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LIEFTINCK, P. - ARTICLES and SPEECHES (1963-1966)

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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

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THE WORLD BANK GROUP OF INTERNATIONAL CREDIT INSTITUTIONS AND THEIR SIGNIFICANCE IN DEVELOPMENT AID

Speech by Dr. P. Lieftinck before a business group
of members of the Dutch Labor Party,
Amsterdam, January 25, 1963



I greatly appreciate the invitation to speak on this topic, for I have the impression that while the subject of aid to less developed countries is attracting increasing interest, the value of the contribution being made to that aid by the World Bank group of credit institutions is insufficiently appreciated, particularly in political and business circles.

Only passing mention is made of the World Bank and its affiliates, IFC and IDA, in the White Paper on aid to developing countries presented to the Dutch Parliament last year, while in the discussion on the White Paper in the House only one speaker stressed the importance of the role of IDA and warmly advocated a liberal contribution to that organization. The lone voice was that of Mr. Ruygers.

The interest of business circles is limited mainly to the question of what amount of the funds lent by the World Bank to developing countries is being spent in the Netherlands and how that amount can be increased. An interesting memorandum on this subject was in fact produced recently by the Working Group set up by the Dutch Central Agency for Foreign Economic Relations to study the subject of exports of goods and services to the developing countries.

A very great deal might be said about the World Bank and its affiliated organizations and the scope of my talk must necessarily be severely limited. I therefore propose to concentrate my attention on the quantitative and qualitative significance of World Bank operations in the field of development aid as a whole, the limitations to which those operations are subject, and the development aid opportunities that present themselves if these organizations are led and used wisely and with an understanding of the progressively changing nature of the development problem.

The dominant body in the World Bank group is the World Bank itself, the International Bank for Reconstruction and Development, which was formed in 1946 and has thus been in operation for about 15 years. During the first five years of its existence (1947-1951), the Bank granted loans totalling over \$900 million, of which just over half was for the financing of postwar reconstruction in a number of devastated European countries, while at the same time a modest beginning was made in the financing of economic development projects in other parts of the world. During the next five years (1952-1956) the Bank acquired wholly the character of a development bank, with the emphasis on aid to the less developed countries, with which it built up an increasingly closer relationship by undertaking thorough studies of their development possibilities and problems, by despatching general

economic survey missions and by providing assistance in the drawing up and appraisal of economic development projects and the determination of priorities. During this period the rate of lending rose from \$300 million to \$400 million a year, and during the next five years (1957-1961) to \$700 million a year. In the fiscal year 1961/62, total loans reached almost \$900 million.

By the end of 1961/62 the Bank had lent a total of almost \$6.7 billion, of which \$4.4 billion was still outstanding, practically all in the less developed countries. Of the latter amount, about \$3 billion had been disbursed, while a further \$1.4 billion remained available to the borrower countries to meet expenditures related to the projects financed by the Bank. The funds are released by the Bank as the expenditure for which the loan has been granted is actually made, thus ensuring that the funds are used for the specific purposes of the loan.

The outstanding loans related to 277 projects in 45 countries. The individual loans vary in size from \$1 million to \$100 million, with a mathematical average of \$16 million. The loans are granted for terms that vary according to the nature of the project from 5 to 25 years, with an average of about 16 years. The rate of interest is governed by the price the Bank itself has to pay on the capital market and is derived from the formula: market rate+1-4% (to cover administrative costs) + 1% (to form the Special Reserve prescribed in the Bank's Articles). The present rate is 5 1-2%.

The major projects financed by the Bank have been in the following fields, in descending order of the total amount lent:

1. Electric power
2. Transportation (mainly, roads, railways and ports)
3. Mining and industry
4. Agriculture (including irrigation and mechanization).

They are mainly projects in the public sector, designed to create conditions conducive to the growth and expansion of private enterprise. The Bank has also, however, granted a number of loans directly to private enterprises (though with government guarantee, in accordance with its Articles), particularly in heavy industry, and also assists them by making loans to national development banks for the financing of smaller industrial projects.

In principle, the Bank only finances projects that merit high priority from the point of view of the basic economic development needs of the borrowing country. The Bank's loans are also limited in principle to the amount necessary to cover the foreign exchange costs, i.e. the import needs, connected with such projects, though in the cases of countries that are already rather more developed and are in a position to compete with foreign suppliers and contractors, the Bank takes a more liberal view and may also lend part of the local cost. The Bank still requires, however, that a fair opportunity shall be given for competitive international bidding, in order to ensure that the proceeds of the loan are used with the maximum efficiency.

It is interesting in this connection to note that the Netherlands ranks 11th among countries in which orders for goods and services have been placed for projects financed by the Bank, with orders totalling \$48 million, or 1% of foreign spending out of Bank loans. The effect of Bank loans on the exports of the Netherlands and the other Western European industrial countries is not, of course, limited to this direct expenditure but is indirectly amplified by the extent to which the purchasing power generated in the development countries as a result of the use of the loans is used to buy imported goods. The amount of this indirect expenditure is difficult to

estimate, however.

In mentioning the Bank's interest rate structure, I have already indicated that the Bank itself resorts to the capital market and has to pay the prevailing interest rate. The Bank has, of course, long passed the stage when it could finance its loan operations out of the paid-up capital subscriptions of its members. These payments on account of capital subscriptions amount to \$2 billion in various currencies, just under \$1.7 billion of which is in convertible currencies, the only ones that may be used to make Bank loans. Over the years, the Bank has supplemented these funds by the issue of bonds for a considerably larger amount, now equivalent to \$2.5 billion. These obligations are practically exclusively in the hands of governmental and private investors. Apart from calls on initial capital, payable out of public funds, amounting to 20% of the original subscriptions of the member countries, the Bank has obtained further funds exclusively on the private capital market and, thanks to the reputation it has built up, at the lowest prevailing interest rates. Other normal sources of funds for the Bank's lending operations are the proceeds of the sale of obligations of its borrowers (mainly obligations approaching maturity), loan amortization instalments and earnings in excess of the amount required by its Articles to be placed to Special Reserve.

That the Bank has for many years been independent of governmental contributions explains, in my opinion, the lack of interest shown in the Bank in political circles both in the Netherlands and in other developed countries and the fact that the Bank is usually ignored in discussions in those circles concerning aid to developing countries. To some extent, this is not a matter for regret, since the politicians have plenty of other things to think about and the Bank's independence enables them to concentrate their attention, so far as the development problem is concerned, on the undoubtedly wide field for other both possible and necessary action, in which the World Bank by its nature and origins can play only a minor role, if any. But both the scope and quality of the work done by the Bank merit, in my opinion, full recognition. I shall return to this point later, when I shall try to clarify the relative importance of the Bank's role in the field of development aid as a whole, and shall also refer in that connection to the Bank's programs of technical assistance, its efforts for the coordination of the various sources and kinds of development aid received by the developing countries or that can be mobilized for them, and its endeavors to obtain an improvement in the investment climate for foreign private capital in those countries by reduction of the risks involved.

I must insert at this point a further comment on an aspect of the Bank's principal activity, development financing. From my remarks about the Bank's independence of further governmental contributions and its policy of resorting to the private capital market as its main source of additional funds, it follows that a prerequisite condition for maintenance and possible increase of its present level of lending is an adequate measure of freedom to issue bonds in the countries with large investment resources. This is particularly important in the cases of countries, like the Netherlands, in which foreign issues are subject to official approval and certain quota restrictions that inevitably require that account be taken of the interests of other applicants. The policy of the Dutch authorities in this respect up to now gives no ground for complaint, but I mention the matter because it is of vital importance to the future of the World Bank and its ability to remain independent of public funds.

Second in importance among the World Bank group of financing agencies is the International Development Association, IDA. In my opinion the possibility is by no means excluded and is even on the horizon that over the course of the years IDA

may come to be equally important as or even more important than the World Bank. IDA was formed in 1960 with an authorized capital of \$1 billion. Its purpose is to supplement the operations of the Bank by making it possible to extend development credits on terms that bear less heavily on the balance of payments of the developing countries than those of the Bank's loans, i.e. on more liberal interest and amortization terms. Credits granted by IDA have so far been subject to the following conditions: an amortization term of 50 years, including an initial 10-year period of grace, free of interest but subject to a service charge of 3-4 of 1% to meet administrative costs. Another difference between IDA and the World Bank is that IDA has power to make its funds available for social development as well as economic development projects. In addition, IDA has wider discretion to finance local costs. Otherwise, IDA applies the same standards as the Bank in regard to the selection of high-priority projects and the efficient use of the credits.

The need for an agency such as IDA was rather slow to be recognized, even in World Bank circles, due to an initial marked reluctance to soften international credit conditions and the preference for a clear choice between loans on conventional terms and outright donations. The unpopularity of donations, particularly in the United States, and the fact that for reasons of national dignity many developing countries (and particularly the larger ones) find loans more acceptable than donations, finally led to the setting up of IDA and the adoption of its credit policy as a reasonable method of achieving the aim in question. The Directors of the Bank, who are at the same time the Directors of IDA, are now entirely reconciled to this solution and consider that IDA will have to be assigned an increasing share in development financing and given the necessary funds for that purpose.

The main reason for this is that over the last six years the total foreign indebtedness of the less developed countries has more than doubled and that interest and amortization obligations arising out of this heavier borrowing have even multiplied by two and a half times. It is estimated that by the end of 1962 the foreign indebtedness of the less developed countries will be not less than \$20 billion, equivalent to \$14 per head of population. In 1962, the service of this debt absorbed 7% of the export income of those countries, compared with 3% in 1956. In absolute figures this is \$2.5 billion a year. This means that, in fact, a capital transfer of \$2.5 billion to those countries was required before any net aid, available for investment, was accomplished.

The above figures are for the developing countries as a whole. The picture differs for each individual country - some bear a heavier and some a lighter burden. It is significant, however, that 19 of the 44 countries studied in this connection by the World Bank had to set aside in one year for service of their foreign debt not less than 10% of their average export earnings over the preceding two years.

The explanation for the fact that the increase in the interest and amortization burden is greater than the increase in the amount of foreign borrowing itself is that while the terms of loans from public (government) sources have become somewhat easier, on average, over the past six years, there has been a relative increase in the flow of loans from private sources to the public sector (chiefly in the form of credits by suppliers) and the conditions of those credits, so far as term and interest are concerned, are relatively more onerous. This private credit, in many cases supported by government guarantee, clearly tends to affect adversely the composition of the foreign debt of the less developed countries and to make the burden of servicing it heavier.

All this demonstrates convincingly the increasing need for aid to be given to the developing countries in a form that bears as lightly as possible, if at all, on

their national incomes and balance of payments. A number of countries have already reached, and others are rapidly approaching, the limit beyond which the taking up of further foreign loans on conventional terms is no longer justified. In addition, a substantial number of the newly-independent countries are not credit-worthy at all, so far as foreign loans are concerned, except on very liberal terms. In addition to aid in the form of outright donations or of loans that need only be repaid in their own currencies, a wide scope exists for development credits of the IDA type and a start has in fact already been made, at bilateral level, mainly through the United States Agency for International Development (AID), at regional level through a special fund (the Social Progress Trust Fund) administered by the Inter-American Development Bank, and multilaterally through IDA.

Of the initial subscribed capital of IDA of just over \$900 million, a little more than \$750 million is in convertible currencies. During the first two years of its existence IDA has already extended credits totalling \$360 million, for projects in 11 countries. As projects become ready for investment more and more quickly, an annual rate of lending of \$300 million will very soon be reached and in subsequent years could easily rise to \$500 - 600 million. The Articles of Agreement of IDA provide that decisions as to the replenishment of its resources for the ensuing period shall be taken every five years. These fresh funds will have to come mainly - and so far as convertible funds are concerned, practically entirely - out of the public funds of the wealthier industrial countries. To allow time for the preparation of projects, an agreement will already have to be reached before the end of the present year about the replenishment of the resources of IDA to meet the needs of the second five-year period. The former President of the Bank has expressed himself in favor of an objective of \$2.5 billion for this second period, equivalent to an average of \$500 million a year. It is greatly to be regretted that the reactions of the bigger European countries to this proposal have been definitely disappointing up to now and that they are talking in terms of an amount of \$900 - 1200 million for a period of 3 years, which would mean a lending capacity of \$300 - 400 million a year - hardly any increase at all over the lending rate already expected to be reached this year. It is not difficult to suppose that the basis for this attitude is a preference for bilateral aid over multilateral aid through IDA because of the opportunity it presents to the lending country to serve at the same time its own political or commercial interests and to lay down its own terms.

I am pleased to note that in the controversy about bilateral and multilateral aid the Dutch Government is taking a more balanced view. I do not, however, agree that less emphasis should be placed on this distinction and I do not find the arguments in support of this contention in the White Paper I referred to earlier convincing. According to the White Paper, multilateral aid is provided for by treaty obligations and the question of a choice only arises in regard to additional funds. My answer to this is that at this time, when the decision about the replenishment of the resources of IDA is about to be taken, the discretionary choice between bilateral and multilateral aid, or rather how far to go with bilateral and how far with multilateral aid, is one that radically affects the whole field of development financing. And the argument that the difference between bilateral and multilateral aid is becoming blurred because there is a shift of emphasis with respect to bilateral aid from project-aid to the financing of national programs, via consortia and consultative groups, ignores the fact that multilateral aid on the IDA pattern, which is the new alternative in the field of development aid, is extended on terms entirely different from those now customary in bilateral aid, and indeed inherent in most forms of bilateral aid. I think I have already demonstrated that from the point of view of the developing countries credits on terms of the IDA type are clearly to be preferred and are becoming more and more of a necessity as time goes by.

I do not deny that our export interests also deserve consideration. Any country that holds itself aloof from bilateral aid in present-day circumstances weakens its ability to compete with countries that do use this form of aid as a means of furthering their export trade. I also recognize that a new contribution to IDA and the furnishing of bilateral aid present problems of domestic financing which can be solved in a number of different ways. A new IDA contribution would have to be made through the national budget, though it need not come out of taxes: it would be possible to float a special public loan for that purpose. Bilateral aid in its most usual forms could be administered by the "Herstelbank" or take the form of government guarantees of commercial credits. I fully appreciate these differences of financial techniques. But if one places the interests of the developing countries first, as I consciously do in this address, then in my opinion it can hardly be doubted that these countries can be best assisted either by multilateral aid of the IDA type or by donations, and preferably in the framework of a coordinated program.

About the third agency in the World Bank group, IFC, I shall speak only briefly. IFC was formed in 1956 with an authorized capital of \$100 million, of which \$97 million has been subscribed and paid. Its purpose is to stimulate foreign investment in private enterprise, particularly industry, in the less developed countries. IFC endeavours to achieve this by helping to mobilize domestic and foreign private capital for industrial enterprises, its own contribution, whether in the form of a loan or of an equity participation, being merely intended to serve as a catalyst. The importance of IFC must, therefore, be measured less by its own participation than by the amount of capital, and particularly foreign capital, it is able to interest in the projects in question and induce to be invested in them. The average size of IFC investments is no more than \$1.25 million, with a limit in practice of \$3 - 4 million. During the first five years of its existence IFC itself invested almost \$45 million but the investments stimulated by IFC total several times that figure. The terms of IFC investments are fixed more or less in accordance with the conditions prevailing on the private capital market, among other reasons because IFC must sooner or later be able to sell its participations in enterprises it finances to enable it to revolve its funds and avoid their depletion.

IFC was not initially an unqualified success, due to a lack of flexibility in its policy and the difficulty of taking from its headquarters in Washington responsible decisions about investment in such a wide and diversified field as industry. Under the new management that took over a year ago, there has been a change in policy and the emphasis of IFC activities has shifted to promoting the establishment and expansion, with IFC participation, of local development banks for the financing of industry in the less developed countries and the mobilizing of capital for that purpose. This new orientation of the operations of IFC opens up significant possibilities and in my opinion is to be welcomed. IFC has not yet reached the stage of requiring to replenish its capital but the need for this will certainly arise in due course.

In the 15 years since the Bank was set up, the World Bank group of financing agencies has built up a unique structure and a vast fund of experience in the field of economic development aid. Use is increasingly being made of this organization to furnish technical assistance for the study and solution of development problems in the member countries.

The experience of the World Bank group has clearly confirmed that shortage of capital is not the only, and indeed in many cases not the principal obstacle to

acceleration of the economic growth of the less developed countries. Inexperience and lack of trained manpower at every level are no less serious limiting factors. I do not agree with the view put forward by Tinbergen in his latest book "Shaping the World Economy" that this is only a short-term problem. In many of the less developed countries the human factor will continue for a long time ahead to be a retarding factor in economic progress, so long as there is no fundamental change, favorable to a free human development, in the intellectual, social and political climate in those countries. And about this I am rather less optimistic. This does not, however, give grounds for scepticism about the value of technical assistance; on the contrary, it is perfectly consistent with this view to regard this assistance as indispensable, particularly when it takes the form of education and training, which can contribute to the overcoming of more fundamental obstacles.

Ever since the Bank entered the field of development lending, it has provided technical assistance for the preparation and carrying out of the projects it has financed. Its activities in this field have rapidly expanded, however, to include the broader field of development planning, i.e. the drawing up of projects for a harmonious growth of less developed economies. The Bank has already, through broadly composed missions of experts, carried out complete economic surveys of 22 countries, designed to ascertain their development potentialities, to draw up programs and indicate priorities for individual projects and to work out financing programs in which local and foreign costs and resources are projected as realistically as possible for the period covered by the program. The Bank has also carried out, and continues to carry out, detailed studies of particular sectors, its reports on which serve as a basis for policy decisions by the governments concerned. The Bank is further repeatedly called upon to advise on organizational reforms of great interest for the solution of development problems, such as the setting up and organization of national planning agencies, the most efficient form of organization of public and mixed enterprises, and on national investment banks and capital market problems. In the entire field of technical assistance, the Bank works in close cooperation with other specialized agencies of the United Nations and with United States and Inter-American organizations that engage in similar or related activities.

Finally, the Bank operates a staff college for senior officials of less developed countries and training courses for junior officials, of which wide use is made. The recent decision of the Board of Governors to earmark \$10 million a year out of the Bank's earnings for the improvement of technical education in those less developed countries where this need is most urgent deserves special mentioning.

The Bank is also giving increasing attention to the better coordination of multilateral aid. Within the World Bank itself this coordination is assured by the fact that the Bank, IDA and IFC have the same President and the same Board of Executive Directors. The World Bank is invited to act as Executing Agency for projects of the United Nations Special Fund, which specializes in the financing of technical assistance and the preparation of investment projects, and the President of the Bank sits on the Consultative Board that assists in the administration of that Fund. The World Bank group of financing agencies maintains day-to-day contact at both top and lower levels with United States and Inter-American economic aid agencies, thereby securing a high degree of cooperation and coordination. Liaison is unfortunately less close with the operations of the Colombo Plan for South and Southeast Asia and with the European organizations, the European Investment Bank and the European Development Fund, due to the regional thinking that prevails in those organizations and that is partly, in my opinion, a legacy of the colonial era.

The World Bank has achieved a certain success in its efforts in recent years to bring about some degree of coordination of the economic aid provided to individual

development countries, for which purpose the Bank has drawn up or appraised development programs by setting up consortia or consultative groups, through which it endeavours to mobilize or coordinate bilateral and multilateral aid in order to promote efficient use of the funds made available by various sources to finance the programs. These coordinative efforts are important from the points of view not only of making a rational choice of projects to be financed but also of finding forms and conditions of aid, adapted to the needs of the developing countries and the obligations they are able safely to assume. I think that the first of these aims, a rational selection of projects, is in practice more likely to be achieved than the second, the adaptation of the forms of aid to needs and credit capacity, but that is after all inherent in a mixture of multilateral and bilateral aid in the forms in which they are at present mainly available. I shall not expand on this subject but would like to express my satisfaction that the Netherlands Government, which has decided, for reasons I can understand, to participate in bilateral aid, not only supports the World Bank's efforts to coordinate development aid as much as possible, but has decided to make its own bilateral aid available only in close association with the Bank, except in regard to aid within the Netherlands Commonwealth.

In a quite separate field, the Bank is considering whether it might be able to make a useful contribution to the solution of an important aspect of the development problem, namely the improvement of the investment climate for foreign private investors who might be prepared to invest in the less developed countries on a greater scale if the special risks that this entails could be reduced or covered by a system of insurances. This is a psychologically and politically delicate matter that many of the less developed countries view with suspicion, an attitude that seems to me also to be, at least in part, a legacy of the colonial era. On the other hand, the importance attached by private capital to legal security is perfectly understandable. Having regard to the composition of its membership, this is a field in which the Bank can only operate with the utmost caution and objectivity. Yet the Bank is probably more suitable as an agency for this purpose than any other international organization, because its interest in the flow of private investment capital to the less developed countries is completely impartial and because it enjoys a high degree of trust among both its capital-exporting and its capital-importing members. The Bank has always, and in my opinion rightly, stood aloof from attempts to set up a code of good behaviour for the capital-importing countries, not because its directors have no faith in principles of law and justice but because these principles should be worked out collectively and the present state of legal thinking in large parts of the world does not permit such development.

In two other fields, however, the Bank is positively active: firstly, in efforts to improve existing procedures for the settlement of disputes between governments and private foreign investors, particularly by promoting methods of conciliation and arbitration, and secondly, in the search for solutions of a multilateral nature to the problem of insuring against certain special risks connected with foreign investment. The Bank is also in touch with other organizations and agencies engaged on these problems. It is still too early to predict the outcome of these efforts, but if they should lead to positive results it would greatly surprise me if the Bank, in view of the confidence it enjoys, were not to play an important role in their achievement.

In conclusion, I should like to say a few words about the relative significance of the operations of the World Bank group in the field of development aid as a whole. If the contributions of the Bank and IDA are measured purely quantitatively, which is usual in statistical publications, they may at first glance appear to represent a relatively modest proportion of the total flow of capital from all sources to the public sector of the development countries. According to the latest available data,

the total gross amount of aid in 1961 was \$8.5 billion, of which about \$4.5 billion was in loans serviceable in foreign currencies and therefore bearing on the balance of payments, and about \$4 billion in the form of donations or of loans whose servicing does not require any transfers of exchange. The latter category includes, for example, loans repayable in local currencies and aid in the form of surplus agricultural commodities, such as is granted on a large scale by the United States.

However, only part of this \$4 billion may be regarded as investment capital for development projects: a substantial proportion is in the form of aid to meet current consumption needs, such as foodstuffs and raw materials for current production. It may reasonably be assumed that less than half constitutes capital aid in the true sense. If we add \$1.5 billion of the second figure of \$4 billion to the first figure of \$4.5 billion, which probably was intended for investment purposes, we obtain a gross total of real capital transfers of about \$6 billion. After deduction from this of \$2.5 billion needed for service of interest and amortization of loans already outstanding, a total net amount of \$3.5 billion remains as transfers of capital available for development investment. The net contribution to this by the World Bank, amounting to about \$800 million, thus represented nearly 25%. IDA's share of real capital transfers not involving exchange obligations, totalling about \$1.5 billion, was probably 10 - 15%.

Qualitatively, however, the relative contributions of both the Bank and IDA are seen to be much higher. A substantial part of the total net capital transfers of \$3.5 billion consisted of relatively short-term credits by suppliers, whereas all Bank and IDA loans and credits are at long term. Moreover, the part of this \$3.5 billion that came from sources other than the Bank and IDA was practically all in the form of bilateral and therefore tied aid, while that of the Bank and IDA (the latter on even more favorable terms) does not have to be spent in any particular country and is correspondingly more valuable.

I should prefer not to go into other qualitative comparisons between Bank/IDA aid and aid from other sources, but the whole of my preceding argument will have made clear to you my conviction that the development aid provided by the World Bank group is in many respects of the highest standard, is carefully adapted to the needs and credit capacities of the receiving countries and represents a very valuable contribution to the solution of the development problem, a task to which this and succeeding generations will be increasingly called upon to devote their utmost efforts.

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No. 51, March 1966

EXTERNAL DEBT AND DEBT-BEARING
CAPACITY OF DEVELOPING
COUNTRIES

PIETER LIEFTINCK



INTERNATIONAL FINANCE SECTION

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This is the fifty-first in the series ESSAYS IN INTERNATIONAL FINANCE published from time to time by the International Finance Section of the Department of Economics in Princeton University.

The author, Pieter Lieftinck, was Professor of Economics at Rotterdam in the prewar period and Finance Minister of the Netherlands in the immediate postwar period, which post he held for seven years. He is now Executive Director for the Netherlands, Yugoslavia, Israel, and Cyprus of both the International Bank for Reconstruction and Development and the International Monetary Fund. This is his second contribution to this series of ESSAYS. The conclusions represent the personal opinions of the author and do not necessarily reflect the views of any government or organization, official or unofficial, with which he is affiliated.

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FRITZ MACHLUP, *Director*
International Finance Section

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INTERNATIONAL FINANCE SECTION

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EXTERNAL DEBT AND DEBT-BEARING CAPACITY OF DEVELOPING COUNTRIES

NEVER before has the problem of accelerating the economic growth of less developed countries been of such fundamental importance, both politically and economically, as today. Not without reason have the 1960's been proclaimed the "development decade." The present generation is becoming increasingly aware that the world is confronted by (1) a widening gulf between the average standards of living of two groups of countries, the industrialized countries and those still predominantly in a primitive state of economic development; (2) a growing disparity between the poverty of the countries belonging to the second group and their greater political influence on world events; and (3) the need for the countries in the first group to take better account of the special demands that are placed on sound financing of the economic-growth process in the developing countries and on increasing their creditworthiness. This paper deals with the third of these points.

FOREIGN-CAPITAL REQUIREMENTS OF DEVELOPING COUNTRIES

Acceleration of the process of economic growth and diversification of production in the developing countries is predicated among other things on increased internal capital formation and/or an increasing, or at least continued net capital inflow from the industrialized countries. In most of the developing countries the possibilities of internal capital formation are restricted by low productivity and by growing consumer demand, in both the private and the public sector, due to the rapid increase in population. Moreover, in order to accelerate their economic growth, most of them urgently need imports of capital goods, raw materials that are not available locally, technical know-how, etc., which for the time being they are not in a position to finance by stepping up their exports. The chief reasons for this are the following:

1. Balanced growth calls for substantial investments in what is known as the infrastructure—roads, ports, means of transportation, electric and other power, water supply and flood control, education, etc.—all of which are prerequisites for further expansion and usually

require considerable amounts of foreign exchange, while they do not in themselves contribute towards increasing export revenue.

2. Generally speaking, growing investments in a developing economy result in increased demand for imported raw materials, mechanical equipment, and replacement parts.

3. Acceleration of investment activity in developing countries generates incomes that tend largely to be spent on the purchase of imported goods.

4. Investment projects which may assist in raising the export capacity of developing countries frequently require a considerable period for execution and start-up and usually set these countries the difficult task of attaining a level of efficiency that will enable them to compete in world markets.

5. The traditional exports of many developing countries, consisting of agricultural produce and raw materials, afford little opportunity for raising their export earnings rapidly; changes in the production structure with a view to greater diversification call for entrepreneurial initiative and investment capital which are scarce, and the process is usually time-consuming.

6. An important factor limiting the rapid expansion of export earnings in the less developed countries is the slow rate at which demand for the traditional imports from these countries increases in the developed countries.

7. A further limiting factor is the willingness of the developed countries to increase their imports from the less developed countries, in view of their reluctance to open their markets any wider for such imports and to adapt themselves to a rational, international distribution of labor based on the comparative-cost principle.

If the increase in exports, or the substitution of imports by domestic production in the developing countries could keep pace with the rise in their external spending, which is both directly and indirectly connected with more satisfactory economic growth and with the investments that growth requires, no net capital import would be required (even though in that case no margin would be left for building up the desired foreign-exchange reserves). Analysis and experience, however, go to show that in general this is not possible. In most cases, the capacity to step up domestic production and reorient the economic structure, which is essential if the import-export ratio is to be changed to such

an extent that capital imports become superfluous or can be substantially reduced, is, in the shorter term, very restricted, while the attainment of a reasonable measure of economic growth by self-financing is a protracted business. Countries rich in raw materials that can readily be exploited and exported, such as petroleum, and with a relatively small population in relation to the wealth of their natural resources, therefore enjoy a favorable position. In most of the developing countries, however, this is not the case and the only alternative is: substantial capital imports, extending over many years—or economic stagnation.

TRADE DEFICITS OF DEVELOPING COUNTRIES: EXTERNAL FINANCING

A recent study (Loan terms, debt burden and development, Agency for International Development, Department of State, April 1965) showed that in the seven-year period from 1956 to 1963 the deficits on the goods-and-services accounts of all less developed countries combined rose from \$5 to \$7.9 billion a year. This was accompanied by an average annual increase of 4.4 per cent in the total gross national product of those countries. The table which follows presents the comparative figures for 1956 and 1963, from which these results are derived, together with a summary of the funds applied to covering the current-account deficits.

TABLE I
GROWTH, CURRENT-ACCOUNT DEFICIT AND FINANCING OF ALL
DEVELOPING COUNTRIES—1956-1963
(in billions of dollars)

	1956	1963
Gross national product	148.0	200.0
Imports of goods and services (excl. from developing countries)	28.1	39.7
Exports of goods and services (excl. to developing countries)	23.1	31.8
Balance on current account	5.0	7.9
Loans payable in convertible currency, gross	1.8	5.4
Interest and amortization	0.8	2.9
Loans payable in convertible currency, net	1.0	2.5
Other sources (grants, "loans" to be repaid in the currency of the recipient country, direct private investments etc.)	4.0	5.4
Total financial resources	5.0	7.9

The most interesting conclusions regarding financing that can be drawn from the above figures are that in the space of those seven years (a) there has been a considerable increase in the amount of loan funds used to cover the current-account deficits of the developing countries and a corresponding decrease in the contribution from other sources; (b) the contribution from net loans has risen from one-fifth to more than one-third; and (c) gross loans have risen by 200 per cent, interest and amortization by 263 per cent, and net loans by 150 per cent.

The 1963 figures for financial resources received by the developing countries, which were used in the above study, are to a large extent borne out by another recent study (The flow of financial resources to less-developed countries, 1956-63, Organization for Economic Cooperation and Development, Paris, 1964), which was based on the financial resources made available by the industrial countries. The latter study concludes that of the net transfers from the developed to the less developed countries in 1963, more than one-third were in the form of loans repayable in the currencies of the creditor countries. Somewhat less than half were in the form of grants and transfers repayable in the currencies of the debtor countries. The remainder (approximately one-fifth) were accounted for by direct private investments. The total amount of the transfers analyzed in this (OECD) study is, however, higher, namely not \$7.9 but approximately \$9 billion, owing to the inclusion by the lending countries of approximately \$1 billion in the form of technical assistance.

Growth of External Debt

A study recently published by the World Bank (Economic growth and external debt, Dragoslav Avramovic and Associates, IBRD, 1964), shows that the external debt of all developing countries, comprising public indebtedness and government-guaranteed private debt, but excluding loans to be repaid in the currencies of the recipient country, repayment obligations to the International Monetary Fund, and debts with maturities of less than one year, rose from \$8 billion in 1956 to \$22.5 billion by the end of 1962. This corresponds to an average annual growth of somewhat more than 15 per cent (compared with an average annual growth of 4.4 per cent in the gross national product). If the payment obligations to the IMF, private debt not guaranteed by the government, outstanding commercial debts, and other similar obligations (excluding debts with maturities of less than one year) are included, then the figure for the end of 1962 must be increased by an estimated \$5 billion to \$27.5 billion.

The geographical distribution of the debt burden of all developing countries combined at the end of 1962 is shown in the following table.

TABLE II
EXTERNAL DEBT OF ALL DEVELOPING COUNTRIES AT END OF 1962
(in billions of dollars)

	Public debt according to narrow World Bank definition	Other	Total
Latin America	8.9	2.5 ^a	11.4
South Asia and Middle East	6.7	0.5	7.2
East Asia	1.0	1.7 ^b	2.7
Africa	3.5	0.1	3.6
Southern Europe	2.4	0.2	2.6
	22.5	5.0	27.5

^a owed principally by Brazil and Argentina.

^b for the most part a rough estimate for Indonesia.

According to the latest available figures, the external debt of the developing countries rose in 1963 and 1964 by 17 per cent in each case (whereas the growth in the GNP declined to 4 per cent per annum) and stood at the end of 1964, according to the narrow definition, at an estimated \$33 billion and, according to the broader definition, at more than \$38 billion. Expressed as a percentage of the GNP, external debt rose, according to the narrow definition, from 5.9 per cent in 1956 to 11.3 per cent at the end of 1962, and to 15.3 per cent at the end of 1964. According to the broader definition, the last two figures had risen to 13.8 per cent and 17.8 per cent.

TABLE III
GROWTH OF EXTERNAL PUBLIC DEBT OF 37 DEVELOPING COUNTRIES
FROM THE END OF 1956 TO THE END OF 1964
(in billions of dollars)

	1956	1958	1960	1962	1964
Latin America	4.3	5.7	6.6	8.9	10.6
South Asia and Middle East	1.4	2.5	3.3	5.1	8.6
East Asia	0.3	0.6	0.7	0.8	1.1
Africa	0.9	1.0	1.2	1.4	1.9
Southern Europe	1.1	1.3	1.5	2.0	2.6
	8.0	11.1	13.3	18.2	24.8

Source: 1965 Annual Report, International Monetary Fund.

The data on external debt collected by the World Bank made it possible to compile a survey of the annual growth in the external debt of 37 developing countries, according to the narrow definition, between the end of 1956 and the end of 1964 (the preceding figures related to 74 countries). Between them, these countries represent 73 per cent of the total population of the developing countries. The foregoing is summarized in the following table, which is also drawn up on a geographical basis.

A large proportion of the "other" debt (cf. Table II), which in the meantime has also risen, is accounted for by these 37 countries and about half of it was contracted by the Latin American countries. It would not be unreasonable to estimate the total external debt (public and "other") of the 37 developing countries at the end of 1964 at between \$28 and \$29 billion.

Servicing External Debt

Table I has already indicated the combined amounts in respect of the service of interest and amortization that the balance of payments of all developing countries had to bear in 1956 and 1963, namely \$0.8 and \$2.9 (0.7 interest and 2.2 amortization) billion, respectively. Expressed as a percentage of the exports (of goods and services) of those countries, the servicing of their public external debt in 1963 amounted to 9.1 per cent of their export revenue, as against 3.7 per cent in 1956. The 1964 figure was probably 10 or 11 per cent. If the service of "other" debt (estimated at \$1.5 billion) is also taken into account, an even higher percentage results.

The table below presents data on the external-public-debt service of the 37 developing countries covered by Table III.

TABLE IV
GROWTH IN EXTERNAL-PUBLIC-DEBT SERVICE OF 37 DEVELOPING
COUNTRIES—1956-1964
(in millions of dollars)

	1956	1958	1960	1962	1964
Latin America	455	779	1,049	1,280	1,442
South Asia and Middle East	95	186	284	378	485
East Asia	22	26	56	62	99
Africa	37	49	63	104	131
Southern Europe	71	60	253	174	341
	680	1,100	1,705	1,998	2,498

Source: 1965 *Annual Report*, International Monetary Fund.

If these public-debt-service figures are expressed as percentages of the exports of the different geographical groupings of countries, the following result is obtained. In Latin America this percentage rose from 6 per cent in 1956 to 15 per cent in 1964; in South Asia and the Middle East from 4 per cent in 1956 to 13 per cent in 1964; in East Asia from 1 per cent in 1956 to 3 per cent in 1964; in Africa from 3 per cent in 1956 to 9 per cent in 1964; and in Southern Europe from 7 per cent in 1956 to 15 per cent in 1964. For all 37 countries together, the percentage rose from 4 per cent in 1956 to 12 per cent in 1964. It must again be pointed out that this still takes no account of the service on the short-term "other" debt (estimated for these 37 countries at \$1 billion).

Structure of External Debt

The external-debt figures of the developing countries, stated above, relate to the loans obtained by these countries. This does not necessarily mean that the funds were transferred in the same year in which the loans were recorded, or that payment of interest and amortization has begun on those loans. Of the external public debt of 37 countries recorded by the World Bank, which amounted to approximately \$21 billion at the end of 1963, more than 1/5 was still unused on that date. The amount paid in 1964 in interest and amortization, namely somewhat more than \$2.4 billion, must therefore be referred to a transferred debt of \$16.5 to \$17 billion. Since the ratio between interest and amortization was approximately 1:3, which corresponds to more than \$600 million in interest and \$1800 million in amortization, it can be deduced that the average weighted rate of interest was in the region of 3.6 per cent and the average amortization period a little over 9 years. If the obligations arising out of "other" debts, whose maturities can be estimated at an average of 2 to 3 years, are included, the percentage of interest becomes somewhat higher and the average amortization period must be considerably shortened.

The table below gives an idea of the percentages of the external public debt of the 37 countries at the end of 1962, which had to be repaid in the 3-year period 1963-1965 and in the 5-year period 1963-1967, respectively.

Since virtually all the "other" debt matured within 3 years, the percentages indicated would have been considerably higher if this "other" debt had been included in the calculations. In the case of Latin America, it would have meant that 50 per cent of the total external debt (longer than 1 year) had to be repaid within three years and 65 per cent within five years.

TABLE V
PERCENTAGES OF EXTERNAL PUBLIC DEBT AT END OF 1962
MATURING IN 1963-65 AND IN 1963-67
(37 countries)

	3 years	5 years
Latin America	36	55
South Asia and Middle East	19	32
East Asia	31	52
Africa	13	50
Southern Europe	41	65

Source: *Economic Growth and External Debt*, Dragoslav Avramovic and Associates, IBRD, 1964

The conclusion to be drawn from these data is that far and away the greatest proportion of the external-debt service of the developing countries consists of amortization obligations maturing at relatively short term. This is in marked contrast to the traditional structure of external government debt, as it existed in the prewar years, when external government loans were commonly floated on the international bond markets in the form of long-term securities. Furthermore, the rate of interest was substantially higher, because the risk was borne by private individuals. Nowadays, the external debt of the developing countries is a combination of long-term, usually low-interest, inter-governmental loans, long and medium-term credits furnished by international institutions at widely divergent interest rates, government-guaranteed medium and short-term private credits, and other short-term debt. This debt structure with its associated payment obligations is little suited to the great and continued need of most of the developing countries for net long-term capital imports. If debt continues to rise further within the present structure, interest payments will become an increasingly heavy burden; even now many countries are faced with the problem of heavy amortization obligations at short term.

Debt and Debt-Service Projections to 1970 and 1975

The Agency for International Development has made a number of informative projections regarding the future financing requirements, the increase in the external debt, and the resulting interest and amortization obligations of the developing countries, by extrapolating their record of growth during the seven-year period 1956-63 (GNP plus 4.4 per cent, imports plus 4.4 per cent, and exports plus 3.8 per cent per annum), on the assumption that the amount of net loans would be

maintained at the 1963 level (cf. Table I). These projections were prepared on the basis of three alternative types of loan terms: (a) terms in line with the average conditions applicable in 1963 to all bilateral public loans made by OECD countries (amortization over 20 years, including a 7-year period of grace, and an average rate of interest of 3.5 per cent); (b) softer terms in line with those which were regarded as standard conditions in 1963 for loans furnished by the members of the India Consortium (amortization over 30 years, including a 7-year grace period, and an average interest rate of 3 per cent); and (c) harder terms, which in 1963 were regarded as standard for loans by OECD countries, excluding the United States (amortization over 16 years, including a 3-year grace period, and an average interest rate of 4.8 per cent). The results of these projections are reproduced in Table VI.

Although the assumptions underlying these projections are hypothetical, important conclusions can be drawn from them.

1. Even if the modest record of growth in their gross national product by 4.4 per cent is maintained (in point of fact this growth rate was only 4 per cent in 1963 and 1964), the current-account deficit of the developing countries will have risen by 87 per cent in 1975, unless there is an improvement in their import-export ratio.
2. If the amount of net loans is maintained at the 1963 level, "other" sources will have to play a proportionately greater part than loans in covering the deficit (in contrast to the historical trend).
3. To keep net loans at the same level, gross loans will have to increase at a rate dependent upon the average loan terms; in the case of type-1 terms by 43 per cent in 1970 and 72 per cent in 1975, in the case of type-3 terms by 88 per cent in 1970 and 150 per cent in 1975.
4. If net loans are maintained at the 1963 level, the cumulative loan debt will rise from \$22.5 billion in 1963 to more than \$60 billion in 1970 and to some \$80 to \$90 billion in 1975, depending on the terms on which loans are made available.
5. Under the conditions assumed under (4), the servicing of interest and amortization will impose increasingly heavy demands, not only in absolute terms, but also when expressed as percentages of exports; if type-3 loan terms are applicable, this debt service will claim \$7.3 billion in 1970 and no less than \$11 billion in 1975, corresponding to 17.8 per cent and 22 per cent, respectively, of assumed exports. Assuming the third type of loan conditions is applicable, of the gross loans of \$9.8 billion in 1970 and \$13.5 billion in 1975, some 75 per

cent would be repatriated to the creditor countries in the form of interest and amortization in 1970 and about 80 per cent in 1975. This may well be an overestimate, because there is always a time lag in the use of loans obtained, but still no allowance has been made for the servicing of "other" short-term indebtedness.

TABLE VI

PROJECTION OF GROWTH, CURRENT-ACCOUNT DEFICIT AND FINANCING, FOR ALL DEVELOPING COUNTRIES

(in billions of dollars)

	1963	1970	1975
Gross national product	200	268.2	333.4
Imports of goods and services (excl. from developing countries)	39.7	52.2	64.8
Exports of goods and services (excl. to developing countries)	31.8	41.0	50.0
Deficit on current account	7.9	11.2	14.8
Loans payable in convertible currency, gross	5.4 type 1	7.7	9.3
	type 2	7.1	8.2
	type 3	9.8	13.5
Interest and amortization	2.9 type 1	5.2	6.8
	type 2	4.6	5.7
	type 3	7.3	11.0
Loans payable in convertible currency, net	2.5	2.5	2.5
Other sources (grants, "loans" to be repaid in the currency of the recipient country, direct private investments)	5.4	8.7	12.3
Total financial resources	7.9	11.2	14.8
Cumulative loan debt	22.5 type 1	61.4	86.8
	type 2	60.4	83.9
	type 3	63.5	93.1
Loan debt as percentage of GNP	11.3 type 1	22.9	26.0
	type 2	22.5	25.2
	type 3	23.7	27.9
Loan service as percentage of exports of goods and services	9.1 type 1	12.7	13.6
	type 2	11.2	11.4
	type 3	17.8	22.0

If the projected debt-service figures are broken down into interest and amortization for the various types of loan terms, the following picture is obtained.

TABLE VII

PROJECTIONS OF INTEREST AND AMORTIZATION, ALL DEVELOPING COUNTRIES
(in billions of dollars)

	1963	1970	1975
Interest and amortization	2.9 type 1	5.2	6.8
	type 2	4.6	5.7
	type 3	7.3	11.0
Interest	0.7 type 1	1.9	2.5
	type 2	1.6	2.1
	type 3	2.4	3.6
Amortization	2.2 type 1	3.3	4.3
	type 2	3.0	3.6
	type 3	4.9	7.4

It is evident from this breakdown that for each of the alternative loan terms the ratio of interest to amortization tends to become 1:2 or 1 to less than 2 (compared with 1:3 in 1963). In the case of the projections based on the type-3 loan terms, it is the relatively high rate of interest that influences the ratio between interest and amortization.

Further Note on Structure of External Debt

The conditions on which public loans are actually made available to the developing countries today are not confined to the three types mentioned above, but show a wide range of variation. Quite apart from the government-guaranteed private credits (predominantly medium-term supplier credits with a term of 5 to 10 years and an interest rate of 6 per cent and more), the soft end of this range includes the development credits of the International Development Association (IDA), an affiliate of the World Bank, the standard terms of which are: term 50 years, including a 10-year grace period, and a nominal interest rate of 0.75 per cent. Loans under the American bilateral AID program fall into two categories, the softer type with a term of 40 years, including a 10-year grace period, and an interest rate of 2.5 per cent (1 per cent during the grace period), and the harder type with a term of 20 years, including a 3-year grace period, and an interest rate of 3.5 per cent. The average terms of all bilateral public loans by the OECD countries

(including the United States), already indicated (term 24 years, including a 7-year grace period, and an average interest rate of 3.5 per cent), lie somewhere between these two types. Next come the average terms of the World Bank loans, namely term 20 years, including a 3-year grace period and an interest rate of $5\frac{1}{2}$ per cent, followed by the average conditions of the bilateral loans by OECD countries (excluding the United States): term 16 years, including a 3-year grace period and an interest rate of 4.8 per cent. Finally, at the hard end of the range, come the usual terms of the (U.S.) Export-Import Bank, namely term 13 years, including 3 years of grace, and an interest rate of $5\frac{1}{2}$ per cent.

The AID study referred to earlier attempted to predict how the relationship between gross and net loan receipts would evolve for the various types of loan terms distinguished in the preceding paragraph. These projections, reproduced in Table VI, cast some light on possible future trends. The results of the calculations reveal that in order to maintain net receipts at a level of \$1 billion per year, the amount of gross lending must rise in the fifteenth year:

— on IDA terms	to \$1.2 billion
— on soft AID terms	to \$1.4 billion
— on OECD (including U.S.) terms	to \$2.5 billion
— on hard AID terms	to \$2.7 billion
— on World Bank terms	to \$3.2 billion
— on OECD (excluding U.S.) terms	to \$3.4 billion
— on Eximbank terms	to \$4.3 billion

Conversely, it is evident that if the level of gross loans is maintained at an amount of \$1 billion per year, net loan receipts must decline. By as early as the fifteenth year, the net remainder on loans furnished on OECD (including U.S.) terms will be very low indeed, while in the case of loans made on less favorable terms the servicing cost will actually exceed the gross receipts from the loans, resulting in a negative balance. The net transfers to the recipient countries will then be:

— on IDA terms	\$0.83 billion
— on soft AID terms	\$0.65 billion
— on OECD (including U.S.) terms	\$0.08 billion
— on hard AID terms	— \$0.06 billion
— on World Bank terms	— \$0.28 billion
— on OECD (excluding U.S.) terms	— \$0.40 billion
— on Eximbank terms	— \$0.48 billion

The conclusions that can be drawn from these calculations are as follows:

a. The harder the loan terms, the greater the amounts of gross loans that must be furnished from year to year in order to maintain a given net capital transfer, the more difficult it becomes to continue to find new sound loan projects (assuming that this sort of loan is tied to a specific project) and the earlier solvency is jeopardized owing to the increase in total debt and debt service.

b. The harder the loan terms, the smaller the net loan receipts become at a constant level of gross capital transfer from year to year, and the earlier the lending process loses its effectiveness, because, instead of reducing an existing financing deficit, it quite rapidly becomes a net burden on the balance of payments (in the case of loans on Eximbank terms, this begins as early as the ninth year, for loans on average OECD—excluding U.S.—terms in the eleventh year and for loans on average World Bank terms in the twelfth year).

EXTERNAL-DEBT PROBLEMS OF DEVELOPING COUNTRIES

The size and structure of the external debt of the developing countries and the associated payment obligations vary from one country to another. The indebtedness of some of them has, however, already reached or approached a dangerous level.

Keeping Debt Service within Limits

The servicing of interest and amortization is already claiming a substantial proportion of the foreign capital flowing into those countries, because that capital is being supplied to an increasing extent in the form of loans repayable in the currencies of the creditor countries, instead of in the form of grants-in-aid and such like. In the past few years, direct investments have accounted for only 4 to 5 per cent of the total capital receipts of the developing countries. Dividend payments to foreign countries in respect of capital invested in the past, on the other hand, constituted a heavy burden. According to data from the World Bank, interest and amortization on loans and dividend transfers from the developing countries have claimed no less than \$6 billion per year over the last few years, which is more than half of the gross capital transfers to these countries from all sources combined. In the light of their existing payment obligations and the fact that those obligations are expected to increase still further as periods of grace expire and fresh loans are raised, there is danger of a situation arising in which the inadequacy of net financial assistance will lead to lack of continuity in the economic growth of many developing countries. Thus, far from being speeded up,

their growth will rather tend to slacken off. Symptoms of this phenomenon can already be seen in a number of countries.

At the present moment, the gross national product of all developed countries combined amounts to an estimated \$1,000 billion and is rising at the rate of approximately \$40 billion a year, that is by 4 per cent (equal to the increase in the GNP of the developing countries over the last 2 years). In terms of this figure of \$40 billion, the gross and the net capital transfers to the developing countries of about \$12 and \$6 billion, respectively, already account for 30 per cent and 15 per cent, respectively, of the present annual growth in the GNP of the developed countries. There is little reason to suppose that these percentages will increase much in the future. Of the gross capital transfers of \$12 billion, \$5.4 billion, that is 45 per cent, was in the form of loans. Now let us assume that this percentage remains the same (in contrast to the historical trend, which shows a powerful increase), and let us further assume that in the coming years the amount of gross loans furnished will rise in proportion to the anticipated growth in the GNP of the developed countries, that is by 4 per cent per annum, or at twice that rate, that is by 8 per cent per year, allowing for the possibility that the developed countries will be prepared to relend for development purposes a large proportion of the amortizations which they receive. Even in the latter case, average loan terms closer to those of the soft AID type than to the OECD (including U.S.) type will be required to maintain the annual amount of net loans at its present level of approximately \$2.5 billion. The harder the loan terms are, the greater the need for fresh financing becomes in each succeeding year.

The burden of external-debt service does not owe its significance merely to the fact that the developing countries have to find the funds with which to meet their payment obligations or that the developed countries have to provide the funds required for continued financing. It is also connected with the degree to which the developed countries are prepared to continue their financing of developing countries in the light of the existing indebtedness of their borrowers and the margin those borrowers still have for contracting additional debt. An important consideration when providing new loans is the schedule of the combined interest and amortization obligations of the borrowing country during the period in which new loans have to be repaid. In many cases, the next few years are already heavily burdened by the service of "other" debts and/or medium-term supplier credits (commonly guaranteed by the government) and it is only after 5 to 7 years that any significant margin is found. The further the repayment obligations are extended into the

future and the lower the interest rate, the greater that margin becomes—and the better the chances that the economic development of the debtor countries will in the meantime have enhanced their debt-bearing capacity.

As far as the economic growth of developing countries is concerned, an increase in their external indebtedness cannot be regarded as a wholly adverse factor. Normally speaking, it means that foreign capital is being brought in to supplement the investment resources available in those countries and is thereby helping to enlarge and accelerate the capital formation required for development. The influx of foreign capital therefore has the effect of strengthening the economy of the borrowing countries. This advantage is offset by the disadvantage of growing external-payment obligations, and the degree to which the developing countries increase their capacity to pay interest and amortization depends on the effect which foreign capital has on their economic growth.

The utilization of foreign capital and its productivity in terms of increasing the national revenue and raising the level of savings and investments are of strategic importance in this connection. Account must also be taken of the fact that the capacity to absorb into the growth process additional capital that becomes available varies from one developing country to another. Finally, it is important to remember that interest on and repayments of external debt have to be remitted, and that it is therefore not simply a question of ensuring that a large enough revenue surplus is created to pay interest and redemption, but also that a wide enough margin is created in the balance of payments on current account, by stepping up exports or by import substitution, to make the transfers required.

Utilizing Foreign Capital Efficiently

Since the purpose of foreign capital imports into developing countries is to help speed up the process of economic growth by raising the level of investment, the rate at which useful investments can be made is of crucial importance. In almost every country there are limits beyond which, in any given period of, say, five years, investment activity on worth-while projects cannot be stepped up, without resulting in the waste of any additional capital used because of a rapid decline in marginal productivity.

In the investment process three phases can be distinguished. In the first phase, the possibilities of development are investigated, certain programs and projects are formulated, their technical feasibility is studied, and their economic and financial value assessed. One of the

cardinal objectives in preparing national-development plans ought to be to work out an efficient procedure for identifying and preparing an increasing number of well coordinated investment projects. In practice, however, this has often been precisely what was missing. Many developing countries have made (or have had made) impressive and ambitious plans based upon econometrically tested models and a complex set of interwoven assumptions, but their feasibility content is not very high and their translation into carefully prepared projects is frequently neglected. The reasons for this are sometimes inadequate knowledge of natural conditions, which first have to be explored, often a shortage of technicians trained in project appraisal, and not infrequently a hesitant, slow-moving bureaucracy that is unaccustomed to taking radical economic and financial decisions. Political considerations, too, sometimes have a habit of intruding.

In the second phase of investment activity, programs and projects are executed, construction (which usually absorbs about two-thirds of the capital) is undertaken, and equipment is installed. The ability to implement an investment program within a given period does not depend only on its size, but also on the existence of and the possibility of mobilizing local resources, competent contractors and laborers, transport facilities, sources of water and power, and the domestic financial resources that are normally required to supplement foreign capital. Shortages of local factors of production and time spent in remedying them frequently lead to serious delays (and cost increases) during the execution phase of investment programs. The possibilities of preventing or eliminating this through foreign-aid channels are limited not only by restraints imposed at the giving end but also by resistance encountered at the receiving end.

The third phase is where the new investments begin to participate in the production process. The capacity to make full and efficient use of invested capital is a highly important aspect of a country's absorptive capacity. The quality of the management, the skill and productivity of the personnel employed, the regularity with which raw materials, auxiliaries and parts requiring replacement are procured and the finished products sold in receptive markets, all have a decisive effect on the contribution of invested capital to increasing the national product. Low productivity, defective quality, underutilization of capacity, inadequate level of replacement and renovation are frequent phenomena in developing countries, which point up the limitations of their absorptive capacity or the rapid deterioration of the capital-return ratio that sets in once a certain level of investments has been passed. One of the main

factors here is the chronic shortage of foreign currency for imported raw materials, auxiliaries and parts requiring replacement, because these requirements are either neglected or underestimated when new projects are taken in hand, or because these requirements are not given proper priority by the authorities of the developing country when they draw up their foreign-exchange appropriations. Another factor responsible for this state of affairs, however, is that many capital-exporting countries tend to tie their official financial assistance, except for that in the form of guaranties, to new investment projects, while current import requirements are for the most part financed by short-term commercial credits or medium-term supplier credits, which are subject to normal business considerations.

Generating Domestic Savings and Capital Formation

In most developing countries per capita income is low (even though individual incomes may vary widely) and the increase in population considerable. Consequently, there is a shortfall in savings and capital formation in relation to the investments required for accelerated economic growth. By raising the volume of the investments which developing countries are capable of making from their own resources, foreign capital imports make it possible to speed up the increase in incomes. The degree to which this is achieved depends on the volume of capital imported, the productivity of the capital (that is, on the capital-return ratio), and on how much of its increased income the population is prepared to save.

It is obvious that the primary issue is the volume of net capital imports—after deducting interest and amortization on loan capital, dividends and amortizations on direct investments, insofar as the latter are repatriated to the countries that provided the capital, and flight of capital (which is by no means exceptional in the case of developing countries). These net capital imports must be sufficient, in terms of both volume and term, to help bring about a continued and noticeable increase in the per capita GNP. To meet this condition successfully, they must attain a reasonable level, according to the absorptive capacity of the country in question, and be continued until the increase in incomes creates a permanent and growing margin of savings that will itself generate enough capital to support the investment process. Otherwise the growth process will be prematurely retarded and the country will be in danger of relapsing into a state of economic stagnation.

In the second place, the increase in incomes depends on the productivity of the added capital. This can be gauged by the increase in

wages and profits, including interest, depreciation, and cost-price-raising taxes, which results from a rise in investments. The better the ratio between the amount of additional capital invested and these proceeds (the gross added value), the greater the rise in incomes brought about by the imported capital. As stated earlier, the productivity of the added capital also varies with a country's absorptive capacity; the factors which influence that capacity determine to a large extent the capital-return ratio. Given a certain absorptive capacity, the choice of investment projects is of cardinal importance. Extravagant and capital-consuming new projects with long construction periods often have relatively less economically useful effect than modest investments which remove bottlenecks preventing rapid increases in the productivity of existing economic activities. In addition, the burden of the first type of projects mentioned on the external-debt service is frequently disproportionately heavy.

In the third place, decisive importance attaches to the inclination to save, that is to say the ratio in which the increase in incomes is allocated to consumption and investment. The higher the level of saving, the greater the extent to which available productive resources are exploited with a view to accumulating additional capital, and hence the greater the increase in incomes. This cumulative process, in which an initial increase in incomes can, by saving and investment, lead to a greater increase in incomes, is the pivot (and the spiral) about which the process of economic growth revolves, and, other conditions being equal, it is the percentage of the increase in incomes which is saved that indicates the rate of growth.

In many developing countries this process can only be initiated or accelerated with the aid of foreign capital. The higher the rate of growth, the easier it will be to meet external-debt obligations and at the same time reduce the investment deficit. Conversely, the greater the proportion of the rise in incomes that is absorbed by external-debt servicing, the more difficult saving becomes. In the past, however, developing countries have not infrequently spent too much of the increase in their incomes on consumption, both in the public sector and, owing to an inadequate tax system, in the private sector. Not infrequently, too, savings are invested in unproductive or in low-productivity projects. Both phenomena have the effect of curbing their rate of growth and reducing their debt-bearing capacity.

Avoiding Too Heavy External Debt

If continued for long enough, imports of foreign capital enable the

developing countries to maintain a deficit on their goods-and-services account, which is covered by a surplus on their capital account. Where the foreign capital is loan capital, it is subject to fixed interest and amortization obligations, and where it consists of direct investments, there is frequently an agreement providing for the remittance of reasonable amounts by way of dividends and amortization. Depending on the volume of imported capital and the conditions on which it is furnished, the burden of the external-payment obligations rises, as discussed earlier, and leads to a corresponding increase in the financing deficit on the balance of payments. There is, however, also a secondary effect which capital imports have on the balance of payments. Basically, investments in the developing countries are stepped up with the aid of foreign capital and the increase generates a rise in incomes. This rise in incomes, however, generally has a large foreign-exchange component, which leads to additional imports of both consumer and capital goods, especially in the early stages of development. Since it is often some time before export capacity can be strengthened enough to match growing import requirements (for which there are domestic but no external financial resources available), the current-account deficit rises accordingly. Apart from grants and similar aid, there is no other cover for this deficit but additional loans, which will normally take the form of short and medium-term credits. In this way the danger arises that in the course of the growth process stimulated by the import of foreign capital, external debt will continue to rise and at the same time acquire an unfavorable structure, until it finally reaches its upper limit, which is commonly set far too high, at which point additional credit becomes a serious problem and a balance-of-payments crisis sets in. Examples of this are not hard to find.

To head off this danger and limit the external-debt burden on the balance of payments to an extent that will enable them to continue to meet their financial-transfer obligations without having to cut back their imports drastically—which would have a detrimental effect on their growth process—the developing countries are faced with the task of bringing about a fundamental improvement in their import-export ratio as soon as their internal and external circumstances permit. The greater the financial-transfer obligations, especially in relation to the overall balance-of-payments figures, the more imperative this need becomes. As noted earlier, however, the process of growth in developing countries is inevitably accompanied by an increase in import requirements. Improvements must therefore be sought in an increase in exports, which must first catch up with the increase in imports and subsequently

surpass it. To achieve this, enough of the investment funds that become available must be applied to strengthening and broadening the export sector. Here, however, opposing forces come into play. In many developing countries a large, and not infrequently a disproportionately large, part of the capital imported and saved is invested in the infrastructure (roads, means of transport, utilities, etc.), which does not add to export capacity or does so indirectly only at a later stage. Moreover, there is a common tendency in these countries to give priority to investments aimed at supplying the domestic market more liberally. The growth in the population is partly responsible for this; expectations of prosperity have risen and there is a growing demand for means of providing more of the basic necessities of life (food, clothing, housing, education, health services, etc.). It is also easier for the business community to orient its expansion towards the domestic market, where the quality demands are lower and, thanks to widespread protection, prices are usually higher than in the international market, while additional costs are involved in winning foreign markets. As a result, the export component of the rise in production due to the increase in investments is relatively small in many developing countries and a considerable period usually elapses before the process of economic growth reaches the stage where domestic circumstances become conducive to an increase in this component. The time it takes adequately to adapt a developing nation's production structure, originally created to satisfy largely domestic needs, to the international market and to invest it with the competitive power to find the necessary sales outlets in that market, depends on a number of factors, natural, human, and administrative, which will not be developed further here. But if, sooner or later, this change in the structure of the economy takes place, it will be accompanied by a change in the structure of the balance of payments due to increased exports and to import substitution. There are many developing countries which are now in this transitional stage; some are already approaching equilibrium in their goods and services balance; the majority, however, have many years of growth ahead of them before their import-export ratio is likely to take a turn for the better.

The success of developing countries in increasing their export revenue is dependent to a large extent upon external circumstances, which for the most part are beyond their control. One way of expanding exports is to increase the supply of primary products (raw materials) or of industrial goods and of services. For most of the primary products the growth in world demand is only moderate, or, put another way, total demand is insufficient to provide the resources needed to cover rising

import requirements in the developing countries. Moreover, the prices of these products are subject to serious fluctuations. Consequently, the developing countries must also concentrate their efforts on exporting industrial goods and services (such as tourism), for which international demand shows a relatively steep upward trend. The range of industrial goods which these countries, on reaching a certain level of development, can start producing for export with any chance of success is limited, however, chiefly to the products of light industry. Some developing countries have succeeded in considerably expanding their exports of these products. Repeatedly, however, they come up against import restrictions imposed on such goods by the industrialized countries and this slows down the rate at which their export revenue can rise. For countries with strong tourist appeal the prospects of raising their revenue from the exchange of services appear promising. Though many developing countries would like to enjoy such a position, only few are favored in this way.

The capacity of developing countries substantially to lighten their external-debt burden within a relatively short space of time by creating an export surplus should certainly not be overestimated. There is a close correlation between the successive stages of economic growth in these countries and the pattern of their external-debt position. Against the background of the foregoing considerations, the broad outlines of this correlation can be presented as follows:

During the initial stage of (accelerated) economic growth, national revenue is insufficient to produce the savings required to step up investments. To enable it to finance a greater volume of investment, the young emerging nation begins to attract capital—for the sake of argument we shall assume that it does so in the form of loans. Since it has during this stage a growing need for net capital imports, it will continue to borrow up to amounts that are sufficient not only to cover part of its investments, but also to cover interest and amortization on its previous foreign loans. In this way, interest and amortization are financed by foreign countries and place no burden on domestic savings, but its external debt rises at an accelerated rate (the interest being subject to the law of compound interest). The longer this situation continues, the greater the external debt becomes. The rise in national revenue should, however, make it possible by degrees to finance a relatively greater proportion of investments from domestic savings.

In the second stage of development, domestic savings have reached a level where the country can meet its investment needs itself, but its savings are still not large enough to pay simultaneously the interest and

amortization on the external debt which it has in the meantime accumulated. It must therefore continue to raise fresh loans, even if only for the amount of its debt service. In a later phase, the country will be able, as it develops further, to take interest payments for its own account, too. At this point the increase in debt ceases and the amount of fresh loans raised may be limited to the country's amortization obligations, that is, its refinancing needs. There is no further need for net capital imports.

During the third stage, the country is in a position to use its own savings not only to finance its investments and its external-interest obligations, but also to start repaying the principal of its loans. This results in a corresponding decrease in the amount of interest payable. When the external debt has been paid off, the wheel has come full circle. How long this cycle takes to complete depends primarily on the total amount to which external debt rose during the first stage and the earlier phase of the second stage; secondly, on the extent to which and the rate at which the country is able to build up a surplus of domestic savings over investments; and thirdly, on the country's ability to earn, or convert, this surplus—which must be reflected in a surplus on its balance of payments—in the foreign currencies that it needs in order to pay its foreign creditors.

When it comes to repaying external indebtedness, there is the added complication that creditor countries require to be paid in their own currency or in a currency acceptable to them. Naturally, this also applies to payment obligations arising out of trade, but in commercial traffic there is usually a greater freedom of choice regarding the countries with which payment obligations are entered into, because to a certain degree imports (and exports) can be oriented towards certain countries. When they seek to raise loans abroad, developing countries usually have a very limited choice of lenders and once they have become debtors vis-à-vis one or more specific countries, this has the effect of adding an element of inflexibility to their transfer problem. This is intimately connected with the limited convertibility of currencies in the world today, which is likely to continue into the foreseeable future. In many cases, the element of inflexibility referred to adds yet another burden to the foregoing obligations and tasks already placed on the shoulders of the developing countries as their external indebtedness increases. For it is often easier for them to find markets for a growing supply of export goods in other countries with weak (inconvertible) currencies, than it is in the capital-providing countries. Frequently, too, they conclude bilateral-trade agreements with certain countries, because this bolsters their exports, although such countries are seldom their creditors. This

means that the developing countries do not simply have to step up their exports, but that they must expand their exports to the industrialized countries with convertible currencies, that is, to those markets in which it is most difficult for them to compete and in which they often meet with considerable resistance to imports.

Actions of Developing Countries to Increase Creditworthiness

Here, as in the following (and final) paragraph, the suggested actions will simply be summarized in the form of several short points, most of which contain only the conclusions that follow from the foregoing analysis.

1. Maintain the greatest possible degree of internal monetary equilibrium. Inflation distorts investment decisions, lessens the inclination to save, and undermines competitive capacity.
2. Carefully draw up a development plan for the public sector and in support of the private sector, aimed at balanced economic growth with optimum utilization of the country's natural comparative advantages.
3. Increase its capacity to absorb foreign capital for investment in projects of high economic priority and in projects that yield a relatively high direct or indirect return in the shortest possible time.
4. Create a favorable climate for attracting direct foreign investment (including foreign entrepreneurial experience) and encouraging the reinvestment of interest, amortizations, and part of the profits on those investments.
5. Make a conscious effort to narrow and eliminate the gap between domestic savings and investments, among other things through the system of taxation and by developing a capital market.
6. Make a determined effort to improve the import-export ratio with respect to goods and services, by stimulating exports and by efficient import substitution.
7. Stimulate to the fullest possible extent the mobility of the nation's productive resources and the capacity of the economy to adapt to new technological advances and changing foreign-market conditions.
8. Impose severe restrictions, especially during the initial development stage, on the raising of short and medium-term foreign loans.

ACTIONS OF LENDING COUNTRIES TO EASE EXTERNAL DEBT

- i. Make as large a proportion as possible of their development aid

available in the form of grants-in-aid, quasi-grants, and direct investments, and, when lending, scale the amounts and terms of its loans to take account of the debt-bearing capacity of the developing country concerned.

2. Confine their loans to a large extent to projects of high economic priority which, directly or indirectly, rapidly yield a high return.
3. Continue to provide sufficient capital to enable the developing countries to pass through the first stage of their development, as described on pp. 21-22; during the second stage the accent may be shifted from grants and soft loans to loans on conventional terms.
4. Wherever possible, provide loans whose proceeds are not tied to the purchase of goods and services in the creditor country itself, but may be used to make purchases in the cheapest market.
5. Make maximum use of the channel of international development-financing institutions, such as the World Bank and IDA (as well as of Consultative Groups sponsored by the World Bank) which are well experienced in the selection of projects, insist on good economic management and performance, and assess the debt-bearing capacity of developing countries.
6. Pursue a liberal import policy with respect to the products of developing countries and support any measures that may prevent excessive fluctuations in the prices of those products (without providing incentives for overproduction).
7. Exercise great discretion when extending short and medium-term credits to developing countries that are still in the initial stage of economic growth.
8. Be prepared, where circumstances so require, to convert short and medium-term loans into longer-term loans on reasonable conditions.

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Prof. dr P. Liefstinck

Ontwikkelingshulp Wereld- bank van hoog gehalte

Uniek apparaat met grote ervaring



Ik ben er van overtuigd dat de ontwikkelingshulp door de Wereldbankgroep verleend, in vele opzichten van hoog gehalte is, aan de behoeften en draagkracht der ontvangende landen met zorgvuldigheid wordt aangepast en een zeer waardevolle bijdrage vertegenwoordigt aan de pogingen tot oplossing van het ontwikkelingsprobleem. Deze overtuiging werd uitgesproken door Prof dr P. Liefstinck voor de Werkgeversgroep voor de Partij van de Arbeid. Het besloot zijn betoog over de Wereldbankgroep van kredietinstellingen en haar betekenis voor de hulp aan minder ontwikkelde landen.

Hij zei daarin onder andere het volgende.

In de ruim 15 jaren die zijn verlopen sedert de oprichting van de Bank heeft de Wereldbankgroep een uniek apparaat opgebouwd met grote ervaring op het gebied van de economische ontwikkelingshulp.

In toenemende mate wordt van dit apparaat gebruik gemaakt voor het verlenen van technische bijstand bij het onderzoek en de oplossing van ontwikkelingsproblemen in de aangesloten landen.

De ervaring van de Bankgroep heeft duidelijk bevestigd, dat kapitaalgebrek niet het enige en in vele gevallen zelfs niet het voornaamste beletsel is voor een versnelling van de economische groei der minder ontwikkelde landen. Gemis aan inzicht en een tekort aan geschoold personeel op alle niveaus zijn niet minder ernstige beperkende factoren. Het is niet slechts een probleem van de korte termijn. In vele onderontwikkelde landen zal de menselijke factor nog geruime tijd een vertragend element in het proces van economische vooruitgang blijven, zolang de geestelijke en sociaal-politieke atmosfeer, gunstig voor een vrije menselijke ontplooiing, geen grondige verandering ondergaat. Daarin is Prof Liefstinck wat minder optimistisch. Dit is echter geen reden om tegenover technische hulpverlening sceptisch te staan; integendeel, ook in deze opvatting past geheel het onmisbaar achten van deze hulp, vooral in de vorm van onderwijs, hetgeen tevens een bijdrage kan leveren om meer fundamentele belemmeringen te overwinnen.

Vanaf het begin van haar werkzaamheden als ontwikkelingsfonds heeft de Bank technische hulp verleend bij het voorbereiden en uitvoeren van de door haar gefinancierde projecten. Spoedig echter is deze hulpverlening uitgebreid tot het bredere terrein van de zgn „development planning”, d.w.z. het opstellen van programma's voor een harmonische groei van onderontwikkelde economieën. Reeds in 22 landen heeft de Bank, met behulp van breed samengestelde missies van experts, een volledige economische „survey” uitgevoerd om aldaar de mogelijkheden van ontwikkeling op te sporen, programma's op te stellen met aanwijzing van prioriteiten, waarin afzonderlijke projecten kunnen worden gepast, en om financieringsplannen uit te werken, waarin kosten en middelen van interne en externe oorsprong op zo realistisch mogelijke wijze over de programperiodes worden geprojecteerd.

Ook voor de ontwikkeling van speciale sectoren zijn en worden doorlopend door de Bank vele diepgaande studies gemaakt en rapporten uitgebracht, waarop beleidsbeslissingen der betrokken regeringen kunnen steunen. Voorts adviseert de Bank herhaaldelijk over institutionele hervormingen, die voor de oplossing van ontwikkelingsproblemen van groot belang zijn, bv over de opzet en organisatie van nationale planbureaus, de meest efficiënte organisatievormen van overheids- en gemengde bedrijven, rationele tariefpolitiek van openbare nutsbedrijven, over nationale investeringsbanken en kapitaalmarktproblemen. Op het gehele terrein van de technische hulp werkt zij nauw samen met andere gespecialiseerde organen van de Verenigde Naties en met Amerikaanse en Inter-Amerikaanse instellingen, die overeenkomstige functies vervullen of werkzaam zijn op aangrenzend gebied. Ten slotte heeft de Bank een trainingsschool voor hogere ambtenaren uit onderontwikkelde landen en trainingscursussen voor lagere functionarissen, waarvan op ruime schaal gebruik wordt gemaakt. Bijzondere vermelding verdient nog dat de Raad van Bewindvoerders kort geleden besloten heeft uit de winst van de Bank 10 miljoen

dollars per jaar te besteden voor verbetering van het technisch onderwijs in de onderontwikkelde landen, aangezien daaraan de meest dringende behoefte bestaat.

Ook aan een betere coördinatie van de internationale hulpverlening geeft de Bank in toenemende mate haar aandacht. In de Wereldbankgroep van kredietinstellingen zelf is deze coördinatie verzekerd. Met de Amerikaanse en Inter-Amerikaanse organisaties voor economische hulpverlening onderhoudt de Wereldbankgroep van kredietinstellingen een vrijwel dagelijks contact, op het hoogste zowel als op lagere niveaus, waardoor een grote mate van samenwerking en coördinatie is verzekerd. Met de activiteiten van het zgn Colombo-plan voor Zuid- en Zuid-Oost-Azië en met de Europese Investeringsbank en het Europese Ontwikkelings Fonds is dit helaas veel minder het geval, omdat in deze instellingen het regionale denken, m.i. ten dele een overblijfsel uit het koloniale tijdperk, overheerst.

Niet zonder succes heeft de Wereldbank in de laatste jaren pogingen ondernomen om een zekere mate van coördinatie te brengen in de economische hulpverlening aan een aantal individuele ontwikkelingslanden, waarvoor zij ontwikkelingsprogramma's heeft opgesteld of kritisch heeft beoordeeld door de oprichting van zgn „consortia” of „consultative groups”, waarin zij bilaterale en multilaterale hulp tracht te mobiliseren, resp doelmatig te organiseren, ter bevordering van een efficiënte besteding van de middelen, die uit verschillende bronnen voor de financiering van die programma's worden beschikbaar gesteld. Deze pogingen tot coördinatie zijn van belang niet alleen met het oog op een verantwoorde keus van de projecten waarvoor financieringsmiddelen worden verstrekt, maar ook met het oog op het nastreven van een assortiment van vormen en voorwaarden van hulpverlening, die aan de behoeften en draagkracht van de betrokken ontwikkelingslanden zijn aangepast. Het eerste doel (een rationele keus van projecten) heeft in de praktijk meer kans van slagen dan het tweede (aanpassing van de vormen van kredietverlening aan be-

(Continued)

L'Echo de la Bourse, Brussels
January 24, 1963

La Banque Mondiale et l'expansion économique de Colombie — Douze pays ont participé mardi à la première réunion de la Banque Mondiale consacrée à l'examen du plan de développement économique colombien et de son financement international pendant les dix-huit prochains mois. Ces pays sont l'Autriche, la Belgique, le Canada, le Danemark, la France, l'Allemagne occidentale, l'Italie, le Japon, les Pays-Bas, la Grande-Bretagne, la Suisse et les Etats-Unis.

La réunion de ce mardi était préparatoire à l'entrée en action du « consortium » de pays et d'institutions financières qui contribueront au financement des divers projets compris dans le plan général de développement.

Ce financement extérieur s'élèvera à 200 millions de dollars par an, plus 40 millions de dollars qui devront constituer un fonds d'investissement privé. La Colombie elle-même fournira 80 pour cent du financement de son plan décennal.

The Financial Times, London
February 13, 1963

COLOMBIA COAL STUDY

A study is to be made of the possibilities of increasing the exploitation of the coal resources of the Cauca Valley in Colombia. The financing of the study is provided for in an agreement signed by representatives of the Government of Colombia, the United Nations Special Fund and the World Bank in Washington on Monday.

The project was approved by the Special Fund in May, 1962, and the Special Fund has allocated \$216,500 towards its cost. The balance of about \$120,000 will be borne by the Government of Colombia. The World Bank will act as executing agency for the study.

Colombia has large coal reserves, perhaps the largest in South America. Its output, however, is only about 2.5m. tons annually. With few exceptions the mines are small, and many are operated without adequate management.

Volkskrant, Amsterdam
January 26, 1963

Lieftinck: Leidt hulp via Wereldbankconcern

(Van onze verslaggever)

AMSTERDAM, 25 jan. — Gebruik makend van zijn verplichte aanwezigheid in Nederland (als commissaris kwam hij woensdag de aandeelhoudersvergadering van de KLM bijwonen) heeft prof. dr P. Lieftinck de Wereldbank en haar dochter-bedrijven, waarvan hij een hoge functionaris is, uitbundig aangeprezen als de tussenschakel bij uitstek voor de financiële hulp aan onderontwikkelde landen. Hij deed dat vrijdagmiddag in een bijeenkomst van de werkgroep van de Partij van de Arbeid. Buiten de president van de Nederlandse Bank, dr Holtrop, waren er weinig monetaire autoriteiten, die het pleidooi om multilaterale hulp van de oud-minister van Financiën kwamen beluisteren.

Prof. Lieftinck constateerde met spijt, dat de belangstelling voor het financiële werk dat de Wereldbank en haar instellingen voor de hulp aan de onderontwikkelde landen doen een steeds geringere belangstelling ondervindt van de politici in de westelijke landen. De bereidheid om de ontwikkelingshulp in multilaterale kanalen te leiden via zijn instelling noemde hij opmerkelijk klein. Daartegenover komt steeds meer de nadruk te liggen op bilaterale hulpverlening, dat wil zeggen de hulpverlening van land tot land. Een voortdurend groter aantal industriële landen geeft, volgens hem, de betreurenswaardige voorkeur aan bilaterale hulpverlening, om daarmee eigen politieke en commerciële belangen te dienen.

Speciale staatslening

De bilaterale hulpverlening brandmerkte prof. Lieftinck als „gebonden hulp“, die onder meer de internationale concurrentie uitsluit. Het Nederlandse standpunt kwalificeerde hij als een middenpositie, waarbij hij bij opbracht voor het Nederlandse besluit om deel te nemen aan bilaterale hulp naast steun aan de multilaterale hulpverlening.

Zijn waardering voor de omvang van

de Nederlandse bijdrage aan de multilaterale hulp leek overigens wel getemperd, want hij wees er zijn huidige opvolger bij het ministerie van Financiën terloops op, dat de geldmiddelen voor deze hulpverlening niet per se uit de belastingmiddelen behoren te komen. „Een speciale staatslening voor een bijdrage aan IDA (een op de ontwikkelingsfinanciering gerichte dochterinstelling van de Wereldbank) is denkbaar.

GRENS BEREIKT

Over het ongecoördineerd verstrekken van kredieten aan economisch achtergebleven landen merkte prof. Lieftinck op, dat sommige hulpbehoevende landen de grens van hun toelaatbare buitenland-

Courier-Post
Camden (N.J.) Courier-Post

TO ADD POWER

PANAMA—Panama is undertaking a \$7,600,000 expansion of electric-power facilities in its underdeveloped central provinces. A World Bank loan will provide more than half the cost.

Telegraaf, Amsterdam
January 26, 1963

Prof. Lieftinck over ontwikkelingshulp: Kapitaalgebrek niet grootste struikelblok voor vooruitgang

Van een onzer verslaggevers

AMSTERDAM, zaterdag — „Kapitaalgebrek is niet het enige en zelfs niet het belangrijkste beletsel voor de vooruitgang in de ontwikkelingslanden. Deze landen hebben tevens te kampen met een gebrek aan inzicht en personeel.“ Dit zei oud-minister prof. dr. P. Lieftinck tijdens een lunchtoespraak voor de werkgroep van de Partij van de Arbeid.

Prof. Lieftinck zei het niet tens te zijn met prof. Tinbergen dat deze belemmeringen slechts voor een korte termijn vertragend op de ontwikkeling in die landen zou werken. Hij meende dat de geest en de sociaal-politieke sfeer zou moeten veranderen en dat dit geruime tijd in beslag zou nemen.

Prof. Lieftinck hield in zijn toespraak een warm pleidooi

voor de activiteiten van de Wereldbank en de bij haar aangesloten instellingen. Hij meende dat er in Nederland grote belangstelling bestaat voor de ontwikkelingssteun, maar dat voor wat betreft de Wereldbank de interesse veelal beperkt bleef tot de orders die via de Wereldbankleningen worden geplaatst en de vraag waar de gelden worden besteed.

Uitvoerig wees hij op de voordelen van multilaterale hulp boven bilaterale hulp en zei verheugd te zijn dat de Nederlandse regering hierin een evenwichtig standpunt inneemt. Voor de ontwikkelingslanden was multilaterale hulp zijns inziens te prefereren, aangezien hierdoor de internationale concurrentie niet wordt uitgeschakeld.



PROF. DR P. LIEFTINCK

se schuld reeds hebben bereikt, andere die grens zeer dicht zijn genaderd en dat vooral jonge landen aan kredietwaardigheid nog helemaal niet toe zijn.

In luttele jaren is de buitenlandse schuld van de achtergebleven landen ruim verdubbeld. Eind 1962 bedroeg hun gezamenlijke schuld aan het buitenland reeds 20 miljard dollar per jaar of ongeveer vijftig gulden per hoofd van de bevolking. Nu reeds moeten ze jaarlijks 2½ miljard dollar aan het buitenland betalen als rente en aflossing op eerder verkregen kredieten. Om hun additionele hulp te verlenen moet dus nu al jaarlijks meer dan 2½ miljard gulden aan hulp worden verstrekt.

February 15, 1963

hoeften en draagkracht), maar dat is nu eenmaal eigen aan een mengsel van multilaterale en bilaterale hulp in de thans overwegend beschikbare vormen.

Nog op een ander terrein overweegt de Bank of zij een nuttige bijdrage kan leveren aan de oplossing van een belangrijk onderdeel van het ontwikkelingsprobleem, namelijk de verbetering van het investeringsklimaat voor buitenlands particulier kapitaal, dat bereid zou kunnen zijn zich op grotere schaal naar minder ontwikkelde landen te richten, indien de bijzondere risico's daaraan verbonden verminderd zouden kunnen worden of door verzekeringen worden gedekt. Dit is een psychologisch en politiek tamelijk gevoelige materie, die in vele minder ontwikkelde landen met argwaan wordt tegemoet getreden. Ook dit verschijnsel is, naar het mij voorkomt, althans ten dele een erfenis van het koloniale tijdperk.

In nog twee richtingen is de Bank actief, te weten in de richting van het zoeken naar een verbetering van de bestaande procedures voor het oplossen van geschillen tussen regeringen en particulieren, met name door bevordering van conciliatie en arbitrage, en in de richting van het zoeken naar oplossingen in multilateraal verband voor het verzekeren van bepaalde buitengewone risico's, verbonden aan investeringen in het buitenland. Ook andere instellingen en organen houden zich met deze onderwerpen bezig en de Bank onderhoudt daarmee een nauw contact. Het is nog te vroeg om een bepaalde uitkomst van deze pogingen te voorspellen, maar indien positieve resultaten mochten worden bereikt, zou het mij zeer verwonderen als de Bank, uit hoofde van haar vertrouwenspositie en samenbindende kracht, bij de verwezenlijking daarvan niet een belangrijke rol zou vervullen.

Prof Loefftinck zei het volgende over de relatieve betekenis, die aan de activiteiten van de Wereldbankgroep mag worden toegekend, gezien in het geheel van de hulpverlening aan de minder ontwikkelde landen. Op het eerste gezicht zijn de bijdragen van de Bank en de I.D.A. samen betrekkelijk bescheiden. Volgens de laatste gegevens bedroeg de totale bruto hulpverlening in 1961 globaal \$8,5 miljard, waarvan ongeveer \$4,5 miljard in de vorm van leningen met rente en aflossingsverplichtingen in buitenlandse valuta en ongeveer \$4

miljard in de vorm van schenkingen of leningen, waarvan de dienst geen buitenlandse transfers vereist. Onder deze laatste categorie vallen b.v. leningen terugbetaalbaar in lokale valuta en hulp in de vorm van landbouwoverschotten, zoals op grote schaal door de Verenigde Staten wordt verleend.

Evenwel, slechts een gedeelte van deze 4 miljard kan worden beschouwd als investeringskapitaal voor ontwikkelingsprojecten; het is voor een belangrijk deel consumptieve hulp (voedingsmiddelen of grondstoffen voor lopende produktie). Men kan gevoelig aannemen, dat minder dan de helft uit kapitaalhelp in eigenlijke zin bestaat. Voegt men 1½ miljard van de laatstgenoemde \$4 miljard toe aan de eerstgenoemde 4,5 miljard, die waarschijnlijk wel voor investeringsdoeleinden zijn bestemd, dan komt men tot een bruto bedrag aan eigenlijke kapitaaloverdrachten van rond \$6 miljard. Trekt men hiervan \$2,5 miljard, nodig voor de dienst van rente en amortisatie van reeds uitstaande leningen af dan blijft een nettobedrag van \$3,5 miljard voor ontwikkelingsinvesteringen beschikbare kapitaaloverdrachten over. Het aandeel van de Wereldbank daarin was, met een netto bijdrage van ruim \$800 miljoen dus bijna 25%. Het aandeel van IDA in de in dat jaar niet met valuta-verplichtingen belaste kapitaaloverdrachten in eigenlijke zin — in totaal ongeveer \$1,5 miljard bedragend — lag waarschijnlijk tussen de 10 en 15%.

Bij een kwalitatieve beoordeling echter verschijnt de relatieve bijdrage van de Bank — en ook die van de I.D.A. — in een ander en veel gunstiger licht. Een niet onaanzienlijk deel namelijk van de evengenoemde \$3,5 miljard aan netto kapitaaloverdrachten bestond uit betrekkelijk kortlopende leverancierskredieten, terwijl de Bank en de IDA uitsluitend langlopende kredieten verlenen. Bovendien, praktisch het gehele bedrag, dat van deze \$3,5 miljard uit andere bronnen dan de Bank is gevloeid, was bilaterale en als zodanig geboden hulp, terwijl de hulp van de Bank, evenals die van de IDA — verstrekt op nog veel gunstiger voorwaarden — internationaal vrij besteedbaar en daardoor meer waardevol is.

De projecten, die de Wereldbank financiert, liggen (in volgorde van de bedragen, die daarvoor zijn verstrekt)

op de terreinen 1. elektriciteitsvoorziening, 2. transportwezen (voornamelijk wegen, spoorwegen en havens), 3. mijnbouw en industrie en 4. landbouw (inclusief irrigatie en landbouwmecanisatie).

In beginsel financiert de Bank alleen projecten met een hoge prioriteit, gezien vanuit het oogpunt der fundamentele economische ontwikkelingsbehoeften van het lenende land en beperkt zij zich in beginsel tot dekking van de buitenlandse deviezenkosten, maar tegenover landen die reeds iets verder ontwikkeld zijn en in staat zijn om met buitenlandse leveranciers en aannemers te concurreren, neemt zij een ruimer standpunt in en draagt zij met haar leningen ook bij in de dekking van de binnenlandse investeringskosten. Aan de eis van het openen van een ruime gelegenheid tot internationale inschrijvingen bij aanbestedingen wordt echter de hand gehouden, met het oog op een zo efficiënt mogelijke besteding der bij de Bank opgenomen leningen.

Het handhaven van het leningsniveau van de Wereldbank en eventuele verdere stijgingen daarvan heeft een voldoende mate van emissievrijheid in de kapitaalrijke landen tot voorwaarde. Dit is vooral van belang met het oog op die landen, waar, zoals in Nederland, buitenlandse emissies aan officiële goedkeuring onderworpen zijn en een zekere rantsoenering wordt toegepast.

Het is niet uitgesloten dat de IDA in de loop der jaren de Wereldbank voorbij zal streven. De IDA werd in 1960 opgericht met een stamkapitaal van 1 mrd \$ met de bedoeling om, ter aanvulling van de Bank, de verstreking van ontwikkelingskredieten mogelijk te maken tegen voorwaarden die een minder zware belasting vormden voor de betalingsbalansen der ontwikkelingslanden dan de leningen van de Bank, dwz kredieten tegen gemakkelijker voorwaarden wat rente en aflossing betreft.

De bewindvoerders van de Bank, die tevens als bewindvoerders van de IDA fungeren, achten het nodig, dat de IDA een toenemend aandeel in de ontwikkelingsfinanciering zal worden gegund en de daarvoor vereiste middelen zal krijgen.

De derde instelling in de Wereldbankgroep, de IFC, heeft tot doel de bevordering van buitenlandse investeringen in de particuliere sector van het bedrijfsleven — met name de industriële sector — in de minder ontwikkelde landen.

(vervolg pag. 5)

Incomplete

El Diario de Pereira
February 8, 1963

El BIR Creó una Sección de Educación

El señor Ricardo Díez - Hochleitner fué nombrado jefe de la nueva dependencia. - Ayudará en las inversiones de carácter educativo.

WASHINGTON, Feb. 7. — El Banco Internacional de Reconstrucción y Fomento, fundó una nueva sección educativa en su departamento de operaciones técnicas, para asesorar los países miembros en la planeación de sus inversiones de carácter educativo.

El Banco anunció aquí, que el

señor Ricardo Díez-Hochleitner fué nombrado jefe de la nueva sección. El señor Díez-Hochleitner fué jefe de la División de Planeamiento Educativo del Consejo Económico y Social de las Naciones Unidas y Secretario Ejecutivo de la Fuerza Táctica Educativa de la Organización de los Estados Americanos. Desde 1953 hasta 1958 el señor Díez-Hochleitner, de 34 años de edad, desempeñó varios puestos de carácter administrativo y educativo en su país natal, España y en Colombia.

La Republica, Bogota
February 9, 1963

División de Educación Crea el Banco Mundial

El Banco Mundial anunció hoy el nombramiento del señor Ricardo Díez Hochleitner como jefe de la nueva división de educación del Departamento de Operaciones Técnicas. La nueva división se ocupará de evaluar los proyectos en materia de educación que se sometan a la consideración del Banco y de su organización afiliada, la Asociación Internacional de Fomento, para su financiación y de ayudar a los países miembros menos desarrollados a planear sus inversiones de educación de modo que éstas tiendan a promover el desarrollo económico de los mismos. En el desempeño de sus atribuciones la nueva división se mantendrá en contacto con los diversos organismos internacionales, gubernamentales y privados que se interesen en dichas cuestiones.

El señor Díez Hochleitner, quien hasta

hace poco ocupó el cargo de jefe de planeamiento de la UNESCO y el de secretario ejecutivo de la comisión especial de educación de la OEA, nació en Bilbao en agosto de 1928 y obtuvo su doctorado en ciencias en la Universidad de Salamanca, realizando después estudios post-graduados en el Technische Hochschule, Karlsruhe, y en la Universidad de Georgetown, en Washington, D. C. En 1955 pasó a ocupar el cargo de inspector general de formación técnica de la Oficina de Educación Iberoamericana. Entre los años de 1952 y 1958 desempeñó una serie de cargos académicos y administrativos en el campo de la educación en España y en Colombia. El señor Díez Hochleitner es Comendador de número de la Orden de Alfonso X el Sabio y de la Orden de Isabel la Católica.

Northwest Arkansas Times, Fayetteville
January 30, 1963



JOHN C. BULLITT of New Jersey is shown at the Senate Foreign Relations Committee hearing in Washington at which his appointment as executive director of the International Bank for Reconstruction and Development was approved.

Bethesda - Chevy Chase Tribune
February 1, 1963

'Challenge of Illiteracy' Theme for Panel Talks

"The Challenge of Illiteracy" is the subject of a panel discussion of one of the two international programs next week scheduled by The Woman's Club of Chevy Chase.

The second program for the same week is a talk on "Economic Development Institute" of the World Bank led by Mrs. Marjorie Billings, Staff Relations Officer of the World Bank on Tuesday, at 2 p.m.

Mrs. Wendall Cleland, chairman of Education will moderate the illiteracy panel given under the auspices of the Public Affairs department on Friday, February 8, at 10:30 a.m.

The illiteracy program on Friday is in line with the project of the General Federation of Women's Clubs which has

accepted this challenge for the United States and also eight countries abroad in cooperation with CARE.

Four of these countries will be represented on the panel: Mrs. Ali Khosropur will speak for Iran, Mrs. Concha Romero James, for Mexico, Mrs. Hishmat Ismail Kahn, for Pakistan and Dr. Sevinch Dibilan Carlson for Turkey. Members gather at 10:00 o'clock for coffee.

Tuesday's discussion on the Economic Development Institute program of the World Bank will include 14 of the wives of men from abroad who are visiting Washington while their husbands attend the Institute.

Dr. Singh of India and Mrs. Monir Jazani of Iran will speak on the role of women in their respective countries.

El Deber, Bucaramanga
February 11, 1963

El BIR Creó una Sección de educación

Washington El banco internacional de reconstrucción y fomento, fundó una nueva sección educativa en su departamento de operaciones técnicas, para asesorar a los países miembros en la planeación de sus inversiones de carácter educativo.

El banco anunció aquí que el señor Ricardo Díez Hochleitner fué nombrado jefe de la nueva sección. El señor Díez Hochleitner fué jefe de la división de planeamiento

Educativo del consejo económico y social de las Naciones Unidas y secretario ejecutivo de la fuerza táctica educativa de la organización de los Estados Americanos.

Desde 1953 hasta 1958 el señor Díez Hochleitner, de 34 de edad, desempeñó varios puestos de carácter administrativo y ejecutivo en su país natal, España y en Colombia.

~~April 1963?~~
Feb-Mar. 1963

Integration and disintegration in the World Economy

Lecture by

Dr. P. Lieftinck



The impressive rise in world production and world trade since 1945 has been one of the most remarkable features of world economic developments during the present century. This comes out all the more clearly by a comparison between the evolution of the world economy after the first and after the second world wars. Such a comparison reveals three major and striking differences: Firstly, the growth of both world industrial production and world trade has been much more marked and much more sustained over the last 15 years than during the period between the wars. Secondly, world trade, outside the Soviet bloc, has expanded at a faster rate than world industrial production since 1945, whereas world trade lagged behind world industrial production in the Twenties and Thirties - a reversal of trend that becomes even more remarkable when it is recalled that trade and industrial production developed more or less in parallel during the 25 years immediately preceding the first world war. Thirdly, there has been a very significant difference in the evolution of prices of international commodities, i.e. an uneven but much steadier trend in the post-war period, compared with a disastrous fall in prices between the wars.

The reasons for these differences are many and various, and I do not propose to analyze them fully, but shall confine myself to a brief indication of the major factors underlying them.

Before the first world war there was a large degree of integration of the world economy, in the sense that, apart from national tariff protection, there was freedom of import and export, a free system of international payments and unrestricted movement of labor and capital across frontiers. It is true that there were world prices and domestic prices, free market prices and cartel prices, and, despite a wide application of the most-favored-nation principle, general and preferential tariffs, of which the latter made for discrimination. But at that time the world was much less divided into independent nations, there was a great deal of uniformity of economic and social structure, and the currencies of most countries bore a fixed relation to gold and therefore to each other, and were freely and mutually convertible. There was a well organized system of international short-and long-term credit. The oceans of the world were free. Europe was still the industrial center of the world economy, much dependent on the exchange of raw materials and manufactures among the old countries, but at the same time no less strongly - indeed, in north-western Europe, even more strongly - orientated

to external, i.e. overseas, expansion. The United States, the second rapidly developing industrial center, was more concentrated on domestic expansion, but since the turn of the century had been displaying, both politically and economically, a growing interest in other countries, not only in the western hemisphere but on the other side of both the oceans by which it is bounded. Most of the rest of the world was still divided into colonial territories, suppliers of raw materials and food-stuffs and regionally linked with a limited number of European mother countries that provided them with manufactures, services and capital and whose prosperity and adversity they shared.

This smoothly functioning system of world trade and production was fundamentally disrupted by the first world war. This was particularly true of the European industrial center. The redrawing of frontiers and the peace terms imposed by the victors on the vanquished threw it out of balance; it was further disarranged by monetary mismanagement; it was partially crippled by the disastrous depression that began in 1929 and lasted for a number of years; and finally it was engulfed by a tidal wave of economic nationalism, causing complete disorganization of the international trade and payments system and seriously hampering the international flow of capital. Thus the process of international economic disintegration reached a climax. Russia embraced the system of communism, withdrew from world commercial relations, and sought its strength in vigorous internal expansion. The United States, where political isolationism rapidly gained the upper hand - which led to its rejection of the League of Nations - , increased its customs tariff protection and played a role in the international capital movements more disruptive of, than conducive to, external monetary equilibrium. It accumulated a large part of the world's reserves of gold and, though no less severely hit than Europe by the great depression, gained and consolidated in the following years, thanks to its unbroken economic unity and its rich resources, the position of the leading center of the world economy that until 1914 had been occupied by Europe.

With the exception of Japan, which began to build up a considerable industrial potential and to participate more and more actively in international trade, the rest of the world remained largely in the pre-industrial era, with very little mutual trade and a continued dependence on Western-European markets, that, particularly in the Thirties, had almost ceased to expand. Overseas territories under foreign flags occupied a relatively favorable position by virtue of the preferential treatment they enjoyed on the

membership of

markets of the mother countries (to the extent that they would otherwise have been subject to tariffs), but, due to the fact that prices of raw materials and foodstuffs rose more slowly in the Twenties and fell more rapidly in the Thirties than those of industrial products, the terms of trade between the industrialized and the raw material producing countries persistently tended to become less favorable to the latter.

Let me mention some figures to illustrate the major world economic trends between the two world wars. Between 1920 and 1928, the volume of world industrial production rose by almost 100%. In the same period, the volume of world trade in industrial products rose by only 20% and world trade in primary products (raw materials and foodstuffs) by 35%. In terms of value, however, world trade in both industrial and primary products fell by about 50% over the period.¹⁾

The picture after the second world war is a completely different one. From 1948 to 1960 the volume of world industrial production rose again, by almost 100%. This time the volume of world trade in industrial products rose by over 140% and that in primary products by 95%. There was also a substantial rise in the value of world trade in that period: the value of trade in industrial products rose by 158%, even more sharply than the volume, and that in primary products by 61%, considerably less than the increase in volume. I shall return to these price developments, so important to the raw material producing countries, in a later stage of this lecture.²⁾

What were the major factors responsible for this extraordinary development of the world economy from 1948 to 1960? Although Europe, its old industrial center, with the lowering of the Iron Curtain, lost a substantial part of its economy to the Soviet bloc, its economic recovery from the war disaster was not this time retarded by a short-sighted policy of "each for himself and the conquered for all". On the contrary, Europe's economic recovery was vigorously promoted by a

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- 1) Cf. "Industrialization and Foreign Trade", League of Nations, 1945
 - 2) Cf. "International Trade 1961, GATT-publication 1962-1965, and reports mentioned therein.

reconstruction program that was drawn up jointly by the Western European countries and on the basis of which the United States lent billions of dollars in Marshall Aid to the members of the Organization for European Economic Cooperation over a period of several - and the most critical - years. The significance of this aid is illustrated by the fact that during the period 1947 - 1950 a quarter of Western Europe's total imports of goods and services, or almost two-thirds of European imports from the dollar area, were paid for out of it. In addition to such other objectives as a balanced inter-European production expansion and the achievement of monetary stability, the Organization for European Economic Cooperation aimed, particularly, at expanding overall European exports and liberalizing inter-European trade and payments by abolition of the quantitative restrictions and bilateral arrangements, initially adopted by almost all of its members. The acceptance of a Code of Liberalization and the institution of the European Payments Union in 1950, followed by the signing of the European Monetary Agreement in 1955, paved the way for rapid progress towards the liberalization of inter-European trade. This course was vigorously pursued during the Fifties and by the end on 1957, the year in which the Treaty of Rome was signed, almost all the members of the OEEC had achieved a measure of liberalization of their mutual trade of as much as 90%. 1)

In the field of monetary policy, too, the European countries showed that this time they were animated by a different spirit from the one that in the Twenties and Thirties had led to such serious disturbances of their internal and external equilibrium. There was no repetition either of the "va-banque" policy that at that time in some countries caused such disastrous inflation, or of the exaggerated national prestige policy that in others had led to the establishment or maintenance of over-valued currencies that hampered the export trade and caused employment to fall far below an economically and socially acceptable level. The over-liquidity that had arisen throughout Western Europe during the second world war and which, despite drastic monetary reforms, emerged again in the immediate postwar period and gave rise to dangerous inflationary pressures, was absorbed and curbed, in

1) Cf. "A Decade of Cooperation, Achievements and Perspectives", Ninth Report of the OEEC, 1958.

some cases soon and in others later, as the combined result of Marshall Aid, the reconstruction of productive capacity and appropriate fiscal measures. And even though the threat of inflation did arise again in subsequent years in a number of countries, governmental policies were increasingly directed, partly under the influence of the International Monetary Fund, at overcoming or curbing this danger by the application of internal corrective measures. Competitive exchange depreciation was blacklisted, but the elimination of structural balance of payments disequilibrium by exchange rate adjustments was no longer regarded as inconsistent with international respectability. Indeed, the simultaneous devaluations of their currencies in September 1949 by a great many European and monetarily associated non-European countries, and the later unilateral devaluations by other countries, have given greater flexibility to the international monetary system and considerably facilitated the re-integration of Europe into the world economy.

The trend of business conditions in Europe was, by any historical standard, exceptionally favorable over the period in question. Fluctuations in general economic activity were relatively mild and there were no really serious depressions. Such crises as did arise were mainly connected with the balance of payments and were due either to world political tensions, such as the Korea crisis of 1950 - 1951 and the Suez crisis of 1957, or to temporary, though sometimes large, balance of payments deficits caused by domestic overspending. Thanks to the application of internal remedial measures and international credit assistance, however, these disturbances were contained and resulted in nothing more serious than a slackening of the general upward trend or, at worst a brief stagnation of industrial production. The business fluctuations were reflected mainly in the level of imports and of stocks of imported commodities. This favorable development of the European economy and the fact that over the course of the years it acquired greater inherent momentum, as a result of which it became less sensitive to cyclical trends in the United States, substantially benefitted the growth of the world economy as a whole. Even though their balance of payments positions compelled some European countries temporarily to take a few steps backward on the road towards the liberalization of trade, there was never any serious question of adopting a protectionist policy as such to shield their economies against unfavorable business conditions. Moreover, the persistent rise of industrial prices since 1945 has contributed substantially to creating an expansionary climate.

I have already mentioned the significance for the recovery of the world economy of the policy of mutual co-operation pursued by the European countries, with the support of United States dollar aid, the prevalence of realistic monetary policies, designed to achieve internal and external stability, and the generally favorable behavior of the business cycle in Europe. No less significant, however, has been the outward-looking trade and payments policy pursued by the European countries towards their overseas territories, the countries of the sterling bloc and, when the time was ripe, the North American continent. The policy of liberalization of imports increasingly applied by the members of OEEC since 1948 was extended, under the Agreement, to the overseas territories of members and voluntarily, but generally, also to the sterling bloc, which included Australia, New Zealand, India, South Africa and Iraq as well as a number of less important countries. The result was that imports from those countries rose considerably more than total European imports, while Europe's export trade with them benefited as well. This process was accentuated by the recognition of the sterling area as a single unit in the European Payments Union of 1950, which enabled the multilateral liberalization of payments between Western Europe and the sterling countries to keep pace with the liberalization of payments between the European countries themselves.¹⁾

The liberalization of imports from the United States and Canada took more time. Despite increasing efforts by the Western European countries to expand their exports to the dollar countries and the rising dollar earnings realized by them from exports to other trading partners, commercial transactions yielding dollars were not adequate to meet the great need for goods from the dollar area that persisted after the end of Marshall Aid. It was due solely to United States military and economic aid, both in Europe and elsewhere, that after the Korea crisis the dollar gap in the aggregate Western European balance of payments was closed and the European gold and dollar reserves began to show a reasonable growth. Between 1951 and the end of 1957 these reserves rose from \$8 billion to \$14 billion (compared with a little over \$6 billion in 1948). This improvement in the reserves position was, however, at first very unequally distributed among the

1) Cf. J. Polk "Sterling, its Meaning in World Finance", 1956

the individual European countries, a fact that delayed joint Western European liberalization of imports from the North American countries for several years. The quota restrictions on imports from the dollar countries were, however, steadily reduced and by the end of 1957 an average liberalization of imports from the United States and Canada of 64% had been reached, while seven of the Western European countries had already freed 80% of their North American imports.¹⁾

By 1958, the process of Western European liberalization of trade and payments, both between the members of the Organization for European Economic Cooperation (including the non-member sterling bloc countries) and with the countries of the dollar area, was rapidly entering its final phase. The circumstances that brought about this situation were reflected in a shift in the international balance of payments positions in favor of the leading countries of Western Europe and to the disadvantage of the United States. This change in the balance of payments picture had deep-seated structural causes and fundamentally important effects in regard to the role that the two great centers of the free part of the world economy have since come to play on the international stage. I should like to pause a moment to consider these causes and effects from the viewpoint of United States postwar policy.

Since the second world war, the policy of the United States (so far as it interests us in this present connection) has been characterized by the furnishing of moral and financial support for the economic reconstruction of Europe, the military strengthening of strategically important countries in the struggle against what is called the communist threat, and economic aid to the less developed areas. Between 1948 and 1960 the United States granted about \$80 billion dollars in foreign aid, 2/3 of it economic and 1/3 military aid. Nearly half the total aid went to Europe, and the remainder to the rest of the free world. A large part of this aid was in the form of goods and services, or was spent in the United States, and therefore resulted in no, or no permanent, loss of dollars or reserves. Nevertheless, despite an almost continuously favorable balance of trade and services, the United States balance of payments showed a cumulative deficit from 1948 to the end of 1957 of about \$18 billion, equivalent to an average of \$1.8

1) Cf. "A Decade of Cooperation, Achievements and Perspectives", Ninth Report of the OEEC, 1958

billion a year. These persistent deficits on balance of payments could not seriously harm the United States so long as its gold reserves were ample - both in their absolute amount and in relation to the dollar balances held in the United States by other countries - and so long as the competitive position of the United States on the world market could be regarded as impregnable. Import quotas for balance of payments reasons and exchange restrictions were not imposed. The tariffs policy of the United States, which in the Twenties and early Thirties had become markedly protectionist and did not begin to show a tendency towards liberalization until after 1935, and even then only on a reciprocal basis, continued its liberal development in the early postwar period. No restrictions at all were imposed on the export of private capital. The International Monetary Fund, which provided large sums to overcome the balance of payments crises that now and then arose, was thereby left complete freedom to use dollars (until a few years ago the only convertible currency) out of a United States subscription of over \$2.7 billion, later increased to over \$4 billion. The United States thus contributed substantially, and in a variety of ways, to the restoration and maintenance of international monetary stability and to the liberalization of trade in the free world. Meanwhile, despite periodic mild recessions, there was a very satisfactory growth of the United States domestic economy and an impressive rise in the average level of consumption.

The 1957/58 recession was not, however, followed by a complete recovery in the rate of growth either of industrial production or of the volume of exports. At the same time, foreign aid was stepped up, rather than cut down, and the export of private capital became a significant factor. The United States balance of payments deficit, which had averaged \$1.8 billion during the preceding years, rose to \$3.5 billion in 1958, \$3.7 billion in 1959 and \$3.9 billion in 1960. The fall in the surplus on trade and services account - a surplus essential for the maintenance by the United States of the level of its foreign aid - reflected a weakening of the United States international competitive ability compared with that of the industrial countries of Western Europe. This was probably only a temporary occurrence, attributable to the fact that in the mid-Fifties the rise in the cost of labor in Europe had lagged behind that in the United States and to the rapid expansion of capacity and improvement in quality of Western European production. By 1960, despite a further mild recession, the United States trade balance was already showing a remarkable recovery and the large overall balance of payments deficit registered

in that year must be attributed to a large extent to the export of private capital. After 1960, this deficit gradually fell and is now almost down to its average level for the period 1948-1957.

This change in the relative economic positions and strength of the United States and Western Europe constituted the deeper cause of the rapid culmination in 1958 and 1959 of the process of liberalization of international trade and payments by the Western European countries. In contrast to the large United States balance of payments deficits, the countries on this side of the Atlantic experienced large surpluses and built up considerable gold and exchange reserves. Consequently, fourteen European countries were able at the end of 1958 to restore the external convertibility of their currencies and thereby to take a decisive step towards complete integration of the world payments system.¹⁾ At the same time, most of them discontinued their remaining quantitative import restrictions and their bilateral trade agreements with other European, as well as non-European countries, and thereby freed a substantial part of the world trade from direct quota restrictions and the discrimination inherent in them. At the same time, the decision to permit convertibility meant that the countries concerned abandoned the right to refer to their balance of payments position as a justification for exceptions to their obligations, as members of the 1947 General Agreement on Trade and Tariffs (GATT), not to discriminate in regard to import quotas and tariffs. Under this Agreement, which had meanwhile been signed by nearly 40 countries, many mutual tariff concessions already had been granted during the preceding years as a result of bilateral negotiations.

Finally, at the beginning of 1961, the nine larger West European countries formally undertook to observe the obligations on the International Monetary Fund Agreement concerning the avoidance of restrictions on current payments. A few other European and a large number of overseas countries, including all the countries of the sterling bloc, although not yet ripe for this final step, had in the meantime adjusted their remaining foreign exchange restrictions to the convertibility of the leading currencies by removing all discriminatory features from those restrictions. The extent to which restrictions on payments are still being applied varies greatly

1) See P. Lieftinck's "Recent Trends in International Monetary Policy", Essay in International Finance, no. 39, September 1962.

with individual countries and is, in general, closely connected with the stage of industrial development which they have reached and the level of their foreign exchange reserves. The same situation prevails with respect to the quantitative import restrictions that are still in force. The more prosperous overseas countries, such as Australia, New Zealand and South Africa, stand, so to speak, in the entrance-hall of the club formed by those countries which have removed all restrictions. India, Pakistan and most countries in the Middle East and in South-East Asia are, however, still experiencing balance of payments problems which will not allow them to abolish their restrictive systems in the foreseeable future. Bilateral trade and payment agreements, except with countries where state trading predominates have, nevertheless, largely fallen into disrepute, because it is more and more understood that such agreement diverts the flow of foreign trade into artificial and less advantageous channels. The educative influence of the I.M.F., which is conducting a strong fight against restrictions and discriminatory practices in international payments, and is working in close collaboration with GATT in its battle against discriminatory trade practices is clearly noticeable in this field.

In the process of restoring world trade and payments that has taken place since the second world war, the countries of Latin America have lagged behind to a considerable extent. Their mutual trade, which amounts to no more than 10% of their foreign trade, showed little or no relative improvement between 1948 and 1960, and the whole of their trade with the rest of the world, 90% of which is with Europe and the United States, rose in value during those years by only 20%. It is to be noted that this rise was entirely due to an expansion of trade with Western Europe; this trade, which showed a large deficit for Europe in 1948, was brought into balance in the Fifties after an increase of 25%. On the other hand, the surplus enjoyed by the United States was lost, and here a balance was reached at a practically unchanged level.

It is a well-known fact that the trade between industrialized countries has a tendency to develop more rapidly than either mutual trade between non-industrialized countries or trade between industrialized countries, on the one hand, and non-industrialized countries on the other. There is also a tendency for countries in the preliminary stage of indus-

trialization to be in need of a greater volume of imports than they are in a position to pay for with their exports. Practically all countries in this stage of development, with the exception of those that are unusually well endowed with natural resources, such as petroleum, are faced with balance of payments difficulties for the solution of which they are dependent on imports of foreign capital. The Latin American countries, at least the larger of them, are exactly in this position, and only Venezuela, with its rich sources of oil, should have no real worries on the score of her balance of payments. American aid amounting to about \$5 billion dollars during the period between 1948 and 1960, supplemented by private foreign investments, mostly from American and Canadian sources, provided considerable support for the balance of payments of a number of Latin American countries. Nevertheless, except during short periods of rising prices on the international markets for primary products, their trade balances have shown a deficit. In fact, the entire rise in the exports of the Latin American countries as a group since the second world war has been due to the increase in Venezuela's exports of oil. Leaving these out of account, this part of the Western world has not only stayed behind in the expansion of the world economy but has shown, as regards external growth, hardly any progress. It is true that there have been differences between individual countries. The performances of Mexico and Peru, for instance, have been to a certain extent impressive, but their achievement has not been able to compensate for the decline that has taken place elsewhere in this area.

There are many reasons for this unsatisfactory state of affairs in Latin America. Predominantly raw materials producers and with little diversification in their economies, the countries of Central and South America are highly dependent for their export earnings on one commodity like coffee, or at best a few commodities, the proceeds of which fluctuate with the cyclical and structural vicissitudes of world market demand. For many years the main trend of the prices for their principal export products has been markedly downward. At the same time, many of these countries have experienced political unrest, creating an unfavorable climate for both domestic and foreign investment; they have suffered from practically chronic inflation, which has retarded their economic development and distorted investment decisions. Their exchange rate policies have been unrealistic, more often than not, and their commer-

cial policies highly protectionist, with much reliance on bilateralism. However, there is also another side to this coin. Neither the commercial policies of the United States nor those of the Western European countries have done very much to assist Latin American exports in post-war years. As regards their agricultural exports, many of these have encountered on both markets, the American and the European, direct import-restrictions and high protective tariffs or other fiscal duties, and the United Kingdom and France have practiced discriminatory tariff and price policies in favor of the countries of the Commonwealth and the overseas territories, respectively. As regards their exports of mineral products, the quota and tariff policies of the United States have been particularly damaging. During recent years the leading West European countries have opened their markets to a greater extent to foreign commodities, including Latin American exports, by reducing direct import restrictions, lowering customs duties and consumption taxes and abolishing bilateral trade and payment agreements, but a number of restrictive measures remain. These necessarily limit Latin America's export earnings and her ability to pay for the imports which, in spite of her protectionism, she needs so badly to sustain her development efforts.

Economic recovery took a much more favorable course in Japan, and the reintegration of that country into the world economy, in spite of prejudicial factors, is one of the most impressive features of the post-war period. Between 1948 and 1960 the value of Japanese industrial production rose by 300% and the country's foreign trade by 400%. In 1960, Japan's share in world trade amounted to the same percentage, viz. 7%, as that of all the Latin American countries together. Seventy per cent of Japanese import and export trade is now conducted with the United States (for which country Japan now occupies a position of equal importance to that of England as a trading partner) and with the countries of South-East Asia. As a market for Australian goods Japan now takes second place, after England, and has outstripped that country as the principal supplier of the Australian market. It would appear that, with the progress

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- 1) Cf. "Economic Policies and Programs in South America", report submitted to the Subcommittee on Inter-American Economic Relationships of the Joint Economic Committee of the U.S. Congress, 1962; also: "Europe's Role in Latin American Development", publication of the Inter-American Development Bank, 1962.

of industrialization also in other countries situated along the eastern edge of the Pacific Ocean (such as Australia), a third great center of the world economy, with Japan as its nucleus, is arising.

During the first few years following the second world war the increase in Japanese foreign trade remained behind the level of recovery in domestic production, but after the Peace Treaty of 1952 and the end of American occupation Japanese trade rose in a phenomenal manner. The large dollar income that had resulted from the occupation was followed, for a considerable time, by special dollar earnings in connection with the maintenance of American bases and the local procurement of military supplies, but this source of foreign exchange gradually diminished, and export earnings became of increasingly vital importance for Japan. Japanese industry lived up to this challenge and, during the Fifties, passed through a process of almost unparalleled rapid expansion which, although accompanied by violent ups and downs in the balance of payments position that periodically required credit assistance from abroad, brought imports and exports to their present high level.

In the course of achieving this result, Japanese exports, especially to the extent that they were directed to the markets of the industrialized countries of the West, had not only to contend with the many trade and payments restrictions that applied to exports from other countries as well, but also with discriminatory treatment based on the low level of Japanese wages. When Japan joined the General Agreement on Tariffs and Trade, many West European countries had, for that reason, exercised their right not to apply the Agreement to Japan until such time as they would have entered into tariff negotiations with that country, and this gave them the freedom to restrict Japanese exports to an exceptional extent. The United States, which had not exercised the right I mentioned and therefore was not allowed to discriminate, found a solution by entering into an arrangement with Japan according to which Japanese exports to the United States of specific categories of goods were "voluntarily" restricted. More than 30% of Japanese exports to the United States still fall under this arrangement. In the meantime, however, the wage-protection argument has lost much of its force. In a modern industrialized country, a rise in the

level of wages is inevitable, and the more such a country participates in the world economy, with labor becoming less abundant and labor productivity reaching standards comparable with those in other industrialized centers, the more a process of international wage adjustment will necessarily occur. In the Japanese heavy industries the level of wages for skilled male workers has now risen to about the level prevailing in Italy, i.e. about 10% lower than in Germany and 20% lower than in England. In smaller size industries, and in those in which a great deal of female labor is employed, considerably lower wages are still being paid, but the system of a double wage-standard is clearly on the decline. Although Japanese competition in Western markets remains severe, not merely on account of the remaining labor-cost differential, but also because of the high quality-standards achieved with respect to certain categories of industrial goods in which Japan has specialized, there is a growing readiness in Western Europe to include Japan in the application of the GATT. Germany, Italy, Great Britain and the Scandinavian countries have already taken this step. This does not imply that each and every Japanese export to these countries is thereby entirely freed from other than tariff restrictions, but it does mean that Japan is being recognized to a greater and greater extent as a mature industrial trading partner.¹⁾

With the increasing strength of its balance of payments position, Japan made considerable progress during the second half of the Fifties with liberalizing its own trade and payments system, which was initially severely restrictive in character. About 70% of Japanese imports are now free from quantitative restrictions, most of its bilateral trade and payments agreements have been abolished, and the yen has become externally convertible for almost all practical purposes. The formal acceptance of the obligations of the I.M.F. Agreement is presently under serious consideration.

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- 1) Compare Statements on: "Interrelation of Japanese and Western Trade Policies", Hearings before the Subcommittee on Foreign Economic Policy of the Joint Economic Committee of the U.S. Congress, 1962; also paper on: "The Pacific and the World Economic Development", published in the Saturday Review, January 12, 1963.

The alienation between the Free and the Communist World that followed the end of the second world war was anything but conducive to a favorable development of the so-called East-West trade. Initially the Soviet Union concentrated a great deal of its attention on reshaping the economic system prevailing in the East European satellite countries in its image, after its likeness, and to the reorientation of their foreign trade eastwards instead of westwards. The whole of the territory under the sway of the Soviet Union was isolated, as far as possible, from the rest of the world and, when the civil war in China came to an end and the Communists came to power in that country, the entire Sino-Soviet bloc was run along lines of economic self-sufficiency. Stalin was profoundly convinced that cutting off the capitalistic world from a market that embraced one third of the population of the globe would permanently and seriously undermine the economic position of the United States and Western Europe. Between 1948 and 1953 (the year when Stalin died) the foreign trade of the Communist bloc as a whole declined from 3.6 to 2 per cent of total world trade, which actually represented an absolute decline.

After the death of Stalin, the new Soviet regime embarked on a fresh policy in this field also. The commercial strategy of Stalin was publicly renounced, a great number of bilateral trade agreements were concluded, by both the Soviet Union and the East European countries, with industrialized countries of Western Europe and raw materials producing countries on other continents. As the result of the expansion of imports and exports thus effected, the foreign trade of the communist bloc rose in value between 1953 and 1960, from 2 to 3.8 per cent of total world trade, representing, in absolute terms, a rise from \$3 billion to \$8.7 billion. The Soviet Union's share in this trade amounted to one third, that of China to one sixth, while the East European satellite countries contributed to the extent of about one half. In 1960, trade between the various countries of the communist bloc among themselves was three times as great as the trade conducted by that bloc with the rest of the world. It is, however, worth noting that the ratio between inter-bloc trade and external trade has, since 1958, shifted in favor of external trade, namely from 4 : 1 to 3 : 1, which indicates a weakening of the autarkic trend. The foreign trade of the communist bloc in 1960 was conducted to the extent of

roughly 60% with the industrialized countries (mainly with Western Europe), while upwards of 30% of it was accounted for by trade with raw materials producing countries. Trade with this latter group of countries particularly is on the increase, which suggests a certain connection between the direction of communist trade and political objectives with respect to the less developed parts of the world.

Of the countries of the free world, the United States has shown the least interest in the commercial overtures made by the members of the communist bloc. A wide interpretation of the concept of "strategic materials" (the United States has imposed an embargo on the export of such materials to Communist countries) and a psychological aversion to everything communist would seem to provide a sufficient explanation for this. The West European countries and Japan have adopted a more liberal position in this respect, and they are exporting increasing quantities of industrial commodities and equipment to the Soviet bloc, in exchange for raw materials and foodstuffs. Trade between West and East European countries has shown a particularly marked increase. The less developed countries have in general very little reservation on this score, and many of them are glad to use the opportunities of trade with the communist bloc to exchange their primary products for goods and services which they may need, and which may be offered them, for commercial or political reasons, by the communist countries. The keen interest taken by the Soviet Union and the other communist countries, in competition with the industrialized countries of the West, in economic aid to the less developed territories, is becoming increasingly apparent in this sector of world trade.¹⁾

It is quite evident from the brief survey of recent developments in the world economy that I have just presented that, in contrast to the international economic disintegration,

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- 1) Concerning the international trade and trade policy of the Communist bloc, see: Samuel Piser: "A New Look at Trade Policy toward the Communist Bloc" (materials prepared for the Subcommittee on Foreign Economic Policy of the Joint Economic Committee of the U.S. Congress), 1961.

which was so characteristic of the period between the two world wars, a strong tendency towards economic integration has for some time been in progress in the free world, in the sense of a gradual liberalization of international trade and payments, particularly among the industrialized countries and the more developed of the primary producing countries, and that even in the communist bloc considerable efforts are being made to increase external trade. If one compares the result of this development with the image of the world before 1914, it is perhaps better to speak of a tendency towards economic reintegration. As a matter of fact, until about 1960, progress in the direction of a free-world-market economy consisted almost entirely in the removal of those restrictions to international trade which were introduced after 1914. The rehabilitation of the world economy, moreover, was and still is incomplete. There are still considerable remnants of direct trade and exchange restrictions, only a restricted number of currencies are freely convertible, and capital and labor cannot yet be as freely transferred from country to country, even between the industrial centers, as was possible before 1914. Customs tariff protection, which used to be the chief instrument of commercial policy, has even increased in significance as compared with the pre-1914 position. Between the two world wars many tariffs were raised and, in spite of the moderating influence exercised in this field by GATT, import duties continue to bear heavily on large sections of world trade. In many underdeveloped countries which are not members of GATT, the trend in tariff protection is definitely upward, in consequence of their desire to industrialize.

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According to 1960 data, by way of illustration, the average tariff on imports of industrial products was 19% in Japan, 17% in England and New Zealand, 16% in Canada, 14% in the case of the countries of the EEC (the rates imposed by Italy and France being somewhat above, and those of Benelux and Germany somewhat below, the EEC average), 12% in Australia, 11% in the case of the United States and a little under 10% in the Scandinavian countries and Switzerland. On agricultural products, with regard to which many direct import restrictions and other measures of price-protection are

1) Cf. "Trade Restraints in the Western Community" (studypaper prepared for the Subcommittee on Foreign Economic Policy of the Joint Economic Committee of the U.S. Congress), 1961.

are still in force (and are sometimes of greater significance), the average tariff was 54% in Japan, 10% in Britain, 18% in New Zealand, and 12% in Canada. As regards the countries of the EEC, the rate was 29% in Italy, 23% in Germany, 22% in France and 10% in the Benelux countries, 12% in Australia, 8% in the United States, well below 10% in the case of the Scandinavian countries and 19% in Switzerland.

Preferential tariffs play a great part in the trade between Great Britain and the countries of the Commonwealth, as well as between those countries themselves, and also between France and the former French overseas territories. Until a few years ago, the Benelux Customs Union was the only post-war example of a radical step towards complete integration of two national tariff areas.

Shortly after the second world war, a serious effort was made to reduce to a minimum, by means of broad international collaboration, restrictions on world trade, particularly in the matter of tariffs. This attempt failed, however. I am referring to the Havana Conference of 1948, from which resulted the so-called Havana Charter for an International Trade Organization. This Charter provided for a system of regulations which, if applied in good faith - for it bristled with escape clauses - should have introduced a large measure of collaboration in the economic field, not merely between the industrialized countries themselves, but also between those countries and the primary producing countries. This Charter also provided for the conclusion of international agreements aiming at stabilizing world prices of raw materials. Due to the fact, however, that it obtained an insufficient number of ratifications, the Havana Charter never came into effect. The General Agreement on Tariffs and Trade (GATT), which did become effective, is restricted to the section of the Havana Charter which relates to commercial policy, and covers even that only to a limited extent. This Agreement, to which 44 countries have now acceded, has had some measure of success, particularly in the consolidation of tariffs and in the suppression of direct import restrictions and discriminatory practices, but it, too, contains some important "escape-clauses", which are frequently invoked, and the hope that this Agreement would lead to a considerable reduction in the degree of tariff protection practised among the Contracting Parties, which, by means of the most-favored-nations clause, might have benefited other countries also, has been fulfilled only to a disappointingly small extent. Since the

Agreement came into existence, there have been repeated bilateral and multilateral negotiations in Geneva on the subject of tariff reductions, but the basic requirements for achieving results of any substance along these lines appeared to be missing.

This is not too surprising when one realizes that, since the end of the first world war, and under the impact of the painful experiences of the inter-war period, the objectives of economic policy have undergone a fundamental change. Before 1914 the view predominated, although it was held in varying degrees, that the principle of international free trade, modified by a reasonable amount of protection to weak but valuable sectors of the national economy against the effects of too severe foreign competition, automatically ensured an optimum level of prosperity. Today, it is almost generally accepted that rapid economic growth, full employment, a leveling out of the business-cycle, and the maintenance of equilibrium in the balance of payments are indispensable factors in the achievement of such an optimum level of prosperity; and that the attainment of these objectives requires an active economic policy and the utilization, if need be, of the modern policy instruments appropriate for that purpose. This has far-reaching consequences with respect to the extent to which, and the limits within which, more sophisticated countries are prepared at present to participate in a further integration of the world economy. International economic integration, as a concept of economic policy, has thereby acquired a different meaning: less stress is now laid on the removal of obstacles to free world trade and more on the building up of international communities, in which the new objectives of economic policy can be collectively pursued in the most effective manner, in functional or regional organisations. This inevitably restricts the range within which economic integration activities can display themselves successfully, as regards both their geographical extent and the policy fields they cover.¹⁾

See Lieftinck: "De Toekomst der Wereldmarkthuishouding", Tweede Druk, 1935. Also: Gunnar Myrdal: "An International Economy", 1956; Gottfried Haberler: "Die Wirtschaftliche Integration Europas in Wirtschaftsfragen der Freien Welt", 1957.

It should be acknowledged that a world economy embracing all countries, whatever their stage of development, in which free competition and market prices would completely govern the international division of labor and the distribution of income, is no more regarded by economists as the best guarantee of optimal prosperity, nor by practical politicians as a desirable, let alone realizable, ideal. A few individual voices are still raised that describe regional economic integration as a disintegration of the world economy and, as such, reject it, but this note is no longer echoed loudly. This is not to say, however, that the development of economically and politically integrated international communities should not continue to be judged on its merits from a global point of view and in the light of the interests of the human race as whole. There is every reason to be alert against too much restriction of horizons. Functional and regional integration may assist in bringing about higher levels of world prosperity, but only under certain conditions (that are tentatively laid down in the GATT). If these conditions are not met, then there is a very real danger that it may lead to serious disruption and disintegration of what has laboriously been built up in the field of world trade and world-wide economic cooperation.

I speak on the assumption that you are generally familiar with the new European organizations that aspire to a more far-reaching freedom of trade and cooperation between their members than was previously conceived of, viz. the European Coal and Steel Community of 1951, the European Economic Community of 1957 and the European Free Trade Association of 1959. As their names imply, the first two were intended as "communities" established not merely for the purpose of abolishing mutual tariffs and quota restrictions - the Coal and Steel Community for coal, iron ore, scrap and steel, the EEC ultimately for all commodities - but also of pursuing common economic policies (and coordinating social policies) both domestic and foreign, behind the shelter of a common outside tariff. The purpose of the European Free Trade Association is a more restricted one - the gradual elimination of mutual tariffs and other trade restrictions - and the Association does not act as a unity in foreign trade negotiations. In 1961, in the Western Hemisphere, two new economic organizations came into being, the General Treaty on Central American Economic Integration, which embraces all of the Central American States except Panama, and the Latin American Free Trade Association,

which counts among its members practically all South American countries and Mexico. The objective of these two regional organizations is the creation of a common market, after the European example, but they differ from the EEC insofar as their inspiration is less political and their aim less ambitious. Recently, in 1962, an Agreement for the Formation of the African Common Market was concluded between Egypt, Algeria, Morocco, Ghana, Guinea and Mali, which has goals similar to those of the Latin American organizations. 1)

It is clear that the EEC is by far the most important of these regional groups. 2) This is true from the political point of view, because the EEC intends to be a decisive step toward a federal or confederal entity in a historically divided continental Europe. But it is no less true from the economic viewpoint, because it embraces a group of heavily industrialized countries that together account for about 25% of the world trade, of which, according to 1960 data, one third consists of mutual trade and two thirds of trade with the rest of the world. This important group of countries are organizing themselves as a single economic unit; internally, with free exchange of goods and services, free transferability of labor and capital and a thorough coordination of their economic and social policies; externally, acting unitedly and, by virtue of their great production and market potential, in a very influential position as trade partners and as participants in the organization of the world economy. Whether the EEC is going to be a factor making for good or for evil, from a world economic standpoint, will, in my opinion, depend on, firstly, whether it develops as an open or a closed community as far as access of participants is concerned, and, secondly, whether in its external economic policy it is world-market-minded or rather isolationist.

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- 1) Cf. R. C. Lawson "International Regional Organisations: constitutional foundations", 1962.
 - 2) Cf. "International Trade 1961", GATT publication 1962-1965.
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The success of the EEC thus far has been impressive. During the first four years of operation (1958-1961) aggregate industrial production of the Six (Belgium was relatively slower) rose by 30% - more rapidly than anywhere else in the industrialized world except Japan. Its foreign trade rose by an average of 40%, its mutual trade by no less than 70% and its combined trade with the rest of the world by 22%. Its current balance of payments showed a large surplus and its combined foreign exchange reserves increased by several billions in gold and dollars. It is difficult, of course, to state with any accuracy to what extent this development should be attributed to the Community and to what extent it is to be explained by the high rate of growth already prevailing in the individual countries and the generally favorable business conditions which have had so marked an effect on all of Europe since 1952. The effective lowering of the internal tariffs on industrial goods did not start until the end of 1961 and is only half completed now, and the liberalization of trade in agricultural products has as yet made scarcely any progress. But the establishment of the Community as such and the first lowering of tariffs had a very noticeable effect on the industrial sector in particular. Moreover, there was considerable anticipation of complete integration on the part of both European and American industrialists.¹⁾

There is, however, little doubt that the economic growth of the EEC will not continue at the same rate as in its early years. As industrial capacity begins to exceed demand - and there are already indications of this in certain sectors - difficulties may be expected. Through the industrial concentration and specialization which the Common Market promotes, the Community's competitive position will be enhanced, but the rise of wages and social security costs, stimulated by the flush of prosperity, and the trend towards social harmonization, has a more or less compensating effect. The agrarian sector gives by far the greatest concern, because here the conflict is most acute between the high cost producing members which are staunch protectionists and the low cost producing members which want to maintain a more open door to the world market. Real Substance still has to be given to the proclaimed common agricultural

1) Cf. "The European Economic Community and the United States" paper prepared for the Subcommittee on Foreign Economic Policy of the Joint Economic Committee of the U.S. Congress, 1961.

policy, and it does not seem too pessimistic to expect that in the foreseeable future the level of protection in this field will not be reduced much below the high average now in effect. Rather the contrary. This should have a retarding influence on the process of rationalization and structural adaptation of agriculture to modern efficiency requirements and, consequently, will constitute a heavy burden on the cost of living in the Community and on the competitiveness of those industries which are still largely dependent on overseas markets.

Inevitably, the lowering and eventual elimination of national tariffs within the EEC and the introduction of a common outside tariff will cause a certain amount of trade diversion at the expense of foreign trade and in favor of internal trade. Against this direct loss of external trade, there may result an indirect gain of such trade, however, from more rapid increases of competitive and purchasing power in the Community as compared with the conditions that would otherwise prevail in the individual countries. This indirect gain may more than offset the direct loss. Whether and to what extent this will occur depends partly on the more or less protectionist character of the outside tariff. Not until this has come into full effect, its significance (particularly for the business sectors engaging in foreign trade) has been demonstrated, and more experience has been gathered about the way in which it is going to be used by the Community as a negotiating instrument vis-a-vis third parties, will it be possible to determine more definitely the consequences of the EEC on world trade.

The question whether the EEC will become an inward-looking or an outward-looking center in international trade - a distinction that is perhaps too sharply drawn and is more political and psychological than economic and structural - is of great importance not only to the business sectors concerned and living conditions in the Community but also, and by no means less, to the outside world - and especially, of course, to the countries that are to a considerable degree dependent on the Common Market for an outlet for their products. Only the former overseas territories of the members of the Common Market (and also Greece) which are admitted as associate members are secure in this regard. The countries

of the European Free Trade Association and a number of other countries in the continental perimeter are, in particular, engaged in such intensive trade with the countries of the Common Market that the existence of EEC and its future orientation in trade policy is of more than ordinary importance to their economic future. Among them, England, by far the largest industrial country of the Outer Seven, with worldwide responsibilities but a very vulnerable balance of payments, stands to lose from isolation from a strong and dynamic continent. After initially having taken a dissenting stand for economic and political reasons, when the successful realization of the EEC could no longer be doubted, England overcame its reluctance, and in the summer of 1961 applied for Common Market membership. This example was followed simultaneously by Denmark and Norway, while Sweden, Switzerland and Austria applied a few months later (15 December 1961). The rebuff with which England was recently met is sufficiently well known and I shall refrain from commenting on the political causes and consequences of this unfortunate decision. Rather I should like to draw your attention for a few more moments to the principal economic aspects of the interruption it caused in the integration process that was so well on its way in Western Europe and other parts of the world.

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The significance of the European/Trade Association must not be underestimated.¹⁾ The countries of this group, according to 1960 data, account for 16% of total world trade (of which about one sixth is mutual trade and almost five sixth is trade with the rest of the world). The countries of the European Free Trade Association carry on an intensive mutual trade with the countries of the European Common Market, 30% of total external trade of the EEC countries being with countries of the Free Trade Association and 36% of total external trade of the countries belonging to this Association being with countries of the EEC. About two thirds of the mutual trade between these groups is in industrial commodities, while one third is in primary products (foodstuffs and raw materials). Both groups have a widespread trade with the rest of the world, which is relatively more important to the EFTA-countries than to the EEC-countries.

1) Cf. "International Trade 1961", GATT-publication 1962-1965.

In this field a complication arises, in that England maintains trade relations with the countries of the Commonwealth based on special, ~~reciprocal~~ preferential arrangements and has made this cooperation subject to an effort to keep its domestic food prices down. In doing so, England's agricultural protection relies on a different technique, namely, the granting of direct farm-subsidies instead of the technique of the levying of autonomous customs tariffs, which is still being applied by the high cost producing countries of the EEC, but will soon be replaced by a system of common variable levies. To integrate England with the continental system, which would mean giving up the preferential system in its trade relations with the other countries of the Commonwealth, is a difficult problem, but England was prepared to collaborate to find a reasonable solution for it. The overseas countries of the Commonwealth, for their part, have abided by the British decision, though reluctantly, in the expectation of English support of their interests in regulating their trade relations with an enlarged European Economic Community. These efforts would, of course, be directed towards a moderation of the continental system of agricultural protection, permanently, or at least for a transitional period which would give them the opportunity to adjust. They were also promised that the preferential treatment granted by them to England would become available as a negotiable instrument in seeking new outlets for their products in the EEC and other countries. Finally, they were given the hope that a stronger Europe could make a greater contribution to meet their capital needs for development. The complication presented by the preferential treatment that France applies to products from its former colonial territories was, automatically, removed by the association of those territories with the EEC.

As a step in the direction of further integration of the world economy, a unification of the EEC and the EFTA would be of monumental significance. With a total population of about 250 million and an average national per capita income of over \$850, the countries of this region together are responsible for about 45% of world trade. Their mutual trade accounts for nearly 18% of total world trade and 30% of world trade in industrial goods. Together they constitute a large industrial center, the oldest in the world, that has attained

its present structure over a long historical process of relatively free development. Though spread over a number of countries, it is closely knit, thanks to exceptionally good harbors, short distances and rapid communications. It is a center where, despite differences of opinion as to the most appropriate methods and instruments to be applied, there is a great deal of consensus on the objectives of modern economic policies. The integrating influence exercised already over many years by the OECD is quite noticeable on this score. The cutting of this region into two separate parts may be compared to the splitting of an economic nucleus, resulting in the release of centrifugal and competing energies, the beginning, though not the end of which, can be seen. In particular, there is a danger that the inward-looking elements in the EEC will gain the upper hand and that the EFTA will concentrate to an increasing degree on trade with other parts of the world and turn away from the continent.

Perhaps this development would not be unwelcome to the countries of the Commonwealth over the short term, but, in my opinion, it is questionable that over the long term, with their industrialization developing, they would find much advantage in it. For Africa, where a number of the many new states have a strong orientation toward France, and others toward England, the entry of England into the EEC would presumably have meant equal treatment on the European markets and provided better prospects for internal and external cooperation among the larger part of the African countries. But all this now appears in a different light.

Again, for the economic relations between Europe and the United States, the recent events on the European scene have far-reaching consequences. Greatly stimulated, if not inspired, by the establishment of the EEC, and in anticipation of England's entry into this organisation, American trade policy has recently been thoroughly reappraised. By the Trade Expansion Act of 1962, the President was authorized to negotiate tariff reductions to 50% of the present level in relations to all imported goods (separately or in categories) and even to reduce the tariff to 0 in respect of certain goods that for 80% or more of their total share in world trade originate in the EEC (including England) and the United States - both on a reciprocal basis. The 80% clause applies particularly

to commodities that occupy a large place in the mutual trade between the United States and the EEC countries. Traditionally, however, any American tariff concession will automatically be extended to other countries with which the United States has concluded a most-favored-nation-agreement. The President was also empowered to reduce or even abolish the tariff in respect of tropical and forest products from underdeveloped countries, in case the countries of the Common Market take a similar step. To permit the sectors of American business that would be affected by a sudden influx of foreign goods under a lower tariff to adjust themselves, important financial and other provisions were promised.¹⁾

The new trend set for American trade policy by the Trade Expansion Act clearly opens up broad perspectives for a further integration in the world economy, provided that the United States' initiative is implemented with imagination and realism and meets with sufficient goodwill on the part of its trading partners. The United States and Canada and the extended European Common Market together account for 90% of all industrial production in the free world. A trans-Atlantic fusion of these two great industrial nuclei would generate a mighty quantity of economic energy and trade. At present 30% of the foreign trade of the United States is directed toward Western Europe and about 12½% of West-European trade is directed to the United States. It can be assumed that this could be extended considerably, to the advantage of world trade in general. It is clear, however, that the refusal to admit England and the other members of the European Free Trade Association into the EEC has dealt a blow to these conjectures, not merely because the 80% clause has practically lost its significance, but also because the United States is now in the position of having to deal with a number of European bargaining partners, the largest of which, little Europe, is under the dominating influence of a continental concept, with all its economic consequences. I shall not expand further on this, but at the moment it would seem that the American vision of a broad Atlantic economic integration has largely lost its foundation.

1) See also President Kennedy's Message to Congress of January 25, 1962; and: "Trade Adjustment in Theory and Practice", paper submitted to the Subcommittee on Foreign Economic Policy of the Joint Economic Committee of the U.S. Congress, 1961.

It is perhaps appropriate at this point to say a few words about the most recent developments in the Western Hemisphere. I mentioned the establishment of two new economic associations in Central and South America. While I do not think that too much can be expected of these organizations since they embrace non-complementary, chiefly raw material producing countries, they could play a useful role, particularly in directing the industrialization process, in which these countries are busily engaged, along not too artificial lines. There is, however, another matter of more immediate importance. I am referring to the establishment in 1961 at the Punta del Este Conference of the Alliance for Progress, for the purpose of strengthening the economic cooperation between the United States and the countries of the southern part of the Western Hemisphere.¹⁾ This Alliance is inspired by the consideration that the economic and social development of Latin America cannot and should not continue to be supported unilaterally by United States aid, but that a common effort is required which should extend even to the field of trade policy, and should aim at an intensification of mutual trade in the broader framework of a closer cooperation between the less developed and the highly industrialized countries of the free world. Among other things, the purpose was set to improve the terms of trade between primary and industrial products and to promote a further liberalization of international trade, particularly in respect of the industrial sector, which would be reflected in a more rational international division of labor. It was hoped that a united Western Europe would participate in such a policy. The Trade Expansion Act which I mentioned earlier is partly an offshoot of the aims of the Alliance for Progress. There is little doubt that the United States, despite the setback in Europe, will try to continue its progressive policy in the Western Hemisphere, but it will now probably be unavoidable to look for solutions more on a regional basis.

In the eastern Pacific, the urgency for a reevaluation of Australia and New Zealand because of the imminent loss of their preferential position on the British market has for the time being diminished. On the other hand, the

1) See "The Alliance for Progress" edited by John C. Dreier, 1962.

chances of these countries being able to find markets for their principal export products on the European continental market on more favorable terms have also diminished. Their attempts to achieve more diversification of their production and export pattern will no doubt be continued and trade with South East Asia and Japan will certainly be of growing importance to them. More generally speaking, I think it is far from being ruled out that with less opportunities to expand trade in the Atlantic region, a new impetus will emerge to establish a closer cooperation in trade and trade policies between the countries on the Pacific, including perhaps even China.

The results of the European impasse on trade relations between the free world and the Soviet bloc are the most difficult to judge. A few tentative conclusions may, however, be drawn. Firstly: the efforts of the United States toward a common, extremely restrictive policy of the Atlantic partners as regards the so-called East-West-trade, which are already encountering increasing opposition, will surely not be more loudly echoed in the different European camps. Each camp will probably be more and more inclined to have its own way. Secondly: the possibility of establishing a united front of all of western Europe in trade negotiations with the Soviet bloc seems more remote than ever. Thirdly: the less agreement there is in the West on seeking constructive solutions in the field of trade, for the problems of the underdeveloped countries, the more inclined those countries will be to accept the alternative possibilities offered them by the Soviet bloc. Finally: the prevailing trend in Western Europe, following the example of the United States and the Soviet bloc, of giving preference to bilateral over multilateral forms of aid to underdeveloped countries, which is disruptive of competitive world trade, will probably receive increasing emphasis.

I shall not attempt any further predictions, nor venture to express a personal view as to whether there is a reasonable prospect that there will occur at some time a breakthrough of the European impasse. The only comment on this topic I feel free to make is that even the Carolingian era, which lasted long, did not last forever.

I thank you for your attention.

February-March 1963