PRINCETON STUDIES IN INTERNATIONAL FINANCE NO. 29

Early Plans for a World Bank

Robert W. Oliver

INTERNATIONAL FINANCE SECTION
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The author, Robert W. Oliver, is associate professor of economics at California Institute of Technology. He spent the academic year 1970-71 on leave in the Economics Department of the International Bank for Reconstruction and Development in Washington. Among his publications are: THE ROLE OF SMALL SCALE MANUFACTURING IN ECONOMIC DEVELOPMENT (1958), AN ECONOMIC SURVEY OF PASADENA (1959), and A PROSPECTIVE ON SOUTHERN CALIFORNIA (1967).

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PETER B. KENEN
Director

Princeton University

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CONTENTS

EARLY PLANS FOR A WORLD BANK

I. INTRODUCTION

This is an account of the early proposals which eventuated in the International Bank for Reconstruction and Development—the World Bank. The major emphasis is upon the work of the Division of Monetary Research of the United States Treasury Department, particularly that of Harry Dexter White,[1] for it was the Bank draft conceived by White which eventually became the Articles of Agreement of the working Bank.

This is an appropriate moment for such an account since the Bank celebrates its silver anniversary in 1971. On March 8, 1946, the Inaugural Meeting of the Board of Governors of the Bank and the Fund was convened at Wilmington Island near Savannah, Georgia, in the United States. The first meeting of the Executive Directors of the Bank and the Fund took place in Washington on May 7. On June 4, Mr. Eugene Meyer, editor and publisher of *The Washington Post*, was nominated by President Truman and elected by the Executive Directors as the

[1] From June 1934 until April 1946, when he became the first United States Executive Director of the International Monetary Fund, a position he held until March 31, 1947, Dr. Harry Dexter White occupied a series of increasingly important posts in the Treasury Department—from Economic Analyst and Assistant Director in the Division of Research and Statistics, to Director of the Division of Monetary Research, all the way up to Assistant Secretary of the Treasury.

After he had left the Treasury, White was publicly accused of being, or having been, a Communist and of passing classified information to unauthorized personnel. The records of the Federal Bureau of Investigation presented in *Hearings before the Subcommittee to Investigate the Administration of the Internal Security Act and Other Internal Security Laws of the Committee on the Judiciary, United States Senate, Eighty-Third Congress* (Washington: Government Printing Office, 1954), pp. 1160 ff, appear to have been generally accepted in this regard, though White, shortly before his death from a heart attack on August 16, 1948, strongly denied the accusation, and his family subsequently prepared and published a book: *Harry White, Loyal American.*

According to the official biography of Henry Morgenthau, Jr., Secretary of the Treasury from January 1, 1934, to July 18, 1945, "Morgenthau in all his years in office had no reason . . . to doubt White's competence or loyalty or value to the department." John Morton Blum, *Roosevelt and Morgenthau,* A Revision and Condensation of *From the Morgenthau Diaries* (Boston: Houghton Mifflin, 1970), p. 462.

It would be unfortunate in any event if opinions about White as a person were permitted to obscure or dilute the facts of the history of the World Bank and the International Monetary Fund.

first president of the World Bank. Formal Bank operations began on June 25, when the member nations were asked for payment of the first 2 per cent of their subscriptions.

This is also an appropriate moment to remember the intentions of those who dreamed about the post World War II world, for some of the components of the Bretton Woods system have come under attack in recent years. There has been much criticism of the system of foreign exchange rates allowed to fluctuate only within a narrow band around fixed par values which are changed infrequently and only in response to overwhelming evidence of balance-of-payments disequilibrium. There has also been criticism of international foreign aid: some feel that charity should begin at home and others believe that existing programs are designed to benefit the advanced rather more than the less developed countries. While this study does not deal with these issues *per se*, it may shed some light on reasons for the exchange rate and international-aid system now in existence.

This story has received scant attention in the literature, partly because most histories have concentrated more on the Fund than the Bank and usually begin with the publication in 1943 of the Keynes Clearing Union Plan.[2] Within the Bank itself it has been taken for granted that little of consequence occurred before 1947, when John J. McCloy became president and charted the course followed by the Bank for the ensuing decade and a half. In a sense, this is a proper perspective, for the Bank nurtured by McCloy, Robert Garner, and Eugene Black was different in some respects from the Bank born at Bretton Woods. In recent years, however, as the Bank has become less concerned about the market for its bonds, it has become anxious to join with other international bodies and governments to "relate aid and development policies to those concerned with trade, monetary policy

[2] In particular see Richard Gardener, *Sterling-Dollar Diplomacy* (Oxford: Clarendon Press, 1956); J. Keith Horsefield, *The International Monetary Fund*, 3 volumes (Washington: International Monetary Fund, 1969); and Roy Harrod, *The Life of John Maynard Keynes* (London: Macmillan, 1951). For descriptions of other aspects of postwar planning, see Ernest F. Penrose, *Economic Planning for the Peace* (Princeton, N.J.: Princeton University Press, 1953); William Adams Brown, Jr., *The United States and the Restoration of World Trade* (Washington: The Brookings Institution, 1950); George N. Halm, *International Monetary Cooperation* (Chapel Hill: University of North Carolina Press, 1945); Raymond F. Mikesell, *United States Economic Policy and International Relations* (New York: McGraw-Hill, 1952); and Department of State, *Postwar Foreign Policy Preparation, 1939-1945*, Department of State Publication 3580, General Foreign Policy Series 15 (Washington: Government Printing Office, 1950).

and private capital Movements"[3]—all of which is interesting in the light of the postwar planning of the early 1940's.

The postwar planners never presumed that the individual parts of the total solution of the world's economic problems should be considered in isolation. Relief, reconstruction and development lending or giving, balance-of-payments adjustments, monetary and trade matters, countercyclical income policies, and national and international politics were all understood to be related, and organizations dealing with the various pieces were supposed to work closely together. The American planners desired the participation by all nations in international economic decision-making, and, with due regard for the limitations unavoidably imposed by nationalism, they were genuinely concerned with the welfare of the planet. Their major objective was to provide a world within which competitive market forces would operate freely, unhampered by governmental interference, for they supposed that market forces would produce optimum results for the entire world.

They sought to make trade barriers as moderate and nondiscriminatory as possible, to provide for international collaboration aimed at high-level employment, and to encourage the movement of long-term capital from capital-rich to capital-poor areas. As Jacob Viner put it, they were

> . . . trying to reverse the whole trend of policy and practice of the world at large in the field of international economic relations since 1914 and especially in the ill-fated years since 1929. [They were] attempting to do this, moreover, in the face of a skeptical world, undecided as to its objectives, and in particular lacking solid faith in the virtues of a pattern of international economic collaboration which can be reconciled with difficulty, if at all, with the comprehensive national planning of domestic economies to which most of the governments [were] strongly committed.[4]

At about the same time (April 1941) that a Committee of the United States Senate was considering the proposal for an Inter-American Bank, White began work on his Suggested Plan for a United and Associated Nations Stabilization Fund and a Bank for Reconstruction and Devel-

[3] Lester B. Pearson *et al.*, *Partners in Development* (New York: Praeger, 1969), p. 228.

[4] In Murray Shields, ed., *International Financial Stabilization, A Symposium* (New York: Irving Trust Company, 1944); reprinted in Jacob Viner, *International Economics* (Glencoe, Ill.: The Free Press, 1951), p. 233.

opment of the United and Associated Nations. His plan was an outgrowth of the Inter-American Bank proposal, though it embodied his own thoughts and the thoughts which had been expressed during earlier discussions within the Treasury Department.

White believed that the first international monetary problem to be solved was that of securing stable, though not rigid, foreign-exchange rates and freely convertible currencies. None of the other American objectives could be attained, he felt, if the various governments controlled and manipulated their foreign-exchange markets as had the Germans during the thirties. He proposed, therefore, an international agency (the Fund) which would help member governments decide which exchange rates should be maintained and would assist them in maintaining these rates by making available appropriate foreign currencies whenever *temporary* balance-of-payments disequilibria developed.

White then proceeded to provide for the attainment of other American objectives. He proposed an International Bank whose primary objectives would be to provide or otherwise stimulate long-term, low-interest-rate loans for reconstruction and for the development of capital-poor areas. He indicated that it might also finance an international development corporation and a stabilization program for international basic-commodity prices, and it might arrange its lending so as to combat international business fluctuations.

White was convinced that private investors could not be relied upon to provide the capital that would be needed for postwar reconstruction. He also felt that even after the postwar transition period, the normal flow of capital from rich to poor areas could not be left solely to the private investment markets of the world. The lessons of the twenties had been that long-term private capital movements tended to enforce, rather than mitigate, the spread of international business fluctuations and that the high interest rates and the relatively short-term maturities of private portfolio investments tended to make unproductive what might otherwise be productive international ventures. Ill-feeling on the part of both borrowers and lenders was the result.

The lesson of the thirties had been that unilateral national action could not bring a revival of international trade and investment along the liberal lines which had existed in large measure during the greater part of the nineteenth century.

This is not to say that White conceived of an International Bank which would supersede private investing, but rather one which would serve as a supplement. It would help to stimulate private investment in the post-transition period by guaranteeing private loans, and it would make loans directly only when it approved a worthwhile project that could not be financed privately at a reasonable rate of interest.

White was anxious that the loans of the Bank should result in permanently raising the standard of living of the borrowing country. He desired to avoid loans that would finance armaments or permit careless budgetary practices. He also wished to avoid loans that would be used for the purpose of repaying old loans. White was specific in stating that a loan could only be made after a careful study and a written report had been made by a competent committee on the merits of the projects to be financed.

The most novel feature of White's proposal was that the Bank might issue its own International Bank notes. These would be backed by a minimum of 50 per cent gold and would be "as good as gold" in international exchange. If the Bank's lending policies had been related to worldwide liquidity requirements, it could have become a sort of world central bank not unlike the supernational bank proposed by Keynes in the late 1920's.

Perhaps the most important feature of White's plan in the long run, a point on which he was adamant, was that the Bank must be truly international. It must not be a rich man's club. The poorest and smallest countries must be represented in the decision-making process, even if not on the one-country-one-vote basis of the General Assembly of the United Nations.

This study does not include a discussion of the reasons for the modifications of White's first draft nor of the negotiations leading to the Bretton Woods Conference. That is another story.[5] Nor does it include an account of the relevant discussions in wartime London among the representatives of various occupied countries. That also is another story.[6] The background of Anglo-American collaboration will be mentioned, as will the early plans of the American State Department, the Council on Foreign Relations, and the Board of Economic Warfare. In general, this is an account of the climate of opinion in wartime Washington regarding the postwar world.

[5] See Robert W. Oliver, *The Origins of the International Bank for Reconstruction and Development*, unpublished doctoral dissertation, Princeton University, June 1957.

[6] See J. W. Beyen, *Money in a Maelstrom* (New York: Macmillan, 1949).

II. ANGLO-AMERICAN POSTWAR ECONOMIC PLANNING

The appearance of recovery from the First World War was achieved during the late twenties, but sources of potential international disequilibrium remained: disequilibrium gold-currency ratios and, hence, exchange rates; an unequal international distribution of gold; large and growing short-term assets held abroad; erratic long-term capital movements; increasingly rigid price and wage structures; war-debt and reparations obligations; high tariff barriers; and the preoccupation of central banks with domestic rather than international monetary policy. With the Great Depression the gold-standard system of balance-of-payments adjustment collapsed, and economic nationalism became the order of the day.

The Background

The Americans, who had rejected many proposals for intergovernment economic cooperation during the twenties, became much concerned over the drift toward competitive currency devaluation, exchange controls, state trading, international cartels, bilateralism, and so forth. Following the 1933 experiment of changing the dollar price of gold, they came again to prefer stable, if not altogether inflexible, foreign-exchange rates, and they deplored foreign discrimination against American exports.

The American State Department sought the acceptance by all governments of lower trade barriers and unconditional-most-favored-nation treatment in international commercial relations, while the Treasury Department began its search for an international monetary system which might allow greater scope for national monetary action than had the gold standard, but which might also insure multilateral international payments, freely convertible currencies, and a reasonable degree of exchange-rate stability.

In 1936 the Treasury Department scored a victory of sorts when the Tripartite Agreement between the United Kingdom, France, and the United States was arranged and competitive devaluation among the major or key currencies ceased. But the dollar remained slightly undervalued relative to the pound, the franc gradually declined in value relative to the pound and the dollar, and gold continued to flow to America. No permanent international monetary arrangement had been found to replace the gold standard by 1939 when the Nazis invaded Poland,

and international monetary matters were high on the agenda of items to be considered by the wartime planners.

For their part, by the time the pound was freed from gold (1931), the British had developed a fear of deflation, particularly deflation dictated by external events. They consistently opposed a return to any international monetary system such as a gold standard which would require permanently fixed foreign-exchange rates. They were more interested than the Americans in the balance-of-payments adjustment process, and they considered balance-of-payments problems more than did the Americans from the standpoint of debtor and/or deficit nations. Some British economists, following Keynes, tended to favor fluctuating (though not necessarily freely fluctuating) exchange rates, and some (particularly those in sympathy with the policies of the Labor Party) tended to favor import restrictions and exchange controls. In either case, they were at odds with most of their American counterparts.

By the mid thirties, both the British and the Americans had become suspicious of international, long-term capital movements, though for different reasons. Following the arguments of Keynes,[7] the British suspected that long-term capital exports might injure the lending country. They were not at all convinced that the exports of the lending country would increase automatically as a consequence of foreign

[7] During the 1920's, Keynes wrote a number of articles and tracts inveighing generally against most international long-term lending and particularly the long-term lending of the United Kingdom. In *A Revision of the Treaty* (London: Macmillan, 1922), p. 162, Keynes wrote: "If European bonds are issued in America on the analogy of the American bonds issued in Europe during the nineteenth century, the analogy will be a false one; because, taken in the aggregate, there will be no natural increase, no real sinking fund, out of which they can be repaid."

In three articles appearing in *The Nation & The Athenaeum*, "Does Unemployment Need a Drastic Remedy?" (May 24, 1924); "A Drastic Remedy for Unemployment" (June 7, 1924); and "Foreign Investment and National Advantage" (August 9, 1924), Keynes argued that loanable funds should be used to purchase domestic rather than foreign securities, since new domestic investment was needed to deal with domestic unemployment. He advocated giving the Treasury discretionary powers over the issuance in London of new foreign securities. See Theodor E. Gregory, "Foreign Investments and British Public Opinion," *Foreign Investments*, Lectures on the Harris Foundation, 1924 (Chicago: University of Chicago Press, 1928), p. 113.

In "The British Balance of Trade, 1925-27," *Economic Journal*, Vol. 37 (December 1927), pp. 551-65, Keynes pointed out that, since 1926, the British had been investing abroad annually more on long-term account than they had been earning net on current account, the difference being made up by a potentially dangerous inflow of short-term capital.

Keynes remained suspicious of foreign investing at least until the Atlantic City meetings which preceded the Bretton Woods Conference in July 1944.

investments, and, at least in the case of British overseas investments, they were concerned that capital outflow might result in downward pressure on the external value of sterling. Thus, after 1931 the Bank of England, in conjunction with the British Treasury, imposed unofficial restrictions against the sale in Great Britain of foreign securities.

The British also felt that the burden of deflation and declining imports might become unbearable for a borrowing country if the lending country should erect barriers against its imports, if the lending country were unable to maintain its national income at a high level, or if the capital outflow from the lending country were highly erratic. In short, the British looked upon long-term capital movements largely in terms of balance-of-payments adjustments. They maintained that creditor as well as debtor nations ought to assume certain international responsibilities, and they apparently felt that, if balance-of-payments problems could be solved, long-term capital movements would require little additional consideration.[8]

The Americans tended to think of foreign-investment problems as distinct from short-run, balance-of-payments considerations. They paid much attention to the extent of, and the reasons for, the defaults after 1930 on American overseas investments, and they became wary of proposals that appeared likely to foster exports of American capital over which they might have no control. They felt, moreover, that a worldwide revival of long-term lending would require more adequate repayment guarantees on the part of the governments of the borrowing countries and that more care would have to be exercised by lenders to insure that the borrowed funds might be productively employed.

Of course, the foregoing is an oversimplified and extremely general summary of contrasting British and American views at the end of the depression decade. Exceptions to, and elaborations of, these approaches were expressed on both sides of the Atlantic. Anglo-American differences were differences in emphasis, moreover, rather than irreconcilable opposites, and there was a wide area of accord. By 1941, the British and the Americans were in substantial agreement that international trade should be balanced on a multilateral, rather than a bilateral basis, that the gold standard should not be resurrected, that the trade and foreign-exchange controls employed by Nazi Germany were detrimental to the peace and prosperity of the world, and

[8] See, for example, James E. Meade, *The Economic Basis of a Durable Peace* (New York: Oxford University Press, 1940), pp. 106-12.

that some system of organized international economic cooperation was probably desirable.

Because of common military and political interests and capabilities and in response to Article VII of the Master Lend-Lease Agreement, the Americans and the British were primarily responsible for planning the postwar international economy.

Keynes' Proposals

In June 1940, John Maynard Keynes accepted an invitation from Sir Kingsley Wood, the Chancellor of the Exchequer, to be a member of a Consultative Council. In this advisory capacity, he worked on many wartime problems, including the Bretton Woods negotiations.

Late in 1940, he prepared a memorandum on the relation between anticipated postwar balance-of-payments problems of the United Kingdom and the wartime liquidations of overseas British investments—a subject which he discussed with American officials in Washington during the late spring and summer of 1941. While in Washington he also had occasion to discuss the embryo Article VII of the Master Lend-Lease Agreement. Upon his return to London in the late summer of 1941, as a part of the British program to implement the Lend-Lease Agreement, Keynes began work on his Proposals for an International Clearing Union. His primary objective was to provide for an international organization which might deal with temporary balance-of-payments difficulties (rather than long-term capital movements) after the transitional postwar difficulties had been overcome.[9]

Keynes recognized that some international agreement regarding international investment would be desirable. In the Preface to his Proposals, he suggested that international economic cooperation should proceed along four main lines: (1) the mechanism of currency and exchange; (2) commercial policy; (3) production, distribution, and pricing of primary products; and (4) international investment. But, though in 1944 he proposed a number of amendments to the American plan for an International Bank for Reconstruction and Develop-

[9] See Ernest F. Penrose, *Economic Planning for the Peace* (Princeton, N.J.: Princeton University Press, 1953), pp. 44-45.

For a summary of the discussions concerning the Keynes Proposals and the other wartime plans for international monetary stabilization, see George N. Halm, *International Monetary Cooperation* (Chapel Hill: University of North Carolina Press, 1945). The basic similarity between the Clearing Union Proposals and Keynes' earlier plan for a Supernational Bank described in his *Treatise on Money* is obvious. (New York: Harcourt Brace and Company, 1930, pp. 395 ff.)

ment, he never devised his own plan for an international investment organization.

There may have been several reasons for this. Keynes may have felt, as did the Americans, that discussions on exchange stabilization should precede the discussions on the other main lines of international economic cooperation. He may have been deterred by his antagonism to international investment. He probably shared the prevailing British opinion that it was for the Americans to initiate any discussions regarding overseas investment.[10]

Keynes insisted that the drawing rights in his Clearing Union were not to be used to finance long-term international investment.[11] In a speech before the House of Lords on May 18, 1943, he stated:

> It is most important to understand that the initial reserve provided by the Clearing Union is not intended as a means by which a country can regularly live beyond its income and which it can use up to import capital goods for which it cannot otherwise pay. Nor will it be advisable to exhaust this provision in meeting the relief and rehabilitation of countries devastated by war, thus diverting it from its real, permanent purpose. These requirements must be met by special remedies and other instrumentalities.[12]

[10] See Roy Harrod, *The Life of John Maynard Keynes* (London: Macmillan, 1951), p. 533: "In regard to international investment, it was agreed that the British ought not to take an initiative, on the ground that they would not be in a position in the period immediately following the war to contribute substantial sums toward it. It was for the Americans to take the initiative in this part of the field."

In personal correspondence with the writer (September 13, 1952), Harrod reaffirmed this point as follows: "The official British view at that time was—and I don't think Keynes dissented—that the U.K. would have few spare funds for overseas investment after the war and that, therefore, if there was to be a big, bold plan on these lines, the U.S. must take the initiative. If the U.K. took the initiative in a big way and then said they could only put up £2-10 they would look rather foolish!

[11] See his Clearing Union Proposal, Sections 36, 41 and 42.

[12] See *Parliamentary Debates on an International Clearing Union*, British Information Services, July 1943, pp. 77; quoted in Halm, *op. cit.*, p. 161. The full text of this speech has been reprinted in Seymour E. Harris, ed., *The New Economics* (New York: Alfred A. Knopf, 1948), pp. 359-68.

In personal correspondence with the writer (September 13, 1952), Harrod emphasized the point further: "[Keynes] was anxious that big post-war reconstruction burdens should be thrown elsewhere, *not* into the permanent institutions. He was most anxious that the Clearing Union should be fully international with all countries having their chance of being plus or minus at the end of a period. He would have opposed and resented the idea that this should be thought of as an agency for distributing U.S. money. And I agree with Keynes most warmly."