INTERNATIONAL ECONOMIC INSTITUTIONS

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Dr. Virgil Salera, Senior Economist, American Enterprise Association, was born in San Francisco, California, on 22 September 1913. He received his B.S. and M.A. degrees from the University of California and his Ph.D. from Columbia. From 1936-38 he was an instructor and graduate student at the University of Minnesota. During 1939-40 he was abroad doing nontariff trade control research in Australia and Argentina. He began his career with the Government in 1941 in the Division of Monetary Research of the Treasury Department and was with the War Production Board in 1942; the Treasury Department in 1943; and during 1944-45 he was with the Foreign Economic Administration working on Lend-Lease matters. He taught successively at Miami University, Ohio, University of Denver, San Jose College, and Iowa State College. He became associated with the Government again in 1951 with the Mutual Security Agency working on international control of strategic trade with the Soviet bloc countries. He also served with the South American countries and returned to be the international specialist on the Senior Staff of President Eisenhower's Council of Economic Advisers. In 1955 he joined the staff of the Pan-American Union and in 1957 assumed his present position. Among his publications are: "International Economics" (with Enke) "Exchange Control and the Argentine Market," and "Elementary Economics" (with Nordin), and articles published in various journals chiefly with respect to Latin America. This is his first lecture at the College.

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CAPTAIN THOMPSON: Admiral Clark, Gentlemen: During this course in the review of basic economics we have heard many distinguished speakers talk from this platform in the general field of economics. In only the last period I am sure several of you were jarred loose of your sacred cows in economics by Dr. Clark. I am sure you will also recall Dr. Piquet's excellent lecture on foreign trade in theory and practice.

To further our interest in the international economic field we have with us this morning Dr. Virgil Salera, of the American Enterprise Association. Our lecturer has had a distinguished career both in Government and with private enterprise in the international economic field. Additionally, he has taught economics in five of our universities and colleges. Those of you in Discussion Group I already know Dr. Salera and can anticipate the treat that is in store for us in a few minutes.

His last position with Government was as an international specialist on the Senior Staff of the Council of Economic Advisers.

Among his publications are "International Economics" (with Enke) and "Exchange Control and the Argentine Market."

Dr. Salera is an old friend of the College, having previously participated in our seminar programs.

The title of his talk this morning is "International Economic Institutions." I would particularly like you to note Dr. Salera's analysis of United States policies and problems relating to these various international economic institutions, especially as they may very well affect you individually in future assignments.

It is a great pleasure to welcome to this platform Dr. Virgil Salera and to present him to the Class of 1959. Dr. Salera.

DR. SALERA: Admiral Clark, Gentlemen: It's a pleasure for me to be here today.

International economic institutions operate not in a vacuum, but in an international political setting. What are the highlights of this setting? We find that there are almost as many interpretations or emphases as there are writers on the subject. Here is a rundown from my angle of vision.

The United States on the one side and the Soviet Union on the other are the centers of today's bipolar world. Such bipolarity appears bound to increase even when account is taken of such developments as the build-up of mainland China and the emerging regional grouping of European states.

It is not bipolarity as such which needs to be discussed today, however. Much on that subject is already public knowledge. What needs to be stressed are the important byproducts of the bipolar situation.

The main byproduct, in my view, is that many countries are increasingly finding great attraction in two not necessarily mutually consistent developments. First, except for most of western Europe, one observes strong tendencies toward international political neutrality. Second, there is great pressure on both centers of the bipolar world, but chiefly on the more productive and generous American center, for increasing amounts of scarce economic resources, if possible on terms largely dictated by the neutralists themselves.

A byproduct only slightly less important is of the Trojan horse variety. I refer to the fact that only one of the bipolar centers has abundant native manpower locally in most countries to do its political dirty work. What is more, that center enjoys such help at virtually no economic cost to itself.

Such is my capsule version of the main political factors at work in much of the outside world. Our attitude today toward international economic institutions and our role as leading members thereof are both profoundly affected by the existence of such forces.

A Wartime Creation: The International Monetary Fund

The International Monetary Fund is the creation of experts who worked during the last war for a period of about three years to draw up an institution which would seek to avoid situations which loomed large in the Great Depression. Two practices dominated trade in the 1930's. One was the independent national manipulation of foreign exchange rates for the purpose of offering foreigners bargains and thus win trade advantages. This was called "competitive exchange depreciation." The other was the rather widespread discrimination against American goods because the world was short of dollars.

What, in terms of the barest essentials, did the Monetary Fund seek to do? First, it sought to outlaw competitive exchange depreciation mainly in return for almost automatic, though not unlimited, access to dollars from the fund when member nations run into short-term export difficulties. The new "ideal" was to have exchange rates changed only with the fund's approval. Second, it sought to end discrimination against dollar trade after the so-called "postwar transition period," which it was hoped would last three and not over five years. Such discrimination was to be ruled out by having the fund itself, guided by legal-type rules, determine when the dollar was really "scarce."

The fund has resources--nominally over $8 billion--in many currencies. But the main usable resources consist of the American contribution of nearly $3 billion. Most of the other currencies held by the institution are not of much use, chiefly because the world already has too much of them. If the nations which issue such currencies allowed their people and foreigners to convert them into dollars at the official exchange rate, the dollars would be gone long before much of a dent would be made in the supply of local currencies.

The fund, with headquarters here in Washington, has an executive staff and a team of researchers. Non-American personnel dominate the institution. But plural voting prevails, which is more or less proportionate to each nation's financial contribution to the fund. Thus, the United States votes about a third of the total votes when decisions are made.

This institution, in my view, but not in the view of all international economists, must be judged a qualified failure. You men in this audience have heard many times that the main thing "wrong" with the military mind is that it is always planning to fight the last war. I doubt whether this charge fits the facts of your situation. But the fund's charter, chapter and verse, calls for fighting the exchange problems of the prewar depression in an era in which nations rank prewar practices at the bottom of their list. No longer do nations want to offer much in return for little. The new aim seems to be almost the reverse! Not deflation, but more or less inflation is the virtual rule. And some inflations offer a lot to write home about! Thus, instead of overexporting, most nations follow policies which lead to overimporting.

Then there is the cumbersomeness of an international bureaucracy. Perhaps the Fund's most glaring failure occurred when Britain refused effective discussion with it before Britain made her big exchange rate change in 1949. British authorities feared--in my view rightly--that there would be leakages of the secret if the matter were first put to the multination institution. Such leakages would surely have played into the hands of speculators against sterling, to the substantial loss of the British economy.

Let me say also that fund dollars which are to be used to tide nations over temporary difficulties, vaguely and loosely referred to as of the "balance of payments" variety, somehow often get tied up for longish periods and generally get untied not because of the fund's role, but either directly or indirectly as the result of more dollars pumped abroad through our foreign aid programs, military and economic.

Finally, I may mention that in the evolution of practice the "postwar transition period" seems to have become something of the never-ending kind. Hence dollar discrimination, though reduced, still prevails in many places. If one pierces the fund's razor-thin public relations veneer, he has grounds for concluding that this is a small mouse for 12 years of labor.

Despite its important weaknesses, the Monetary Fund continues to play a role. It does so by supplementing the international reserves of many countries--reserves which such nations now regard as insufficient. The argument that these nations make is about as follows: Prices worldwide and the value of trade have risen considerably since the war, but the volume of international means of payment--mainly gold and dollars--has not kept pace. As a result, every time there is a world economic strain, for example, the one that occurred during the Suez crisis of a year or so ago, the reserves appear to be too small to withstand the resultant shocks. Some friends thus implore us either to raise the price of gold, unchanged since 1934, or to expand the resources of the Monetary Fund, or to do both.

What is the United States position on these two questions--the price of gold and the resources of the Monetary Fund? I'm going to stick my neck out and state what the position is, although I, naturally, cannot speak authoritatively, because I'm not in the Government. We oppose an increase in the price of gold, because the benefits would accrue indiscriminately to gold-producing countries, of which Russia is a leader, though not in first position. In view of political circumstances, it may be better to use ad hoc arrangements and to tailor them to needs as we size up situations.

Regarding the Monetary Fund, President Eisenhower recently reported that the United States is prepared to support moves to increase its resources. In fact, he has instructed Secretary Anderson to prepare that kind of provision for the forthcoming Monetary Fund's annual meeting in New Delhi, India. Given the "international institutionalist" spirit of the times, this probably is unavoidable. I have two comments.

Perhaps there is merit in German views that more international credit means more inflation. I also personally wish we could achieve our goals through less bureaucratic and more effective means. I refer to simple arrangements among a few of the leading central banks of the world, as was the case before the last war. For the facts of life are that the different national currencies are not of equal economic significance, Monetary Fund legalisms to the contrary notwithstanding.

Well, that's my very brief treatment of the Monetary Fund. I now want to move on to another very big but quite different subject and the institutions related to that subject.

The Poorer Nations and Development Institutions

Most of the world's people are very poor. Doing something in a big way about the problems of poverty is now at the center of the political stage in many countries, more or less as the maintenance of our military-technological lead is at the center of the American political stage. If I may anticipate a later point, let me say that the long and short of this very serious development issue is that much can be done to improve per capita output and levels of living cumulatively, and largely through the application of known low-cost techniques without massive infusions of taxpayer-supplied dollars from the United States.

The best-known institution in this field is the World Bank, formerly known as the International Bank for Reconstruction and Development which was also established at the same Bretton Woods Conference of 1944 that produced the Monetary Fund. Like the fund, the bank also has a fairly elaborate expert-drawn charter. But the facts of world financial life were accepted at an early date, and the bank soon became a simple, practical operation.

Like the fund, the bank's main usable resources were the $3 billion-plus contributed by the United States, though several foreign countries--Germany, Switzerland, Canada, and a few others--have also helped with such resources. I am speaking here of usable resources not nominal resources. These contributions--the Government contributions to the bank, in the form of capital--serve mainly to cushion losses, if sustained, not as lendable funds per se. The Bank's lendable resources are provided mainly by private investors in various countries who buy the bank's securities. The investors are found principally in the United States, although the Swiss, the Germans, the Canadians, and the Belgians are in the picture as well. Hence, the bank had to be run along "sound" lines as judged by investors, not as set forth by experts on the sidelines. The net result has been that the bank's management, largely American, has followed well-established practices of the kind that have evolved in the investment banking field.

The bank is a symbol of a simple institution that has done well, as contrasted with an elaborately planned Monetary Fund which has had a questionable record.

Briefly, the bank operates as follows: Applications for loans from foreign parties are followed by careful on-the-spot investigations of each project. There are two basic questions: First, will the foreign project expand exports and/or reduce imports such that, other things equal, repayment of the loan seems a reasonable prospect? Second, is the borrowing country's economic policy of the kind that minimizes wasteful local expenditures, so that the bank-financed project's benefits will not be dissipated? Affirmative answers to these two questions usually lead to a loan. Most such lending has been for basic transport, irrigation, port, and power projects. These projects underpin an expanded domestic effort, and thus set the stage for much-desired cumulative growth.

Loans by the bank have risen above the $3 billion mark, in about a decade, and are proceeding at not much below half a billion a year. The record to date, however, has been more satisfying to the United States than to the borrowing nations who are anxious to expand rapidly.

Strictly American lending institutions, old and new, are also in the picture. The oldest, our Export-Import Bank, dates from 1934. Its resources come not from private investors, but from congressional appropriations, which recently added $2 billion to the bank's lending authority. Most of the bank's loans, like those of the World Bank, are for development projects or equipment used therein. The biggest difference, perhaps, is that "Exim" loans must be used to pay for equipment of American origin, whereas the proceeds of World Bank loans may be used elsewhere in what are often cheaper markets. Lending terms and the present volume of loans outstanding are very similar in the two cases, that is, Exim and the World Bank.

Thus far I have been talking about traditional loans--the kind which were once unashamedly referred to by debtor and creditor alike as repayable loans. But recall my opening remarks about the role of today's political factor. There has been one dominant response to requests for American capital. Under the somewhat deceptive slogan of "Loans not aid," there has been a demand for so-called loans repayable not in dollars (or other convertible currencies) but in the borrowing nation's own easily manufactured money. Misguided American foreign policy is largely responsible for making such a practice "respectible," as may be observed from the record of transactions under P. L. 480.

However, let me add that similar provisions were in the Marshall Plan of a decade ago.

In any case, other governments are happy that we have shifted in part to a policy under which we supply capital and allow at least nominal payment in local currency. They are happy because nominal local currency repayment really isn't likely to represent true repayment except to a small extent, for example, to defray American Embassy costs abroad. Let me add that foreigners naturally do not express their views in public in just that vein.

Today the main purveyor of local currency loans is the United States Government Development Loan Fund. It began operations last year with $300 million, and in the current fiscal year has available an additional $400 million, though the President requested, I believe, $625 million.

We are likely to see not only an expanding volume of this kind of "lending," but also a costly proliferation of bureaucratic agencies. Three recent official suggestions illustrate my point: Chronologically, they are the proposed International Development Authority, which was recently approved in principle by the Senate; the President's proposal before the United Nations for a Middle East Development Institution; and, finally, the State Department's promise of support for an Inter-American Development Bank. The latter, incidentally, is an idea which had been put forward several times by our Latin American friends and several times rejected by our Government.

Is such new-fangled lending likely to be only a substitute for, rather than in addition to, bona fide repayable dollar loans? As some of my previous remarks have indicated or implied, we can be sure that our foreign friends will not be happy with a substitutionary role.

I want to be rather candid at this point. You will detect that I have more than a small measure of misgiving about trends in the field of development financing. Is this just because I, and men of like views, feel that change per se at this end is bad for us and our foreign friends? Not at all. I don't think so, but I can't develop the details here, in part because it's a long story. I will say that I submitted my views to the Joint Economic Committee last November, and for what they may be worth they can be read in the compendium of papers that committee printed at that time. I would merely like to express some summary views about the nature of the problem, the direction in which solutions are to be found, and by implication the requirements of a long-term policy that we can live with.

My basic point is that there has been altogether too much emphasis of late on the importance of free or quasi-free American resources for development and a disturbing distaste abroad for constructive reforms that will unleash all manner of latent local resources for the job which all people, Americans included, agree has to be done. In nation after nation, no matter how poor, at least nine-tenths of a satisfying total job is a local job for which local resources, suitably galvanized into action, will produce the desired result. In a few cases--Mexico is a pretty good example--the local effort and, no less important, local policy, have teamed up to do the nine-tenths that can be done locally if only there is the will and steadfast devotion to basic principles. The foreign "tenth" in such cases has yielded very high growth returns per dollar involved, essentially because it has been added to a substantial and cumulative growth element of domestic origin. And this foreign "tenth" has consisted largely of private foreign capital.

Let me contrast this minority situation, of which Mexico may be taken as an example, with the majority case among the underdeveloped countries. In doing so I am acutely aware that no two countries are exactly alike or are confronted with identical shortcomings of effort and/or politics.

Critically important are the relations between the government--the national government mainly--and the country's private sector. Such relations generally are inexcusably poor. All manner of devices are used to assure that officials cut themselves in on a substantial part of earnings in operations subject to regulation. And few areas escape regulations. This is "profit-sharing" without capital contribution and risk-sharing, a phenomenon which is as damaging to economic growth as taxation without representation was to political calm in Colonial America. Not only do the geese produce fewer eggs under such a situation, but only a part of those that are produced is available for investment "hatching" because the officials' extra-legal share generally is consumed as eggs. Of course there are other reasons too. I want to emphasize that part.

In the language of saving and investment, this means that saving is smaller than it could easily be and so growth-promoting investment is also deficient. Even more important, to continue in the jargon of economics, those who could easily step up their marginal rate of savings are given minimal opportunities to do so. And yet every theory of economic development gives great prominence to the role cast for a high marginal savings rate.

Poor physical protection of property is another remediable weakness. Details include destruction by mob action in frequent political clashes, pilferage in plants, mainly after working hours, and, in the important field of agriculture, the planting in many countries of low-yield crops which are of little or no interest to thieves instead of high-yield items which are subject to heavy stealing. Poor protection may be overcome in many cases, to be sure, but it involves diverting scarce investible resources from output-producing equipment to expensive fences, heavy metallic barring of windows and doors, an inordinate number of locks, and the like.

We must also emphasize the action and constant threats of action to enlarge the sphere of government production at the expense of that which traditionally is carried out most efficiently and resourcefully by local private enterprise. This situation is worst of all where constitutional safeguards are poor. Given the heavy risks attached to any kind of enterprise, such action and threats are acutely stifling and do much to account for the observed concentration of private activity in rapid-turnover commerce and owner-operated apartment buildings.

These problems to which I have just alluded do not disappear when government displaces private industrial activities under fairly administered constitutional safeguards, as in India today. As you may know, most of heavy industry in India is reserved for government investment and operation. In addition, a large part of other major industries is to be entered "increasingly" by the government. This leaves exclusively to private firms mostly activities of second-order attractiveness. I might say here that the second-order industries in an Indian-type situation can account, as they are now accounting for fairly substantial activity.

India, to be sure, is almost unique among the less-developed lands in having a senior civil service of high quality with devotion to duty. But even if such a civil service were free to abandon normal government work to deal instead with industry, it would be grossly inadequate to the ever-changing technical and economic requirements involved in the efficient operation of industrial establishments. The necessary ingenuity, drive, flexibility, and competitive rivalry are absent when the inordinately complex and nonroutine job is taken over by a government.

Let me continue with India for just a bit more. That important country's economic problems, as you know, are much in the news these days. The basic reason is a simple one: When the Second Five-Year Plan was formulated in 1955, her officials and economic planners took a big gamble. They planned to use far more foreign resources than they could pay for from their exports and expect to get from repayable loans. The difference, or what is now called their deficit, they hoped, would be provided as aid just because the West would not wish to see India collapse economically.

One can deeply sympathize with India's desire to raise the pitifully low average income of her people. The end of the policy is laudable. But some of the means that have been employed are deplorable. For India's planners have deliberately toyed with a large-scale financial crisis when perfectly satisfactory alternatives existed. The West, I'm sure--and this was written before the President indicated recently that we would be prepared to provide assistance--will not let India down; but every step must be taken to avoid a recurrence of this kind of episode.

The United States is not a cow fed in heaven and milked on earth. If such a precedent is successfully established, every other underdeveloped nation will get the green light to live far beyone its means and then pressure the United States to bail it out. The United States cannot and should not be expected to automatically foot the bills when other people's enthusiasm outruns good sense. In this connection, I must point out that we narrowly averted a congressional resolution just a couple of months ago that would have assisted rather than opposed the forces working to establish just such a precedent.

I must return to my main theme. It is that there is a great deal which the countries can do for themselves. This is what is meant by self-help. Once the countries really get going and keep going--during which the friendly ones will, of course, continue to receive all manner of American public and private assistance of the traditional sort--they can expect true additional help from the outside. Briefly, they can expect additional private investment and additional repayable loans from international agencies. They will then be well on the way to achieving self-sustaining growth.

You will note that I have not mentioned the "Soviet economic offensive," this morning. It is conventional these days to do so in a context of this kind. This is mainly because I believe it to be greatly exaggerated, though it is something that cannot be ignored. My argument swings on the following hinges.

First, the State Department exaggerated the situation when it laid emphasis last winter on the Soviet's promise of $1.9 billion of economic aid to the non-Communist nations of the underdeveloped world. That got big press and TV play. But almost nothing was said about the fact that such aid is only running at about $200 million a year, or merely a small fraction of the current contribution of the West.

Second, the Soviet people are poor, and probably will not allow their leaders to make large handouts. Significantly, when Soviet spokesmen promised large aid to their "brothers" at last winter's Cairo Conference, there was no mention of the whole business in the Russian press or radio. Moreover, what Russia lends or gives will probably be mainly to her own poor but politically powerful relation, China. Speaking of the Sino-Soviet relation, let me add that the informed in the less-developed nations know that Russia can take on balance, rather than give. Last year, for example, Russia drained China to the tune of 300 million U. S. dollars net, the size of China's adverse bilateral trade balance.

Third, few responsible officials in the less-developed lands prefer the Russian fire to the western frying pan. They don't want to jeopardize access to large western trade and capital assistance, of the kind they have been experiencing for a long time, just to try to get a little something from the Soviets.

Finally, our answer to a Soviet challenge, in any case, is not to mimic them, but to assist and expedite the evolution of policies and practices which strengthen native enterprise forces, for these are the ones which find a deep-rooted, natural, and mutually beneficial tieup with the West and western institutions and no less naturally resist native forces of subversion that mistakenly side with the world's worst imperialism.

In particular, we must not be stampeded into doing things just because "something new" is said to be called for.

That winds up my discussion of less-developed country problem and the institutions related to it.

Emerging European Economic Regionalism

The final set of institutions that I wish to discuss are those that are emerging in Europe. Chief among them is the European Common Market.

Americans may fairly claim some contribution to the emerging European regionalism of Western Europe. For we did much to speed the restoration of this advanced and tested area's economic position during and following the Marshall aid period, especially through such bodies as the Organization for European Economic Cooperation and the European Payments Union. The Europeans then took the ball themselves to develop the Coal and Steel Community. And only a little over a year ago they signed the Treaty of Rome, which establishes the Six-Nation Common Market, or, as it is formally known, the European Economic Community. They also signed the Euratom Treaty at the same time.

The Common Market is not something that governments have approved. European business itself is making all manner of specific plans and designing its investments on the assumption that the Common Market will proceed more or less on schedule. Simultaneously, though with limited success to date, forces continue to work to transform the Common Market into a broader and more elastic Free Trade Area covering most of Europe.

What does the Common Market Treaty seek to do? Its major provisions would at least eventually--

1. Remove customs duties and quotas among Member States;

2. Set up a common tariff and common commercial policy toward outside nations;

3. Abolish obstacles to the free movement of persons, services, and capital between Member States;

4. Establish common agricultural and transport policies, though these would still be rather restrictive;

5. Establish a Social Fund to help labor adjust to a changing market, an Investment Bank for projects in the Community, and a Development Fund for use in the overseas territories of some Member States, mainly France and Belguim.

It is expected that the Six Nations will gradually merge into a single economic unit as far as trade restrictions are concerned. There will be three 4-year stages, the first of which is to begin next 1 January, when tariffs will be cut 10 percent across the board. Thereafter, the changes are to follow a less specific timetable. The commitment is to have a minimum cut on any product of 25 percent by the end of the first 4 years and 50 percent by the end of the second 4-year period. Changes in the final period will be worked out later.

To assure that import quotas are not used to frustrate tariff changes, import quotas are to be enlarged by 20 percent next January. Further quota increases are to occur in stages, until quotas as such are eliminated in 12-15 years.

How are the tariff cuts to be calculated? The agreed basis is the average rate which has been charged, not rates weighed by amount of trade. This yields higher tariff rates than the low-tariff members--Belguim, Netherlands, and Germany--desired, inasmuch as France and Italy have relatively high rates. Implied there, of course, is the proposition that the Belgians, the Dutch, and the Germans have a larger volume of trade than the other two. Moreover, special situations will be recognized, which will have the effect of keeping rates fairly high for some sensitive industries, mainly in France and Italy.

Restrictions on movements of capital are to be progressively relaxed. But there is a big loophole for countries in serious balance of payments difficulties. (This kind of loophole, I may add, is found in all international economic agreements since the last war.)

Labor was a touchy subject, mainly because of Italy's unemployment situation. All that was agreed upon was that freedom of movement was to be attained by the 12th to the 15th year.

The farm policy agreements in the European case, as well as elsewhere, are largely verbiage. (I might add that you can make the same kind of caustic remark about many things in our own farm policy, particularly as it applies to relations with foreign countries.) If freer trade hurts any nation's farmers, minimum prices may be set by the governments in question and imports restricted to protect such government-set prices.

Anticartel language also seems strong, as it nominally prohibits monopolistic and cartel practices. But another loophole has been provided: Such practices may continue if they help to "improve production or distribution . . . or promote technical progress . . . and consumers receive a fair share of the benefits." It seems to me that we can only be sure that economists attached to the organization will write a lot of papers.

Still, significant progress is represented by the Rome Treaty. Already, for example, American firms are redesigning their overseas investment and distribution systems to fit the emerging pattern in Europe.

Now for a word about the Free Trade Area idea. This is being pushed mainly by Britain, with strong support from European countries outside The Six and with fair support even from within The Six. France is the major stumbling block--and here I'd like to quote "The Economist"--". . . for in this century to date this most self-sufficient of European economies has not really cared a button for free trade." And, of course, it's also fearful of German industrial superiority.

A central place in the Free Trade Area idea is accorded to national autonomy regarding tariffs and quotas with outside nations. That is to say, each member nation under the free trade idea is to be free to establish its own tariffs and quotas with countries in America, Asia, and Africa.

The Common Market, you will recall, seeks to establish a common tariff wall for all of The Six. France in particular fears that under a Free Trade Area goods might enter from the outside through a low-tariff country and be transhipped duty free into the Common Market. The British are prepared to deal with this matter. They propose use of certificates of origin, so that the higher minimum Common Market tariff rates could be applied to outside unprocessed goods which entered through a low-tariff nation.

In my view, and in that of many Europeans, something like the Free Trade Area idea will eventually win out.

Even partial success for European economic integration will be important to the United States and the world. It will give Europe more of the benefits of economies of large-scale production. It should yield the advantages of increased specialization. Higher per capita real incomes will be attained. The movements may even result in eventual federation. But here I am back to the political, where I started. The two are sides of the same coin. May I suggest that you keep the second side in mind as you reflect on whatever has been said about "political economics."

Thank you.

CAPTAIN THOMPSON: Gentlemen, Dr. Salera is now ready for your questions.

QUESTION: You mentioned in your talk the insignificant amount of Russian loans. Several weeks ago on CBS they spoke of the ruble war and in there they attributed a lot of the influence the Russians are having in their loans to the small interest payments. Will you comment on that?

DR. SALERA: Yes. The Russians have been charging, I think, not over 2.5 percent. They are erecting a steel mill in India, for example. The low interest terms are per se a favorable thing as viewed by the recipient country, and I think one can be sure that the Russian planners gave considerable emphasis to that type of consideration. But until the volume becomes rather substantial, that consideration is in my view bound to be a secondary one.

Low rates are important if you can count on a large volume at such rates, and if you can count on the Russians being disposed to financing projects--this is a much more important consideration--which are tangential to their own political interests as they view them.

As to the CBS program, I did not see it on TV, but I happened by accident to have heard it over the radio a week after it was telecast. I was quite interested in it, partly because of the sort of thing you referred to; and I sent for a copy of the transcript of the program to have in my file. I just got that this morning, incidentally, in a rather attractively bound pamphlet, with a nice cover, nice paper, wide margins, and so on.

The issue here is a very important one. I'm not trying to dodge it. I'm not trying to minimize its significance. I said that the funds involved are relatively small. I used the phrase "a promise of 1.9 billion." That included funds, so-called stringless loans--which since have been withdrawn--from Yugoslavia, as we all know. The thing that was omitted from the Department release--at least I read that material very carefully and use a red pencil liberally--was the current amount. It's running around 200 million. That figure, incidentally, was mentioned in the broadcast.

So I would summarize the situation by saying that low interest rates on these loans would be very good if recipient countries could count on a substantial volume of the funds in question for projects that are basically in their interest and not too important to the Soviets politically.

QUESTION: What does the United States expect or want in the way of interest rates and period of return on loans from the World Bank?

DR. SALERA: The World Bank is an organization that encompasses over 60 countries. We are the most important single country in terms of voting strength. But the U. S. Government does not determine World Bank policy. It has an important role in the formulation of policy in indirect terms.

First, the director from the United States on the World Bank is instructed in terms of the interdepartmental machinery that is set up under congressional statute. Secondly, the bank management is American management. Mr. Black, the president, is from Wall Street.

But the bank has to set rates which enable it to do two things: first, cover the interest cost on its own debt, which is incurred in its borrowing from investors, which runs around 3 or 3.5 percent, in that range, between 3 and 4, plus administrative costs, which run about 1 percent, and finally plus costs involved in accumulating some sort of reserve for contingencies. The bank has been charging around 5 or 6 percent. The interest has gone as high as 6.

Now, that rate, although high in relation to the Russian rate, is still very low in relation to long-term interest rates in these countries. There are very few countries where you can borrow for a long term at anything like 5 or 6 percent.

As to when we expect the money to be returned, these loans run for different terms depending on the project. Very few of them run for less than 10 years. They run up to about 15 or 20 years. I think thus far there have been very few loans for over 20 years.

Are you asking a question now about the repayment prospects?

STUDENT: No.

QUESTION: India is a fascinating country. In 1954 out there they were throwing out or easing out or forcing out all United States and British capital, at least in the Bombay area. At the same time, the Indians were jamming the gold and precious metals markets and buying gold trinkets and everything else at a fantastic rate.

DR. SALERA: Do you mean the Indian Government?

QUESTION: No, sir. The individual Indians. I wanted to buy a pair of earrings and couldn't, because the clerks wouldn't wait on me. There were Indians there who had much more money. I just wondered if there has been a change in India, or if they expect to do everything by governmental loans.

DR. SALERA: I am not an Indian expert really. I try to find out as much as I can about India from various sources. Let me say that I did not say in my speech and do not mean to give the impression that the Indian Government is trying to do everything in the economic area.

The people who take a position quite opposed to mine will emphasize that thus far the Indian Government has run only something like 3 percent of the industrial sector, and that even when the current plan is finished in 1961, they will run it only up to about 7 percent.

Well, that kind of material has to be interpreted with care, because don't forget that about 80 percent of the people in India still are working on the land. They live in small villages and they're very small-scale farmers. Industry as such is relatively small.

The big question concerns what is projected, what the Indian Government is committed to do, at least in general terms, under the very deceptive label of the Industrial Policy Resolution of 1948, as modified in 1956. That resolution says that India must move toward a socialist form of society. That's general, of course. But the specifics are rarely mentioned in the United States. I happened to have gotten so concerned about this that I stuck my neck out and listed them in one of the congressional documents so that those Members of Congress who read this material will at least see a listing of two important schedules.

Schedule A lists all the classic heavy industries, and, of course, the armament industry. Those industries, in 12 major categories, are reserved to the government. That means that private business which is now in them can stay in them, but no new private firm may enter. I understand that can be twisted and stretched through administration action, but I don't think very far.

Now, the Tata Steel Works and the India Iron and Steel Company, the two privately owned steel companies, are expanding. Kaiser is helping Tata to expand, for example. The Indian position in steel is relatively good. India has, literally, one of the cheapest sources of steel in the world. They should do well out in that part of the world, particularly if they confine themselves to a relatively few types of products in which their production economies are most marked. But the other categories--heavy machinery and things like that--are reserved for the government.

You have, then, 12 major industrial categories--generally the heavy industries, the highly capitalized sectors--reserved to the government. Then a second category, Schedule B in this resolution, lists about 10 other fairly important areas, and these are areas in which private firms may enter if they wish. But the Indian Government has served notice that it will enter increasingly into these areas.

So here you have a blueprint calling for very substantial Indian Government participation in industry. Today the Government's share in these areas is small, mainly because they are in the early stages of the industrialization program. One must not be deceived by that kind of statistics.

Now, as to your question on how much we can expect. I think it turns largely on the evolution of policies in the political context of India. There are controversies going on in India pretty much of the kind that go on in this country as between Republicans and Democrats.

One feels very sympathetic to the Indian position and aspirations, and much can be done. There's no question about it. I and some other people with like views would attach a lot more importance to the agricultural sector, at least in the transitional period. You can't quickly get the people off the land in India. Where are they going to go? They're there. And their condition has improved very markedly. I think that is true all over the underdeveloped world--China, Peru, Mexico, internal Venezuela, and so on.

Most of the world's farmers are only working about half as effectively as they could work without much in the way of expensive capital and so on. You don't have to equip Indian farmers the way you equip our Iowa farmers, because the Iowa farmer is a capitalist. He has many, many thousands of dollars worth of equipment.

QUESTION: I have two questions that are somewhat interrelated. They are about the underdeveloped countries in Asia. These countries are determined to move ahead and, in fact, have to if they are going to fight some of the subversive influences within their countries. Long-term private loans are very difficult to get. What other alternatives are there besides Government loans or aid from the United States? The second thing is that in this matter of aids versus loans, isn't it better for a country to have some feeling of responsibility for repaying a loan even in its native currency rather than getting direct handouts all the time?

DR. SALERA: The first question, what can be done to get resources used far more effectively than they are being used on the average today in view of the apparent difficulties and slowness with which the private sector can be activated or what-have-you--that's a mighty big subject. I think there are two or three things that might be said here.

First, it's indispensable that the people who do advisory work appreciate what the problem is, and then, secondly, having appreciated it, examine every important detail with that context in mind. And then when you get into the oil sector or the transport sector or the farm credit sector or the way they administer regulations and so on, you evaluate each of these specifics in the light of this general sizing up of the picture and get as many of the facts as you can. Then you analyze them suitably--which means not everlastingly--and recommend as forcibly as you can in the light of that operation.

One can get into all kinds of particulars. One can evaluate the proposals of a given ministry in a given area, point out the production-deterring things, and in the process point out with as much emphasis as possible what can be done--generally it's simple--to remedy the situation, and go on down the line.

Now, as to your second question, the answer is, briefly, yes. But let's not kid ourselves about the word "loans" here. We are now accumulating local currency at a very rapid rate. Sure, we do use these currencies for many purposes: Fulbright programs the building of a new embassy, and things like that.

But my own view, and the view of many that I have talked to, is that the eventual "solution" will be cancellation. These countries aren't going to get measurably better in the next 10 or 15 years. They will wish to improve and they'll be able to present the same political argument, namely, "We're poor and you're rich, and you're asking us to turn over to you resources that you don't need." You'll get the moralists, the religious people, and so on, pleading their case, at least in general terms.

Yes. I think the loan emphasis is better than the aid emphasis.

QUESTION: You mentioned the OEEC, in which the United States participates. You also mentioned briefly the aims of the European Economic Community. Up to now we have been dealing unilaterally with these nations in terms of their augmenting their contributions. We have also been dealing multilaterally through NATO. I can see some conflict with regard to the United States position NATO-wise versus the European Economic Community. Could you clarify the United States position on that?

DR. SALERA: Let me see if I understand your question. You first referred to the OEEC, the Organization for European Economic Cooperation, the Marshall Plan organization, which is continuing. Then you referred to the European Economic Community, the Common Market apparatus, and then to NATO. Are you referring to a possible conflict in the United States behavior in NATO on the one hand with the OEEC on the other?

QUESTION: No. My basic question is this: We supported EDC and it's now defunct. I presume we are supporting the European Economic Community in its overall aspects.

DR. SALERA: I think so.

QUESTION: It occurred to me that there might be a possible conflict between our position in NATO, from an economic point of view, dealing with 14 nations versus this coalition of Six Nations, which we also must support.

DR. SALERA: I think that probably the best way to answer that question is to point out that, if you make a rundown of all these European agencies, you'll find one is a 7-government agency, one is a 10-government, one is a 15- or 17-government, one is a 6, one is a 4, and so on. I don't think the varying size of the agencies is per se an obstacle to coordinate work on the part of our Government.

Now, NATO, as you know, has as a matter of practice divided its work with the OEEC. It stayed out of the OEEC area, or, what is the same thing, it relied on American personnel on the OEEC side to carry the ball in the more strictly economic areas and to exchange information and so on, so that things done with the economic hand do not clash with things done through NATO with the military hand.

Now, I guess I'll go back to my original proposition. There's no reason, I think, why our Government can't keep informed about developments in the Common Market area and take steps from day to day and week to week in the light of asessments of the military requirements on the one hand and the economic requirements on the other. Insofar as the general objectives of the Common Market are attained, it should make for a stronger, not a weaker, military base in Europe.

Now, whether the Common Market and the federation implications would lead to the third-force idea in some large proportion, if that is regarded as the most likely outcome--and that's another question--that might bring about some conflict between OEEC and NATO. But, again, I am outside of my field and I don't think my comments in that area are worth much. Actually I personally have very little confidence in my views in that field.

QUESTION: You mentioned the World Bank, to which the United States is the major contributor; and you also mentioned the U. S. Export-Import Bank. It looks to me as if we have two institutions almost in competition with each other. We don't use them both in the same area, do we?

DR. SALERA: That's a good question, sir. I might say that when Mr. Eisenhower assumed office in 1953, one of the first decisions he made was more or less that we don't do so; further, that we don't need them both in about the same area, particularly the development area.

I think the policy stuck to that more or less for a couple of years and then the pressure was on to use the Export-Import Bank's resources for development or lending more or less along World Bank lines or in areas that the World Bank had been cultivating. But we never really departed from the pre-Eisenhower position, because the Export-Import Bank also makes political loans, not just loans to accelerate exports of American products.

Viewing it along purist lines, we don't need both. But the American position is coordinated through the National Advisory Council here in Washington. I personally feel that having the two around is a good thing and that questions of efficiency are relatively minor in this case. I personally think that the other issues in this broad field are so much bigger that I wouldn't spend much time arguing this one.

QUESTION: Do other countries have similar institutions to our Export-Import Bank?

DR. SALERA: They don't have things that are similarly labeled. The British, for example, have their Export Guarantee Department, which does a somewhat similar job. They are the biggest contingent creditor by far of India. I may add that the British stake in the current international financial situation in India is much larger than ours. That will probably not be true a year from now, but it is right now.

QUESTION: There are various individuals who take the position that many of these neutral countries, such as India and Afghanistan and perhaps Thailand and various others, which are in need of economic assistance, by the very nature of their present society are probably going to end up inclined toward socialism. In all probability they will shy away from communism, because they are religious countries. We hope they will. The point is, can they ever come up with a socialistic, democratic government or society that the United States can do business with and feel that it's willing to support? Otherwise what other alternative exists?

DR. SALERA: I think the answer is yes. I am convinced that the answer is yes. But I am equally convinced that the particular way in which a Socialist-type society evolves can be influenced by American policy. Although I don't say so in so many words, I am arguing in effect: For heaven's sake let's use our leverage to bolster those local forces which are naturally with us and not forever give priority to the government's wishes and plans.

Take India. India is not of one mind on these basic policy questions. Tata officials were in town pleading very earnestly four years ago for a certain kind of American policy. I happen to know because I was close to things at that time. They wanted the United States to buck socialist plans in India. They are now a staunch advocate of large United States loans or what-not to the Government of India. They have relaxed their efforts.

Now, I am not implying that we should have followed the officials' suggestions four years ago and stuck our necks our politically in India. But there are numerous ways in which we can help the evolution of local policy along lines that experience, not just abstract reasoning, but experience and abstract reasoning tell us are in their own best interest.

The fact is that in most of the underdeveloped countries there are large latent resources that remain latent. They have remained latent for a long time. Our challenge, it seems to me, is to get as large a proportion of those activated as we can on the basis, if you will, of the self-interest of the individuals in question. You will get a much better overall performance if you do it that way, I am convinced, because people all over are dominated by self-interest and self-interest properly channeled, as it is in most western societies, leads to a good "social" performance. So I say, let's exploit those parts of the American experience and the American actualities which are exportable. A very substantial portion of them are.

Some of our friends, good Americans, have argued just the other way around--that American productivity devices won't work abroad; that they work only in the United States. That's just rank nonsense. You can't apply them in a mechanical way in other countries. You don't farm in India the way you farm in Iowa. But the fruits of agricultural extension can be tapped very easily with minor modifications in techniques in most of the world.

I personally have had experience in Latin America on this front. But the local official in too many cases is the farmer's worst enemy. Why? Because the tradition has been such that the local officials, I mean the regional officials, are forever trying to steal the poor farmer's hogs and chickens. It's a very pervasive thing.

But we're going to have a tough time getting the officials' rapport with the small farmer. The American point four people on the whole have had good luck in that regard, partly because the Americans are Americans and partly because their record is clean. All they want to do is help. But all too often the local official cannot contact the rural people that he is officially supposed to help. Many rural people don't have trust in him.

We can break that down, I think, not by issuing "pronunciamientos" in Washington, but by working in all of these relatively small cases by establishing contacts, by encouraging your graduates of technical schools to get out there and help to improve the productivity of the farm sector of the economy. A lot can be done.

QUESTION: You said that our contribution to the World Bank was $3 billion. You also said that the main source of lendable funds that the World Bank had was from the sale of securities to private investors. What's happened to these $3 billion? Or has there been a greater sale of securities than the contribution?

DR. SALERA: I said in my talk that the American Government's contribution is a cushion. Actually, in detail, the first 20 percent of the American contribution is to be available for lending by the bank. The 80 percent remaining, is held as a reserve to pay off losses if they should be realized.

Now, you raised a question having to do with the limits on the bank's borrowings in the private market on good terms. The limit appears to be fixed. It is pretty much fixed by the size of the American Government's guarantee. You see, up to that guarantee Uncle Sam stands behind the World Bank's debt dollar for dollar. Beyond that we don't know. Let me put it this way: The bank might become so well established and the relations between the bank and its creditors and debtors may be so good that the bank in the future may be able to market its securities, without additional contribution from the United States, on terms about as good as those enjoyed by the U. S. Treasury.

The President has recently instructed the Secretary of the Treasury to go to New Delhi and tell the governments there that we're prepared to discuss with them ways and means of increasing everybody's contribution; the main objective of others, however, is to get more from Uncle Sam, because it's dollars that are most critically necessary. I personally hope that we will achieve a situation in which the World Bank can borrow on its own all that is necessary. But I'm not too optimistic, because I think we'll encounter great pressure to make American goods available on far easier terms.

CAPTAIN THOMPSON: Dr. Salera, on behalf of the College, I wish to thank you for a most informative and interesting talk. Thank you very much.

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