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Aid Without Tears: Opportunism in Foreign Development Policy

J. P. Morray*

With the entry of the Soviet Union into the field of foreign development aid in 1953, the competition between two economic systems commenced a new phase. Though the Soviet programs have hardly been functioning long enough to provide a basis for conclusive judgments, certain features of the Soviet system of operation are apparently working to its advantage. Payment for capital aid is being accepted in local currencies, surplus commodities or in products of the factories which the aid constructs. This is feasible for the Soviets, because their economy is not disrupted by an increase in the supply of anything. Resulting price declines hurt no interest but rather accord with basic economic goals. Loans are made at interest of 2½% or less. It is not necessary that rates be set high enough to lure investment with the prospect of high earnings. Fixed amounts of capital can be allocated to foreign states as a part of the budget of a long range economic plan. Development aid can be concentrated in strategic areas. The local government can be given full control over the enterprises constructed, since the amount and disposition of profits they earn are of no concern to the Soviet Union.¹

These are formidable characteristics in a competitor for the opportunity to play a part in the economic development of the peoples of Asia, the Middle East, Africa and Latin America who need capital beyond their own

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¹ For details on foreign assistance activities of the communist bloc countries see: Public Service Div., U.S. Dept. of State, *The Sino-Soviet Economic Offensive in the Less Developed Countries* (European and British Commonwealth Series, No. 51 (1958)); Zyzniewski, *Soviet Foreign Economic Policy*, 73 *POL. SCI. Q.* 206, 229 (1958); Speech of Allen W. Dulles before the U.S. Chamber of Commerce, *New York Times*, Apr. 29, 1958, p. 8 (late city ed.); Kotschnig, *International Aid for Underdeveloped Areas*, 38 *DEPT. OF STATE BULL.* 304, 305 (1958); Armstrong, *Soviet Economic Challenge to U.S. Policy*, *Id.* at 203; *THE COUNCIL FOR ECONOMIC AND INDUSTRY RESEARCH, INC., FOREIGN ASSISTANCE ACTIVITIES OF THE COMMUNIST BLOC AND THEIR IMPLICATIONS FOR THE UNITED STATES* (Comm. Print, Senate Special Comm. to Study the Foreign Aid Program, 85th Cong., 1st Sess., 1957); Letiche, *Soviet Foreign Economic Policy: Trade and Assistance Programs, in Report on the Soviet Union in 1956* (Symposium of the Institute for the Study of the USSR, Munich, 1956).

resources. How well is the United States equipped to meet this challenge? To answer this question, the six agencies, national and international, which the United States Government employs as instruments of foreign development must be examined.

EXPORT-IMPORT BANK

The Export-Import Bank was established as an anti-depression measure in 1934 to aid in financing exports and imports.² It serves to promote the sale abroad of United States products by making financing available to foreign buyers in situations not served adequately by private banking institutions. In effect, it is a bank which uses government resources to extend the American banking system.

The loan request may be initiated by the United States exporter, who is required to furnish credit information on the foreign purchaser. This will include such items as balance sheets, profit and loss statements, credit reports and a statement as to the probable effect of the export on the purchaser's operations.³

Credit applications may also begin with a request from the foreign buyer. This is commonly the procedure where a "project loan" is sought either by a foreign government or by private enterprise to cover purchases from several different United States suppliers of goods and services to be utilized in an integrated project. If a project proposed to the Bank appears to be of interest, Bank officials visit the country concerned to form judgment on the project's soundness as a credit risk and to negotiate modifications thought desirable by the Bank. Project loans may in fact be proposed and promoted by the Bank itself as a means of serving some sector of the American economy which is in particular need of sales outlets. This was the procedure employed in 1956 to help raise the price of cattle by Bank financed sales to Mexico.⁴

The Bank functions only as a "lender of last resort," that is, its funds are not available in competition with private banks. Legislation creating the Bank provides: "It is the policy of the Congress that the Bank in the exercise of its functions should supplement and encourage and not compete with private capital."⁵ Bank officials seem to be scrupulous in adhering to this policy. The great majority of "exporter-credit" type of applications

² Exec. Order No. 6581 of Feb. 2, 1934. Eximbank was first given a statutory basis in 1935. 49 Stat. 4 (1935). The Export-Import Bank Act of 1945 is the statutory basis of the present Bank. 59 Stat. 526 (1945) as amended, 12 U.S.C. §§ 635-35i (1952), as amended, 12 U.S.C. §§ 635-35i (Supp. V, 1958).

³ Eximbank, General Policy Statement 7-8 (1955).

⁴ *Hearing on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 26-29 (1957) (statement of Samuel C. Waugh).

⁵ 59 Stat. 527 (1945), 12 U.S.C. § 635(b) (1952).

come from exporters now well known to the Bank. If there is any possibility that a loan would offend the private bankers by trespassing, the Export-Import Bank will consult with the private bank which customarily finances the applicant's transactions and give it the opportunity to take the business for itself. In order to facilitate relations with commercial banks, the Bank maintains a separate department, the Private Capital Participation Division, whose sole function is to maintain close liaison with private financial institutions active in overseas trade. The Bank uses the facilities of private banks for making funds available to borrowers under the Bank's guarantee and for receiving payments of interest and principal. Private banks frequently participate on their own account in Bank loans.⁶ Since private banks prefer to put their funds in short term credits, the Bank assumes that credit for periods of less than one year may be obtained on reasonable terms from private sources. Accordingly, the Bank generally limits its consideration to transactions involving credit of one year or more.⁷ In fact, the Bank is attempting to expand credit facilities from private sources by a promotional campaign designed to stimulate the interest of private bankers, life insurance companies, endowment funds and pension trusts,⁸ in the profit opportunities in financing overseas transactions and by requiring the exporter to make efforts to find private financing for at least a part of every sale. The President of the Bank, Samuel C. Waugh, formerly president of a private bank in Lincoln, Nebraska, and an officer in the American Bankers Association, has stated that it is Bank policy to provide not more than 60% of the financing needs, while the minimum down payment from the buyer need be only 20%. The exporter is thus induced to search for private financing for at least the remaining 20%.⁹ There is reason to believe that Mr. Waugh was justified in telling Congress that "they are the best friends we have in this business, the private bankers."¹⁰

The Bank has had enough experience to know what type of transactions are of interest to private banks. This is the principal reason it provides vir-

⁶ Eximbank, Financing United States Overseas Trade 9-10 (1956), where examples are given of (a) participation on a guaranty-on-default basis, (b) participation without recourse in the short term maturities only, (c) participation without recourse and *pari passu* with Eximbank, and (d) full purchase of claim from Eximbank.

⁷ Eximbank, General Policy Statement 4 (1955). The average term of Bank loans is 6½ to 7 years. The maximum term by Bank policy is 20 years. For cotton financing the usual term is 12 to 18 months, for electrical equipment 15 to 18 years. *Hearings on the Mutual Security Act of 1957 Before the House Committee on Foreign Affairs*, 85th Cong., 1st Sess. 335 (1957) (statement of Samuel C. Waugh).

⁸ EXIMBANK, ANNUAL REPORT, pt. 1, p. 14 (1957); *Hearing on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 4 (1957) (statement of Samuel C. Waugh).

⁹ *Id.* at 37.

¹⁰ *Id.* at 17.

tually no financing for imports from abroad.¹¹ The American importer is expected to conduct his business within the facilities offered by the private banking system, even though these may not be as accommodating as the importer would like. During periods of "tight money," banks sometimes decline to finance imports because of an inadequate supply of funds to meet all requests for loans. In such cases the Export-Import Bank declines to supplement private banking facilities, on the theory that the need is raised only by a governmental policy against inflation which the Bank is bound to respect.¹² The same policy would probably affect the Bank's attitude toward exports if the application were clearly of the type private banks have welcomed in times of easier money.

The Bank is authorized by law to provide insurance against loss from war or expropriation of the security interest in exported goods.¹³ Here, too, the Bank is faithful to the limitation that it is not to compete with private insurance companies. The Bank's coverage is available only after the exported goods have been off-loaded in foreign ports, leaving to the private companies coverage of the shipment as far as they are willing to carry it.¹⁴

The capitalization of the Bank is one billion dollars, to which the United States Government is the sole subscriber. The lending authority of the Bank is now fixed at \$7 billion following an increase of \$2 billion approved by Congress in 1958.¹⁵ The Bank borrows from the Treasury on notes as necessary to maintain its supply of funds.¹⁶ Interest on the Treasury notes is fixed by the Secretary of the Treasury at rates based on "the current average rate on outstanding marketable obligations of the United States."¹⁷ The interest rates paid by the Bank are therefore varied. They have ranged from 1 $\frac{7}{8}$ % to 3 $\frac{1}{2}$ %.¹⁸

Interest charged the borrower by the Bank is a matter for negotiation in each case. It is always higher than interest paid by the Bank. It follows current rates charged by private banks on their loans of shorter maturity. At present rates are in the range of 4 $\frac{1}{2}$ % to 6%.¹⁹ In view of the Bank's

¹¹ Eximbank, General Policy Statement 4 (1955).

¹² *Hearing on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 35 (1957) (statement of Samuel C. Waugh).

¹³ 67 Stat. 28 (1953), 12 U.S.C. § 635(c) (Supp. V, 1958).

¹⁴ *Hearing on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 39 (1957) (statement of Samuel C. Waugh).

¹⁵ Act of May 22, 1958, 72 Stat. 133.

¹⁶ 59 Stat. 528 (1945), as amended, 12 U.S.C. § 635d (Supp. V, 1958). Until 1958 the upper limit on the Bank's borrowing authority was \$4 billion. This has now been increased to \$6 billion. Act of May 22, 1958, 72 Stat. 133.

¹⁷ 61 Stat. 131 (1947), 12 U.S.C. § 635d (Supp. V, 1958).

¹⁸ *Hearings on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 11-12 (1957) (statement of Samuel C. Waugh).

¹⁹ *Hearings on Increased Export-Import Bank Lending Authority Before the Senate Committee on Banking and Currency*, 85th Cong., 2d Sess. 10 (1958) (statement of Samuel C. Waugh).

solicitude for the private banking system there is probably no desire to provide conspicuously low rates, which would cause exporters to concentrate as much rather than as little as possible of their financing with the public bank at the expense of the private sector.

This mark-up on money lent by the Bank enables it to meet its own administration expenses and to accumulate earnings, which are used to pay a 2½% dividend each year to the United States Treasury on its capital stock. The balance of the earnings is available for making new loans and as a reserve to cover potential defaults by its borrowers.

The conservative character of the Bank's operations is attested by its good loss record. For the 23-year period ending 1957, losses amounted to only one-half million dollars in loans totalling \$5,277 million for a bad-loan ratio of .01%.²⁰ Obviously the Bank has taken seriously the statement in the act to the effect that "it is the policy of the Congress that . . . loans . . . shall . . . offer reasonable assurance of repayment."²¹ Since repayment must be in dollars, the Bank must be satisfied that foreign exchange will be available to the borrower to service the debt. These two Bank conditions, that the credit risk must be a good one and that repayment must be in dollars, seriously limit the usefulness of the Bank to a foreign government planning a development program. They also put the Bank in the position of dictating changes in the foreign government's policies and maintaining a creditor's surveillance during the term of the loan.²²

As an agency of the United States Government, the Bank's loans must conform to United States overall economic and political programs. This is achieved by subjecting all loans approved by the Bank's Board of Directors to review by the National Advisory Council on International Monetary and Financial Problems, composed of the Secretary of State, the Secretary of the Treasury, the Secretary of Commerce, the Chairman of the Board of Governors of the Federal Reserve System and the President of the Export-Import Bank.²³ Compliance of Bank policy with Council decisions is assured through the powers of the President of the United States to dismiss the directors of the Bank at any time.²⁴

²⁰ *Hearings on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 7, 9 (1957) (statement of Samuel C. Waugh). Nationalist China is delinquent on loans totalling \$31.4 million which have not yet been declared losses. *Ibid.*

²¹ 59 Stat. 527 (1945), 12 U.S.C. § 635(b) (1952).

²² "We attach conditions, certainly . . . We sit down with the representatives of a country and discuss problems in a banker-borrower relationship, discuss with that particular country the economic changes that we think should be made within the country . . . They can always refuse our conditions . . . but on that basis, if our judgment is sound, they do not get the money." *Hearings on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 24-25 (1957) (statement of Samuel C. Waugh).

²³ 59 Stat. 512 (1945), as amended, 22 U.S.C. § 286b (1952), as amended, 22 U.S.C. § 286b (Supp. V, 1958).

²⁴ 68 Stat. 677 (1954), 12 U.S.C. § 635a(c) (Supp. V, 1958).

The result of this subordination of the Bank to the Council is that factors in addition to the borrower's ability to repay in dollars enter into the Bank's willingness to approve a loan and affect the conditions on which it will be granted. In line with the United States Government's program to promote the widest possible scope for private enterprise, the Bank prefers to extend credits to private entities rather than to foreign governments if the project is of a commercial nature.²⁵ Borrowers from certain countries or whole areas may become ineligible for reasons of foreign policy. Borrowers from other countries may be given especially favorable consideration. The Bank frequently asks the United States embassies for their comments on particular borrowers.²⁶ Loans for the purpose of promoting the production, for example by exploration and mining, of raw materials needed in the United States economy receive favored treatment. Even if the credit risk is not one the Bank would normally accept, a loan out of especially appropriated funds will be made on a "certificate of essentiality" from the Director of the Office of Defense Mobilization.²⁷

Though the requirement is not written into the law, credit will be extended as a general rule only to finance purchases of materials and equipment produced or manufactured in the United States.²⁸ Thus American producers get maximum profit advantages from the Bank's credits. This "tied loan" condition is sometimes specific even as to the area of the United States in which the purchase must be made, as, for example, when a loan to Mexican borrowers was approved only for purchase of cattle in states of the drought area.²⁹ United States shippers are also subsidized by the loans. In the absence of a determination by the Maritime Administration that United States vessels are not reasonably available, they have an exclusive right to carry the products whose export is fostered by Bank loans.³⁰ These restrictions on the use of the credits are enforced though the costs to the foreign purchaser are increased. As the Bank began in 1934, so it continues, primarily the servant of United States exporter interests.

²⁵ Eximbank, General Policy Statement 13 (1955).

²⁶ *Hearing on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 37 (1957) (statement of Samuel C. Waugh).

²⁷ Defense Production Act of 1950, § 302, 64 Stat. 801, 50 U.S.C. App. § 2092 (1952), as amended by Defense Production Act—Extension, 72 Stat. 241 (1958); Exec. Order No. 10480, § 311, 18 Fed. Reg. 4939 (1953).

²⁸ *Hearing on Increased Export-Import Bank Lending Authority Before the Senate Committee on Banking and Currency*, 85th Cong., 2d Sess. 15 (1958) (statement of Samuel C. Waugh).

²⁹ *Hearing on Export-Import Bank Loans Before the House Committee on Banking and Currency*, 85th Cong., 1st Sess. 26 (1957) (statement of Samuel C. Waugh).

³⁰ Eximbank, General Policy Statement 13 (1955). This restriction applies to exports fostered by loans made by any instrumentality of the United States Government. 48 Stat. 500 (1934).

DEVELOPMENT LOAN FUND

The Development Loan Fund was established as a function of the International Cooperation Administration by the Mutual Security Act of 1957.³¹ It replaced the annual "Development Assistance" programs carried out under the Mutual Security Act of 1954.³² This important change in the approach to financing overseas projects followed the entry of the Soviet Union into the foreign aid field and a series of studies of United States foreign aid by various groups³³ which recommended an increase in "development aid," as distinguished from military aid and defense support.³⁴ The Fairless and Johnston Committees had stressed the difficulties raised in administering development programs through annual appropriations for each country. This made long-range planning impossible and therefore made the projects less attractive to private investors, contractors and technicians needed for effective operation. The State Department had also been embarrassed by the publicity given the "illustrative programs" used to justify appropriation requests, which worked to create expectations in the recipient countries that the programs were firm before the Department considered them so. The Loan Fund technique is designed to give development programs an increased stability through the assurance that certain funds are available for use as they are needed in later years. It also gives the Administration a greater independence of Congress in the negotiations with applicants for loans.

By the Mutual Security Act of 1958 the status of the Fund was changed on the request of the President³⁵ from that of a component of the Inter-

³¹ 71 Stat. 357 (1957); 22 U.S.C. §§ 1870-76 (Supp. V, 1958).

³² 68 Stat. 840 (1954).

³³ International Development Advisory Board, *A New Emphasis on Economic Development Abroad* (Johnston Report, 1957); MIT Center For International Studies, *The Objectives of U.S. Economic Assistance Programs* (1957); RESEARCH CENTER IN ECONOMIC DEVELOPMENT AND CULTURAL CHANGE OF THE UNIVERSITY OF CHICAGO, *THE ROLE OF FOREIGN AID IN THE DEVELOPMENT OF OTHER COUNTRIES* (Comm. Print, Senate Special Comm. to Study the Foreign Aid Program, 85th Cong., 1st Sess., 1957); Committee for Economic Development, *Economic Development Assistance* (1957); National Planning Ass'n, *A New Approach to Foreign Economic Assistance* (Special Report No. 47, 1957). Benjamin F. Fairless, summarizing the views of the President's Citizen Advisory Group on the Mutual Security Program of which he was Coordinator, stated: "[We] recognize the necessity for some economic development expenditures by our Government to help bring the recipient countries more completely into the orbit of free society." *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 62 (1957).

³⁴ "Defense support" refers to aid necessary to assure the maintenance of United States military bases abroad or to enable a country to raise and support military forces, "assistance specifically designed to sustain and increase military effort." 68 Stat. 838 (1954), as amended, 22 U.S.C. § 1841 (Supp. V, 1958).

³⁵ H.R. Doc. No. 338, 85th Cong., 2d Sess. 6 (1958).

national Cooperation Administration to that of a government corporation.³⁶ It is therefore virtually another government bank.³⁷

Congress has declared the purpose of the Fund to be "to strengthen friendly foreign countries by encouraging the development of their economies through a competitive free enterprise system; to minimize or eliminate barriers to the flow of private investment capital and international trade; to facilitate the creation of a climate favorable to the investment of private capital; and to assist, on a basis of self-help and mutual cooperation, the efforts of free peoples to develop their economic resources and to increase their productive capabilities."³⁸ The emphasis in the act on utilizing the Fund to promote private enterprise is respected by the Administration in its announcement of lending policies. Applications for loans are invited from private investors, both United States and foreign.³⁹ The creation of certain basic public facilities is also to be fostered, though this may involve loans to governments, if these will promote private investment. "The fund is also helping to make possible the creation of those basic public facilities on which private enterprise depends. Without facilities such as roads, power, and communications, the manufacturing and extractive industries cannot function. The fund had before it many such basic facilities projects which, when completed, would encourage and attract private investors."⁴⁰

In testimony supporting the request for the creation of the Fund, John B. Hollister, Director of the International Cooperation Administration, stated: "[W]e would use the Fund to concentrate on the development of the private sector of the economies of countries we wish to help."⁴¹ He mentioned these techniques: (1) direct loans to private businessmen, (2) guaranteeing loans to private businessmen, (3) loans to public industrial or agricultural development banks which in turn will make investment capital available to private entrepreneurs and farmers, (4) buying the obligations of new productive enterprises which, after they have shown their ability to earn profits, can be resold to private individuals, (5) joining with private capital in a single venture, (6) financing activities which

³⁶ Mutual Security Act of 1958, § 203, 72 Stat. 263.

³⁷ Even before its incorporation the Fund had been described as being like a bank by Secretary of State Dulles. *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 127 (1957).

³⁸ 71 Stat. 357 (1957), 22 U.S.C. § 1871 (Supp. V, 1958).

³⁹ PRESIDENT'S THIRTEENTH SEMI-ANNUAL REPORT ON THE MUTUAL SECURITY PROGRAM 19 (1958).

⁴⁰ *Ibid.* "[T]he recently created Development Loan Fund is intended to help private enterprise initiate projects in the less developed countries." DEPT. OF STATE, DEPT. OF DEFENSE, INTERNATIONAL COOPERATION ADMINISTRATION, BACKGROUND FOR MUTUAL SECURITY FOR FISCAL YEAR 1959, 27 (1958).

⁴¹ *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 787 (1957).

support or supplement or improve opportunities for privately financed ventures.⁴²

Foreign private capital investment is to be encouraged, if not, indeed, lured, by making the loans to private businessmen conditional on investment of a reasonable amount from their own resources.⁴³ The climate for foreign investment is to be improved by giving priority to those projects which earn or save foreign exchange, facilitating the conversion of profits into dollars.⁴⁴ The sale of obligations of going concerns to private interests is to be fostered by making loans on debentures which, though not themselves carrying voting rights, would acquire equity voting rights on resale to private owners.

Though the Fund has been referred to as a source of "soft" loans,⁴⁵ this impression is contradicted by the terms of the act and statements of the Administration. The law prohibits grants from the Fund and provides that no loan shall be made except "on the basis of firm commitments by the borrowers to make repayment and upon a finding that there are reasonable prospects of such repayment."⁴⁶ The Administration insisted in its testimony before Congress after one year of operation that a "sound loan" policy was being followed.⁴⁷ The fact that the loans may be repaid in local currency, "soft" currencies, may have been the source of the earlier belief that the loans were really to be disguised gifts. Whether the United

⁴² *Ibid.*

⁴³ PRESIDENT'S THIRTEENTH SEMI-ANNUAL REPORT ON THE MUTUAL SECURITY PROGRAM 17-18 (1958).

⁴⁴ *Ibid.*

⁴⁵ Skeptics in Congress believed this to be the intended function of the Fund. Representative Passman of Louisiana referred to it as a "worldwide WPA." *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 796 (1957).

⁴⁶ 71 Stat. 357 (1957), 22 U.S.C. § 1872 (Supp. V, 1958). This is similar to the standard set by Congress for Export-Import Bank loans. See text at note 21 *supra*.

⁴⁷ The following exchange took place in the 1958 hearings before a House subcommittee between Representative Alexander of North Carolina and C. Douglas Dillon, Under Secretary of State for Economic Affairs:

Mr. Alexander. Mr. Secretary, all through your statement here, you used the words "businesslike basis," "sound projects," "economically and technically sound," "sound banking basis." Is that description not a little erroneous with regard to what you are actually doing?

Mr. Dillon. I do not think so. No.

Mr. Alexander. These are soft loans, are they not?

Mr. Dillon. These are sound loans repayable in local currency

Mr. Alexander. Are you telling the committee that these are loans that sound banking practices would make other than that they are repaid in foreign currency?

Mr. Dillon. That is correct.

Hearings on Mutual Security Appropriations for 1959 Before the Subcommittee of the House Committee on Appropriations, 85th Cong., 2d Sess. 371 (1958). See also *Hearings on the Mutual Security Act of 1957 Before the House Committee on Foreign Affairs*, 85th Cong., 1st Sess. 1231 (1957) (statement of John B. Hollister).

States Government is able to make use of the currencies repaid remains to be seen.⁴⁸ But that the borrower must give a firm commitment to repay and that the project must be economically sound with a "reasonable prospect of repayment" is the announced policy of the Fund.⁴⁹ The intent to resell obligations to private investors suggests a conservative lending policy. Loans are made on the basis of individual project proposals, as are loans by the Export-Import Bank. No annual country by country programming is undertaken.⁵⁰ In accordance with the bank character of the Fund the Administration hopes that ultimately it will earn its own administration expenses and operate at a profit.⁵¹

The interest rate charged on loans for basic facilities such as roads, harbors, railroads and dams is at present $3\frac{1}{2}\%$. This rate is fixed to exceed by a small amount the cost of money to the United States Treasury.⁵² These loans offer a maximum term of 40 years with a grace period of three to five years before amortization begins. On manufacturing, extractive and other profit earning enterprises the interest rates are to follow the Export-Import Bank and private lenders on similar projects. At present these rates stand at $5\frac{1}{4}\%$ to 6% .⁵³

The loan agreements, though permitting repayment in local currencies, are dollar-denominated and contain "maintenance of value" provisions. If the rate of exchange between the local currency and the dollar changes, the amount of local currency to be repaid is adjusted accordingly. Although one Administration spokesman indicated that the applicable exchange rate was to be based on the free market value,⁵⁴ in practice official controlled rates have been used. Under the Honduras Highway Development Agreement, for example, the Fund is to receive local currency at the rate

⁴⁸ It cannot use them for financing exports to the United States without defeating the purpose of helping the foreign state earn dollars. *Hearings on Mutual Security Appropriations for 1959 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 2d Sess. 911 (1958) (statement of W. M. Rountree).

⁴⁹ PRESIDENT'S THIRTEENTH SEMI-ANNUAL REPORT ON THE MUTUAL SECURITY PROGRAM 17 (1958).

⁵⁰ *Ibid.*

⁵¹ *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 829 (1957) (statement of John B. Hollister).

⁵² *Hearings on Mutual Security Appropriations for 1959 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 2d Sess. 371 (statement of C. Douglas Dillon).

⁵³ PRESIDENT'S THIRTEENTH SEMI-ANNUAL REPORT ON THE MUTUAL SECURITY PROGRAM 18 (1958).

⁵⁴ *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 835 (1957) (statement of John B. Hollister).

used by the Honduran government for authorized transfers to the United States of dividends, interest or investment capital by local residents.⁵⁵

The borrower undertakes by the loan agreement to submit monthly progress reports and to maintain books and records on the use of the goods and services financed by the loan. The Fund reserves the right to inspect the books and to observe the project at any reasonable time.⁵⁶

The Fund is forbidden by law to compete with private capital, the Export-Import Bank or the International Bank for Reconstruction and Development.⁵⁷ The Chairman of the Board of Directors of the Export-Import Bank and the United States Executive Director of the International Bank are *ex officio* members of the Board of Directors of the Fund.⁵⁸ Coordination with the other two institutions is thus assured. The ability of the Fund to accept repayment in local currencies is, of course, the feature which opens to it a category of loan applications of no interest to the other lenders. In practice there is referral of applications from the Fund to the other institutions and *vice versa*.⁵⁹ There seems little possibility for a borrower to play one against the other in a negotiation for better terms. In view of the concern expressed during hearings on the Fund by the President and Chairman of the Board of the Export-Import Bank over the risks of excessive borrowing and over the effect of a soft loan policy on a borrower's attitude toward hard loans, it is likely that the Bank's representation on the Board acts to give lending policy a more conservative character than might otherwise be the case.⁶⁰ Insofar as the Fund loans are successful in improving the foreign exchange position of the borrower the soundness of the loans made by the other lending institutions is improved.

The Fund enables private investors to spread their resources across a broader field by supplementing their own investments with government

⁵⁵ *Hearings on Mutual Security Appropriations for 1959 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 2d Sess. 897 (1958).

⁵⁶ *Id.* at 900.

⁵⁷ 71 Stat. 358, 22 U.S.C. § 1872 (Supp. V, 1958).

⁵⁸ The other members are the Under Secretary of State for Economic Affairs (Chairman), the Director of the International Cooperation Administration and the Managing Director of the Fund. Mutual Security Act of 1958, § 203, 72 Stat. 263.

⁵⁹ PRESIDENT'S THIRTEENTH SEMI-ANNUAL REPORT ON THE MUTUAL SECURITY PROGRAM 19 (1958); *Hearings on Mutual Security Act of 1958 Before the House Committee on Foreign Affairs*, 85th Cong., 2d Sess. 732 (1958) (statement of Dempster McIntosh).

⁶⁰ *Hearings on the Mutual Security Act of 1957 Before the House Committee on Foreign Affairs*, 85th Cong., 1st Sess. 326 (1957) (statement of Samuel C. Waugh): "We want to be very careful that soft loans are not made in areas where they now have hard loans and can service hard loans. Then another point . . . I want to emphasize . . . is the ability of any country to absorb more than a given amount of debt, regardless of whether it is hard or soft. In other words, I think from banking experience, more individuals have been ruined by too much credit than they have been by not enough credit." *Id.* at 331.

funds. The Administration considers that the Fund will give further stimulus to United States private investment abroad under the investment guaranty program described below, by adding one more aid to hesitant investors.⁶¹ The capital contribution from the Government cannot endanger private control of the joint venture, since the Fund may not purchase equity securities.⁶²

Though there is no general "tied loan" policy requiring that the proceeds of the loan be spent for United States goods and services, borrowers have informally agreed in some cases to spend the bulk of their loans in the United States.⁶³ By a 1958 amendment of the act, the Fund must give consideration before financing a proposed project to "the possible adverse effects upon the economy of the United States, with special reference to areas of substantial labor surplus."⁶⁴ This is designed to discourage the promotion of enterprises which might take markets away from American producers. This consideration will necessarily inhibit to some extent the policy of trying to improve the foreign state's exchange position through an increase of exports or a decrease of imports.

Congressional solicitude for American business is also expressed in the direction given to the executive branch by the 1958 act to conduct in cooperation with representatives of private enterprise "a study of the ways and means in which the role of the private sector of the national economy can be more effectively utilized *and protected* in carrying out the purposes of this Act, so as to promote the foreign policy of the United States, *to stabilize and to expand its economy and to prevent adverse effects*, with special reference to areas of substantial labor surplus."⁶⁵

Some congressional control over the operation of the Fund is conferred by the Government Corporation Control Act.⁶⁶ An annual budget must be submitted, and by an affirmative vote Congress can limit the use of

⁶¹ *Id.* at 1269 (statement of Charles B. Warden, Chief of Investment Guaranties Staff, International Cooperation Administration).

⁶² 71 Stat. 357 (1957), 22 U.S.C. § 1872(b) (Supp. V, 1958).

⁶³ *Hearings on Mutual Security Appropriations for 1959 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 2d Sess. 381 (1958) (statement of C. Douglas Dillon).

⁶⁴ Mutual Security Act of 1958, § 203, 72 Stat. 263.

⁶⁵ Mutual Security Act of 1958, § 205, 72 Stat. 267. (Emphasis added.) When Senator Dworshak of Idaho complained that United States aid by promoting metals production overseas had created a "Frankenstein" menace to domestic mining interests, Mr. Dillon, Deputy Under Secretary of State for Economic Affairs, explained that fear of war had necessitated stockpiling. Normally, adverse effects upon U.S. producers have to be "taken into account." *Hearings on Mutual Security Appropriations for 1958 Before the Senate Committee on Appropriations*, 85th Cong., 1st Sess. 192 (1957).

⁶⁶ 59 Stat. 597 (1945) as amended, 31 U.S.C. §§ 846-52 (1952), as amended, 31 U.S.C. § 846 (Supp. V, 1958).

corporate funds.⁶⁷ Congress has retained somewhat tighter control over the Fund than over the Export-Import Bank by denying to the former an authority to borrow from the Treasury.⁶⁸ Thus the Fund must request a new appropriation from Congress each time it anticipates an exhaustion of past appropriations.⁶⁹ The Fund operates as an instrument of United States foreign policy under the guidance of the Secretary of State.⁷⁰ To keep this subordination clear, it is stated explicitly in the 1958 amendments to the act.⁷¹ The Undersecretary of State for Economic Affairs is Chairman of the Board of Directors.⁷² Thus it is likely that considerations of the "national interest" are going to cause the Fund to discriminate in favor of loans to certain areas.⁷³ From the point of view of the underdeveloped states this subordination to the State Department means that they must prepare their loan applications not only with a view to making them sound economically, favorable to private enterprise and considerate of American industry, but also must prove their utility to the State Department's campaign to save the world from communism.

SURPLUS AGRICULTURAL COMMODITIES

Since the enactment of the Agriculture Trade Development and Assistance Act in 1954,⁷⁴ United States surplus agricultural commodities with an export value of approximately \$3,774 million have been sold for foreign currencies under agreements with foreign governments or exchanged on a barter basis for raw materials useful to United States

⁶⁷ 59 Stat. 598 (1945) as amended, 31 U.S.C. § 849 (1952).

⁶⁸ Borrowing authority for the Fund to bring its capitalization to two billion dollars had been requested by the Administration. *Hearings on the Mutual Security Act of 1957 Before the House Committee on Foreign Affairs*, 85th Cong., 1st Sess. 532 (1957) (statement of Secretary of State Dulles).

⁶⁹ Authorized capitalization of the Fund is \$1,125 million. 71 Stat. 358 (1957), 22 U.S.C. § 1873 (Supp. V, 1958). Congress appropriated \$300 million in 1957 and \$400 million in 1958. 71 Stat. 602 (1957) and 72 Stat. 1100 (1958).

⁷⁰ Secretary of State Dulles: "I believe this fund, at least in the first instance, should be operated primarily as an instrument of foreign policy. That is what it is for." *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 105 (1957). Secretary of Treasury Anderson, commenting adversely on the proposal to create an International Development Association (the "Monroney Plan"), explained that "the national interest requires a capacity for *bilateral* financing." *New York Times*, Mar. 19, 1958, p. 3 (late city ed.). (Emphasis added.) Development needs must be exploited for political purposes in the "national interest."

⁷¹ Mutual Security Act of 1958, § 203, 72 Stat. 263.

⁷² *Ibid.* The present incumbent, C. Douglas Dillon, is a former Vice President of Dillon, Read and Co., investment bankers. The Manager of the Fund is Dempster McIntosh, former banker, exporter and President of Philco International Corporation.

⁷³ Secretary of State Dulles: "The purpose of the State Department is to look out for the interests of the United States." *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 120 (1957).

⁷⁴ Public Law 480, 68 Stat. 454 (1954), 7 U.S.C. §§ 1691-1724 (Supp. V, 1958).

industry.⁷⁵ The act declares a congressional policy that foreign currencies accruing as a result of the program shall be used, among other purposes, "to encourage economic development."⁷⁶

The principal purposes of the act are thought by both the Administration and Congress to be other than foreign development. Secretary Dulles made this clear in the hearings before congressional committees which explored the need for a Development Loan Fund. "The disposal of surplus agriculture commodities does not promote long-term economic development," he said. "In the main, it is foodstuffs that are consumed right away, and while it helps to keep people alive, it is a totally distinct program from long-term economic development."⁷⁷

When Congress used the word "development" in the title of the act, it was focusing its attention on the development of new markets for American agricultural products. In scoring the Administration for not being sufficiently aggressive in carrying out this primary purpose of the act, a House committee in 1957 tried to dispel any doubts as to priorities: "One need look no further than the title of the act itself to discover the first, and in the opinion of this committee, the most important tangible benefit Congress had in mind: development abroad of new and expanded commercial markets for American agricultural products."⁷⁸ In effect, the committee told the Administration to get out and sell, and to make this the primary duty of the agricultural attachés on the embassy staffs, who are "to represent American agricultural production in foreign countries."⁷⁹

The Administration denied having ever mistaken the primary purpose of the act.⁸⁰ The Assistant Secretary of Agriculture assured Congress that

⁷⁵ *President's Eighth Semiannual Report on Activities Under Public Law 480, Jan. 1-June 30, 1958*, H.R. Doc. No. 431, 85th Cong., 2d Sess., 39 DEPT. OF STATE BULL. 423 (1958). Some of the surplus commodities being exported under the act are wheat, wheat flour, feed grains, rice, cotton, tobacco, dairy products, fruits, fats and oils. *Id.* at 424.

⁷⁶ 68 Stat. 455 (1954), 7 U.S.C. § 1691 (Supp. V, 1958). The act also authorizes the use of surplus commodities for disaster relief. 68 Stat. 457 (1954) as amended, 7 U.S.C. § 1721 (Supp. V, 1958).

⁷⁷ *Hearings on Mutual Security Appropriations for 1958 Before the Subcommittee of the House Committee on Appropriations*, 85th Cong., 1st Sess. 107 (1957).

⁷⁸ H.R. REP. NO. 432, 85th Cong., 1st Sess. 10 (1957), 1957 U.S. CODE CONG. & AD. NEWS 1425.

⁷⁹ H.R. REP. NO. 432, 85th Cong., 1st Sess. 12 (1957), 1957 U.S. CODE CONG. & AD. NEWS 2183.

⁸⁰ The long "Declaration of Policy" contained in the opening article of the act (68 Stat. 454 (1954), 7 U.S.C. § 1691 (Supp. V, 1958)) could have been interpreted to mean that Congress regarded the sale of surpluses not as the end, but as a new means to help achieve other named objectives, such as expanding international trade, facilitating convertibility of currencies, encouraging economic development, promoting collective strength and fostering in other ways the foreign policy of the United States. The drafters of this article must have thought that the naked objective of expanding our sales abroad was somewhat ugly and needed to be attractively wrapped. Are congressmen secretly ashamed of the policy of sending out government drummers to win sales away from foreign producers?

the "administration of this entire program is directed toward protecting and expanding our dollar market abroad. That is our first priority."⁸¹ In the "usual marketing" clause the act directs that United States exporters be protected from loss of their dollar earning markets as a result of the increased availability of the same commodities on terms involving no foreign exchange.⁸² Participating governments must agree to respect this limitation on the use and resale of the commodities.⁸³ Transshipment to other countries is forbidden without approval of the President of the United States.⁸⁴ Shipments on a barter basis are not allowed to countries considered to be dollar markets unless an increase in total imports of the commodity can be assured. Only where commercial trade in the commodity has been negligible may it be shipped on a barter basis without this specific showing of an addition to trade.⁸⁵ While these policies protect the American exporter, they deny the foreign governments any possible savings in dollar exchange.

To the end that new markets be created for the American exporters, foreign currencies generated by sales under the act are available for bearing the major part of the cost of market promotion projects. The exporter or private trade association who initiates the project is expected to make some financial contribution.⁸⁶ These projects employ market surveys, extensive advertising, trade fair exhibits, cooking demonstrations and the distribution of free samples of such products as ice cream, cheese, citrus juices, doughnuts, cigarettes, frankfurters, popcorn and potato chips fried in American soybean oil.⁸⁷

The capture of markets from the U.S.S.R. is particularly gratifying to the Administration.⁸⁸ But the magnetism of American salesmanship cannot be so selective. Some of the new customers caught within its field are drawn from local suppliers. The campaign has also aroused misgivings

⁸¹ *Hearings on Extension of Public Law 480 Before the Senate Committee on Agriculture and Forestry*, 85th Cong., 1st Sess. 28 (1957) (statement of Earl L. Butz). "[T]he basic purpose of Public Law 480 is to facilitate the movement of surplus agricultural commodities." *President's Sixth Semiannual Report*, H.R. Doc. No. 212, 85th Cong., 1st Sess. 5, 37 DEPT. OF STATE BULL. 281, 283 (1957).

⁸² "[T]he President shall (a) take reasonable precautions to safeguard usual marketings of the United States . . ." 68 Stat. 455 (1954), 7 U.S.C. § 1701(a) (Supp. V, 1958).

⁸³ *President's Seventh Semiannual Report*, H.R. Doc. No. 323, 85th Cong., 2d Sess. 4, 38 DEPT. OF STATE BULL. 476, 478 (1958).

⁸⁴ 68 Stat. 455 (1954), 7 U.S.C. § 1701(d) (Supp. V, 1958).

⁸⁵ *Seventh Semiannual Report*, *supra* note 83, 38 DEPT. OF STATE BULL. 476, 478 (1958).

⁸⁶ A total of 163 market development projects in 28 countries had been put into operation by December 31, 1957. The equivalent of \$9 million, or approximately three-fourths of their total cost, had been borne by the United States Government from its foreign currency accounts. *Id.* at 481.

⁸⁷ *Ibid.*

⁸⁸ *Hearings on Extension of Public Law 480 Before the Senate Committee on Agriculture and Forestry*, 85th Cong., 1st Sess. 3 (1957) (statement of Earl L. Butz).

among friendly nations who are competitors in the world market.⁸⁰ They are not included within the protections of the "usual marketings" proviso. One congressional report dealing with the act emphasized that long staple cotton should be pushed by the Administration even though it competed with similar commodities produced outside the United States.⁸⁰ Foreign as well as United States exporters are beneficiaries of the proviso that the act is to be administered so as not to disrupt world prices "unduly."⁸¹ This concern to sustain the world price seems to be the guiding factor in fixing the price for sales for foreign currencies at a figure "comparable to those prevailing in the market for export sales for dollars."⁸² Foreigners are to be "developed" by inducing them to buy American products, but at no loss to the exporters.

Another purpose of the program is to substitute surplus agricultural commodities for some of the dollars previously made available to foreign governments as United States government expenditures and as aid under the Mutual Security Act.⁸³ In other words, a part of our dollar expenditures which would otherwise go abroad is diverted to the Commodity Credit Corporation to enable it to cut its losses in the domestic price support program. Since fiscal year 1955 portions of the appropriations for mutual security objectives have been used to finance the purchase of agricultural surpluses from the Commodity Credit Corporation for export and resale abroad for foreign currencies, which are then to be used for mutual security objectives.⁸⁴

Such expenses as housing construction for United States military personnel, base construction, propaganda in the language of the country, the support of local military forces, translation and publication of United

⁸⁰ These were aired at the International Wheat Surplus Utilization Conference held at Brookings, S.D., in July 1958. See also "Slippery Problem: World Butter Surplus," *New York Times*, sec. 3, p. 1, July 27, 1958 (late city ed.). The act accounted for 26% of total United States agricultural exports during the period 1954-57. *Sixth Semiannual Report*, *supra* note 81, 37 DEPT. OF STATE BULL. 281, 282 (1957). For an opinion minimizing effects on other states, see NATIONAL PLANNING ASSOCIATION, *AGRICULTURAL SURPLUS DISPOSAL AND FOREIGN AID* 21 (Comm. Print, Special Senate Comm. to Study the Foreign Aid Program, 85th Cong., 1st Sess., 1957).

⁹⁰ H.R. REP. No. 683, 85th Cong., 1st Sess. (1957), 1957 U.S. CODE CONG. & AD. NEWS 1434. See also 70 Stat. 199 (1956), 7 U.S.C. § 1852(b) (Supp. V, 1958), where Congress directs that the price and amount of extra long staple cotton offered for sale be such as to dispose of the entire surplus by export "in an orderly manner and within a reasonable period of time."

⁹¹ 68 Stat. 455 (1954), 7 U.S.C. § 1701(a) (Supp. V, 1958).

⁹² *Seventh Semiannual Report*, *supra* note 83, 38 DEPT. OF STATE BULL. 476, 478 (1958).

⁹³ *Sixth Semiannual Report*, *supra* note 81, 37 DEPT. OF STATE BULL. 281, 283 (1957).

⁹⁴ 68 Stat. 843 (1954) as amended, 22 U.S.C. § 1822 (Supp. V, 1958). Amounts allocated from mutual security funds for this purpose have been as follows: FY 1955 \$350,000,000, FY 1956 \$300,000,000, FY 1957 \$250,000,000, FY 1958 \$175,000,000.

States oriented books at low prices, educational exchange, maintenance of Hungarian refugees and embassy payrolls are some of the varied obligations of the United States Government which can be met out of local currency funds.⁹⁵ They have also been used to purchase raw materials for United States industry under the stockpiling program of the Office of Defense Mobilization. Since most stockpile objectives have been met, these purchases are now virtually suspended.⁹⁶ Some barter exchanges continue to be negotiated.⁹⁷

Under section 104(g) of the act loans may be made from the currency accumulation by agreement with friendly nations "to promote multilateral trade and economic development."⁹⁸ The provision to the purchasing country of a substantial amount of local currency for these purposes has been an important aid in the selling campaign.⁹⁹ Projects are selected which are agreeable to both parties. The primary purpose of the act may not be neglected in these negotiations. "[I]n considering loan projects for agricultural purposes care is exercised [on the side of the United States] to avoid encouragement of production which would result in reduced outlets for United States agricultural commodities."¹⁰⁰ Development is not for such potential competitors. Loans of these local currencies are sometimes combined with dollar loans from other sources, such as the International Bank or the Export-Import Bank.¹⁰¹ If dollars are used to repay the local currency loan, interest is charged at 4%. If repayment is in the local currency, interest is 5%, and a maintenance of value clause applies.¹⁰² Strategic materials and services may also be accepted in repayment.

The support of private enterprise by these loans depended prior to 1957 on the active cooperation of foreign governments. They were "encouraged" to reloan a part of their 104(g) loans to private investors, and agreements to set aside the equivalent of approximately \$150 million for this purpose have been obtained from 16 countries.¹⁰³ These agreements provide that loans will be made available on a basis which treats United States nationals, nationals of other friendly countries and local citizens

⁹⁵ 68 Stat. 456 (1954) as amended, 7 U.S.C. § 1704 (Supp. V, 1958); *Seventh Semiannual Report*, *supra* note 83, 38 DEPT. OF STATE BULL. 476, 483-87 (1958).

⁹⁶ *Id.* at 481.

⁹⁷ *Id.* at 489. The materials acquired are placed in a "supplemental stockpile." 70 Stat. 200 (1956), 7 U.S.C. § 1856 (Supp. V, 1958).

⁹⁸ 68 Stat. 457 (1954), 7 U.S.C. § 1704(g) (Supp. V, 1958).

⁹⁹ *Sixth Semiannual Report*, *supra* note 81, 37 DEPT. OF STATE BULL. 281, 283 (1957).

¹⁰⁰ *Hearing on Extension of Public Law 480, Before the Senate Committee on Agriculture and Forestry*, 85th Cong., 1st Sess. 6 (1957) (statement of Earl L. Butz).

¹⁰¹ *Seventh Semiannual Report*, *supra* note 83, 38 DEPT. OF STATE BULL. 476, 486 (1958).

¹⁰² *Id.* at 484; *Sixth Semiannual Report*, *supra* note 81, 37 DEPT. OF STATE BULL. 281, 290 (1957).

¹⁰³ *Seventh Semiannual Report*, *supra* note 83, 38 DEPT. OF STATE BULL. 476, 485 (1958).

equally as to interest rates, terms and conditions. Lending procedures are established and the loans administered by lending agencies of the foreign governments. The United States continues to seek agreements of this kind as to proceeds from sales made prior to fiscal year 1957.

By the Cooley amendment enacted in August 1957 these procedures were changed to the advantage of United States businessmen.¹⁰⁴ Henceforth, a portion of the currencies is to be reserved for loans directly from the United States Government through the Export-Import Bank. The category of eligible borrowers is narrowed to (a) United States business firms and their branches, subsidiaries or affiliates and (b) domestic or foreign firms which aim at increasing markets for United States agricultural products. Each loan approval is subject to veto by the government of the country concerned. The prohibition on loans that would promote competing agricultural production is made explicit, and a further proviso prohibits loans for the manufacture of *any* product to be exported to the United States in competition with United States products. Again, development abroad is subordinated to development at home where a conflict appears.

The amendment authorized the use of 25% of the currencies for this purpose. The Conference Report on the amendment added that the full 25% was to be used "unless there are compelling reasons for using a less amount."¹⁰⁵ During the first six months of operation under the amendment sales agreements were negotiated with Israel, France, Mexico and Pakistan reserving 25% of the proceeds and with Greece reserving 15%.¹⁰⁶ These allocations to the Export-Import Bank diminish the portion of the proceeds available for loans to foreign governments. This proportion declined during the first half of fiscal year 1958 to 40% of the proceeds of sales as compared to 62% during fiscal year 1957.¹⁰⁷ American businessmen to this extent have replaced foreign governments as the agents of "development."

The act also contains authority to make grants, as distinguished from loans, for development purposes.¹⁰⁸ In order to protect the loan program, the Administration has elected not to use this except in special circumstances. Approximately 3% of sales proceeds have been allocated to grants, mainly to India.¹⁰⁹

¹⁰⁴ 71 Stat. 345 (1957), 7 U.S.C. § 1704(e) (Supp. V, 1958).

¹⁰⁵ H.R. REP. NO. 683, 85th Cong., 1st Sess. 4 (1957), 1957 U.S. CODE CONG. & AD. NEWS 1433.

¹⁰⁶ *Seventh Semiannual Report*, *supra* note 83, 38 DEPT. OF STATE BULL. 476, 483 (1958).

¹⁰⁷ *Id.* at 484.

¹⁰⁸ 68 Stat. 456 (1954) as amended, 7 U.S.C. § 1704(e) (Supp. V, 1958).

¹⁰⁹ *Seventh Semiannual Report*, *supra* note 83, 38 DEPT. OF STATE BULL. 476, 483 (1958); *Hearing on Extension of Public Law 480, Before the Senate Committee on Agriculture and Forestry*, 85th Cong., 1st Sess. 22 (1957).

GUARANTY OF PRIVATE INVESTMENT

A program to encourage private United States investment abroad by offering a United States Government guaranty against certain peculiar risks began in 1948 as a feature of the Marshall Plan.¹¹⁰ The original protection was available only in the European area and covered only convertibility from European currencies into dollars in the amount of the original investment. It was hoped that this inducement would reduce the need for government aid by bringing in capital from private sources. This initial program did not receive much response from the investment community.

The coverage has been steadily broadened in succeeding years.¹¹¹ The Government is now authorized to act as an insurer against losses from the following causes: (1) non-convertibility, (2) expropriation and confiscation and (3) war.¹¹² No protection is offered against losses from general devaluation of a foreign currency, unfavorable exchange rate, taxation, wage regulation, labor unrest and business risks that attend any investment.¹¹³

The investor may insure any amounts he chooses up to the maximum allowable. For coverage against expropriation and confiscation of an equity interest, this maximum is fixed at 200% of the dollar amount of the investment.¹¹⁴ Undistributed earnings and realized capital gains as well as the original investment are given protection. War risk coverage applies only to physical property. It cannot exceed 90% of value, so that the investor remains a co-guarantor as to 10%.¹¹⁵

The investor pays a fee of one half of one percent for each of the three

¹¹⁰ 62 Stat. 144 (1948).

¹¹¹ For the stages in the development of the program, see TIDD, *The Investment Guaranty Program and the Problem of Expropriation*, 26 GEO. WASH. L. REV. 710 (1958) and Note, *United States Agencies and International Organizations Which Foster Private American Investment Abroad*, 71 HARV. L. REV. 1102, 1112 (1958). The House Foreign Affairs Committee has constantly pressed for extensions of coverage. Senator Dirksen has championed the program in the Senate. *Hearings on Mutual Security Appropriations for 1958 Before the Senate Committee on Appropriations*, 85th Cong., 1st Sess. 182 (1957).

¹¹² 68 Stat. 847 (1954) as amended by 70 Stat. 558 (1956), 22 U.S.C. § 1933(b) (4) (B) (Supp. V, 1958).

¹¹³ For a discussion of the meaning of "expropriation" and "nonconvertibility" as used in the act, see Note, *United States Agencies and International Organizations Which Foster Private American Investment Abroad*, 71 HARV. L. REV. 1102, 1119 (1958).

¹¹⁴ This limit does not appear in the act but is fixed by administrative policy. Tidd, *The Investment Guaranty Program and the Problem of Expropriation*, 26 GEO. WASH. L. REV. 710, 711 (1958).

¹¹⁵ This is to reduce the temptation to cut investment losses by stirring up war. Because the Senate Foreign Relations Committee fears a losing business might foster insurrection or revolution, these are still excluded from coverage despite repeated proposals from the House. *Hearings on the Mutual Security Act of 1957 Before the House Committee on Foreign Affairs*, 85th Cong., 1st Sess. 1271 (1957) (Representative Walter H. Judd).

types of protection.¹¹⁶ Though the law authorizes fees to be fixed at higher rates,¹¹⁷ the National Advisory Council on International Financial and Monetary Problems decided that rates must be very low if the coverage is to serve its purpose. The rate schedule is to be re-examined in 1967.¹¹⁸ In the meantime it is not likely to be raised, though it may be lowered. The bulk of the risk is thus being borne by the American people rather than by the business interests assured. There is no attempt to confine the program to safe situations.¹¹⁹ Geographical coverage is now limited only by the requirement that the country concerned have concluded a guaranty agreement with the United States and that the investor have obtained consent of the foreign government to inclusion of his investment under the agreement.

Any United States citizen or United States company in which United States citizens own a majority interest is eligible. The investment must be either new or an increase of an existing investment. It may be in the form of money, equipment, materials or licenses to use patents, processes or techniques. Equity interests as well as loans and right to royalties are insurable. Guaranty contracts run for a period of 20 years. Loans for periods of less than three years and equity interests to endure less than five years are not insured.¹²⁰ Applications are made to the International Cooperation Administration,¹²¹ which will tailor the terms of the contract to the individual situation. The administration of the contract is assigned to the Export-Import Bank, to whom fees are paid.

The bilateral guaranty agreements negotiated by the Administration with foreign governments provide for a recognition of the United States as subrogee after it has paid claims of the assured.¹²² Claims and funds thus acquired by the United States are to be accorded no less favorable treatment than if they were privately owned. The agreements do not purport

¹¹⁶ International Cooperation Administration, *Investment Guaranty Handbook* 17, 21, 25 (1957).

¹¹⁷ One percent for nonconvertibility protection, 4% for expropriation/confiscation and 4% for war risks. 68 Stat. 847 (1954) as amended, 22 U.S.C. § 1933(b)(4)(E) (Supp. V, 1958).

¹¹⁸ *Hearings on the Mutual Security Act of 1957 Before the Senate Committee on Foreign Relations*, 85th Cong., 1st Sess. 568 (1957) (statement of Charles B. Warden).

¹¹⁹ "Our program is for the areas of risk where the country position is occasionally so weak that it is no longer bankable . . . We cannot ever take refuge in the more simple and the safer tests of the banker." *Hearings on the Mutual Security Act of 1958 Before the House Committee on Foreign Affairs*, 85th Cong., 2d Sess. 1089 (1958) (statement of Charles B. Warden). There is no problem in this operation of staying clear of private insurance preserves. Because the risks are so unpredictable, private companies do not offer protection.

¹²⁰ *Id.* at 1703.

¹²¹ This may be changed to the Development Loan Fund in the future under authority of a 1958 amendment to the act. *Mutual Security Act of 1958*, 72 Stat. 267.

¹²² As of April 1958, guarantee agreements had been negotiated with 37 states. Not all covered all three types of insurance. For complete table see *Hearings on the Mutual Security Act of 1958 Before the House Committee on Foreign Affairs*, 85th Cong., 2d Sess. 1699 (1958).

to add any obligations on the part of the foreign government to treat an American investor in any particular manner.¹²³ They usually provide that negotiation and arbitration shall be available for the settlement of disputed claims, except war claims, to which the United States is subrogated.¹²⁴

The makers of American policy respond to the claims of the poorer states for an opportunity to develop their economies with this program to encourage American private investments abroad. Foreign governments are to be educated to accept the investor, and the investor is to be made bold by guaranties.¹²⁵

Because our own economy has developed mainly under private enterprise, it is easy to leap to the conclusion that other people will derive the same benefits as Americans from the expanded activities of the American investor. Our government programs to facilitate more overseas investment are frequently justified rather piously in terms reminiscent of an earlier "white man's burden." The government has enacted these measures, the country is told, "in recognition of the contribution that American private enterprise can make to the efforts of free world countries to develop their economies more fully"¹²⁶ Perhaps so. But a glance at the profits for Americans in such a policy ought to make us rather suspect that opportunism has affected the formation of official opinion more than a little.

By assigning the task of development to private investors, Americans are saved the tax burden of financing a program out of public funds. This is clearly one of the reasons Congress expresses such faith in private investment over public aid. The profits to the investors themselves are large. It is not possible for outsiders to know with precision how much total return is being received and accumulated. An indication of their measure may be found in the statement of Alvin Mayne, based on his experience as Director of the Division of Economics and Statistics of the Planning

¹²³ The protection of American businessmen abroad is sought through bilateral Treaties of Friendship and Navigation. Treaties with 16 countries were negotiated during the decade 1946-56. See Walker, *The Post-War Commercial Treaty Program of the United States*, 73 POL. SCR. Q. 57 (1958); Walker, *Modern Treaties of Friendship, Commerce and Navigation*, 42 MINN. L. REV. 805 (1958); *Hearing on Commercial Treaties Before the Subcommittee of the Senate Committee on Foreign Relations*, 83rd Cong., 1st Sess. (1953).

¹²⁴ See, for example, agreements on guaranty of private investments with Pakistan, May 26, 1955, 6 U.S.T. & O.I.A. 2045, T.I.A.S. No. 3269, and with Honduras, Apr. 22, 1955, 6 U.S.T. & O.I.A. 2049, T.I.A.S. No. 3270. But the agreement with India, Sept. 19, 1957, contains no such provision. 8 U.S.T. & O.I.A. 1442, T.I.A.S. No. 3900.

¹²⁵ "Some of the answers for the less-developed areas lie in the education of foreign countries on climate matters Too few governments are as yet convinced that investments must be worked for and must be encouraged." *Hearings on the Mutual Security Act of 1957 Before the Senate Committee on Foreign Relations*, 85th Cong., 1st Sess. 569 (1957) (statement of Charles B. Warden).

¹²⁶ DEPT. OF STATE, DEPT. OF DEFENSE, INTERNATIONAL COOPERATION ADMINISTRATION, *THE MUTUAL SECURITY PROGRAM FISCAL YEAR 1959, A SUMMARY PRESENTATION* 119 (1958).

Board of Puerto Rico, that an expectancy of 30% profit on investment is needed to draw private capital from abroad.¹²⁷ It is not surprising to find the rentiers satisfied that they have devised the best of all possible arrangements. Their emissaries are called entrepreneurs. But they return as well laden with riches as conquistadors, so perhaps it is not yet certain how they are finally to be characterized.

A suspicion of opportunism is strengthened when the nature of the world wide political struggle is seen as one between capitalists and socialist ideals. Private entrepreneurs must be enabled to move into these areas of the new frontier before they are occupied by socialists. The guaranty program is a GI insurance for the dollars of capitalism which volunteer for duty at the fronts of the Cold War. Our government is not being fully candid when it expresses a desire for the "development" of other economies. It is not a neutral in this competition for new votaries between capitalism and socialism. It is concerned to see, not just development, but capitalist development. It is for this mission that our private investors are called to serve as the agents of destiny.

The other face of American policy appears in the United Nations Economic and Social Council, where since 1946 the underdeveloped countries have been urging the establishment of a Special United Nations Fund for Economic Development (S.U.N.F.E.D.).¹²⁸ The United States has consistently opposed this.¹²⁹ The reason offered is that the money wanted to make the program significant cannot be made available as long as the Soviet Union refuses to negotiate disarmament on our terms.¹³⁰ Yet the amounts under discussion range from only \$250 million to \$500 million per year. A proportionate American contribution of 40% would hardly

¹²⁷ William H. Stead, *Fomento—The Economic Development of Puerto Rico* (National Planning Association Pamphlet No. 103) 92 (1958).

¹²⁸ See U.N. Doc. No. A/3556 (1957) and General Assembly Resolution 1030 (XI) (1957).

¹²⁹ The question was discussed at the General Assembly in 1957. The Economic and Social Council had recommended the creation of SUNFED. U.N. EcoSoc. COUNCIL OFF. REC., 24th Sess., 994th meeting 203 (1957). A draft resolution to this effect was sponsored in Committee II of the Assembly by Argentina, Ceylon, Chile, Egypt, Greece, India, Indonesia, Mexico, Netherlands, Venezuela and Yugoslavia. U.N. Doc. No. A/C.2/L. 331 (1957); see 38 DEPT. OF STATE BULL. 64 (1958). The American delegate, Walter H. Judd, dealt with the strong movement in favor of this resolution in the following words: "Let me make it completely clear that the United States is not prepared at this time to support the establishment of a United Nations capital fund. The United States will vote against any resolution introduced at this session to establish such a fund, and we shall not participate in any preparatory commission that might be established now to draft the charter of such a fund." 38 DEPT. OF STATE BULL. 62-63 (1958).

¹³⁰ "The U.S. position on this subject is clear. Such a fund would require resources of at least \$400 million to \$500 million a year . . . The establishment of such an international development fund consequently depends on the achievement of a substantial measure of disarmament, and, here again, the Soviets are the chief stumbling block." Walter M. Kotschnig (Director, Office of International Economic and Social Affairs, U.S. Dept. of State), *International Aid for Underdeveloped Areas*, 38 DEPT. OF STATE BULL. 304, 311 (1958).

exceed \$200 million per year. There is no doubt that the transfer of this amount from the Development Loan Fund, which has been given appropriations of \$300 million in 1957 and \$400 millions in 1958, would be gratefully received by the majority of the nations of the world.¹³¹

This adamant refusal to support economic development through a United Nations fund is calculated to leave the field free to private enterprise.¹³² If countries hungry for development can receive foreign capital only as private investment, they cannot easily keep the door closed on our offer. But our business community knows with what reluctance the door is opened. This is publicly explained as a residual resentment against colonialism, expected to pass as soon as the Americans are seen to be good capitalists instead of bad capitalists. Investors are not so confident. Their security abroad has not recovered from the liquidation of colonialism as a political system.¹³³ Before that cataclysm they could count on the protection of familiar laws and courts and an understanding local government dominated by Europeans. That protection gone, neither treaties nor general international law offers a satisfactory substitute.¹³⁴ With the retreat of European judges and administrators, businessmen must look for their protection to a new and native intellectual class which gives the imperatives of nationalism priority over the rights of contract and private property. It is a sign of the times that the Soviet delegate was vigorously applauded at the Afro-Asian Peoples Solidarity Conference in Cairo in 1957 when he urged the expropriation of foreign owned enterprises to be an effective way to make progress on economic development.¹³⁵

¹³¹ The following amounts were appropriated by Congress for bilateral development assistance from 1954 to 1956, exclusive of development aid in the "defense support" and "special economic assistance" categories: \$199 million, 68 Stat. 840 (1954); \$262 million, 69 Stat. 435 (1955); \$250 million, 70 Stat. 734 (1956).

¹³² The Special Projects Fund approved by the General Assembly in December 1957 on a proposal of the United States is not a capital fund. U.N. Doc. No. A/Res/1219 (XII) (A/C.2/L.331/Rev. 1) (1957), reprinted 38 DEPT. OF STATE BULL. 71 (1958). It is to be used to finance surveys of natural resources, industrial and agricultural research projects, and technological institutes. The United States regards it as a fund which will promote private investment. 38 DEPT. OF STATE BULL. 310 (1958).

¹³³ "In recent years the rate of all private capital invested in the less developed areas of Asia, the Middle East and Africa has averaged only \$119 million per year. This is obviously only a small fraction of the needs of these nations for outside capital." DEPT. OF STATE, DEPT. OF DEFENSE, INTERNATIONAL COOPERATION ADMINISTRATION, BACKGROUND FOR MUTUAL SECURITY FISCAL YEAR 1959, 27 (1958). Sixty-two per cent of new United States direct private investment abroad in 1956 went to oil investment, where the profits are great enough to keep investment flowing in spite of risks. Oil excluded, only \$79 million, 4% of the total net flow, went to Asia, the Middle East and Africa. *Id.* at 28.

¹³⁴ See Tidd, *The Investment Guaranty Program and the Problem of Expropriation*, 26 GEO. WASH. L. REV. 710, 722-28 (1958).

¹³⁵ New York Times, Dec. 28, 1957, p. 1 (late city ed.). The Chief of the Investment Guaranties Staff of the International Cooperation Administration referred to this "astonishing development" as one of the recent causes for a reluctance to invest abroad. *Hearings on the Mutual Security Act of 1958 Before the House Committee on Foreign Affairs*, 85th Cong., 2d Sess. 1089 (1958) (statement of Charles B. Warden).

Against these Marxian winds sweeping Asia, Africa and the Middle East the guaranty program offers a "shield for business abroad."¹³⁶ It is aimed to serve as a substitute for the old colonial regimes that formerly gave business security. That some kind of shield should be necessary does not speak well for international private enterprise as a vehicle of development. Apparently these backward states have to be developed in spite of themselves. The reluctance of their governments to take the steps necessary to create a favorable climate for investment from abroad lends support to the thesis that foreign enterprises use the human and material resources of their host countries more to the advantage of the economy that sends them than of the nation they penetrate.¹³⁷ The extractive industries which feed raw materials into the machines of Western factories are of obvious utility to the Western investor who carries them away for a profit and to the Western industrialist who buys them for resale in his products at more profit. But the wages paid to local labor and the taxes or royalties paid to local governments do not create a general feeling of satisfaction with the distribution of benefits from the operation. Since private investors focus on profits, they cannot give primary importance to the development needs of local economies.

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

As the largest contributor of capital to the International Bank for Reconstruction and Development (IBRD) the United States controls the largest bloc of votes, 30%, on the Board of Governors and in meetings of the Executive Directors.¹³⁸ Since the British control 12% of the votes, the Anglo-American combination is large enough for effective control over policy. Therefore the operations of the Bank and its affiliate, the International Finance Corporation, must also be included in an examination of United States foreign development programs.

The IBRD was established in 1945 following the approval by a majority of the states represented at the Bretton Woods Conference in 1944 of the Bank's Articles of Agreement.¹³⁹ Sixty-four states are now members of the Bank.¹⁴⁰ Although represented at Bretton Woods, the Soviet Union

¹³⁶ Phrase used to describe the program in *Time*, July 28, 1958, p. 60.

¹³⁷ See *BARAN, THE POLITICAL ECONOMY OF GROWTH* (1957); *MYRDAL, RICH LANDS AND POOR* (1957). For a summary of the limitations of private investment as a means of economic development, see *THE RESEARCH CENTER IN ECONOMIC DEVELOPMENT AND CULTURAL CHANGE OF THE UNIVERSITY OF CHICAGO, THE ROLE OF FOREIGN AID IN THE DEVELOPMENT OF OTHER COUNTRIES* 53-56 (Comm. Print, Senate Special Comm. to Study the Foreign Aid Program, 85th Cong., 1st Sess., 1957).

¹³⁸ IBRD, Articles of Agreement, art. V, § 3, 60 Stat. 1440 (1945), 2 UNTS 134 (1947), (hereinafter cited as IBRD, Articles of Agreement); IBRD, *TWELFTH ANNUAL REPORT* 50 (1957).

¹³⁹ 60 Stat. 1440 (1945), 2 UNTS 134 (1947).

¹⁴⁰ IBRD, Supplement to the Twelfth Annual Report 1 (1958).

has never become a member. Poland withdrew from membership in 1950,¹⁴¹ and Czechoslovakia was expelled in 1953 for non-payment of the balance due on its capital subscription.¹⁴² Yugoslavia is the only communist state member. The Bank is not, strictly speaking, a World Bank, though this is its popular name.

The widespread defaults by governments of the poorer countries in the 1930's on their bond issues floated in the capital markets of Europe and the United States had left investors exceedingly wary of advancing funds to such borrowers. These defaults were attributed to the inability of the borrowing governments to make effective use of the capital raised and to manage their financial affairs prudently.¹⁴³ The International Bank aims at reviving the flow of private capital across national boundaries by giving Western investors increased security. The old channel directly from investor to foreign government had ceased to inspire confidence. The new Bank was designed to reassure investors by giving them, instead of the discredited security of the borrowing governments, the security of a guaranty of repayment by the governments of the United States, Great Britain and the other strong, capitalist states. The Bank is thus able to borrow by the sale of its obligations in Western capital markets. These are safe investments and sell readily, because they are backed by the capital subscriptions of the member governments, and in particular by the United States.¹⁴⁴

The Bank then makes loans to those governments which are members of the Bank, or to private borrowers on the guarantee of the government in whose territories the project is located.¹⁴⁵ The bank is in a position to do what private investors had not been able to do, to study each project carefully, to protect investors from imprudent borrowers and to police the

¹⁴¹ IBRD, SIXTH ANNUAL REPORT 47 (1951).

¹⁴² IBRD, TENTH ANNUAL REPORT 26 (1955).

¹⁴³ "Capital raised through sales of securities in foreign capital markets had frequently made little or no contribution to the productive capacity of the borrowers. Many of the loans had also been made without reference to the ability of the borrowers to service new, or even existing, foreign debt. These lending practices undoubtedly contributed to the widespread defaults in the 1930's." IBRD, *THE WORLD BANK: POLICIES AND OPERATIONS* 6 (1957).

¹⁴⁴ At the end of Jan. 1958, the Bank had a funded debt of \$1,401 million, a little more than half from the sale of its bonds to purchasers in the United States, most of the remainder from sales to purchasers in Canada and Western Europe. IBRD, Supplement to the Twelfth Annual Report 8 (1958); IBRD, *THE WORLD BANK: POLICIES AND OPERATIONS* 92-109 (1957). The Bank's bonds are now legal investments in most of the United States for trust funds, insurance companies, savings banks and commercial banks. Some states have made them legal investments for public funds, e.g., state employees' pension funds. Federal legislation exempts the Bank's obligations from certain provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934, according them the same general treatment under these acts as United States Government, state and municipal bonds. United States banks have helped develop the market for the bonds by acting as underwriters and distributors. *Id.* at 93-95.

¹⁴⁵ IBRD, Articles of Agreement, art. III, § 4.

use of borrowed funds to assure that they are used only for purposes approved by the lender. All these functions are imposed upon the Bank by its Articles of Agreement.¹⁴⁶ The Bank is a truly international institution, corporate in form, through which investors from many different countries are enabled to put their funds safely to work earning interest in many other countries.

It is also truly international in the respect that the loans are not tied to purchases in any particular country. Borrowers may call for competitive bids from suppliers of different countries and buy where they find the best values. The Bank is apparently careful in exercising its control over the use of loan funds not to recommend particular suppliers or favor one country over another.¹⁴⁷

The total authorized capital stock of the Bank is \$10 billion.¹⁴⁸ The capital subscription of each member government is divided into three parts: (1) Two percent of each subscription is payable in gold or United States dollars, which may be used freely by the Bank in any of its operations. (2) Eighteen percent of each subscription is payable in the currency of the subscribing member. The most important assets of the bank in this category are the subscriptions from the hard currency countries, United States, Canada and Western Europe. These funds may be lent only with the consent of the member whose currency is lent. The United States and Canada have given consent as to their full eighteen percent. Other states have given consent as to varying amounts. (3) The remaining eighty percent of each subscription is not available to the Bank for lending but is subject to call if required by the Bank to meet its obligations.¹⁴⁹ It is this part of the subscription which gives private lenders their security.¹⁵⁰

Although the Bank is not permitted to make loans which any private bank wishes to make on reasonable terms,¹⁵¹ the Bank operates at a profit. This it achieves like any well run bank, by charging more interest for the money it lends than it pays on the money it borrows. Loans are made for

¹⁴⁶ IBRD, Articles of Agreement, art. III, §§ 4 and 5.

¹⁴⁷ IBRD, Articles of Agreement, art. III, § 5(a); IBRD, *THE WORLD BANK: POLICIES AND OPERATIONS* 47 (1957).

¹⁴⁸ IBRD, Articles of Agreement, art. II, § 2(a).

¹⁴⁹ IBRD, Articles of Agreement, art. II, § 5.

¹⁵⁰ By an exchange of letters with the Secretary of the Treasury, President Eisenhower recently indicated that the United States is to seek an increase in the authorized capital of the Bank. *New York Times*, Aug. 27, 1958, p. 1 (late city ed.). That this should be necessary when the Bank has outstanding only \$1.7 billion in bonds while the total of unpaid subscriptions subject to call amounts to \$7.4 billion is probably due to the insistence of investors that the United States subscription by itself continue to cover all amounts outstanding as they increase. As the United States is now subject to call of only \$2.5 billion, plans are being made to raise this before the level of Bank debt approaches it too closely. IBRD, *TWELFTH ANNUAL REPORT* 50 (1957).

¹⁵¹ IBRD, Articles of Agreement, art. III, § 4(ii).

terms of 5 to 25 years at interest rates which follow the private banking market.¹⁵² Earnings are credited to reserves. The Bank has not had any defaults in payments of interest or principal on its loans.¹⁵³ Principal amounts repaid and proceeds from the sale of loans to private investors from the Bank's portfolio make further funds available for relending.

Under the guidance of its first permanent president, John J. McCloy of the United States, the Bank formulated and announced its policy in making loans:¹⁵⁴

It cannot be too often emphasized that the Bank must rely on private investment funds rather than on its paid-in capital for the main portion of its loanable resources The Bank cannot make imprudent loans. It must act with care and wisdom in building up its portfolio, for on that portfolio, and on the confidence which it will inspire in the investing public, the Bank must ultimately rely for its capacity to raise funds.

This conservatism added to the fact that the loans must be repaid in hard currencies has prevented the Bank from making any spectacular contributions to the development of the economies of any country. After four years of operation the Bank was pessimistic about the possible pace of development: "The most striking single lesson which the Bank has learned in the course of its operations is how limited is the capacity of the underdeveloped countries to absorb capital quickly for really productive purposes."¹⁵⁵ These difficulties were rooted primarily in the burden of debt, and debt in foreign exchange, which every new transaction of the Bank imposed upon the borrowing state. It was not enough that a project promised increased production through a more rational use of human and material resources. The increase must improve the foreign exchange position of the borrowing state sufficiently to offer good prospect that the added debt could be serviced. These considerations led naturally to the position that the foreign government must look primarily to private in-

¹⁵² The total of accumulated net earnings and loan commissions stood at \$324 million as of Jan. 31, 1958. At that time the interest rate on Bank loans was 5½%. IBRD, Supplement to TWELFTH ANNUAL REPORT 7 (1958).

¹⁵³ IBRD, THE WORLD BANK: POLICIES AND OPERATIONS 74 (1957); IBRD, TWELFTH ANNUAL REPORT 10 (1957).

¹⁵⁴ IBRD, SECOND ANNUAL REPORT 15-16 (1947).

¹⁵⁵ IBRD, FOURTH ANNUAL REPORT 8 (1949). What this discovery really teaches is the poor adaptation of the Bank to the problems of the underdeveloped countries. This ineptitude in all capitalist governments, including their government banks and their international agencies, is suggested by United Nations data on the economic aid they rendered during the three-year period 1954-1956. These show that the least developed states received the *lowest* per capita amount of economic aid, including grants and loans of terms longer than 5 years. Those states with a per capita gross national product of less than \$100 are considered to form the group of least developed. It includes Afghanistan, Burma, Ethiopia, India, Indonesia, Iran, Liberia, Nepal, Pakistan, Thailand and Yemen. Aid to South Korea is excluded as a special case. No data was available on economic aid to Jordan. UNITED NATIONS STATISTICAL YEARBOOK 456 (1957).

vestments from abroad rather than to its own borrowing as the medium of development. "There is a vast difference . . . between the amount of money which can usefully be employed and the amount of additional external debt which the underdeveloped countries can prudently assume. At best, therefore, Bank financing, which imposes an additional burden of external debt, can provide only a part of the foreign capital necessary for development It is plainly desirable that direct private investments on mutually fair terms, be the major source of foreign capital for development."¹⁵⁶

Under the leadership of Eugene Black of the United States, former Vice President of the Chase National Bank of New York, who became President of the International Bank in 1949,¹⁵⁷ this concentration of the Bank's resources on improving the advantages to private entrepreneurs of investing equity capital in the borrowing country has continued to be one of the principal characteristics of policy. Loans directly to private borrowers have been limited on account of the requirement in the Articles of Agreement that all loans be guaranteed by the government or the central bank of the territory where the project is located.¹⁵⁸ Governments have not been willing to sponsor private enterprises, and private entrepreneurs are unwilling to subject their operations to the surveillance of the guaranteeing government. These inhibitions on the Bank's ability to promote private investment were one of the reasons for the creation in 1956 of the International Finance Corporation, which makes investments in privately owned enterprises without government guarantees.¹⁵⁹

The Bank is able to help private investors, however, in several other ways. It concentrates its loans on the development of such basic facilities as power and transport. The availability of these services enables private investors to establish their operations with more convenience and a smaller investment of their own. In the absence of a willingness on the part of private capital to advance loans for building these facilities and with the end of the colonial regimes which were able formerly to supplement private lending with government appropriations for public utilities, this was a field where the Bank's resources were clearly needed by prospective investors. Many such projects have been financed, while those of a primarily social character, such as sewage, water supply, housing, hospitals, and schools have normally been rejected.¹⁶⁰ This emphasis naturally is more satisfying

¹⁵⁶ IBRD, FOURTH ANNUAL REPORT 13 (1949).

¹⁵⁷ Mr. McCloy, whom Mr. Black succeeded at the International Bank, became chairman of the board of the Chase-Manhattan Bank in 1955.

¹⁵⁸ IBRD, Articles of Agreement, art. III, § 4(i).

¹⁵⁹ See text beginning at note 174 *infra*; IBRD, THE WORLD BANK: POLICIES AND OPERATIONS 51 (1957).

¹⁶⁰ *Id.* at 43.

to foreign investors than to local inhabitants. It reveals a serious deficiency of the Bank as an institution for promoting the welfare of the people of the underdeveloped countries.

The private sector of the local economies has also been aided by loans directly to industrial enterprises where a government guarantee could be obtained and by loans to government banks for relending to manufacturing and mining enterprises, for the most part privately owned.¹⁶¹ There has also been a substantial volume of loans for the development of agricultural potential by means of irrigation, land clearance and flood control. One loan of \$10 million in collaboration with American, British and Indian private capital was made to the Industrial Credit and Investment Corporation of India "to encourage the growth of private industry in India."¹⁶²

The Bank also affects the investment climate through the influence it brings to bear on local governments to modify their policies, not only to give better security to the Bank of repayment on its own loans, but to provide more incentives to foreign investors. There is no doubt that the Bank performs this function.¹⁶³ Basing its policy on the responsibility under the Articles of Agreement to encourage international investment¹⁶⁴ the Bank has frequently insisted as a condition on approval of a loan that steps be taken to establish financial and monetary stability and to reach a settlement with foreign creditors on obligations in default. The Bank advises also that it will be deterred from lending where an expropriation of foreign private interests for political reasons takes place, raising an obligation to use scarce foreign exchange resources as compensation.¹⁶⁵ Bank officials make no secret of the fact that they are on the side of capitalism in its competition with socialism in the underdeveloped countries. Mr. Black has been characterized as the world's best salesman of the private enterprise system.¹⁶⁶ It would be unrealistic to suppose that he subdues this bias when considering what loan applications to approve. Nor is it likely that the faculty of the Economic Development Institute in Washington, where officials from borrowing countries come to study development problems under the Bank's tutelage, is neutral or indifferent. Mr. Black has made clear that

¹⁶¹ *Id.* at 68.

¹⁶² *Ibid.*

¹⁶³ Mr. Black wrote in 1951: "As an international institution, we are in a position not only to make loans without the accusation of ulterior political motives, but also to recommend to the borrowing countries such reforms in fiscal and monetary matters and their general economic policies as we consider an essential prerequisite for their economic development, for the soundness of our loan operations, and conducive to all private investment, local and foreign." IBRD, Letter M-2204 of March 26, 1951 to Mr. Charles Symington (mimeographed reprint by IBRD).

¹⁶⁴ IBRD, Articles of Agreement, art. I(ii).

¹⁶⁵ IBRD, *THE WORLD BANK: POLICIES AND OPERATIONS* 49-50 (1957).

¹⁶⁶ *Time*, June 25, 1956, p. 80.

neither he nor anyone else in the Bank favors state planning in any form.¹⁶⁷

The absence of the Soviet Union from the councils of the Bank and the dominating position of the United States and England enable it to function with quiet efficiency. To insulate it from pressures that might be brought by borrowers through the United Nations, where they are in the majority, a clause was inserted in the agreement establishing the relationship between the Bank and the United Nations to the effect that "it would be sound policy [for the United Nations] to refrain from making recommendations to the Bank with respect to particular loans or with respect to terms or conditions of financing by the Bank."¹⁶⁸ Also, the United Nations specifically recognizes that "the action to be taken by the Bank on any loan is a matter to be determined by the independent exercise of the Bank's own judgment,"¹⁶⁹ that is, by the independent exercise of judgment by the governments of the United States and England.¹⁷⁰

The Senate has recently passed a resolution proposed by Senator Monroney calling upon the National Advisory Council to study the feasibility of establishing an International Development Association, which would be authorized to make longer term loans, at lower interest rates, repayable in local currencies.¹⁷¹ This would add to international financing institutions a bank with a function similar to that of the Development Loan Fund. It is not surprising that the Senate specified that the new association is to be an affiliate of the International Bank. The President in directing that the study be undertaken repeated the condition that the proposed agency operate as an affiliate of the Bank, which, he said, "has carried on [its] activities on a basis that has earned for the bank the confidence of all major private capital markets."¹⁷² One need not be a seer to predict that the new agency will bear no resemblance to SUNFED, that it will respect the wishes of private banks of the West and that it will be used primarily to manure opportunities for private investment.

INTERNATIONAL FINANCE CORPORATION

The International Finance Corporation was established by international agreement in 1956 as an affiliate of the International Bank. This followed

¹⁶⁷ IBRD, Letter M-2204 of March 26, 1951 to Mr. Charles Symington (mimeographed reprint by IBRD).

¹⁶⁸ Agreement Between The United Nations and The International Bank for Reconstruction and Development, art. IV (1947), 16 UNTS 348 (1948).

¹⁶⁹ *Ibid.*

¹⁷⁰ The Governors of the Bank serve at the pleasure of the government of the member state which appoints them. IBRD, Articles of Agreement, art. V, § 2. Five of the Executive Directors, including the United States and British Executive Directors, are also appointed by their respective national governments for two-year terms. Art. V, § 4. Because voting by both Governors and Executive Directors is weighted according to capital contribution, the United States and England together control all decisions. Art. V, §§ 3, 4.

¹⁷¹ S. Res. 264, 85th Cong., 2d Sess., 104 Cong. Rec. 13505 (1958).

¹⁷² New York Times, Aug. 27, 1958, p. 6 (late city ed.).

several years of discussion and controversy at the United Nations, at the Bank and within the United States Government.¹⁷³ The inability of the underdeveloped states to make a satisfactory advance toward industrialization under Bank loan policies raised the pitch of demands for SUNFED. In the United States, officials were aware of this clamor, but they were also aware that it was irreconcilable with American policy and, further, that strong pressure was developing in Washington for a reduction in the expenditure of public funds for foreign aid. The International Finance Corporation was finally accepted, with strong support from Mr. Black of the Bank, as a way out of the impasse.

The purpose of the Corporation as defined in the Articles of Agreement is "to further economic development by encouraging the growth of productive private enterprise in member countries, particularly in the less developed areas."¹⁷⁴ This general purpose is to be achieved by (1) making supplementary investment capital available to private investors, (2) seeking "to bring together investment opportunities, domestic and foreign private capital, and experienced management," and (3) helping to create conditions conducive to the flow of private capital.¹⁷⁵ Though the Corporation may not finance an enterprise against the objection of the government of the territory in which the enterprise is to operate, a guarantee by the government is neither sought nor accepted.¹⁷⁶ In fact, the Corporation will not lend to any enterprise in which a government has an interest unless the Corporation is satisfied as to its essentially private character.¹⁷⁷ The Corporation will concentrate its resources on industrial projects. Thus the effect will be to minimize the participation of local governments in the industrial sector by strengthening the freedom of investors to enter an economy without government support. Local planning is by-passed. "[T]he IFC will not usually concern itself with the priority of the project as against other development projects in the same country."¹⁷⁸ Profitability, the extent to which other private investment will be promoted and diversification in the IFC portfolio are the chief criteria in allocating IFC resources.¹⁷⁹ Housing, hospital and schools do not qualify.¹⁸⁰

IFC funds are derived from capital subscriptions which become pay-

¹⁷³ A detailed account of these negotiations is given in Matecki, *Establishment of the International Finance Corporation: A Case Study*, 10 INTERNATIONAL ORGANIZATION 261 (1956).

¹⁷⁴ IFC, Articles of Agreement, art. I, Dec. 5, 1955 [1956], 7 U.S.T. & O.I.A. 2198, T.I.A.S. No. 3260 (1956).

¹⁷⁵ *Ibid.*

¹⁷⁶ IFC, Articles of Agreement, art. III, § 3(ii), Dec. 5, 1955 [1956], 7 U.S.T. & O.I.A. at 2202; IBRD, WORLD BANK: POLICIES AND OPERATIONS 110 (1957).

¹⁷⁷ IBRD, WORLD BANK: POLICIES AND OPERATIONS 112 (1957).

¹⁷⁸ *Ibid.*

¹⁷⁹ *Ibid.*; IFC, The International Finance Corporation 5 (1956).

¹⁸⁰ IBRD, World Bank: Policies and Operations 112 (1957).

able in full in gold or dollars upon acceptance of membership.¹⁸¹ Authorized capital stock is \$100 million of which \$93 million had been subscribed as of July 25, 1958.¹⁸² Only members of the Bank are eligible for membership in the Corporation,¹⁸³ which numbered 55 countries in July 1958.¹⁸⁴ A schedule of authorized subscriptions which also determines the voting power of the members, was included as an annex to the Articles of Agreement. The United States controls approximately 34% of the votes, the United Kingdom approximately 14%, so that between them they determine policy.¹⁸⁵ Although the Corporation is a legal entity distinct from the Bank, thus assuring that the riskier ventures of IFC will not affect the prime quality of the Bank's bonds, the two organizations work in complete coordination. This is assured by the fact that the members of the Board of Governors and the Executive Directors of the Bank are *ex officio* members of the corresponding boards of the Corporation to the extent the state each represents is a member of both organizations. The President of the Bank is *ex officio* Chairman of the Board of Directors of the Corporation. The President of the Corporation, who is the chief of its operating staff, is nominated by the President of the Bank.¹⁸⁶ The first to hold this office is Robert L. Garner of the United States, who has previously been Vice President of the Guaranty Trust Company of New York, financial Vice President of General Foods Corporation and from 1947 to 1956 Vice President of the International Bank. Two of his three principal assistants are Americans, the third British.¹⁸⁷

The IFC will invest only in association with private capital. Ordinarily private investors are expected to put up more than half of the capital required. Particularly favored is a participation of both foreign and local capital in one project.¹⁸⁸ This serves to promote the growth of a local capitalist class prompted by its economic interest to defend and collaborate with Western investors. All enterprises to which IFC had committed funds during the first two years of its operation are companies in which European or United States interests have substantial participation.¹⁸⁹

¹⁸¹ IFC, Articles of Agreement, art. II, § 3(c), Dec. 5, 1955 [1956], 7 U.S.T. & O.I.A. at 2200.

¹⁸² IFC, Press Release No. 17, July 25, 1958.

¹⁸³ IFC, Articles of Agreement, art. II, § 1, Dec. 5, 1955 [1956], 7 U.S.T. & O.I.A. at 2199.

¹⁸⁴ IFC, Press Release No. 17, July 25, 1958.

¹⁸⁵ IFC, FIRST ANNUAL REPORT 17 (1957).

¹⁸⁶ IFC, Articles of Agreement, art. IV, § 5, Dec. 5, 1955 [1956], 7 U.S.T. & O.I.A. at 2207.

¹⁸⁷ Vice President: Beevor (British); Assistant to President: Demuth (U.S.); General Counsel: Sommers (U.S.). IFC, Press Release No. 1, July 25, 1956.

¹⁸⁸ IBRD, THE WORLD BANK: POLICIES AND OPERATIONS 111 (1957).

¹⁸⁹ The following commitments of IFC funds had been made as of July 25, 1958:

1. Siemens do Brasil Companhia (Brazil) (owned by Siemens of Germany) \$2 million. IFC, FIRST ANNUAL REPORT 7 (1957).

But IFC as an investor was made subject to certain limitations in deference to the prejudice of American businessmen against government share ownership in industry.¹⁹⁰ Its financing may not take the form of investments in capital stock. On the other hand, it can acquire rights to participate in the growth of the business. It may make a portion of the return on its investment contingent on earnings.¹⁹¹ It may acquire conversion rights and the option to purchase shares. These may be exercised only after the rights have been transferred by the Corporation to others.¹⁹² Thus the Corporation carries a part of the risk during the initial years of a venture and passes the full potential for profitability to private buyers. The Corporation may not manage an enterprise,¹⁹³ though it will normally insist that experienced and competent management be employed.¹⁹⁴ This is likely to favor managers from the already industrialized countries, since they serve to reassure investors.

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2. Engranes y Productos Industriales, S.A. (Mexico) (owned by Mexicans and Americans; American president; license arrangements with Borg-Warner Corp. of Chicago). \$600,000. IFC, Press Release No. 6, Aug. 13, 1957.
 3. Bristol de Mexico, S.A. (Mexico) (majority stock owned by Bristol of Canada, a subsidiary of the Bristol Aeroplane Co. Ltd. of England). \$520,000. IFC, Press Release No. 7 of Sept. 11, 1957.
 4. Empress Mínera de Mantos Blancos S.A. (Chile) (controlled by a Panamanian corp. controlled by Mauricio Hochschild and associates). \$2.2 million. IFC, Press Release No. 8, Sept. 16, 1957.
 5. Duncan's Holdings Ltd. (Australian) (associated with Hickson and Welsh of London). \$660,000. IFC, Press Release No. 9, Sept. 27, 1957.
 6. Olinkraft (Brazil) (subsidiary of Olin Mathieson Chemical Corp.). \$1.2 million, IFC, Press Release No. 11, Mar. 10, 1958.
 7. DLR Plásticos do Brasil (Brazil) (licensing arrangements with Bendix Aviation Corp. of Detroit, Russell Manufacturing Co. of Middletown, Conn., and Sheller Manufacturing Co. of Chicago). \$450,000. IFC, Press Release No. 13 of May 5, 1958.
 8. Steel Corp. of Pakistan Ltd. (Pakistan) (associated with Kloeckner Industrie Anlagen of Duisberg, Germany, which owns minority share interest and supplies equipment). \$630,000. IFC, Press Release No. 14, July 7, 1958.
 9. Merchant Bank of Central Africa, Ltd. (Federation of Rhodesia and Nyasaland) (international group of shareholders, including citizens of U.S., U.K., Belgium, France and Italy). IFC, Press Release No. 15, July 14, 1958.
 10. Willys-Overland do Brasil (Brazil) (Willys Motor, Inc., of Toledo, subsidiary of Kaiser Industries Corp., owns large minority interest, with American Overseas Finance Co. and Chase International Investment Corp. also participating). \$2.4 million. IFC, Press Release No. 16, July 11, 1958.

¹⁹⁰ Matecki, *Establishment of the International Finance Corporation: A Case Study*, 10 INTERNATIONAL ORGANIZATION 261, 270 (1956).

¹⁹¹ This is usually in addition to a fixed interest charge of 6% or 7% with maturities of 5 to 15 years. IFC, FIRST ANNUAL REPORT 7-11 (1957). IFC, *The International Finance Corporation* 6 (1957).

¹⁹² IFC, Articles of Agreement, art. III, § 2, Dec. 5, 1955 [1956], 7 U.S.T. & O.I.A. at 2201.

¹⁹³ IFC, Articles of Agreement, art. III, § 3(iv), Dec. 5, 1955 [1956], 7 U.S.T. & O.I.A. at 2202.

¹⁹⁴ IBRD, *THE WORLD BANK: OPERATIONS AND POLICIES* 113 (1957).

CONCLUSION

The key principle in American policy toward the economic development of other countries is that private business interests be permitted and helped to extend their overseas activities. These activities are mainly aimed at selling American goods or investing private capital abroad with the prospect of gains and profits convertible into dollars. It is assumed that the benefits to local populations incident to this profit-motivated expansion of operations by United States businessmen will be sufficient to satisfy the expectation of economic progress in the peoples of the underdeveloped areas. That this premise requires re-examination is demonstrated by the continuing insistence on the part of those peoples, against United States opposition, that development funds be provided through the United Nations, and in particular through agencies less subject to domination by the wealthiest industrialized and investor states. It would appear that such reappraisal can no longer be postponed without serious risk to the national interest of the United States.