the capital requirements of those countries at $19,000 million a year are put in conjunction with the then rate of lending of the Bank—about $300 million a year—the contrast is overwhelming. But the calculations are now recognised to be largely meaningless, and there is little point in discussing what the "correct" figure should be. At the same time, the Bank has doubled its rate of

lending and has concentrated more on the under-developed countries in Latin America, Asia and Africa. Of the total inflow of long-term capital into those areas from outside, the Bank may be providing not far short of a quarter.

Nevertheless, even $700 million a year may seem an insufficient contribution to the development of those areas. How is it possible to reconcile the Bank's rate of lending with its dictum that as much money can be advanced as there is good reason to expect to see repaid?

First of all, there are good grounds for supposing that the real need for capital in many parts of the under-developed world has been grossly exaggerated. When one finds, for example, that real income rose by over 5.5 per cent per annum in Latin America between 1945 and 1955 and that even per capita income rose nearly as fast as in Europe—3.5 per cent per annum compared with 4.5 per cent per annum—it is difficult to suppose that a vast inflow of capital would have made a great deal of difference. It might perhaps have helped to avoid bottlenecks in power and transport; but on the other hand it is arguable that, if the price of power and transport services had at least kept pace with the universal inflation, there would have been less need to borrow abroad to finance capital expenditure and less difficulty in offering adequate security to foreign lenders or investors.

Secondly, most of the under-developed world has enjoyed throughout the greater part of the post-war period highly favourable terms of trade. This has put it in a far stronger position to finance imports of capital goods without resort to foreign borrowing, especially where part of the higher export income was retained in the hands of the central government or its agencies. On the other hand, these high prices added fuel to inflationary fires that were already well stoked and the Bank has hesitated to make loans to countries that seemed to lack either the will or the capacity to keep inflation within measure.

Thirdly, some countries were unable to borrow more because they were simply not creditworthy. However the Bank measures creditworthiness—and obviously there can be no single index that registers it, since political factors, trust in the good faith of the debtor, the efficiency of the administrative machine, the volatility of export earnings, the use to which borrowed funds are put, and so on, must all enter—there is some limit beyond which the Bank cannot safely go in lending to a given country if it is obliged to show prudence and a regard for the interests of the guarantors of its loans. It is not possible to say with any precision how far the efforts of the Bank to keep within a ceiling of creditworthiness have caused it to reject (or rather, turn aside, since it never formally rejects) loan applications. Even within the Bank there

might well be disagreement about the influence of any notional ceilings on decisions to proceed with or discountenance a specific loan operation. But there are unquestionably countries to which the Bank will not lend because their creditworthiness is rated too low and others to which loans will be made only after more than usually rigorous examination.

Sometimes, when a very large project is involved, the Bank may be doubtful whether foreign exchange earnings will be sufficiently enlarged to enable the debt to be serviced and may, on those grounds, be unwilling to shoulder the whole responsibility without participation by other influential lenders or without substantial grants towards the cost. There are also cases where, if the Bank is not on the best of terms with an intending borrower, no new loans are likely to be made; but such cases often reflect the disappointment of the borrower over *past* failure to secure a loan, so that it is only the number of loan applications that is affected, not the number granted.

Two conditions governing the Bank's lending policy and limiting its loans arise directly out of its Charter. The Bank normally lends only against specific projects and confines its participation to financing the foreign exchange component, i.e. payments for imported equipment, technical services provided by foreigners, etc. Both of these conditions are open to criticism and both are subject to exceptions.

The first condition implies that a government with a large investment programme cannot come to the Bank and obtain from it funds to supplement its normal revenue and cover any deficit in the Budget. It has to submit projects one by one, justify each, and accept Bank supervision right through to their completion. This condition was introduced at Bretton Woods with a view to preventing unproductive borrowing. The Articles of Agreement were subsequently interpreted, however, so as to allow the Bank to make or guarantee loans in support of "programmes of economic reconstruction and the reconstruction of monetary systems including long-term stabilization loans"; and although no stabilization loans have ever been made, the loans to European countries were negotiated not in terms of specific projects but on the basis of the loophole left by the "except in special circumstances" clause that was finally inserted in the Charter. Other loans, although nominally made against specific projects, have seemed on occasion, to be only loosely connected with those projects, which were not contingent on Bank finance and appeared to be the subject of the loan contract almost by accident. The Bank has also made loans to Development Banks, which are able to feed in capital to local undertakings that are not specified in advance, although each loan made locally still requires Bank approval if it involves the use of Bank funds and is in excess of some agreed minimum. This

last provision, if rigorously enforced, would represent the *reductio ad absurdum* of the specific-projects approach. It is hard to believe that the Bank can exercise really effective control over loans made by, say, the Ethiopian Development Bank.

An unkind critic would say that the whole idea of financing economic development project by project smacks of paternalism and a pedagogical outlook. The Bank is not willing to lend a country the money it thinks it needs because the money may be misused. The Bank wants not only to ensure eventual repayment, but also to see to it that the borrower will make the best use of the capital. It comes near to taking for granted that it is a more reliable champion of the borrower's best interests than the borrower himself.

This may seem presumptuous but it is very often true. The difference in competence in matters of economic development between the staff of the Bank and the administration of many under-developed countries is striking. What is more, the Bank's attitude is rarely resented, because many of the under-developed countries prefer to have technical assistance and foreign capital wrapped up together and supplied by the Bank. It is a measure of the success of the Bank in its dealings with the under-developed countries that they should place so much confidence in it, and accept almost without question the specific-projects approach to international lending. Yet the same countries complain both of the insufficiency of Bank lending and of the long interval that usually elapses before it is possible to complete arrangements for a loan from the Bank.

From the Bank's point of view the merit of the system is that it can offer the borrowing country much-needed guidance on the elements of development policy. It can use each project as an object lesson in order to demonstrate how to plan and organize large-scale capital expenditure. This is true not only of the individual project that is being financed but also of the whole investment programme of the borrowing country. At the project level, the Bank has wide experience in finding suitable engineering consultants; in making sure that the scheme has been thoroughly examined, all the constructional and financial difficulties considered and the best alternatives reviewed, before it is embarked upon; and in assessing the full social value that it may afford, directly and indirectly. At the national level, the Bank has always laid stress on its unwillingness to consider a project in isolation from the pattern of national development into which it is designed to fit. It has encouraged its members to prepare comprehensive investment plans, not because it believes in Planning with a capital "P," but so as to make sure that each Bank-financed scheme will fit into a consistent and systematic programme of action. It has found again and again that under-developed

countries are taking no adequate thought for their future, or that their governments think it enough to have a shopping list of schemes with no internal consistency except perhaps their power to satisfy constituents or supporters up and down the country. The Bank attaches importance, therefore, to seeing the whole programme as well as confining its support to projects for which there is ample justification on economic and social grounds. It would be much more difficult to achieve the same leverage on the concrete, positive plans of member governments if general loans were made without reference to the details of the objects on which the money was to be spent.

From the point of view of the borrower, the system has obvious defects. It is impossible, for example, to raise money for various forms of social investment which the Bank rules out as unproductive; housing, schools, health services, and so on. The objection is not urged against roads although roads also are unproductive in the sense of yielding no revenue. The attitude of the Bank—on the whole, a justifiable attitude—is that governments are generally under stronger pressure to find capital for social purposes than for long-range economic development. If the Bank helps them to meet part of their total requirements, this should ease their difficulties in covering the remainder; but by limiting itself to so-called productive investment, the Bank can help to redress what might otherwise be a lack of balance in the general pattern of investment.

There is also a slowing down in the pace of lending. While some loans are concluded within a matter of months, others take literally years. This has meant that, in the early years of the Bank at least, it took a long time to work up steam and the sanctioning of loans lagged behind the submission of schemes. But after ten years, this effect can hardly amount to very much. The exhaustive scrutiny to which projects are submitted may delay the granting of loans, but it need not affect the peak rate of lending attained, provided member countries are not discouraged from feeding in new propositions by the uncertainty surrounding the old. The Bank assumes that countries seeking long-term capital can afford to wait, and indeed should wait, for loan approvals instead of rushing ahead without adequate preparation; and that if a country needs capital quickly for balance of payments reasons its proper recourse is to the Fund or other sources.

There is an obvious danger that the elaborate precautions taken by the Bank to ensure that it makes good loans may create some resentment among borrowers who have satisfied themselves in advance that their schemes meet all the criteria that the Bank could possibly lay down. There is a tendency in the Bank to erect project appraisal into a mystique when in fact it calls for no more than good organizing capacity, en-

gineering experience and economic and financial insight. The combination of these may be rare but it is not unique. As the Bank educates its members in project appraisal and begins to receive a more sophisticated assessment of the schemes which it is asked to finance, it may be able to relax some of its present vigilance and give prompter approval.

While the Bank's insistence on project loans may be justifiable when the borrower is weak and inexperienced, it is irksome to countries that need no education in large-scale planning and administration. The system of rigorous supervision and control over disbursements that is an almost inseparable part of the project approach has been the subject of adverse comment by countries that have already devised effective instruments of financial supervision and feel that, having given adequate security for a loan, they should be dispensed from covenants and procedures that are both superfluous and harassing. Sometimes countries that have started out as critics of the degree of control exercised by the Bank have later expressed complete satisfaction with the procedures followed and have even found in them a model to follow; but the stronger and more experienced the borrower, the greater his difficulty in swallowing the system of investigation, appraisal and supervision on which the Bank insists.

The second condition, that limiting Bank loans to the foreign exchange component in capital expenditure, could be a more serious handicap and more difficult to justify. One purpose of the limitation is to prevent borrowing countries from assuming too large a burden of foreign indebtedness in relation to their earnings of foreign exchange. But this already enters into the Bank's assessment of the creditworthiness of the borrower, and seems more relevant to the total external indebtedness that may safely be incurred than to the division between external and domestic sources of capital in each individual project. It is perhaps more reasonable to regard the condition as one intended to secure that the Bank is not normally called upon to promise more than about half the total capital and that local capital will play an effective part in any project financed by the Bank. If this is the right interpretation, there is some point in establishing a convention that the Bank's share should be governed by a formula that has an air of plausibility and can easily be applied. There is a further administrative convenience in that the Bank can supervise disbursements and release foreign exchange only against approved expenditures.

An over-scrupulous application of this condition would tend to discriminate against particular types of project and country. It would be natural, for example, for countries that were anxious to borrow as much as possible from the Bank to submit for its consideration the kind of

project that had a large foreign exchange component, and they might be tempted to amend their investment plans so as to give preference to such projects over others which, if the condition did not apply, would be more attractive. Suppose, for example, that a country has a shortage of electric power and is faced with the choice between thermal, hydro and nuclear generation. The cost in foreign exchange per unit generated may follow a different order from the total cost per unit including local currency outlays, and the total cost may itself depend upon the proportion of the capital supplied by the Bank at, say, 5 per cent and the proportion supplied locally at an opportunity cost that may be twice as high or higher. The eventual decision may be in favour of nuclear power, with a high outlay on imported equipment financed with relatively cheap capital rather than on hydro-electric power involving a heavy expenditure of scarce local capital; yet if it were possible to borrow the whole of the necessary capital from the Bank, the decision might be reversed.

In the same way, some countries would be in a better position to take advantage of Bank lending than others because they would find it easier to put up, out of local savings, a supplement to the foreign exchange supplied by the Bank. A country so poor, or with so undeveloped a capital market or fiscal system that it could hardly take even the first steps in development, might badly want to borrow from the Bank but have great difficulty in matching the Bank's contribution with domestic savings. The countries likely to make most extensive use of the Bank would consequently be neither so rich that they had no need to borrow abroad, nor so poor that they could not meet the Bank's conditions.

The Bank has not, however, held rigorously to the position that it should supply no local currency but only foreign exchange. In the Fifth Annual Report it summarized its policy by laying down three conditions for the finance of local expenditures: "(a) if the project to be financed is of such economic urgency that the country's ability to undertake foreign borrowing—which is more or less limited in all cases—is better utilized in financing this project than in financing the direct foreign exchange costs of alternative projects; (b) if the local currency costs of the project cannot reasonably be met out of available domestic resources; and (c) if it is apparent that, unless foreign exchange is made available to the borrowing country to be employed for the import of either consumer goods or raw materials, the local currency expenditures involved in the project will lead to inflationary pressures."

These conditions are unexceptionable: but it is difficult to believe that, translated into action, they would make loans to cover local expenditure so extraordinarily rare, especially when any other kind of loan hardly

existed up to fifty years ago. In an under-developed country almost any increase in capital investment heightens the danger of inflation and reacts on the balance of payments; it is quite arbitrary to single out the direct impact through imports of capital goods and distinguish it from the inevitable indirect impact through imports of consumer goods and raw materials. The shortage of capital from which such countries suffer normally finds expression in a physical shortage of specific equipment that can only be procured from abroad; but the shortage of capital is not limited to the lack of industrial equipment and does not arise merely from the absence of domestic capacity to produce that equipment.

The Bank has in fact made a number of "impact" loans, mainly to Italy, and has also, on occasion, made local currency loans, not attempting to determine the exact impact but financing a certain proportion of the total cost of the project. The first "impact" loans were to the Italian Cassa per il Mezzogiorno and received special justification on the grounds that, while the existence of a well-developed engineering industry in the north of Italy would make it unnecessary to provide for large foreign exchange costs, the indirect effect of expanding incomes on the balance of payments was likely to be particularly pronounced. Similarly, a recent loan to the Japan Development Bank for the finance of hydro-electric installations has been made to cover expenditures in Japan, not abroad, because Japanese industry is quite capable of furnishing the necessary equipment, but Japan has good reasons for trying to raise foreign capital.

The purposes for which the Bank has made loans are circumscribed by the conditions under which it operates. Two-thirds by value of the loans made so far (excluding reconstruction loans) have been for power and transport; and of the loans to industry nearly half has gone to iron and steel, leaving only $300 million for all other industries in thirteen years of operation. To some extent this reflects the inevitable concentration of the Bank on large loans; apart from steel, chemicals, and a few other exceptions, industry is, so to speak, a retail borrower while power and transport borrow wholesale. In part, it is the fact that the Bank supplies loan capital rather than equity capital that accounts for the pattern of its lending; public utilities in all countries raise most of their capital by the issue of bonds while industry relies heavily on share capital. In part, also, the concentration on public utilities does no more than reflect their enormous capital requirements in comparison with industry—a concentration that may be particularly marked in the early stages of industrialization.

Taking it all in all, the under-developed countries are wise to raise foreign capital in the form in which they can get it from the Bank, in

large amounts and at low cost, rather than in the form of a large number of small industrial investments on which the private investor is likely to want a far higher return. Given the central place that industrialization takes in the process of economic development, however, neither the Bank nor the under-developed countries can neglect measures to speed up industrial growth with the help of foreign capital. If the scale of the Bank's lending for this purpose has so far been disappointing, this is due not only to the circumstances already mentioned but to two other factors of major importance. One is the reluctance of private firms to accept a government guarantee, with the loss of freedom of action that this implies, and the equal reluctance of governments to give guarantees to private firms for fear of charges of undue preference or of the subordination of public interests and projects to private. The second factor is the unwillingness of the Bank to finance manufacturing industries in government ownership.

A European observer, living in a mixed economy, cannot altogether share the ideological hostility of the Bank to public enterprise in manufacturing industry, although he may recognize its imperfections; and the Finance Minister—and still more the Central Bank—of an under-developed country may see inconveniences in relying too exclusively on private foreign investment for the development of new industries. These are large matters and cannot be fully discussed here. The Bank is much too intelligent to see the issues in black and white, and its bias rests as heavily on experience in the actual conduct of industry in under-developed countries as on the economic philosophy natural to Washington.

It may yet prove that, in seeking a way round these difficulties, the Bank has found a better and more economical way than direct investment of harnessing international capital to industrial development. In the past, it made quite incidental use of development banks as a channel for the financing of public utilities and agricultural development; more recently it has helped to set up development banks for the specific purpose of assisting industrialization. In doing so, it has insisted that they should not be the creatures of governments but should, as far as possible, be run either as private corporations or with representatives drawn from private industry on their Boards. It has, however, no absolute rule against providing finance through a government-owned development bank and has, for example, made loans to the Ethiopian Development Bank, which is a public institution, and to the Herstelbank, which is a mixed institution but under government control. Indeed, it would be absurd for the Bank to insist that money supplied against a government guarantee not only *should* but *must* be administered by a bank free from direct government control. There is no inconsistency in feeding capital

to private industry through a government-owned financial institution and believing at the same time that industrial development is best left to private enterprise; and it would be difficult for an inter-governmental financial institution, feeding capital to private industry against government guarantees, to argue otherwise.

The major limitation on the Bank's lending is the simple requirement that its loans must be made on commercial terms. This is a requirement that the Bank has faithfully observed if we may judge from the fact that, so far, no Bank loan has ever been in default in more than a technical sense. The Bank took the view right from the start that it should charge each country the same rate of interest, irrespective of any difference in credit ratings, and it would obviously have created almost insuperable administrative difficulties to have adopted any other rule. The rate of interest payable is based on the rate that the Bank would itself have to pay currently if it were to make a bond issue of similar maturity in Wall Street. To this is added a 1 per cent commission charge and ¼ per cent to cover administrative costs. This yields a rate which, in recent years, has never been lower than 4 per cent and never higher than 6.

These rates cannot be said to be unattractive so long as the trade of the under-developed countries is expanding. Each Annual Meeting sees an attack on the 1 per cent commission charge; but the $100 million that it has so far brought in represents a very small liquid reserve against possible defaults on a total indebtedness over thirty times as large. The members of the Bank that are in a net creditor position can argue that they have had no dividends on their subscriptions and that the net income earned has contributed over twice as much to the Bank's reserve as the commission of 1 per cent.

If one takes the view, as some economists do, that only massive capital investment can bring about rapid development of the under-developed countries, all this is largely irrelevant. If the under-developed countries cannot afford to borrow more because of the service charges involved, then these charges must be reduced. The Bank would then remain the agency through which loans were made, but the terms of the loans would be adapted to the capacity of the borrowing country to pay.

The Bank's attitude to this proposal has been that, whatever is done to help under-developed countries, its present relationships with those countries should not be disturbed. The Bank takes the view that capital is by no means the only stumbling-block to development and that it has been far more the lack of satisfactory projects and the lack of trained men to run them, that has prevented it from lending more. It would

TABLE IV

NET INCOME AND RESERVES OF WORLD BANK, 1946-58
($ MILLION)

	Net income (appropriated to reserve)	*Commission on loans (appropriated to special reserve)*
1946-48	4.3	3.1
1948-49	10.5	5.0
49-50	13.0	5.7
50-51	16.1	6.4
51-52	18.1	7.6
52-53	20.6	9.6
53-54	23.2	11.7
54-55	24.9	13.3
55-56	28.6	14.7
56-57	35.9	16.7
57-58	42.1	20.2
Cumulative to June 30, 1958	236.4	113.9

Source: Annual Reports of I.B.R.D. (The figures of net income were revised in the *Twelfth Report*, p. 53, and do not sum to the cumulative total shown in that *Report*.)

welcome grants or other help in supplementation of Bank loans and it is anxious to encourage a much larger volume of private loans against the credit of the borrower and aid offered by other countries individually or collectively.

It is difficult to see how, under the terms of its charter, the Bank could itself initiate a change in the system of lending. It is, however, free to take the lead in proposing to its members arrangements for collective assistance on non-commercial terms and it has shown itself willing to help to operate such arrangements provided they seem practicable and workmanlike. One possible arrangement would be to set up a special fund, replenished from time to time, out of which grants could be made towards the capital cost of approved schemes, including bank-financed projects. In the latter projects, the only difference from present arrangements would be that instead of commercial banks participating (or perhaps in addition to such participations) the special fund would take up part of the loan at a nil or reduced rate of interest or make a grant by foregoing its right of repayment. Other projects—for example, in the field of education—that would not qualify for bank finance might nonetheless obtain a loan or grant from the fund.

It would be an illusion to suppose that such a fund could, for years to come, operate on a large scale—a scale larger, say, than the Bank's own operations. If it is grants, not loans, that under-developed countries require, they seem more likely to obtain them bilaterally than internationally; and if the grants are to be for non-productive purposes it may well take a long time to process applications and to make dispositions to use such grants.

There is no immediate likelihood that any fund along the lines described above will be set up, if only because the proposal commands little support in the United States which would inevitably be the main contributor. The proposal favoured by the American government involves the setting up of an International Development Association, as an affiliate of the International Bank, to make loans repayable in whole or in part in local currencies. The Bank, in spite of its opposition to "fuzzy" loans, is ready to accept this proposal. It already has the power, when full service of its loans is proving impossible because of acute exchange stringency, to accept service payments, within limits, in the local currency. What is now proposed is that it should, through the International Development Association, make use of funds contributed multilaterally and including local and other currencies that have accumulated through the sale of agricultural surpluses and through other programmes. The use of such funds by themselves could add nothing to the real resources at the disposal of countries that have already taken advantage of the original sales or grants. But the administration of local currencies would presumably be coupled with fresh resources of foreign exchange; and with continued injections of foreign exchange and a stock of local currencies to provide a *masse de manoeuvre* the Bank would be in a stronger position to shape and reinforce the investment programmes of under-developed countries.

Some of the Bank's critics appear to have in mind loans at 2 or 2½ per cent interest on the Russian model. Perhaps that model will be copied or the Russians themselves may make more use of it. But up to now, low interest loans to non-Communist countries have been made to a small group of countries of great strategic importance, have been trifling in magnitude and have cast a spell quite out of proportion to their value, still more in relation to the sums actually disbursed.

The principal innovation of the Bank as a means of stepping up the flow of capital to the under-developed countries has been the establishment, after long delays, of the International Finance Corporation in July 1956. The Bank suffers from the disadvantage that it can lend only against a government guarantee, which is neither readily given to a private business nor willingly sought by it. I.F.C. is not subject to

this limitation. It can ally itself with a private undertaking and supply debenture capital just like any other investment bank. It cannot take an equity but it can make loans that carry a contingent participation in future profits or an option to convert part or all of the investment to shares at a later date, and if the venture is a success, it can reap a capital profit when it disposes of its bonds to a holder who is not restrained, like I.F.C., from making use of the conversion rights.

It is too early to judge the success of I.F.C. It was expected to find plenty of customers and to contribute to the flow of private capital to under-developed countries by allying itself with corporations operating in those countries. In the first two years of operation, however, I.F.C. made only ten investments totalling $10 million. It may be that I.F.C. will be forced to confine itself to the blue-chip type of business and that such businesses in under-developed countries will prefer to finance themselves out of profits or else turn to their own shareholders for additional capital. On the other hand, many large corporations, even when they can raise the capital through a new issue, are glad to be able to find a convenient way of reducing their total capital requirements and may be prepared to make use of I.F.C. in order to extend the range of their foreign operations. It is perhaps significant that only four of the first 11 loan commitments are to companies owned entirely by local interests, while the others are either to subsidiaries of large international companies or to companies jointly owned by foreign and local interests.

It is unlikely that I.F.C.'s scale of operations will ever be very large even in terms of the total capital invested in the undertakings in which it participates. But it may be able to accelerate its growth if, as it now contemplates, it can make local currency loans and so free borrowers from the uncertainty surrounding the terms on which they can eventually obtain dollars for repayment. There is also scope for an extension of the arrangements with local investment banks and other financial institutions which can submit or investigate suitable projects and join in financing them.

Throughout the post-war period, one nagging doubt about the Bank's lending has made itself felt from time to time. What would happen to loan applications if primary produce fell heavily in price? The under-developed countries have until recently felt the steady pull on their development of favourable prices. These prices raised incomes directly, and indirectly made possible a further expansion by holding off the normal deflationary pressure exerted by the balance of payments. The same forces have created opportunities of investment in the products affected and a general shortage of capital because of the conditions of boom encouraged by high exports and high investment. When these

forces become reversed, as has happened over the past two years, can the Bank count on a continuing pressure to borrow? Or must it acquiesce in a cyclical fluctuation in its loans? Up till the middle of 1958 lending has gathered speed rather than fallen off. To some extent this may reflect the administrative lag in processing applications; it may also reflect pressure to maintain public capital expenditures as tax revenues fall off with the exports that normally sustain them; it certainly indicates a willingness on the part of the Bank to take a long view of its members' prospects. Whatever the explanation, the reactions, so far at least, have been reassuring and the Bank is busier than ever.

V. THE BANK'S PLACE IN THE INTERNATIONAL CAPITAL MARKET

The object of the Bank has always been to supplement and stimulate private foreign investment, not to supersede it. This implies that the Bank should make loans only to borrowers who would be unable to raise capital from private sources under reasonable conditions. But it may be taken to imply much more: both as to the scope for private foreign investment in under-developed countries and as to the ultimate rôle of the Bank in its relations with governmental and inter-governmental lending institutions.

The Bank may withhold its support from borrowers or types of project on the grounds that they should be financed privately, while the borrower is unwilling to make use of private investment either because of its cost or on social and political grounds. Nor is this mere hypothesis. Governments seeking to develop their own oil deposits have never obtained a loan from the Bank for this purpose. In most of the countries to which it has lent the Bank has taken a position hostile to public ownership of manufacturing industry, arguing that nationalisation is calculated to slow down economic development and is not the most fruitful use of capital borrowed from abroad. It has even preached this doctrine to Austria while continuing to lend to Yugoslavia.

At the same time, the Bank is under no obligation to refrain from competition with governmental lending institutions. The export of capital has always been associated in the outlook of the under-developed countries with imperialistic influence and the improper exercise of power by lending countries in order to secure property rights or advance the commercial interests of investors. The setting up of the Bank was, from their point of view, a blow against imperialism of this kind. They were far more willing to welcome capital from an international institution than to rely either on private investment or on loans from friendly gov-

ernments. To say this is not to endorse the curious notions now widely entertained about what foreign investors did and did not do over the past century; whether the view of history subscribed to by would-be borrowers is fact or myth, their present-day attitude is real enough and most of them entertain warmer feelings towards the International Bank than towards the other agencies from which they might borrow.

But it is not only the under-developed countries that have a stake in the emergence of the Bank as the major source of international capital requirements. There is a danger that each of the big industrial countries will employ its own financial strength to secure its exports of capital goods against competition in the markets of the under-developed countries. The United States set up the Export-Import Bank nearly twenty-five years ago, partly at least as a means of pushing American exports; loans made by the Export-Import Bank are tied loans while the funds supplied by the International Bank can be spent freely on imports from the most economical source. Other countries such as Japan have begun to create lending institutions similar to the Export-Import Bank and even where no such institution exists, it is more and more the rule that large construction contracts are awarded in the under-developed countries to exporters supplying capital simultaneously for periods up to ten years and sometimes even longer.

This situation is due to a large extent to the absence of an international capital market such as existed before 1914. Major projects could then be financed through a public issue in London or elsewhere and the capital so raised could be applied to buy equipment for cash on the best terms offered. Today, however, very few governments could float a public loan in any capital market but their own; and large enterprises still in private hands have little chance of raising money abroad by public issue unless they happen to be branches of international concerns borrowing in the country of origin. On the other hand, the capital requirements of the under-developed countries are very large and their bargaining position as borrowers has greatly improved. They can take advantage of the competition in capital goods in order to insist on favourable credit terms and have been successful in obtaining in this way at least part of the capital that they would have raised, half a century ago, in the London market.

There are, however, some notable disadvantages in an arrangement of this kind. First of all, since the loan is tied, the cost of the equipment purchased is almost inevitably higher than it would otherwise be. Secondly, there is the restriction of international competition because of the need to furnish capital and equipment simultaneously. An exporting country may produce excellent equipment at low cost and yet be too

short of capital to offer long terms of credit. If, in the long run, ability to lend is to determine success in the competition between exporters of engineering products then one more source of imbalance will be added to international trade; for it is likely to be the richer, more advanced country that can lend most readily and that can thus reinforce what may well be a growing technical superiority in engineering.

From the point of view of industrial efficiency, moreover, it is a mistake to involve engineering concerns in what is normally banking business; they may have difficulty in raising the capital and will charge into the price all the inconveniences and costs that entry into this unfamiliar territory involves. No doubt an Export-Import Bank may save them from most of these inconveniences; but it creates at the same time a bilateral relationship between debtor and creditor that seems more likely to give rise to political friction than an international relationship through the World Bank. Finally, once countries have pledged their credit through medium-term commercial loans, they cannot expect to pledge it again with the Bank so as to obtain long-term capital. Since what they really need is long-term capital, and medium-term credit is a *pis aller*, their interests clearly call for an expansion in Bank lending rather than in medium-term credit.

All this is recognized by the Bank. Indeed, there have been times when it has been almost excessively vehement in its warnings of the dangers of reliance on medium-term credit. There are obviously circumstances in which it is as sensible to take advantage of suppliers' credit as to make use of hire purchase; the procurement of equipment on hire purchase does not rob a sound concern of its creditworthiness and may even, on occasion, make it a more promising debtor. Provided the facts are known and fully disclosed, the Bank can have no complaint against the borrower although it may think him misguided. The real issue is whether the Bank can so revive the long-term capital market that it makes suppliers' credits relatively unattractive.

It would be useful in examining this question, to have fuller data establishing the trends in international lending. We know something of the scale of foreign investment in recent years by the major creditors, although the data do not seem to have been brought together to provide aggregates for the world as a whole. We know little of the scale of suppliers' credits except when they are provided through institutions like the Export-Import Bank, or have been insured by credit insurance agencies like the British Export Credits Guarantee Department.

The outflow of private long-term capital from the United States to other countries has been running at about $3 billion a year and from the United Kingdom at about $600 million a year. Most of this invest-

ment, however, represents the ploughing back of profits by existing undertakings and new issues in New York and London come to a very much smaller total. Very few out of the limited total of new issues are on behalf of under-developed countries unless Canada is included under that heading. Taking bond issues alone, most of the public issues of foreign bonds in the American market since the war have been for Canada. In Europe, issues of foreign bonds have reached a much smaller total, the chief markets being the United States, Switzerland, and the Netherlands; there were a few issues for Norway and Denmark in Sweden and none at all in Germany until 1958. The only countries outside Europe and the British Commonwealth that feature in the list of borrowers are Israel (exclusively in the United States), the Belgian Congo (in Switzerland), Cuba (in the United States) and Peru (an electric power company made three issues in Switzerland). Table V shows the total public issue of foreign bonds in the five principal markets (the United States, the United Kingdom, Switzerland, Sweden and the Netherlands) in each year between 1953 and 1957, excluding issues by the United States, Canada, Israel and the High Authority.

TABLE V

FOREIGN BONDS PUBLICLY ISSUED IN 5 PRINCIPAL CAPITAL MARKETS (EXCLUDING ISSUES BY THE UNITED STATES, CANADA, ISRAEL, AND THE HIGH AUTHORITY)

($ MILLION)

	1953	*1954*	*1955*	*1956*	*1957*	Average *1953-57*
Total	135	246	222	111	58	154
Less re-funding (New money)	96	218	189	68	41	122
Less private (Government and municipal new issues)	94	160	163	47	34	100

Source: International Bank (from unpublished data).

Over those five years the amount of new money raised for governments and municipalities averaged no more than $100 million. In the same period, the International Bank alone (whose issues are excluded from the figures in Table V) raised more money by bond flotations. Thus although the International Bank plays a relatively small part in the total international flow of capital, it is far from insignificant in relation to new issues of foreign bonds.

Its main competitors are governmental agencies. If we leave on one side economic assistance by way of grant, the Export-Import Bank is by far the most important example of such agencies. Leaving out of account exporter credits and the special line of credit extended to the United Kingdom in 1956, loans made by the Export-Import Bank in recent years have been at an average annual rate of about $400 million, or about the same rate as loans by the International Bank before the spurt in 1957-58. The Export-Import Bank also obtains a substantial part of its funds through repayment of outstanding loans, so that the net increase in capital has been slower than the net increase in outstanding debts to the International Bank. Moreover, many of the larger loans by the Export-Import Bank are made for non-commercial reasons and are not strictly comparable with those made by the International Bank. For ordinary purposes, the latter has established its position as the principal supplier of international long-term capital.

Critics of the Bank—for example, in the United Kingdom—sometimes affect to see little real difference between the Export-Import Bank and the International Bank on the grounds that in many parts of the world the International Bank is generally regarded as an American institution, staffed by Americans, favouring the use of American equipment, and lending American dollars. It need hardly be said that this is a complete travesty, although there are countries with such an imperfect acquaintance with the Bank that they mistake the travesty for truth. To take the last point first: of the loan disbursements of the Bank, over half the total in the past two years has been in currencies other than dollars and the proportion has been mounting fairly steadily. This alone shows that the borrowers do not place all their orders in the United States: no country is anxious to contract an obligation to repay dollars if some other currency will serve to achieve the purpose of the loan. The same point emerges more forcibly from an examination of the actual loan expenditure of borrowers over the past few years. The proportion spent in the United States has fallen progressively from 54 per cent in 1954-55 to 44 per cent in 1956-57 and 39 per cent in 1957-58; in the United Kingdom, it has moved from 24 per cent in 1954-55 to 11 per cent in 1956-57 and 19 per cent in 1957-58; while in Germany it has risen from 6 per cent to 18 per cent over the same period.

These figures go some way to discharge the Bank from the remaining accusation that its staff is biased in favour of American equipment and that this bias is effectively communicated to the borrowing countries. The increased disbursements in Germany in no way correspond to any hidden pressure exerted by German engineers in Washington and more probably reflect the success of German exporters of capital goods in

re-establishing themselves in world markets. The fact is, as anyone who has worked in the Bank can testify, that although there is probably greater familiarity with American engineering consultants and practice, and greater convenience in using them, the staff of the Bank is international both in composition and outlook, and is moved chiefly by the desire to secure for borrowers the best available advice irrespective of nationality. The professional staff includes members drawn from over 40 different countries and they are recruited on very high standards of competence, with a bias, so far as any bias exists, in favour of free competition.

But if the Bank is very far from being just another Export-Import Bank, it is not on that account non-competitive with the Export-Import Bank. It does not and cannot actively compete in the sense of soliciting business; but it can do business with borrowers who might, in other circumstances, have gone to the Export-Import Bank or some similar national institution. The interesting issue is why borrowers should *prefer* to come to the International Bank.

No doubt the Bank would say that the borrower only comes when he has exhausted other possibilities, that if he comes before doing so he cannot hope for a loan, and that it is not preference, therefore, but the absence of an alternative source of finance that moves him. But as the case of suppliers' credits shows, one can push this argument too far, and borrowing countries can shape their course so as to come oftener or less often to the Bank according as they find it a more or less convenient source of capital than other lenders. It is also by no means evident that the Bank can play its proper part if it acts merely as a lender of last resort to whom borrowers turn once they can get no more from other reputable lenders. To be put in this position might well prevent the Bank from conducting its operations on a sufficient scale to give it the commanding position which it now enjoys in its dealings with borrowers, particularly in under-developed countries.

From the point of view of borrowing countries, the Bank possesses some undoubted advantages. It makes loans for longer periods than other institutions; the maximum (apart from the thirty-year reconstruction loan to France) has been twenty-five years and the average on all loans outstanding in 1957 was just under fourteen years. This does not prevent the Bank from making medium-term loans, too, but no loans for periods of less than five years have been made since 1951. The loans are not tied, and, unlike IMF loans, do not have to be repaid in convertible currencies. If American equipment is dear and currencies are not fully convertible, there is an advantage to the borrower in coming to the International Bank rather than to the Export-Import

Bank and this appears to have been a factor of some importance in the middle fifties. The borrower who has disbursements to meet in some currency other than dollars can usually rely on borrowing the exact currencies that he requires; but at times he may be forced to acquire some of the necessary foreign exchange through the sale of borrowed dollars. Loan disbursements in Deutschemarks, for example, had reached nearly $200 million by the middle of 1958, while the full West German subscription in Deutschemarks came to just under $60 million. It was not uncommon, until a few years ago, for disbursements in inconvertible currencies to involve the use of dollars and Swiss francs because the local currency subscription had not been reached; the Bank suffered, as was pointed out at the 1951 Annual Meeting, from a scarcity of *soft* currencies!

VI. THE BANK AND ECONOMIC DEVELOPMENT

The Bank's part in the process of economic development seems to have been conceived by its founders exclusively in financial terms. But in the process of lending the Bank soon found that shortage of capital was only one of the obstacles to more rapid development. It was convinced of the need to deal comprehensively with those obstacles and this conviction led it to take the initiative in devising new methods of technical assistance to member countries.

The first of these was the preparation of a series of economic surveys, undertaken at the request of member governments, and reviewing the action that the governments concerned might take in order to overcome the obstacles to more rapid development. The "general survey missions" include a variety of experts, drawn mainly from outside the Bank, who spend about a year or eighteen months preparing a comprehensive report which is submitted to the government commissioning it and subsequently published by the Bank. The first such mission visited Colombia in 1949 and since that time survey missions have reported on 15 different countries.

The reports have had a mixed reception, due largely to a misunderstanding of what such a mission can and cannot hope to accomplish. The missions, after a fairly short briefing in Washington, tour the country to be surveyed for perhaps three months, talk to a large number of officials and others, and then return to Washington to begin the drafting of their report. It is this stage and the lengthy correspondence with officials that accompanies it that occupies most of the time. The facts in the Report are likely to be rigorously checked and the perspective which they are given is also likely to be as undistorted as the circum-

stances allow. It is, however, the policy recommendations that are the heart of the matter and these recommendations are unlikely to include many novel proposals never previously considered in the country visited. They may, however, give prominence to suggestions made during the visit by officials too junior to command a hearing; or they may put in a fresh perspective conflicting views between which the government is hesitating. The reports may be unsatisfactory to the economist and social theorist because they fail to set out the theoretical basis for recommendations which are urged without jargon in order to carry more conviction. But the economist who serves on such a mission may also entertain private doubts about the helpfulness of his subject in face of some of the dilemmas of under-developed countries; and if a social theorist ever served on such a mission he might equally feel more at home in *ex post* analysis than *ex ante* prescription.

Apart from general survey missions, the Bank has sent missions to advise on special problems, such as the development of a local capital market. It also makes use of operational missions of two types; those that are exploratory and precede loan applications or loan approvals; and those that are supervisory and are sent after disbursement has begun in order to examine whether the loan is working out satisfactorily. Neither of these missions represents an extension of the Bank's functions in quite the same way as the general survey mission, although both play an important part in loan operations and the first type may produce a report that closely resembles one of the published surveys.

A second field of activity has been the nomination of experts, including officers of the Bank, to assist member governments in organizing economic development. The Bank is able to suggest specialists qualified to deal with specific technical problems such as railway operation, port administration, steel production, etc., and it can also recruit advisers, consultants and others for such posts as economic or financial adviser, head of a development bank, member of a development board or governmental planning agency. Members of the staff of the Bank are sometimes nominated for such duties and given leave of absence to allow them to be undertaken; the frequency with which their services are sought is a sufficient indication of the prestige of the Bank and of its staff as experts in economic development.

The more the Bank has come to grips with the problems of development the more it has been impressed with the importance of education and training, skill, experience and knowledge in all sections of the community; and especially in managers and administrators. It recognizes also the need to change institutions and attitudes and the power of education to bring about such a change. Most of all the Bank feels the

lack in under-developed countries of policy-makers able to enter into discussion on equal terms with its own staff.

It was this desire to train the top administrators in under-developed countries that induced the Bank to set up the Economic Development Institute in 1955. The Institute, organized on the principle of a staff college, runs six-monthly courses in Washington for about a score of senior officials from the under-developed countries. These courses, although making use of case-studies drawn from the Bank's experience, necessarily also attempt to distil from that experience some general principles of policy. It is indeed one of the functions of the Institute to act as a bridge between the practitioners of economic development, whether in the Bank or in national administrations, and academic economists engaged in analyzing the process of development.

One expression of these hopes is represented by the booklets which the Institute has begun to issue, starting with a study of "Development Banks" by Mr. Diamond, a member of the original staff of the Institute. Another departure that may bear fruit has been the holding of a conference at the Institute, also on Development Banks, between members of the staff of the Bank and key officials of some of the principal Development Banks in the under-developed countries. Perhaps at a later stage the Institute may sponsor a conference with academic economists on selected problems of development.

The Bank itself has experimented with methods of encouraging academic research into such problems. For example, it invited Professor Tinbergen to prepare the report which has since been published by the Economic Development Institute as "Design for Development." It also promoted studies of the regulation of the electric power industry in Latin America and the relation between population growth and economic development in low-income countries, such as India. The Economic Staff of the Bank has produced a great deal of valuable material, some of which has appeared in article, and some in book, form.

There is still too little contact, however, between the academic world and the Bank. Economists often imply that the Bank has evolved no theory on which to base its activities and the Bank at times shows scepticism of the value of general theories. The fact is that, as has become increasingly apparent, the theory on which we were all brought up, which took for granted a firm institutional framework, has only a limited value as a guide to the vast structural upheavals that accompany development. It is futile to work with fixed parameters when it is precisely the movement of the parameters that calls for explanation. Anyone seeking to prepare a programme of action for under-developed countries must therefore be on his guard against two opposite dangers: the too

facile assumption that what works in advanced countries will work equally effectively in other countries with different attitudes, institutions, and resources; and the temptation to follow the thread of causal sequence only so long as it does not pass the boundaries of economics.

Just as it is important to national administrations that there should be informed critics able to express an independent view on the policies that they are pursuing, so the Bank stands in need of skilled comment by independent experts. Such comment is most likely to come from academic economists and the Bank should seek it actively by ensuring that suitable opportunities are created. This is another reason why publication of documents and occasional conferences are of value; they not only spread information but force the reviewer or the speaker to take a position for or against the views expressed.

VII. CONCLUSION

The Bank has shown itself capable of adapting itself to changing circumstances: of altering its methods of operation and starting fresh experiments in international organization. The purposefulness of the Bank exercises a strong attraction over able men in all countries and the calibre of its staff in turn reacts favourably on its prestige in the countries which it serves. It retains the idealism and enterprise with which it started and has succeeded in mixing this with hard-headedness and thoroughness. Few international organizations have maintained so lively an atmosphere or one so favourable to the purposes for which they were established.

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