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# INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

**Washington, 25, D. C.**

**PRESS RELEASE—Third Annual Report** **CONFIDENTIAL**
**HOLD FOR RELEASE Until 10:00 A.M.**
**Washington Time, Wednesday Sept. 29, 1948**

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The Third Annual Report of the International Bank for Reconstruction and Development, as approved by its Executive Directors, was presented to the Board of Governors at their annual meeting in Washington today by the Bank's President, John J. McCloy. Its financial sections cover the fiscal year ended June 30, 1948; other sections of the report deal with the accomplishments of the Bank through August 31, 1948. It also analyzes major economic problems facing various areas of the world and suggests certain lines of action to meet these problems.

## ACTIVITIES OF THE BANK

The report points out that the Bank embarked on several new types of financing operations during the past year. It authorized the granting of its first credits for development purposes, in two loans to Chile. The pattern set by this financing, the report states, is promising.

The year also witnessed the Bank's first loans to private enterprises and its first use of its guarantee powers, in loans to four leading Dutch shipping companies secured by mortgages on ships, with the subsequent sale to a group of private United States banks of the greater part of the notes evidencing the loans under the guarantee, as to principal and interest, of the International Bank.

The total loans made by the Bank are: $250 million to France and $195 million to the Netherlands, made during the period covered by the Second Annual Report; and the following during the period covered by this report: $40 million to Denmark; $12 million to Luxembourg; $16 million in two loans authorized to instrumentalities of the Chilean government, which loans are to be guaranteed by the government of Chile; and, $12 million in six loans to four Dutch shipping companies—a total of $525 million.

With regard to the uses to which loans have been put, the report states that most of the disbursements were made for the purpose of assisting in financing large general programs of reconstruction by supplying essential capital goods such as industrial and agricultural machinery; equipment for transportation systems, steel mills, etc.; as well as basic raw materials. While most of the expenditures financed by the Bank's loans were made in the United States, substantial amounts were spent in other countries. As of June 30, 1948, out of the $470.1 million disbursed by the Bank, the areas of expenditure in round figures were as follows: $356.4 million in the United States;

$50 million in Latin America; $12.5 million in Canada; $47.7 million in Europe; and, $3.5 million in Africa, the Near East and Far East.

One of the significant developments of the past year has been the establishment of procedures whereby the Bank carries out the mandate of its charter to ensure that the proceeds of any loan are used only for the purposes for which the loan was granted. As the first step in this system of supervision, the Bank requires that the proceeds of a loan are subject to withdrawal by the borrower only upon satisfactory certification that expenditures have been or will be made for the purchase of the specific goods or services authorized in the loan agreements. Subsequently the Bank conducts an investigation, generally carried out in the borrowing country by the Bank's field representatives, of the end use to which the goods are put.

In addition to loans already made, there has been an impressive increase in the number of projects brought to the Bank for its consideration. Covering a great variety of fields, these include such projects as power developments, transportation and communication facilities, irrigation and other agricultural projects, migration programs, mining development, shipbuilding and industrial plants. The Bank has sent missions of investigation to 13 countries in Latin America, Europe, the Middle and Far East, and a number of similar missions are planned for the near future. Altogether, the report states, active discussions are now being conducted concerning productive projects in more than 20 of the Bank's member countries.

During the past year there have been encouraging developments also in connection with the creation of a broader market for the Bank's bonds. The Bank sold its first non-dollar bonds—an issue of 2½% Swiss Franc Serial Bonds amounting to 17 million francs (approximately $4 million), which was purchased in its entirety by the Bank for International Settlements at Basle, Switzerland. Although up to the present time the Bank has had ample funds for its loan operations, the report states that from a long-range viewpoint it is clearly desirable that the Bank should supplement its borrowing in the United States by tapping other sources of capital.

The financial statements for the fiscal year, ended June 30, 1948, show an excess of income over expenses of approximately $4 million. This was sufficient to eliminate a deficit of some $1 million existing on June 30, 1947, and provide a net profit of approximately $3 million on June 30, 1948.

In spite of its activity in these varied fields, full realization of the Bank's potentialities cannot be expected, the report states, as long as economic and financial stability in large areas of the world continues to be threatened by political tensions and unrest.

"By developing its activities in different directions," the report says, "both with respect to the size and character of its loans and with respect to the techniques it employs to channel capital into productive international investment, the Bank has grown in flexibility, strength and stature. As it continues to acquire experience and to gain the confidence of its members, the Bank should gradually be able to play an increasingly effective role in helping to raise production levels and living standards throughout the world."

## THE SITUATION IN EUROPE

Loans which the Bank has already made to Europe, by permitting the borrowing countries to sustain for a time the necessary volume of essential imports, according to the report, have helped prevent a disastrous drop in production and possible economic collapse. The Bank has been fully aware, however, that these loans, vital as they were, provided only a partial solution to Europe's problems. It has been clear for some time that United States financial assistance to Europe, in the form of the European Recovery Program, would greatly exceed for the time being any amounts which the Bank might lend.

ERP funds are being used primarily to furnish urgently-needed food, fuel and raw materials. The report points out, however, that the fundamental need of Europe is for a far-reaching reorganization of its economy. It will not suffice, the report says, to restore European production and trade as they existed before the war. The magnitude of Europe's problems makes thinking in pre-war terms unrealistic. New and bold concepts are required if Europe's fundamental weaknesses are to be corrected and new sources of strength provided. The volume of production must be greatly increased, the costs of production substantially reduced, and there must be a reorientation of Europe's trade channels to conform to the fundamental changes which have taken place in world conditions. The basic objective of ERP, the report says, is to enable Europe, by its own efforts, to achieve a fundamental readjustment in the structure of its economy.

The report continues: "The effect of ERP cannot, therefore, be measured either by the particular types of goods it enables Europe to import, or by the specific uses to which those particular goods are put. The test is a much more fundamental one. It is whether the European countries participating in the program, during the period while ERP funds are available to help support their consumption standards, will be able to use the opportunity thus afforded to expand, modernize and reorganize their productive mechanisms and to effect the necessary changes in the pattern of their trade."

Reduction of the balance of payments deficits of ERP countries by 60% to 75% by 1952—which is the stated goal of ERP—may well appear difficult, the report says, but is a minimum requirement. If by the end of the ERP period these countries are to become independent of extraordinary outside aid, the report states, more must be accomplished than has yet been faced up to. The measure of accomplishment must be what is necessary, rather than what has been possible in the past.

Among difficulties facing Europe the report lists the "plague" of world-wide inflation, shortages of goods, governmental expenditures for purposes not directly productive, and lack of firm financial policies. It says substantial opportunities exist to increase industrial output through better management techniques, the standardization, concentration and specialization of production, removal of unnecessarily restrictive trade union practices, and in some cases longer hours of work.

There is also need for a substantial program for modernization and expansion of Western Europe's plant and equipment. This cannot be accomplished, the report says, without the continued diversion of a considerable part of production from consumers' to producers' goods; and while such a policy is severe, ERP countries cannot become self-supporting by 1952 unless they maintain the discipline necessary to carry it out.

The report stresses the importance of freeing intra-European trade. Trade barriers in whatever form, it says, tend to breed productive inefficiency, and unless the markets for European products can be broadened and greater freedom of intra-European trade attained, the hope for ultimate European recovery will be dimmed and the opportunity afforded by ERP will be lost.

It continues: "Unless the Western European countries can, by union or otherwise, find the key to unlock the gates which now obstruct the free flow of goods, manpower and capital among them, there is grave doubt whether they can in the foreseeable future sustain their peoples at a standard of living approaching prewar levels."

With regard to the problem of Germany, the report says that the low level of production in Bizonia—still only about 50% of prewar levels—has been due primarily to chaotic monetary conditions, the almost complete disruption of trade connections, and the over-all political uncertainty. It says that the condition of Germany has direct and immediate repercussions on the economic situation in the rest of Europe.

The shift in world trade patterns is another factor which affects Europe. Before the war Western Europe normally depended on its trade with the Far East, particularly Southeast Asia, to provide it with dollars to finance its import surplus from the Western Hemisphere. The report points out that this situation no longer obtains, and says that the long-run need is clearly for Europe both to increase its exports to the dollar area and to decrease its imports from that area.

As to the Bank's proper role during the ERP period, the report states that two points furnish a significant indication of this. The first is the necessity that the ERP countries maintain as high a rate of investment as is compatible with monetary stability. The second is the insufficiency of ERP funds to meet all of Western Europe's investment requirements. It was expressly assumed, in determining the amount of United States aid, that the Bank would advance substantial credits to Western

Europe during this period. The report continues:

"It seems clear, therefore, that there is a real need for Bank financing in addition to the financial assistance made available by the Economic Cooperation Administration. Furthermore, since the first claim on ERP funds will be necessarily for those imports most immediately essential, the long-range investment field seems obviously the one most appropriate for Bank assistance."

The Bank intends to supplement ERP, the report says, to the extent that the Bank's resources and the credit standing of ERP countries permit, primarily by financing projects which involve permanent additions to Europe's productive capacity, and which will stimulate trade. It will also ensure that such projects are consistent with any over-all investment program formulated by the Organization for European Economic Cooperation. It is not possible to estimate the extent of possible Bank assistance at the present time. To the extent that ERP funds are made available in the form of grants rather than loans, and that loans out of ERP funds are made on terms which do not interfere with Bank financing, ERP aid will facilitate rather than impede the Bank's operations in ERP countries.

The report states that the Bank believes there are substantial opportunities for the development of the productive resources of its member countries in Europe which are not participants in ERP. It is unfortunate but nonetheless true, it continues, that existing political difficulties and uncertainties which may have a direct effect on the economic and financial conditions in those countries present special problems which have thus far prevented the Bank from making loans in those countries. The Bank hopes, therefore, that the existing uncertainties can be clarified to an extent which will enable it to render financial assistance in the development of such countries, which will be of benefit not only to them but to Europe generally.

There is a clear inter-dependence, the report says, between European recovery and economic progress in the rest of the world. The rehabilitation of Europe, by providing both an increased source of supply for the goods needed for development and further industrialization of such other areas as Latin America and Asia, and an increased market for their products, will contribute substantially to their prosperity. Equally, the further development of other areas of the world, as both a market and source of supply, is essential to the long-run economic well-being of Europe.

## LATIN AMERICA, ASIA, AFRICA, MIDDLE AND FAR EAST

The Bank's continued interest in assisting European recovery has not prevented a definite increase in its activities in other parts of the world during the past year. In the long run, the report states, the problems of the Bank's underdeveloped member countries will undoubtedly constitute its primary concern.

Apart from the two loans to Chile for hydro-electric and agricultural development, several other development loans are in an advanced stage of negotiation, and discussions are in progress with regard to other projects in many different countries. Nevertheless it remains true that the number of sound, productive investment opportunities thus far presented to the Bank is substantially smaller than was originally expected.

The report attributes this fact in part to the length of time required to complete engineering and other technical studies necessary to bring projects up to the point where they are ready for financing. In large measure, however, it reflects other specific difficulties: the lack of economic, financial and in some cases political stability; lack of local capital; lack of technical skills and trained managerial personnel; lack of planning. It shows clearly that sound development requires much more than simply making available large sums of money.

For almost all underdeveloped countries, the report says, it is necessary to secure help from foreign technicians and also to institute programs of technical training to build up an adequate local supply of skilled personnel. Direct investment by foreign business enterprises has the special advantage of supplying technical and managerial skills, as well as capital.

Defining the Bank's role in the development field, the report states:

"The Bank is convinced that its resources cannot be used effectively to expand production and to raise living standards unless they are invested in well-prepared and well-planned projects. It is also convinced that sound development is best promoted, not by sporadic injections of large amounts of capital, but rather by a steady flow of capital in moderate amounts. The Bank's approach to its underdeveloped member countries has been framed accordingly. That approach is one of willingness to help its members to analyze their development problems, to work with them in mapping out the broad lines along which their development may be advanced most soundly and rapidly, and whenever possible to select for initial financing those projects which seem most likely to contribute to such advance. Where economic or financial conditions in the borrowing country are such that they endanger the productive purposes and the repayment prospects of a Bank loan, such a loan will normally be conditioned upon measures designed to bring about financial and monetary stability and, where necessary, re-establishment of the country's credit. This approach by the Bank necessarily varies from country to country."

It is important for an underdeveloped country, the report states, to work out an over-all development program in order to minimize spotty and wasteful investment. Such a program should be based on the existing natural resources, the country's location, climate and type of population, and the financial and administrative resources available. It should attempt to balance the increase of production to meet essential domestic needs with the development of exports to accessible markets. The program should favor the application of the limited supplies of capital to projects which will result in the greatest increase in production and trade in relation to the size of the investment.

Primary development needs may be for improvement in transportation and communication facilities; for power projects; for water systems and other public utilities; for improved techniques in the production and processing of agricultural products; for industries, irrigation projects or resettlement programs—to list but a few of the forms which the report points out development projects may take.

In almost every case, the report says, the establishment or expansion of appropriate manufacturing and processing industries is an essential aspect of sound development. It will normally be advisable to lay initial stress on light consumer goods and processing industries which employ small amounts of capital equipment per worker and can build upon traditional skills in the introduction of mechanized techniques.

The report continues:

"The Bank is not, of course, interested in promoting any particular pattern of development nor has it formulated any detailed policies regarding the types of projects which it is willing to finance. Nonetheless, there are certain broad general principles which must guide its action. First, because the Bank's resources are limited in relation to the total development needs of its member countries, it must emphasize those strategic projects which will eliminate production bottlenecks or generate increased output of related goods or in related areas. Second, as an international agency, the Bank is particularly interested in projects which are likely to contribute to a better balance in world trade. Third, the Bank's Articles of Agreement provide that 'the most useful and urgent projects, large and small alike' must be dealt with first; the Bank must satisfy this requirement either by financing such projects itself or by helping to promote conditions necessary for their financing from other sources. And finally, the Bank's loans must be confined to projects for which financing through private or other channels is not available on reasonable terms."

If the Bank is to play its role of encouraging and supplementing private international investment, the report says, it must emphasize those basic undertakings which on the one hand are relatively less attractive to private capital, and on the other, will help to promote the flow of such capital into other sectors of the economy.

Since successful development in most cases depends just as much upon the provision of technical assistance from abroad as upon the availability of foreign capital, the report terms it an important concern of the Bank not only to provide financial help, but also to ensure that adequate technical assistance is available to define the shape of a sound over-all development program. The Bank avoids any gratuitous interference in the internal affairs of any country, but is prepared to undertake, upon request, a broad investigation of conditions in any underdeveloped member. The Bank is also ready to recommend, upon request, qualified independent experts to advise member countries in such fields as agriculture, engineering, finance and taxation.

The granting of loans by the Bank, the report says, need not await formulation by the borrowing country of an over-all development program or adoption by it of all necessary economic, financial and administrative measures. To the contrary, it is hoped that it will frequently be possible for the Bank to select particular meritorious projects for financing concurrently with the initiation by the borrower of such measures.

The major effort in the development of any country, the report says, must be made by that country itself. Therefore, while foreign assistance may be essential, the labor and the greater part of the capital must be supplied locally. Some part of the necessary foreign capital may be obtainable from public sources, through inter-governmental lending and International Bank loans. In the long run, however, sound development requires financial assistance in amounts which only the free flow of private capital can provide.

It is desirable that a considerable part of the foreign capital employed for development purposes be in the form of equity investments. The report points out that such investments would tend to avoid an undue burden of fixed charges which might impair the credit of the borrowing country or intensify its balance of payments problems during a period of declining trade or falling prices.

In cases where development projects which come to the attention of the Bank appear suitable for private financing, the Bank may be able to suggest possible sources of capital, or bring the projects to the attention of investing groups, or otherwise assist in arranging the necessary financing. The Bank may sometimes also be able to facilitate the raising of private capital for meritorious projects, the report says, by making loans to cover part of the capital cost.

In addition, the Bank itself can assume the risk of loans made from private funds through the use of its guarantee powers. Such loans, the report points out, establish a direct relationship between the private lender and borrower which may lead to other credit operations without the Bank's intervention. The Bank also is examining the possibilities of granting limited guarantees—for example a guarantee of transfer of interest—to reduce the special risks involved in international financing without eliminating the private character of the investment.

In general, the Bank may be able to contribute to the flow of private capital by encouraging the development of principles and practices fair to capital-exporting and capital-importing countries alike. Many of the Bank's policies are designed to help overcome some of the existing obstacles to private international investment.

The real measure of the Bank's effectiveness, according to the report, will not be so much the number or amounts of its loans and guarantees, significant as they may be, but rather its success in influencing attitudes—in promoting a realistic, constructive approach to development problems on the part of its members, and in fostering a greater degree of confidence among investors.

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## INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

**Washington, 25, D. C.**

### WHAT THE INTERNATIONAL BANK IS

The International Bank for Reconstruction and Development is an international institution designed to finance sound projects for reconstruction and development both in war-devastated countries and in underdeveloped regions. Its Articles of Agreement were drawn up at the United Nations Monetary and Financial Conference at Bretton Woods, New Hampshire, U.S.A., in July, 1944. It came into existence on December 27, 1945, when the signatures to its Articles of Agreement were received from the necessary number of governments, and officially began operations in Washington, D. C., on June 25, 1946. As of September 1, 1948, the Bank had 47 member nations.

The Bank is a world-wide effort to guide international investment into economically sound channels. Its main objectives may be summarized as follows: 1) To assist in the reconstruction and development of territories of member nations by facilitating the investment of capital for productive purposes; 2) To promote private foreign investment by means of guarantees or participations in loans and other investments made by private investors; and when private capital is not available on reasonable terms, to supplement private investment by providing loans for productive purposes out of its own capital, funds raised by it, and its other resources; 3) To promote the long-range balanced growth of international trade and the maintenance of equilibrium in balances of payments.

All powers of the Bank are vested in its Board of Governors, consisting of a representative appointed by each member country, which meets normally once a year. The Board of Governors has delegated most of its powers to the Executive Directors, at present fourteen in number, who meet normally once a week at the Bank's headquarters in Washington. Five Directors are appointed by the five countries which have subscribed the largest amounts to the Bank's capital stock (United States, United Kingdom, France, China and India); the other Directors are elected by the Governors of the remaining members. The Executive Directors represent all of the Bank's member nations.

The Management of the Bank is headed by its President, John J. McCloy, who is ex officio chairman of the Executive Directors, and its Vice President, Robert L. Garner, who is the Bank's general manager. The operating staff consists of some 400 persons representing more than 20 different nationalities.

The Bank's capital is derived from shares subscribed by its member nations on the general basis of their relative economic resources. Total subscribed capital is the equivalent of more than $8 billion subscribed in currencies of various members. Only 2 per cent is paid in gold or United States dollars and is immediately available for lending; 18 per cent is paid in the currencies of the various member nations and may be used for loans only with the consent of the respective member country. The remaining 80 per cent of the subscribed capital is in the nature of a guarantee fund which cannot be used for loans and can be called only to meet the obligations of the Bank. Additional loanable funds must come from sale of the Bank's own bonds to private investors. Funds which the Bank has had available to date for lending amounted to approximately $740 million out of its subscribed capital and operations; approximately $254 million from the sale of its bonds; and approximately $8 million from the sale of notes received by the Bank in connection with the Dutch shipping loans—a total of approximately $1 billion. As of September 1, 1948, the Bank had granted loans totaling $525 million. Its available lending funds on that date were approximately $475 million.