Morgan Guaranty Trust International Council,
June 16, 1972 (vol 1)
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Folder 12

Morgan Guaranty Trust
International Council - June 16, 1972

July 24, 1972

Mr. Alfred H. Von Klemperer
Senior Vice President
Morgan Guaranty Trust Company of New York
23 Wall Street
New York, New York 10015

Dear Mr. Klemperer:

It gives me great pleasure to acknowledge receipt of Morgan Guaranty Trust Company's $1,000 check which you forwarded in recognition for the assistance given you by Robert McNamara.

We are deeply grateful to both you and Mr. McNamara for this generous gift. Unrestricted contributions to the School are especially needed and we appreciate it very much.

Please accept our warm thanks.

Sincerely,

Lawrence E. Fouraker
Dean

LEF:PKM

cc: Mr. Robert S. McNamara

bcc: Financial Office
Howard Whitmore
E. A.
PKM

HARVARD UNIVERSITY

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION

GEORGE F. BAKER FOUNDATION

OFFICE OF THE DEAN

SOLDIERS FIELD
BOSTON, MASSACHUSETTS 02163

July 24, 1972

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

Dear Mr. McNamara:

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We are very grateful to you for your thoughtfulness and generosity in having this check sent to the School. Please accept our warm thanks for this unrestricted gift in support of the School's programs.

You continue to be such a good friend to the School and we appreciate your support and interest. Many thanks.

Sincerely,

Lawrence E. Fouraker

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LEF:PKM

President has seen

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Lawrence E. Fouraker
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President has seen

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COMMUNICATIONS SECTION

DRAFT 6/3/72

Informal Comments -- Morgan Guaranty Trust International Council

When Tom first asked me to speak to you today on the needs of the developing countries, particularly as they relate to the potential for trade with and investment in those nations, I was reluctant to do so. I feel quite uneasy in trying to forecast anything relating to the future of those nations. However, let me start by sketching their problems as I see them, and then we can turn to your questions and comments.

I. Their Present Status

I shall be referring to the 95 developing countries which are members of the World Bank -- essentially all of the developing nations of the world excepting those of Eastern Europe, North Vietnam, and North Korea.

They are populated by approximately 2 billion people with an average per capita GNP of $180 per annum (compared to approximately $3000 in the U.S.). In their world:

. Malnutrition is common.

The FAO estimates that at least a third to a half of the world's people suffer from hunger or nutritional deprivation. The average person in a high-standard area consumes four pounds of food a day as compared with an average pound and a quarter in a low-standard area.

. Infant mortality is high.

Infant deaths per 1000 live births are four times as high in the developing countries as in the developed countries (110 compared with 27).

. Life expectancy is low.

A man in the West can expect to live 40% longer than the average man in the developing countries and twice as long as the average man in some of the African countries.

. Illiteracy is widespread.

There are 100 million more illiterates today than there were 20 years ago, bringing the total number to some 800 million.

. Unemployment is endemic and growing.

The equivalent of approximately 20% of the entire male labor force is unemployed, and in many areas the urban population is growing twice as fast as the number of urban jobs.

. The distribution of income and wealth is severely skewed, and in some countries becoming more so.

In India, 12% of the rural families control more than half of the cultivated land. In Brazil, less than 10% of the families control 75% of the land. In Pakistan, the disparity in per capita income between East and West, which amounted to 18% in 1950, became 25% in 1960, 31% in 1965, and 38% in 1970.

. The gap between the per capita incomes of the rich nations and the poor nations is widening rather than narrowing, both relatively and absolutely.

At the extremes that gap is already more than $3,000. Present projections indicate it may well widen to $9,000 by the end of the century. In the year 2000, per capita income in the United States in terms of today's prices is expected to be approximately $10,000; in Brazil, $500; and in India, $200.

One particular feature of the present situation deserves special emphasis: the burgeoning population of the developing nations.

Including the Peoples Republic of China, the LDC population in 1970 was about 2.5 billion. By 1980 it will increase at least 27% to 3.2 billion and by 2000 to a probable 5 billion.

The rapid growth of population means:

. continued heavy pressure on public services, educational and health facilities, and the further rapid growth of cities and their slums;

. absorption of the increases in the labor force will become more difficult and growing unemployment likely.

It is clear, I think, that a rapid rate of economic growth throughout the developing world is needed both to improve the lot of the present population, hundreds of millions of whom barely exist on the margin of life and to permit the absorption of the population explosion that it is too late to avoid.

II. The Past Record

Overall the growth rate in the 1960s was impressive historically, averaging 5% per year, but the poorest countries (per capita incomes of less than $200) with over 67% of the LDC population, grew at only 3.9%.

And the differences between the poorest of the developing countries and all others were even greater after population growth is taken into account. Per capita income during the 1960s, in the poorest countries with 67% of the population, grew at only 1.5% annually. In contrast, GNP per capita in the major oil exporting countries, which account for 4% of the population, rose 5.2% per year.

III. The Future Requirement for Growth

The developed countries have generally agreed that in contrast to the 5% GNP growth rate of the 60s, they should assist the LDCs in achieving a 6% rate of growth in the 70s and that objective begins to set the requirements for Aid and Trade.

IV. The Need for Aid

The Pearson Commission and others have estimated that to support a 6% growth rate concessional aid from governments would have to amount to .7% of GNP by 1975. It is now about 1/2 of that, and there is no likelihood it will rise above .35% by 1975, and unless there are prompt and marked changes in attitudes, it is difficult to foresee any great improvement in the second half of the decade.

The consequences of this deficiency are clear:

- The deficit in concessionary aid will penalize the poorest countries, containing the bulk of the people, the most. They will not be able to achieve the growth objective.
- But even for those LDCs which are somewhat better off, the low level of concessionary aid will force them to seek other forms of external finance at higher rates and shorter terms. Under these circumstances, mounting debt problems for the developing world are inevitable.

Since the mid-50s, publicly guaranteed debt of the LDCs has been growing at about 14% per year. At the end of '71 it stood at over $60 billion and annual debt service exceeded $5 billion. Debt service has been growing at the same annual rate as the debt: 14%, twice the rate at which export earnings, from which the debt must be serviced, have been growing. Such a relationship cannot continue indefinitely.

V. The Requirement for Trade

If the LDCs are to offset shortfalls in concessionary aid and keep debt burdens within manageable proportions they must expand their export earnings.

The general outline of the problem is clear. There are 3 broad categories of LDCs:

- Those countries which export fuel -- fuel accounts for 1/3 of all export earnings but 3/4 of the earnings revert to 6 countries with 3% of the population.
- Those countries, many with very low income, which remain highly dependent on agricultural products.
- Those countries which have the possibility of increasing their earnings through exports of manufactures.

The inelasticity of demand for agricultural raw materials means that the growth of consumption of such products is not likely to exceed 3 to 4% per year. But even for LDCs dependent on such exports the developed countries can provide assistance. Three quarters of the LDCs agricultural exports compete with products produced, often with high subsidies (note sugar in the US and meat and butter in EEC), in the developed countries. Gradually, over time, such subsidies should be removed in the interests of both LDCs and DCs. Moreover the LDCs would benefit substantially from the extension of stabilization agreements beyond coffee to cocoa and other commodities and financial assistance to support such agreements.

For the countries with capabilities for manufactured exports -- with populations totalling over one billion -- we have estimated that achievement of the 6% growth rate requires an increase in their export earnings of nearly 10% per year, and this in turn necessitates an increase of their manufactured exports of 15%.

Such a rate was achieved in the 60s when manufactured exports of LDCs grew from $2 billion in '60 to $7 billion in '70.

What is needed in the 70s is that the momentum be maintained. The LDCs have a natural comparative advantage in products with a high labor input: textiles, garments, footwear, vegetable oils, processed foodstuffs, plywood, furniture, glassware, wooden products, electronic sub-assemblies.

But there are two problems:

- The developing nations have clung too long to inward-looking, import-substitution policies resulting in high cost operations carried out behind protective trade barriers.
- The developed countries discriminate against imports from LDCs in a number of ways -- e.g., they maintain higher tariffs on the manufactured goods the poorer countries support than on manufactures from DCs (on manufactured imports from rich and poor nations tariffs were:

US 7% and 12%; in the UK 9% and 14%; in the EEC 7% and 19%); further tariffs rise with the degree of fabrication: in the US there is no duty on hides but 5% on leather and 10% on shoes. In the EEC cocoa beans from non-associated countries 3% duty vs. 18% on processed cocoa products; and even more repressive is the whole series of restrictive non-tariff barriers (quotas, subsidies, etc.) the DCs have erected over the years (the US now restricts cotton textiles, shoes, ceramic tiles, beef, flatware, rolled steel, plus a long list of agricultural products). The growth in restrictions is in the products in which the LDCs initial export production is most likely.

The LDCs must realign their industrial policies by liberalizing their import regime, by supplying local credit on more reasonable terms for export-oriented industries, and by maintaining realistic exchange rates.

The DCs must move from excessive protectionism to more equitable and less restricted import policies.

In this connection, the proposed General System of Preferences (adopted by Japan, the Nordic countries, and the EEC, but not by the US) is a step forward. But it is a small step -- in total it is unlikely to increase LDC exports by as much as $1 billion per year. In contrast, if their exports are to grow 15% per annum through the decade, they must rise from $7 billion in '70 to $28 billion by '80 (at $28 billion the imports into the DCs would amount to only 7% of their manufactured imports and less than 1% of their GNP).

Such an expansion of trade would be beneficial to both parties but the short-term pains of adjustment will be severe. And much of the rising tide of protectionism springs from the fears of those whose jobs and investments will be displaced.

It is a political fact of life that the DCs must adopt realistic policies to cushion the impact of import competition by retraining, relocation, and refinancing.

Few have done so and certainly not the U.S. Until this is done, labor and management opposition and trade liberalization will be great -- and justly so.

VI. The Role of and Outlook for Private Investment

There is a substantial annual flow ($2.5 billion) of direct private investment to LDCs, but it is heavily concentrated in a few regions and in a small number of industries. It makes an important contribution to financial resources and to transfers of technology and management skills. Yet the climate for private investment has deteriorated. LDCs do not consider the open-ended return of capital justified, particularly in industries where technology changes slowly. More and more countries are limiting the areas for foreign investment or require gradual transfer of managerial control. Increasingly, the LDCs will explore whether the same productive capacity and employment opportunities cannot be created at a smaller cost to them. Their alternatives range from long-term supply contracts for raw materials in exchange for capital and technical assistance in extraction and processing industries to portfolio investments in LDC corporations.

Even given the most optimistic assumptions for aid and trade during the remainder of this decade, the probability of widespread political instability in the developing world throughout the remainder of this decade is great. And the problems that will create for private investment will be compounded by a rising tide of nationalism. It is these two forces which have led to the recent spate of nationalization of private investments. Almost surely more lie ahead.

But that isn't to say there is no further opportunity for private investments in the LDCs. They represent a huge and expanding market. Moreover, we do live in an interdependent world (Japan will need to import, by 1980, 30% of the world's production of 6 or 8 of the major raw materials) and we must learn to conduct business in such an environment.

Multinational companies are particularly vulnerable to the tides of nationalism, but their vulnerability can be reduced by making them more truly multinational in ownership, management, and control and by ensuring that they fully take account of the effects of their operations on the economy of the country in which they are operating.

Investment risks can be highly selected, diversified geographically, insured governmentally, protected against by taking advantage of international arbitration conventions, and shared with such organizations as IFC.

There are signs that these matters are being thought about -- but not enough. In Japan, the Ministry of International Trade and Industry is drawing up a code designed to ensure that multinational corporations will harmonize their policies with those of the countries in which they operate. But efforts to develop in the OECD uniform policies to be followed by the developed countries in protecting the investments of their citizens have come to naught and each government continued to go its own way.

VII. Conclusion

In sum, if development is to be effective, i.e., if it is to improve the lives and opportunities of the 2 billion people in the LDCs, important changes, by both the developed and developing countries, affecting aid, trade, and investment are necessary. There has been little progress recently in addressing these issues.

MORGAN GUARANTY INTERNATIONAL COUNCIL

New York City, June 16, 1972

Members who attended:

The Rt. Honorable Lord Shawcross, Chairman

Thomas S. Gates, Vice Chairman

Stephen D. Bechtel, Senior Director, Bechtel Corp, San Francisco

Harry O. Bercher, Director, International Harvester Co., Chicago

Fred J. Borch, Chairman, General Electric Co., New York City

Jorge Born, Chairman and President, Bunge & Born, S.A., Buenos Aires

Vasco T. Leitao da Cunha, Rio de Janeiro, Brazil

Hobart Lewis, President and Editor-in-Chief, The Reader's Digest Association, Inc., Pleasantville, N.Y.

Roger L. R. Martin, President, Compagnie de Saint-Gobain-Pont-A-Mousson, Paris, France

Maersk McKinney Moller, A. P. Moller, Copenhagen, Denmark

John H. Moore, President, Brascan Limited, Toronto, Canada

Robert D. Murphy, Honorary Chairman, Corning Glass Intl., New York City

Donald S. Perkins, Chairman, Jewel Companies, Inc., Chicago

Pol Provost, Chairman and President, N. V. Houtindustrie de Coene & Co., Kortrijk, Belgium

George Russell, Director, General Motors Corporation, Detroit

William S. Sneath, President, Union Carbide Corp., New York City

Juan T. Trippe, Honorary Chairman, Pan American World Airways, Inc., New York

William S. Vaughn, Director, Eastman Kodak Co., Rochester, N.Y.

Dr. Alberto J. Vollmer, Central El Palmar, S.A., Caracas, Venezuela

Dr. Giorgio Cappon, General Manager, Institut Mobilaire Italiano, Rome

Edward R. Kane, Senior Vice President, E. I. DuPont, Wilmington, Del.

5-15

MORGAN GUARANTY TRUST COMPANY
OF NEW YORK
23 WALL STREET, NEW YORK, N.Y. 10015

THOMAS S. GATES

New York

March 15, 1972

Ernie will meet with Van Klemperer 4/11

Mr. Robert S. McNamara, President
International Bank for Reconstruction
and Development
1818 H Street, N.W.
Washington, D.C.

Dear Bob:

I am glad and grateful that you will participate in the meeting of our International Council. We will have in mind your wishes concerning the nature of your presentation. We will circulate prior to the meeting a briefing paper laying out the various trade, financial and political issues involved and a number of our members will be prepared to contribute to the discussion with a specialized knowledge of specific points.

My colleague, Alfred Von Klemperer, who acts as Executive Secretary of the Council, will be working on the preparation of the program. With your permissiDn I have asked him to be in touch with your secretary to get the name of a member of your staff with whom he can coordinate his work to take into account the World Bank's thinking on the subject.

I would like to invite you cordially to attend, if convenient, the dinner which we are giving for the Council on the preceding night, June 15th, to which we also invite our Board of Directors. In fact, you are more than welcome to be our guest for the program during that day when we will have a session on "The Effects of Today's Changing Social Climate on Corporations", a presentaion on the U.S. political scene (hopefully Stewart Alsop) and a briefing session by our own people on the U.S. economy and financial markets and on the effects of the Smithsonian agreements on foreign exchange markets.

We will be in touch with you again well before the meeting.

Sincerely,

Tom Gates

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MORGAN GUARANTY TRUST COMPANY
OF NEW YORK
23 WALL STREET, NEW YORK, N.Y. 10015

THOMAS S. GATES

New York February 23, 1972

Mr. Robert S. McNamara, President
International Bank for Reconstru-
ction and Development
1818 H Street, N.W.
Washington, D.C

Dear Bob:

About three years ago you were our honored guest at a meeting of our International Council of which I am now Vice Chairman. I wonder whether you would be willing to participate in a more formal way in our next meeting on Friday, June 16th. We plan to use most of that day for a session under the general heading of "The More Important Problems in International Finance and Trade". We would not try to cover the whole countryside but would concentrate on such specific subjects as non-tariff barriers, the enlarged EEC, GATT revisions, the Hartke/Burke Bill and American "protectionism", and European attitudes towards American investments. We hope to have a U.S. government official and, if we can get him, an EEC Commissioner to take the American and European points of view for this discussion. In the second, related part of this session we would have a discussion on some of the key needs of the developing countries. This would include tariff preferences for the developing countries, the effect of nationalization and expropriation in developing countries, the role of arbitration in international investment disputes, the ability of developing countries to compete with the industrialized nations in international trade and to what extent, if at all, SDR's should be used for aid purposes.

It would give us great pleasure if you could make the introductory remarks to the section dealing with developing countries. You will remember that we do not have formal speeches from the guests but merely informal remarks lasting not more than twenty minutes. There will be considerable time for discussion in which our speakers participate at their

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MORGAN GUARANTY TRUST COMPANY
OF NEW YORK
23 WALL STREET, NEW YORK, N.Y. 10015

THOMAS S. GATES

New York
February 2?, 1972

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entire pleasure - usually very actively. These are off-the-record meetings with no record kept of the proceedings.

For your information I enclose copies of the last three programs and a copy of our latest Annual Report which on the inside of the back cover lists the Council members.

Pat Patterson joins me in extending this invitation to you and we hope very much that you will be able to accept.

Best wishes.

Sincerely,

Tom Gates

Enclosures