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Transcript of interview with

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Interview with Burke Knapp

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Knapp: This is Burke Knapp speaking, my present capacity being vice-president of the Bank, and I'd like to recall some of the events in which I have participated in the Bank, perhaps starting with a little of my own personal history and how I first came to the Bank.

When I first came to the Bank in 1949 from the State Department, the Bank had a loan department which was charged with the conduct of loan operations and an economic department which was charged with all the economic work, including the reports on country economies--appraisals of credit worthiness, development programs and so on and the appraisals of economic projects set up. Mr. Rist was at that time the head of the economic department, and Paul Rosenstein-Rodan was the deputy director of the economic department. And I was asked by Mr. Rist and then by Mr. Garner, vice-president of the Bank, to come as the number two man in the economic department, the idea being that I would take over the act of executive function of getting the studies out, leaving Paul Rosenstein-Rodan to concentrate more on the development of economic policy and the development of his very fertile ideas, which he came up with very frequently. I came to the Bank in that capacity in December 1949 and remained about eight or nine months, until the fall of 1950, at which time I was

requisitioned by the United States government to return to the State Department and take an assignment as the economic adviser to the United States delegation at NATO.

I was given leave from the Bank for that purpose and had planned to return to the Bank in the fall of 1951. However, just about the time that I was due to come back, events developed which resulted in my assignment for another year to Brazil. The United States government had agreed with the Brazilian government to establish a joint economic commission for the preparation of an economic development program in Brazil, and a gentleman who had done some work for the Bank by the name of Francis Truslow Adams had been designated by the United States government to do this job, and he had taken a trip with his family to Brazil and very unfortunately was seized with a heart attack and died on the boat on the way down. Mr. Eddie Miller, who was then Assistant Secretary for State for Latin-American Affairs, appealed to Mr. Black to find somebody to replace Mr. Adams. I think various efforts were made, but finally the finger was put on me, and I was given a further leave of absence from the Bank for another year to do that job.

This was a very interesting venture in international cooperation and planning for a development program, drawing up development projects. It was interesting because it was a joint venture between the United States government and the Brazilian government, but it was also interesting because at the time this program was being prepared the bulk of the finance, external

finance to carry out the program, was expected to come from the World Bank. This was therefore a rather irrational set-up since the World Bank would not directly participate in the planning activities and yet was supposed to follow up with finance, and this put me in a somewhat dangerously ambiguous position because I was on leave from the World Bank and yet I could not speak for the World Bank and represent them. But there was some implication--at least the Brazilians inferred some implication from all of this--that the World Bank would follow up with money required after the planning period had been completed.

Well, I stayed in Brazil for a year. It was a two-year job. I stayed for a year, and then my place was taken over by Merwin Bohan, who completed the job in Brazil, and I came back to the Bank in the fall of 1952.

I had expected to come back to the Bank in more or less the capacity in which I left. But just at that time that I came back, a basic reorganization took place. In effect, the economic department was merged into the loan department except for residential functions having to do with overall economic studies. The bulk of the economic work in connection with country appraisals and project appraisals was moved into the loan department, and then the loan in turn was split into four area departments plus the technical operations department. So that upon my return I found myself quite unexpectedly cast in the role of director of the department for the western hemisphere, my experience in Brazil for one year being the sole qualification

for being an expert on Latin America. At least it was some start.

So, speaking from a personal point of view, I then found myself in the unexpected position that whereas I had been in Brazil engaged for the United States and Brazilian governments preparing this development program, I now found myself, so to speak, on the other side of the desk back in the World Bank reviewing the projects that were coming up for financing, which had resulted from this program of the so-called joint commission.

This might have worked very well in the sense that, after all, I had gained some experience; I knew the Brazilian end of the picture and knew these projects as they were coming forward. But there intervened at that particular time a serious financial crisis in Brazil. Basically this resulted from the Korean War and a tremendous overstocking and wasteful dissipation of exchange reserves which occurred at that time. And despite the fact that coffee was booming and very high receipts were being obtained for coffee exports, Brazil simply overspent its income and dissipated its monetary reserves and fell very heavily in debt.

This, so far as the World Bank was concerned, greatly affected their credit worthiness; and just at the time when Brazil had hoped to obtain the fruits of this work which had gone into the preparation of the development program, their credit worthiness declined very rapidly, and the World Bank began to go very slow in the financing of projects emanating from the joint

commission. This situation was, of course, particularly embarrassing to me, particularly troublesome to me; and leaving my own role out of it, Brazil took this very ill and indeed alleged that there had been a default by the World Bank on its commitments to help Brazil carry through its development program. And the tension that built up between Brazil and the Bank at that time has never really been dissipated and continues to some extent to this day, with still a feeling (a misconception, but a definite feeling) in Brazil that the Bank let them down at that time. In fact, in the end the Brazilian government appealed to the United States government partly on the allegation that the World Bank had not come through on commitments that had been made, but partly on the more general ground that whether that was true or not, Brazil desperately needed assistance to carry out its program, which had been prepared by the joint commission, and eventually the Export-Import Bank took over a large share of the responsibility for financing these projects in Brazil and, so to speak, finally underwrote a large part of the program.

Q: How did it come about that the Brazilians got the impression that the World Bank was going to finance a program which the United States government had sort of drawn up?

Knapp: Well, it was a series of misunderstandings and misinterpretations of pieces of paper, paper that had been passed around, and conversations that were held. It would be too long a

story, and I don't have the documentary material to analyze that. The Bank had been asked at the time the commission was set up whether in principle it would be prepared to provide finance for those projects, and the answer was naturally yes. And furthermore--and this was the thing which gave it the ironic twist--the very fact that my services were lent for this carried to the Brazilians an implication that this meant that the weight of the World Bank was behind it, although that was not the understanding of the Bank nor was it my understanding at the time that I took the assignment. It only developed gradually that this sort of psychology existed.

Q: How did people in the United States government feel about all this?

Knapp: Well, there were some people that felt very strongly about it. There were people that felt strongly on both sides. Before I answer that question, I want to make this point: that one of the issues involved was how far the Brazilians should be asked to take remedial action, to pull in their belts, so to speak to get themselves out of their hole, rather than simply relying upon some outside agency willy-nilly, despite the decline in their credit worthiness, to come in and finance these projects. The World Bank was saying, "Sure, we're prepared to finance these projects if Brazil takes the essential steps to restore its credit worthiness." On the other hand, the

Brazilians were not prepared to take those steps and appealed to the United States on a political basis, and there were many people in the United States government who were very susceptible to this appeal. I should say that first among them was my successor in Brazil, Merwin Bohan. Merwin Bohan felt very sincerely and very strongly that the United States in agreeing to go through this exercise in planning had undertaken a moral commitment to follow through with money. There was nothing on which he could base this except just his sort of dedication to the job and feeling that nothing should be allowed to stand in the way of the fulfillment of the program on which a great amount of technical talent had been expended. There were some very tempestuous meetings within the United States government essentially between those in the United States government who felt that the United States had undertaken a political responsibility which had to be discharged and those who sided with the World Bank in saying, No, they shouldn't have a blank check and they should be required to meet certain standards of the World Bank, the Export-Import Bank or any other source. In a way this whole incident was a dress rehearsal for subsequent relations between Latin America and the United States government in a much wider panorama--the conflict between those who said and still say today that the Latin-American countries must do more to put their own house in order before they're entitled to ask for external assistance and those who say that for political reasons or because of past commitments or because of the need for

stalling Communist development in Latin America, the United States must go ahead and provide even without too much of a quid pro quo being asked in terms of domestic effort and pursuit of sound international economic policies. This is an issue which has been brought to the fore with the new Kennedy Administration emphasis on issues of self-help and the Inter-American Conference which is going on at Montevideo right at this moment, is trying to grapple with exactly this question.

Q: What sort of steps did the World Bank want Brazil to take in reestablishing its credit worthiness?

Knapp: Well, basically these were control of inflation as far as internal development was concerned, and that in turn meant balancing the governmental budget and restricting credit to the private sector of the economy to amounts that could be accommodated without inflationary consequences, and specifically on the external side adopting exchange rates conducive to achievements of reasonable balance in international accounts and exercising some austerity in their import program. Again, this was all at a time when the internal measures for restoring balance were at all times very difficult, just because Brazilians had got into the habit of highly expansionary internal finance. On the external side, on the other hand, because this was at a time when the coffee movement was proceeding at a great rate, a restoration of their balance in international payments could have

been accomplished without great difficulty. My own interpretation is that the real reason that they did not achieve a reasonable balance in their international accounts was that the measure above all necessary to achieve that purpose was a depreciation of the currency, which was completely artificially overvalued by 1951-'52, and the Brazilians shrank from adopting this venture because of its impact domestically, because it would have given a further short-term twist to the screw of internal inflation.

Q: Was there discussion in the Bank at that time as to the relation between inflation and balance of payments disequilibrium and credit worthiness per se?

Knapp: Oh, yes. Yes, I think Brazil is almost around the Bank one of the two or three classic cases of how inflation leads to balance of payments disequilibrium and hence to destroying a country's credit worthiness. So it is in the International Monetary Fund. The Brazilian history of the past ten years is a classic case of not only the destructive effects of inflation as such, but the destructive effects of artificial manipulated exchange rates. It's only within, in fact, the last year that Brazil has finally taken definitive steps to restoring an equilibrium rate of exchange, which by now they have practically achieved. And I think it's been one of the best grounds for hope on that Brazilian situation.

Q: Did anyone in the Bank argue that it is possible for a country to be credit worthy and still have some degree of inflation?

Knapp: Well, some degree, yes. I suppose nobody can be too doctrinaire on the subject. After all, we've lent a lot of money to countries who have been going through inflation, sometimes rather severe degrees of inflation. I think basically our experience confirms that a country's capacity to service external debt stems back very fundamentally to whether it's following a sound monetary and fiscal policy. I'll leave it at that, but the Brazilian case is certainly an outstanding case of that.

Well, I might go on to talk a little bit about the organization of the Bank when I first returned, because I was in a sense one of the first guinea pigs. I had had no part...I had been away isolated in my mission to Brazil when this reorganization was discussed in the Bank, and I really had no significant part in the preparation of those reorganization plans, although I came to be advised that they were pending somewhat before they were instituted. But I became a guinea pig in the sense that the key to the reorganization plan was the establishment of a proper functioning relationship between the area departments on the one hand and the technical operations department on the other. I think the question of whether the economic appraisal of countries was done within an economic department or within four loan departments was an important

subject, too, but scarcely the key issue; that probably could have been worked out successfully either way. But what was regarded from the beginning and certainly was demonstrated in practice to be the key administrative and operational problem involved in this structure was the question of what balance could be established and what cooperative and joint working relationships could be developed between the area departments on the one hand and the T.O.D. on the other.

The concept of the organization was, of course, in the first place that the Bank's lending had to be focused on the country problems; that the economic development, being the function discharged by sovereign governments, was a country problem. Also, credit worthiness was something that you measured on a national basis defined for a country. And, of course, the loan department had already been organized internally for this reorganization, with the people having country assignments, but the establishment of four area departments emphasized and fortified the country approach. Incidentally, I think this is absolutely essential, and the reorganization of the United States foreign aid program as presently going on is based on exactly that--that the whole administration of U.S. foreign aid is to be put on an area country basis, which I feel confident will contribute very greatly to the efficiency of that operation.

Having established that you were going to do this on a country basis and that therefore you wanted area departments and country desks, the question then was: what about the technical

backing up of the work? Granted that the economic work should be done in the area departments and merged with the actual conduct of loan operations, should that equally be said of the engineering work in the technical projects?

Well, there were two concepts, I think, which argued against that. The first was simply the inefficiency of having each area department equipped with its own engineering staff who had specialties--hydroelectric engineers, railway engineers and so on--and they wouldn't always be equally in demand in the various areas and it would be a more efficient operation to pool them together in a separate pool and let them be shared out among the area departments that needed them.

But there was more to it than that. The second point, and a very important point in the minds of those that planned the reorganization and a very important point in the operations as set up, was the thought that to a certain extent there ought to be a sort of internal balance of power. There ought to be an autonomous and independent review of the merits of projects. The concept was that if the loan departments, the area departments, which are called the loan departments, were given their hand in the sense not only of appraising the credit worthiness and deciding on loan operations, but also on passing themselves upon the merits of projects, that they might become overeager to do the lending business and to cultivate their clients and that the engineers and technical personnel established in those departments might tend to be overridden by the loan officers

themselves and perhaps even the directors of departments. Then the concept behind the organization of the T.O.D. was to create certain checks and balances, to assure that the thing in which the Bank has always so much prided itself--that its appraisal of the merits and feasibility and the remunerativeness of particular projects--, to make sure that that appraisal was conducted by people who, by the nature of the job which they hold in the organization, the department in which they worked, were not committed to the lending business.

Now, I don't want to overstate this. I don't want to set up a complete antithesis between loan officers desiring to do business and technical people desiring to say no. It's a matter of degrees. But, be that as it may, there's a built-in checks and balances system. And in practice I have no question but that this has been extremely valuable on the grounds of efficiency, to pool our technical talents, but also on the grounds to make the project go through a double hurdle. It has to go through the loan department concerned, and that loan department has to make a determination that this is a sound project and that it fits within the development requirements of the country concerned. Then it also has to go through this detailed technical scrutiny and vetting, at which level bugs have been found many times, which might not have been brought to the attention of the Bank and the Bank's management so successfully unless there had been an organization charged with that responsibility.

Q: Has there ever been an occasion where the loan or area department has recommended a loan and then it has subsequently been dropped altogether because of the recommendations of the technical operations department?

Knapp: Yes. I amend that only to say that there certainly have been occasions in which loan officers have proposed loan operations, not necessarily recommended them, but proposed them for consideration, and then they have been found wanting after this technical scrutiny had been undertaken. That happens a great deal, and there's no reason why it shouldn't happen, because as you go through many projects that prima facie look like good starters, they just don't survive the examination to which they are put.

Q: What are the sort of things which are most likely to hold them up or cancel them? Is it the engineering feasibility per se or is it cost per se?

Knapp: It's more the cost benefit ratio. The engineering feasibility has usually been determined by the time a project is brought to the Bank in the sense of just sheerly can this thing be done. The more delicate problems become the cost benefit ratios. The question of whether there exists adequate organization and management to carry out the project, questions of whether the financial aspects of the project have been

adequately established, including both the arrangements for the financing of the execution of the project to the extent that financing was not supplied by the Bank, and questions related to the financial viability of the project after it's been brought into operation. It is on questions like that that many times a project turns out to have defects, although sometimes these defects can be cured and remedied by the imposition of appropriate conditions with respect to the organization and execution and financing of a project.

I'd like, if I may, go back to the point of these checks and balances. Up to that point I was rather endorsing and praising, and I still endorse this. But I think one has to appreciate and consider that there's a price you pay for the checks and balances. It results in a better lending program; it results in better projects. But, as against that, it has to be said that there are countervailing considerations. It sets up internal strains as between the departments, built-in strains. That's one way to describe it. Another way to describe it is that two people are trying to do the same job or two people are looking over each other's shoulder; there's a diffusion of responsibility, and there's an opportunity for conflict when views differ between the two departments, especially between the area department concerned and T.O.D. And secondly, it could be said that it's just cumbersome and time-consuming, and to that extent inefficient if your object is to get out the maximum amount of work in the shortest possible time.

Well, that problem was faced--that that was the price that would have to be paid--and it was thought worth the price, and I think experience has shown that it's worth the price. The Bank could have made a lot of decisions a lot faster, but they would have been less well-based; and although some things might have been done a lot faster, many errors might have been made which have been avoided by the more cumbersome and time-consuming, elaborate examination that's given to loan proposals.

But I come now to the question that given these built-in checks and balances, how are problems to be resolved if problems did arise between area departments and T.O.D.? There had to be some machinery established for the resolution of these internal disputes that might arise. And essentially this is the function of the management of the Bank--essentially to take the views if they are different views presented by the area department on the one hand and T.O.D. on the other and reconcile them or decide between them. The administrative device by which management airs these disputes and reaches a decision is the staff loan committee. The staff loan committee is, of course, a council of the principal department heads of the Bank. The most important questions which are brought before the staff loan committee, aside from occasional papers, abstract papers setting forth issues of Bank policy, but the formulation of Bank policy is done very largely in the form of decisions on particular loan operations as they come and present themselves. It is almost characteristic of the issues that come up on loan policy that if

a difference develops, it will be an issue between the area department on the one side and the technical operations department on the other side.

With the machinery which was set up in 1952 and which still operates, these issues are first brought up at the level of the working party--the working party being in a sense a sub-committee of the staff loan committee, almost the same departments represented on it. An attempt is made there to work out an agreed position. Of course, if there is no issue, agreed positions can be worked out and papers circulated to members of the staff loan committee without a meeting, so much the better. We try to hold staff loan committee meetings only to focus on issues which raise important questions of policy.

On the other hand, if a working party does not reach agreement or if it reaches agreement but nonetheless individual department heads represented on the staff loan committee differ within the conclusion of the working party, it's customary to have a meeting of the staff loan committee, which is chaired of course--and always has been chaired--by a vice-president, a member of management. The staff loan committee does reach decisions in the sense that it is not a body which votes on a majority vote basis. The management of the Bank reserves the right to make the decisions. The staff loan committee by its constitution is advisory to the management, but that's the formal structure, the prerogative to disregard heavy majorities in the staff loan committee. However, as a matter of practice staff

loan committee discussions are extremely influential, and normally if there is a strong consensus which develops in the staff loan committee, the management is guided by that conclusion.

Q: Would you be willing to cite any of the cases where management has, so to speak, overruled the staff loan committee and perhaps something about why?

Knapp: Well, just offhand I can't think of any particular cases I would want to cite for that, but let me take one for example. I think the staff loan committee in general would take a very much more relaxed view on the question of whether the Bank should lend money to industrial development banks in our member countries which are owned and controlled by government. But this happens to be a subject on which Mr. Black personally has very strong views. He doesn't believe that governments are in general capable of administering loans to private industry effectively, and he's taken a pretty rigorous opposition that he just doesn't want to start down that line. I would say in general that the ways in which management has overridden the staff loan committee would be in terms not of doing things that the staff loan committee wouldn't want to do but in declining to do things that the staff loan committee on the whole might have gone along with. But I must say I don't think at the moment of any particular

country situations where this final management veto has been interposed. I'm sure there have been some.

Q: Was there any question of this sort on the question of the loan to Australia in 1950, which, as I understand it, was a very quick loan in terms of the negotiation involved?

Knapp: No, I don't think the issue arose there.

Q: I was just wondering if this might have been a loan that management was very anxious to make and therefore in a sense it cut the red tape of the staff loan committee.

Knapp: No, I don't think so.

Perhaps I might go on to relate this staff loan committee organization (I'm perhaps doing this in a somewhat personal vein). As originally organized the chairman of the staff loan committee was Bob Garner, who was the vice-president, the only vice-president of the Bank, following the 1952 reorganization until 1956. The pattern of the relations between the area departments and the technical operations department was set under Bob Garner, and Bob was the one who, by lending his personal support to the autonomous character of the technical operations department, did a great deal to build up the morale and independent mind and character of that department. Being at that time the head of one of the area departments, I frankly can

recall a great impatience that I had when I wanted to get ahead with an operation, and an operation which in itself was obviously a very constructive one and one which was being pressed very hard by a country. I confess to having felt at times a sense of frustration at what seemed to be questions of small and niggling detail which were being raised on the side of the technical operations department before they would give this particular operation a go-ahead signal. Occasionally, these issues were brought up to the management level, which meant that Bob Garner either in a formal staff loan committee confrontation or at other times in a more informal type of arbitration which would take place in Garner's office with a small select group or perhaps simply between myself and the director from T.O.D. alone. I can only say that this kind of experience that I had gave me a lot of very useful training for my own experience later as the chairman of the staff loan committee. The reorganization which took place in 1956, as I recall it, when Garner left his post to become the president of I.F.C., resulted in the establishment of three vice-presidents of the Bank in his place--Bill Iliff, Dave Sommers and myself. And the division of functions among us left me with the basic task of getting ahead with the Bank's operational work, chairing the staff loan committee and trying to reconcile the pressing needs for Bank assistance to member countries with the need for establishing that on a sound basis, both in the sense of observing prudent limits on a country's credit worthiness but also in the sense of assuring that the projects financed by the

Bank represented a reasonable approximation to the most useful employment of the money invested in them.

Just parenthetically, one should never suppose that in this real world that you can always achieve the highest priority investment, the absolute maximizing of marginal productivity of capital invested. So we can't pretend to be perfectionists. Some people accuse us of being perfectionists, and possibly they're right. Possibly we do overdo it. But all I want to say is that I'm perfectly conscious of the balance that must be achieved between getting ahead in the real world and the job to be done on the one hand and absolutely squeezing out the last drop of productivity of each investment.

Q: What is your own view or the view of the staff loan committee of the argument that it doesn't make too much sense to pay so much attention to an individual project, particularly if that project might have been financed anyhow and all the Bank is doing is freeing funds in a country for use in some marginal project?

Knapp: Well, this is a very difficult question obviously. The first step in getting an answer to it is to be aware of the question and to realize that concentration of money on a particular project doesn't necessarily identify the marginal use to which the money is being put. We can first of all say that at least we're assuring that the particular project that we're working on is done right. That's a minimum. Beyond that, all

that that line of thought emphasizes, it seems to me, is the great importance that the Bank view projects not in isolation but in relation to the whole development program of a country, and that indeed in making a judgment on any project ideally our review should encompass that whole country's development program. This is an issue that in the history of the Bank has gone through different stages. I think (in fact I know) that in the early days of the Bank the project approach was greatly overemphasized as compared with looking at the development program as whole. And it took some time in the Bank to persuade the management that you had to take a broader view. After the stage at which the management people like Gene Black and Bob Garner, who had not had previous experience in that sort of field, became convinced of the validity of this overall approach, it then became necessary to convince the governments with whom we dealt that it was an appropriate approach. All too often the governments with whom we dealt felt that this was (a) unnecessary and time-consuming, and (b) an improper expansion of the Bank's field of interest and an encroachment on their national sovereignty. It took some time. Although the issue has become much less important now in developing working relationships between the Bank and governments, it took a long while to convince governments that we meant business in this field, and some of them still don't understand why we should insist upon it.

On the other hand, if when the Bank was confronted with a particular project, it began to review first the whole sector

within which that project fell and then even more vitally the whole development problem of the country, this had some advantages as well as disadvantages for the country seeking the loan. It meant that it tended to involve the Bank more widely. Sometimes countries found when they had made an application for one particular project, the Bank's scrutiny of the sector that lay behind the project and then the wider development program led to further loan proposals that might even be initiated by the Bank for the expansion of this particular project into other areas or its supplementation by complementary projects in other areas. Countries began to see that they had something to gain rather than something to lose.

Q: I'd like to ask a question about the technical operations department. When they're doing their cost benefit analyses, how widely do they go into the economic question of external economies, for example, in determining whether a project is economically feasible, and does this ever become an issue between the T.O.D. and the area department economist?

Knapp: Well, I don't think that's become very much of an issue. I think it's true to say that the initial T.O.D. analysis tends to be a little more narrowly confined to the directly productive impact of the project concerned. But I wouldn't want to say that they haven't adequately appreciated the external economies that might flow from the project as well. That's true today. I think

there was a time when the T.O.D. was first organized that there was a little bit of the antithesis between engineers and economists--the engineers taking a somewhat more narrow view and the economists taking a broader view. But over a period of time there's been a tendency to bring more and more economic and financial talent into the T.O.D. itself in connection with project appraisal. I think it's generally true that the economist takes the broader view than the engineer, but you've got a good deal of that broader view incorporated right now in the personnel of T.O.D.

I was going to say a little more about the reconciliation of these departmental views. I guess I only wanted to conclude what I was saying on the subject of organization--to say that when the three vice-presidencies were set up, I undertook this task of reconciling views on loan policy as especially reflected in positions to be adopted on key issues in any particular projects. But I did this, so to speak, as a representative of the management, and Mr. Black and Mr. Iliff and Mr. Sommers also took a very continuing interest and a hand in that kind of thing. Either they attended the staff loan meetings (Mr. Black would very rarely attend the staff loan meetings but the other vice-residents attended a great deal, especially when there are issues upon which they have strong views), and beyond that, if the other members of the management are not attending staff loan meetings, I take my own soundings among them to get their views, either in anticipation of meetings or to make a final check with my

colleagues on management after we've reached a decision on the staff loan committee to make sure that we have a united front. Frankly, this kind of a system, which we've had with three vice-presidents, and then since Mr. Sommers' departure a year or so ago, just the two of us, can operate effectively only if you've got people that are pretty much in gear in the sense of having the same mental processes and basic policy orientation. I think that without trying to gild it too much, that deep issues have sometimes come up that have found members of the staff loan committee and members of management all over the lot in terms of their views on the subject. And yet on the whole, I think we have developed a philosophy as to what we're about and a pretty well-developed body of techniques as to how to achieve our objectives that have led to a fairly (and on the whole surprisingly) harmonious approach and agreement on major policy issues presented to the Bank.

Q: How would you reconcile the notion on the outside of the Bank that the absorbent capacity of underdeveloped countries is considerably greater than the amount of lending that the Bank is likely to make given its particular procedures and if you can comment about this?

Knapp: Well, absorbent capacity is a word that means different things to different people. If it's used in the sense of the capacity of a country to service loans repayable to foreign

exchange, then there obviously are prudent limits, though they never can be measured by any exact formula, and I think it's perfectly true that the Bank in general has counseled limits of credit worthiness in that sense that are lower and more conservative, more prudent, than many other people in the countries concerned or, let's say, in academic economic circles might be prepared to accept.

But absorbent capacity is also used in another sense, and I think the more interesting question is: what is absorbent capacity in a more technical sense of the capacity of a country to receive and absorb and put to productive use outside capital irrespective of the terms of repayment? Now, here, I must say that I think there are often differences of opinion based upon a lack of definition of what is meant. The Bank's experience has been that there is a definite limitation--a very serious limitation--on the capacity of countries to absorb capital and invest it in productive uses of a kind that the Bank customarily finances, the development of public services, investment in infrastructure, or in agricultural or industrial uses. On the other hand, even in a country which suffers from those limitations might still be able to absorb more aid and put it to other uses--for example, investment in education or in public health or housing or other uses that are not immediately productive. Or even going beyond that, a country, of course, has a practically endless capacity to absorb foreign aid if it's

simply going into consumption, to lift the level of living standards of the country concerned.

Now, sometimes when the Bank says that a country has only a limited absorptive capacity, other people feel that our estimates are too low or even that our estimates are refuted by actual experience, that a country has shown itself to be capable of absorbing a great deal more. And in many of those cases that are cited, the country is indeed absorbing foreign assistance, but it is not absorbing it and investing it effectively.

Q: I wonder if now you could say a bit about IDA, its background and relation to credit worthiness and what not.

Knapp: Well, we became convinced three or four years ago in the Bank (Mr. Black became personally convinced) that the capacity of the borrowing countries to repay in foreign exchange was really the limiting factor on what the World Bank could do, and we began to feel our way toward possibly finding a way in which the Bank could supply junior mortgage money to countries on a repayment basis somewhat more liberal than the Bank's regular terms.

In the first place, this obviously involved getting more money from governments. One couldn't expect to borrow money in the markets and relend it on soft terms or more lenient terms than the Bank itself observed. So it was primarily a matter for governments to take the initiative, and among the governments the obvious one to take the initiative was the United States

government. So there had been a certain amount of talk about this at the official level when, so far as I know, pretty much to our surprise and to Mr. Black's surprise, a resolution was introduced into the United States Senate by Senator Monroney. And, Senator Monroney urged the Administration to study the prospects of establishing some kind of an international agency under the sponsorship of the World Bank to make loans that would be on lenient terms. What Senator Monroney specifically had in mind was loans repayable in local currency. This was the device that had been used by the United States government in the distribution of food stuffs, the sales of surplus food stuffs under Public Law 4(e), and also a device that they had adopted for bilateral lending purposes through the Development Loan Fund. And, essentially Senator Monroney's idea was to extend this to a multilateral basis, but also--and in Senator Monroney's mind probably the most important aspect--to find some way to delegate to a multilateral agency the responsibility for administering local currency funds, Indian rupees, for example, that had been accumulated by the United States government under its bilateral programs. So Senator Monroney's mind at the time seemed rather confused on this subject. This was a local currency institution, an institution that would lend some foreign exchange--again for repayment in local currency--and an institution which would also administer local currency resources derived from contributions from national governments and in particular from the United States government.

The fact that the initiative was taken in the United States Senate, which voted a resolution introduced by Senator Monroney, is just a curious historical accident; but it did accelerate the process of the creation of IDA. The United States government at this instigation took the matter up in first bilateral and international discussions, in which Mr. Black was also consulted at frequent intervals; then formally introduced a resolution at one of our annual meetings, and the board of directors of the Bank was delegated the task of drawing up the charter of an institution, and the institution was, as it was known, duly created.

During the evolution of the articles of agreement of IDA, the original notions about this being a local currency institution were largely changed. The management of the Bank took a very dim view of the idea of lending foreign exchange against repayment of local currency. We didn't want to have the responsibility of administering these local currency funds, and in fact we were inclined to denounce it as almost a dishonest device which encourages people to think the institution is getting some repayment but you're really not. And we were even more alarmed at the prospect of having to take over a pot of Indian rupees or other local currencies from the United States government and be responsible for their administration.

Q: What did Senator Monroney think the Bank would do with these local currencies?

Knapp: Well, frankly, as I said before, Senator Monroney was possibly somewhat confused in his own mind on the subject, but his idea very simply was that we would accelerate the internal development of India by lending out these rupees. Perhaps it's not worth the time now to analyze just why this was a rather naive concept. But the fact is that the Indians themselves were very much opposed to this idea of having an international institution accumulate rupees, whether from the repayment of loans or by transfers from other governments, and it would have involved us very deeply in monetary and fiscal policies of India in a way that we certainly would not want to assume.

So the charter of IDA left it wide open as to what the terms of repayment might be demanded. In fact, under the leadership and management of the Bank, the board of directors of IDA has formulated a policy which has prevailed up to now-- namely, that the loans made by IDA will be extended in foreign exchange and will be repaid in foreign exchange, with, however, very liberal terms of repayment, which have so far taken the form of 50-year loans with over a ten-year period of grace and no interest at all, only a service charge of 3/4 of 1% annum.

As to this second function, to which Senator Monroney attached so much significance, the administration of local currency resources, to be contributed by member governments, the charter at the insistence of the United States government and with no support from other governments, was written in such a manner as to authorize IDA to take over such funds from, for

example, the United States government; but this was hedged about with restrictions, and particularly it was made perfectly clear that such funds would be transferred to IDA only with the consent of IDA and further with the consent of the country whose currency was being transferred. And up to this time no such action has been taken. In fact, a bill that was issued in the United States Congress at the last session to authorize the United States government to make such transfers was not enacted--I'm told because of some fairly sub-rosa, but nevertheless influential, opposition from farm interests in the United States. Frankly, many of us hope that this provision of the charter will remain a dead letter. And indeed, it might not have ever been written into the charter had it not been, again, for the historical accident that Senator Monroney happened to take this particular initiative. No doubt he was placated at least by seeing the articles of agreement provide for this possible contingency.

One thing I might add is that the management of the Bank was very chary about having IDA created with resources as small as a billion dollars. I think generally in the Bank it is felt that IDA will stand or fall in accordance with whether that proves to be simply a starting mark or whether it remains only on that scale.

It isn't just that we wanted to have more money to do a bigger job. What we were concerned about particularly--and what we're still very much concerned about--is the fact that if the resources are that small, there's a very perplexing and difficult

and burdensome problem of having to make a reasonable allocation. What it means is--talking about IDA given something like \$160- to \$170 million a year over the next five years--that that amount is so small in relation to the justifiable demands that might be placed upon it that we have to impose a more or less arbitrary rationing. In the case of the Bank, we never had to ration money. We always claimed--and I think it's true--that we've always been able to raise all the money for the Bank that was required to finance Bankable projects brought forward by countries with adequate credit worthiness. But in the case of IDA, while maintaining project standards, we are taking a very much more liberal view of credit worthiness standards. Again, there are huge demands, and the rationing of the money is a very heavy responsibility to place upon the management. And what's more, it inevitably takes us into a realm of political judgments, which is a very hard task to place upon an international professional administration. If IDA were expanded to three times its size, we would be able much more easily to place our operations on the basis of handling the justifiable projects that come forward without trying to make artificial and arbitrary judgments on allocation.

Q: Is it anticipated that the Bank will investigate respective IDA projects in the same way that it investigates World Bank projects?

Knapp: Oh, yes--yes indeed. We have somewhat more freedom of action under the charter in choosing the kinds of projects which we might finance. We can lean a little in the direction of taking those things which have come to be known as social projects rather than directly productive economic projects. My own definition of these is things that are less investment in future productivity and more satisfaction of current welfare requirements, like housing, water supply, other municipal services. Our sort of doctrine in the main in the past has been that those things were the fruits of economic development and that we would rather invest in the means of economic development and let countries develop the taxable capacity and the productivity that would enable these amenities to be provided.

But anyway we may be able to lean in that direction, but even where we do expand out toward projects beyond the scope of the normal bank operations, we shall insist upon the same rigorous standards of setting a project up in the right way--whatever it might be.

Q: Will the Bank cover its own costs of operation in connection with these types of operation?

Knapp: Yes, I think so. You see, IDA is set up as a separate organization financially. There are no separate staff, but every week or month we have a system of internal reporting in our staff as to who is spending time on IDA, and a calculation is made on

the time spent on IDA affairs, and the Bank bills IDA for those services, without, however, charging for overhead, which is pretty much assumed by the Bank on such things as the salaries of the board and top management and building expenses and so on. IDA will have income and an income in foreign exchange which should be adequate to meet these expenses incurred on its behalf.

Of course, the whole idea of having IDA as a separate organization is anomalous and was really resorted to only because of considerations of legislative convenience. It would have made much more sense simply to amend the Bank charter to confer upon the Bank new functions. But it was felt that to take legislation to parliaments all over the world, to amend the Bank's charter in that respect, might open discussions of the Bank charter, invite more amendments, etc., etc., and it was therefore set up as a completely new and separate organization even though under the same top management.

Another consideration was to emphasize to the world, especially to the investors in Bank bonds, the completely different financial status of the two institutions; and they are indeed run completely differently. They are completely different entities so far as their financial accounts are concerned. This was to, as I say, assure investors in Bank bonds that their interest in the Bank would not be diluted by the diversion of funds into the softer IDA channels.

Q: I have heard that IDA is something that the United Nations would rather like to have had some part in handling. This raises the question of the Bank's relations to the UN and other organizations. I wonder if you could say a bit about that general aspect of the Bank.

Knapp: Well, that's a very broad subject, our whole relations to the United Nations. But let me comment first upon an aspect of the history of IDA which is interesting. At the same time that these ideas were generating about IDA as an institution to be associated with the World Bank, there were at the same time discussions within the United Nations pressed forward by the United Nations Secretariat and by the underdeveloped countries in the United Nations councils looking toward the creation of a so-called SUNFED, Special United Nationals Fund for Economic Development. SUNFED was the brain child of a group of experts brought together by the Secretary-General of the United Nations to make a recommendation as to how the United Nations organization as such, not for the moment including the World Bank as a specialized agency of the United Nations, might forward economic development through financial investment. And the committee of experts recommended this agency, and indeed there still continue to be rather active committee deliberations under the United Nations Economic and Social Council discussing the formation of SUNFED.

The issue, therefore, between SUNFED and IDA became rather acute at one time, and it was the United States government primarily that decided to go for an agency under the management of the World Bank rather than one under the management of the United Nations. The considerations were twofold: one, that an agency administered under the United Nations would presumably be dominated by the underdeveloped countries if the voting was on a unit basis, complicated by the fact that in the United Nations the Soviet Union and the rest of the iron curtain countries would be members and participate in the management. And for those rather obvious political reasons, the United States felt that it would rather contribute its money to something under sounder professional and technical management than could be expected under the United Nations administration.

Now, of course, the underdeveloped countries themselves tend to favor SUNFED for the simple reason that they want to escape some of the rigorous administration and management of these funds, or, as they would put it, they would like to have a much larger voice in policies of the institution and the administration of funds.

In a sense the creation of the Special Fund of the United Nations under Mr. Paul Hoffman was a compromise made by the United States in the United Nations to satisfy the clamor for something in which the underdeveloped countries had more representation and voice. You will recall that this is an institution providing monies to finance technical assistance

activities in the underdeveloped countries, but to finance technical assistance projects of a size and scope rendering them too large for the normal United Nations technical assistance program. In practice, the Special Fund so-called has focused on surveys of natural resources, on surveys of development of potentialities and requirements in particular sectors of the economy, in financing technical education, technical institutes and that kind of thing, and to a certain extent in what they call pre-investment studies related to specific projects.

There has been some possibility of rivalry and friction in this field, because obviously if one institution, namely, the Special Fund, is administering a study of a project and the Bank or IDA is called upon to finance it, it might work harmoniously; but if there were differences of opinion, it might be very unfortunate. I'm glad to say that this possibility has been largely obviated by the fact that Paul Hoffman has not built up his own organization to carry out these studies but calls upon different agencies and institutions to actually execute them. In the case of anything that looks as if it might be financed by the Bank in the future--indeed, more broadly, in the case of anything in which the Bank might be thought to have some special expertise, such as a power survey or a transport survey or even many things like mineral surveys or agricultural surveys--the practice has developed of the Special Fund designating the Bank as the executing agent, which means really that the role of the Special Fund is largely limited to negotiating underlying

agreements and providing the money, and the technical assistance project is carried out by the Bank's staff or by consultants hired by the Bank and supervised by them. However, the Bank also has a program of technical assistance, and sometimes there is real conflict between our aspirations or intentions in that field and those of the Special Fund.

Just to mention one example, the Special Fund is showing an interest recently, joined with the regional agencies of the United Nations, such as ECLA in Latin America, to dominate or to assert a much wider role in the field of country economic surveys and giving advice to countries on development programs. And this is a field in which the Bank has been very active and in which we expect to continue to be very active. It's also, however, a very tremendous field of activity in which, so far as we're concerned, we have no desire to assert a monopoly. There's room for many different agencies to carry on this function in different countries.

Well, I might go on to comment a little on our relations with the United States government, because there, too, there have been vast (and still remain) possibilities of conflict and duplication and certainly an ever-present need for coordination of our activities with theirs.

The starting point of our relations with the United States government perhaps is to point out that the United States director of the Bank is a senior official of the United States Treasury, and the United States governor for the Bank is the

Secretary of the Treasury. Also, formally our relations with the United States flow through that channel, and one might expect that the Secretary of the Treasury and the Assistant Secretary, who serves as the United States director for the Bank, would be the official who would coordinate the activities of the Bank with those of the other agencies of the United States government.

Well, it doesn't really work this way, because obviously the Secretary of the Treasury and perhaps equally obviously his Assistant Secretary have a great many things to do other than that. Their handling of the relationship with the Bank is only a small part of their overall official functions. As a matter of fact, the management of the Bank has taken upon itself, keeping the United States director informed, the task of trying to gear in more closely with the other agencies of the government.

The agency with whom we probably have the most direct and frequent contact is the State Department, not because we are seeking political guidance, and not because they are seeking to impose political guidance upon us, but simply because we find there the people who are closest to the real problems. If there's a problem in Latin America, the Assistant Secretary of State for Latin America is likely to be the best informed about it.

It's the regional breakdown of the State Department which keeps the senior officer close to the country problems, and also they are likely to be closest to the sources of information on what's going on in the country, and very often a State Department

channel is our best channel for getting reports and advice on developments in borrowing countries that are of interest to us.

However, at the same time there are occasions in which it's useful to take a reading on what is current United States policy in some countries in which we're operating. We are very sensitive about this. We strongly maintain our autonomy and independence, to the point where many State Department officials and many American ambassadors abroad are rather resentful of our stiff-necked attitude. But we do feel that it would be very damaging for us to become regarded as a political instrument of the United States government.

On the other hand, the United States is our principal shareholder. They provide a large part of the money required by the Bank and its operations, and de facto the United States government could always mobilize a majority of the board against any operation on which they wanted to impose a political veto. I should emphasize that this happens on only very rare occasions. But if there is any doubt as to whether the United States government will support an operation by the Bank, it's just as well for us to know that at an early stage of the game, and the way we usually find that out is through contacts with the State Department.

Then comes the question of our relationship with the other lending agencies of the United States government and especially the Export-Import Bank and the Development Loan Fund. Now, taking the Export-Import Bank first, this is of course a

relationship which has gone on since the very beginning of the World Bank. I think it's interesting to recall that at the time the World Bank was created at the Bretton Woods Conference in 1944, the Export-Import Bank had a very limited role in making development loans. In fact, up to the outbreak of the war they had not been in that field at all, and they had simply been financing commodity exports with the sole motivation of promoting export trade in the United States. It was a few limited wartime operations which brought them into the field of development financing. They financed, for example, the steel mill in Brazil; they financed agricultural development in Haiti to produce wartime sources of material that normally were imported from Southeast Asia. There, again, we got into a few special operations in which the motivation was not the export of U.S. goods but the development of some project, and usually in most cases a project more specifically in the United States interests than a project in the interests of the borrowing country.

But after the end of the war in Europe and before the end of the war with Japan, there arose a proposal in the Congress to extend the activities of the Export-Import Bank in the postwar period. The World Bank, although the charter had been agreed upon at Bretton Woods, still was going to take quite a while to organize, and it was felt there was an emergency need for loans to countries to redevelop their economies after the end of the war. And an amount of a billion dollars or a billion and a half dollars was appropriated to the Export-Import Bank for that

purpose. And, as a matter of fact, they then began getting into the development lending business on a substantial scale, particularly in Latin America before the World Bank ever came into operation.

When the World Bank did come into operation--and this was before my time with the Bank--I understand there was a period of uneasy relationships between the World Bank and the Export-Import Bank. But there seemed to be quite enough for both to do, and these conflicts apparently never became very serious. And at the time that I joined the Bank in 1951, the relationships were pretty harmonious, partly because the Export-Import Bank was concentrating quite heavily in Latin America, and partly because of the personalities involved.

Q: In the case of the Latin-American operations with Ex-Im, did the management of the Bank feel that the Ex-Im was undermining the Bank's attempt to get around fiscal policies established, for example?

Knapp: Well, this was and is a problem, in a sense. In the first place, if the World Bank has made a substantial investment in a country, it naturally will be very unhappy to see the safety of that investment endangered by overlending from any other source, including the Export-Import Bank. And the Export-Import Bank may be driven at times to make loans, which at least stretch the standards of credit worthiness, because of the political

pressures that are upon them as an instrument of U.S. foreign policy and as an instrument of U.S. commercial policy and promotion of U.S. exports. So that's a problem.

There is also the problem, stated perhaps more broadly, that you allude to--the problem of the standards of lending in the sense of the conditions that are being posed. Perhaps the World Bank is withholding money from a country because it's following a loose fiscal policy and thereby endangering its credit worthiness. That's one case. But another case might be the Bank withholding assistance from a project because it doesn't feel that the engineering has been adequately done or that, for example, the management has not been set up right or that in the case of a self-liquidating type of project that adequate rate policies have been established. All those standards can be undercut by an offer of money from another source public or private. And this is a problem with which we're constantly working. The Export-Import Bank would normally be the last to undercut our standards. Their own standards also are very high. On the other hand, they're one of the very few lenders who can compete with us in terms of the terms on which they offer their money. Other lenders--for example, European financial groups with the support of export guarantees from their respective governments--sometimes in the past at least they've been quite irresponsible about the terms on which they would advance money. There's precious little concern for the project or its productivity or even how it was being run. They just sell goods

and take their profit and get out. But that kind of competition, if you want to call it that, has been ameliorated by the mere fact that they were not in a position to offer long-term money at reasonable interest rates. So over the last ten years it has been the Export-Import Bank that has been the principal source of that long-term money.

The Export-Import Bank has a real problem with which one must have some sympathy. They were established as a banking agency. They are supposed to conduct their affairs with prudence, and indeed they've had a very remarkable success--not as remarkable as the World Bank, which has never had a default, but the ratio of defaults in the Export-Import Bank in the total business done is minuscule, and they've piled up a very large amount of earnings and reserves. So they've on the whole operated conservatively. And they're very proud of their own autonomy within the United States government. Especially they're very proud of being established as an agency reporting directly to the Congress. They regard themselves as somewhat independent of the government.

But, on the other hand, they are subject to political pressures. They have to play the game, and sometimes they are subject to very compelling pressures. For example, the State Department or in some cases no doubt even the White House pressures them to be the instrument of accomplishing some political objective.

Returning to the question of our relations to the Export-Import Bank, there was a problem depending on personalities. When the Eisenhower Administration came in, the first Secretary of the Treasury was Secretary Humphrey. George Humphrey decided that he wanted to play down the role of the Export-Import Bank, largely as an economy move, and there was a certain tendency in the first year or two of the Eisenhower Administration to cut back the activities of the Export-Import Bank, and in a sense this left us somewhat a clearer field. However, this led to violent protests, from especially United States manufacturers and commercial interests, who alleged that they were being put at a clear disadvantage in relation to the European countries. This was a time when production of goods in European countries was expanding; their capacity to export was expanding; and price competition was becoming very severe. So, great pressure was brought upon the Administration to change its policy, especially from interested Congressmen and Senators. Senator Capehart was one of the most vocal in that respect. And there was indeed a swing of the pendulum almost to the other extreme.

Up to the time that George Humphrey came in, and even more so after he came in, there was a certain philosophy that anything the World Bank could do, it would do. And the Export-Import Bank would pick up things that for one reason or another the World Bank was not in a position to do. But the incident or the event which marked the swing of the pendulum in the other direction was when, probably in the second year of the Eisenhower

Administration, the National Advisory Council endorsed a new policy with respect to the relationship between the institutions. And, the policy was that in any case where a foreign country wanted to execute a project employing United States goods and services, the Export-Import Bank would be the first line of resort; and that only in cases where the borrower wanted to have international competition for the supply of goods and services would it be encouraged to go to the World Bank.

Well, of course, as a matter of fact, in most cases if a country knows its own best interests, it wants international competition. But, nonetheless, this meant that American manufacturers of equipment were encouraged to go around the world and work up projects and bring them to the Export-Import Bank for financing as the preferred and normal method of approach. And under that definition of the respective functions of the two institutions, there's more danger of rivalry over prospects than there was before. But I think if one weighs up the whole picture between the World Bank and the Export-Import Bank, the fact is that there's been very little real friction, and there has been a certain amount of consultation and coordination. Broadly speaking, the relationship has been pretty much one of each going his own way and doing useful things and there being enough to do around the world to keep both institutions busy.

Q: How about the Development Loan Fund?

Knapp: Well, the Development Loan Fund is quite a different thing, starting with its own charter. The Development Loan fund, you will recall, was set up to provide soft loans, the definition of which at that time meant loans repayable primarily in local currency; and it was clearly recognized that this was a supplementary, subsidiary form of financing; and so it was written into the Development Loan Fund charter that they should not make a loan if the loan were available on reasonable terms from private sources or if a loan would be made by the Export-Import Bank or the World Bank. The standard practice of the Development Loan Fund whenever they've received an application has been first to consult the Export-Import Bank and secondly the World Bank to see if anybody else would pick it up. So that clearly there, the DLF is the last line of resort.

Furthermore, in the case of the Development Loan Fund it's been possible to work out joint operations much more easily and simply than with the Ex-Im Bank, although it happens we're at the closing stages of the negotiation of a loan in which there will be that sort of relationship. This is the loan on the Volta River project in Ghana, to which the DLF will also be a party. But that's a very unusual operation. And, perhaps the underlying reason why it's been very difficult to have a joint operation between the Ex-Im and the World Bank is that such a joint operation would almost inevitably take the form of the Ex-Im Bank financing the dollar procurement on a project and the World Bank financing a nondollar procurement. That might appeal to you as a

logical division of function. But, when you bear in mind that we have to sell a lot of our bonds to American investors, we, too--we the World Bank--want to have a share in dollar procurement. Our appeal to the American investor in the extreme would disappear. That would overstate it, but our appeal to the American investor would be greatly diminished if we were simply seeking money to spend on exports by other countries. So that's made it very difficult to have joint operations with the Ex-Im Bank. But a joint operation with the DLF takes place in several cases because the DLF has not only adopted a liberal policy with respect to terms of repayment but also has ended up with quite a liberal policy with respect to type of expenditures which it can finance. In particular, it has in many cases financed local currency expenditures on projects. And, we've had a number of instances in which there was a natural marriage of convenience in which the World Bank would be financing the foreign exchange expenditures of a project in a foreign country and the Development Loan Fund coming in to finance part of the local currency expenditures. This has happened particularly in Latin America. And, in fact, in such cases we have a sort of a delegation of authority which is given to the World Bank from the Development Loan Fund to represent its interests in the administration of such loans--in the supervision of the execution of a project, in the receipt of progress reports after the project comes into operation and so on.

I think it's also true to say that this is also partly a matter of personalities, and the personalities who happen to have been in charge of the Development Loan Fund up to the present time are generally individuals who for one reason or another work more freely and cultivate a warmer relationship with the Bank than some of the people from the Ex-Im Bank.

Q: Who in the Bank really does the talking on matters of coordination? Would it be you, for example?

Knapp: Well, it goes up and down the line. I would say that it's our desire and hope that the really effective coordination be done at the level, so to speak, of the country officer. In other words, the fellow that's handling Peru at the World Bank should be in touch with the fellow handling Peru in the Ex-Im Bank or the DLF or elsewhere. That's the best level, right at the operating officer level. The next level would be at the area of the area department head. Usually if these matters attain any importance, that is at the level at which they get discussed. In the case of the World Bank, our individual loan officer will learn about the problem, but it will be the department head who will conduct the conversations with the other institution. However, it may very well get referred to higher authority, in which case it usually falls on me to carry on the conversations. But it may also get to the level of the president of the Bank. And, this is complicated somewhat by the fact that these other

agencies aren't always organized on a geographical basis.

There's no particular geographical organization, so that it's sometimes difficult to find the right counterpart with whom to talk if you're looking at a particular country problem.

The new American aid agency, AID, which is expected to emerge from Congress very shortly and which will take over the American foreign aid program except the Ex-Im Bank, which will continue as an autonomous agency, will definitely be organized on a geographical basis. That is, great emphasis is being placed upon the idea that we have always emphasized here in the World Bank that the basic approach to development is on a country basis; and if that approach is valid, it should find reflection in the internal organization of an institution.

Well, another aspect of our inter-agency relations is that of the relation with the International Monetary Fund. This is really a very intimate working relationship and one which, on the whole, has given rise to surprisingly little friction. On the other hand, it must be said that there is certainly still room for closer concentration and coordination between the two institutions. Here, very definitely, it's at the area level that this coordination takes place, and very rarely are there issues that need to get appealed to a higher level. There still are unfortunate cases in which there's a duplication of work or a duplication of missions that go out from the Bank and Fund. There is a constant problem of getting a more effective overall integration of the effort, especially of course in the field of

economic surveys and economic reports. As far as the actual subject matter of the work we do, financing economic projects as such, the provision of short-term stabilization assistance and the consultation on exchange rates are subjects which are very much removed. For example, I've always felt that it was right to create the Bank and Fund as quite separate institutions--indeed with separate boards of directors--although there were some at the time of Bretton Woods and some since which have advocated that for the sake of economy and to avoid conflicts it might be better for the two institutions to merge together in a single one. As I say, I can't agree with that.

Whereas the contact between the Bank and the Fund at the area levels is quite close, it has to be said that the contact at the level of the managements of the institutions is quite spasmodic. Personally, I think this is unfortunate, but here it has definitely been a matter of personalities. Per Jacobsson and Merle Cochran, who have been administering the Fund now for several years, have not been very responsive to consultation and coordination at the management level. They'd much prefer that it be left at the level of the area departments.

Q: How about in the earlier days before Mr. Jacobsson?

Knapp: Well, we used to have, for example, when Ivar Rooth was in charge of the Fund, I was at that time a director of an area department, I used to see quite a little bit of him. I used to

have lunch with him from time to time and review with him a particular area in which I was in charge. And, he did this with the other area departments, although I think I had a closer personal relationship with Mr. Rooth than the others. But even then I don't think that he had that kind of consultative relationship with Mr. Garner, then the vice-president, or with Mr. Black. There's been a certain aloofness of the Fund management in relation to the Bank. And, frankly, this perhaps is still a reflection of the period when the Fund was very much the junior partner. There was a long period of years in which the Fund rather languished and the Bank forged ahead very strongly. That was true certainly even in the first years of Mr. Jacobsson's regime, and it may have been that the Fund management felt that the closer they got to the Bank management, the more they might themselves fall under this domination. That may account for the aloofness. Actually, the Fund has emerged in recent years into its own, so to speak, and has been engaged in very large-scale operations and acquired a reputation which allows it to stand very much on its own feet. This should have destroyed any inferiority complex that might have plagued the earlier relationship. But it has to be said that it's still not very intimate at the management level.

Q: How about the relations between the economic staffs or the research staffs of the two? Outsiders of the Bank sometimes felt

that the economic research done in the Fund that was published at least was more notable than that of the Bank.

Knapp: Well, I think that's certainly true with respect to published material, because the Bank hasn't published much of anything.

Q: Did the staffs consult with each other?

Knapp: Yes, there's a certain amount of consultation, but really, I think, the economic research and analysis of the two institutions has been directed toward rather different things. And there's a certain conscious division of labor. For example, commodity studies are done in the Bank, although they might have been expected to have been done in the Fund because they're so much related to general international payments problems. The country studies done by the Fund and the Bank are done in close cooperation by the staffs of the two institutions. But they have quite a different orientation. The Fund's short-term horizons and perspectives require writing one kind of a report. The Bank reports are directed far more toward the real as distinguished from the financial side of the country and toward the medium- and long-range and very long-range appraisal rather than short-term problems.

There again, there's probably room for a good deal of more efficient integration and coordination of economic research with

the two agencies, but I don't think one should exaggerate what could be done in that respect.

Q: There's one side issue that perhaps you could comment on. I have heard that in the early days of the Bank at least, the economics department had some difficulty formulating highly theoretical issues as the Fund was at that time doing, because the management of the Bank didn't understand the highly technical language of the economists and rather frowned on the reports of this sort.

Knapp: I think so. Neither Mr. Black nor Mr. Garner when they came to the Bank had any economics background as such, and indeed neither of them understood the language. But, they had to learn it the hard way by having it come up from their staff. Not wanting to admit they didn't understand it, they just had to learn it.

Q: How about the relations with Latin America?

Knapp: I was going to mention that. There's a special problem of relations within the Latin-American area. I mentioned that already in connection with the Ex-Im Bank, but all this became subject to another dimension of complication when the Inter-American Development Bank was founded. I think, actually, that as far as the Bank and the World Bank were concerned, they never saw much need for the creation of a regional institution, which

might to a considerable extent be thought of as a duplication of international machinery. And, our concern about that was not only for the Latin-American area, but our feeling that possibly this would be a prelude to drives to set up regional institutions in other parts of the world: a bank for Africa, a bank for the Middle East and a bank for Asia and so on. Well, fortunately that hasn't happened. But within the area of the western hemisphere the advent of the Inter-American Bank has already begun to create some problems, additional problems of coordination among the institutions.

So far this has not been very serious, partly because the Inter-American Bank has fairly limited resources and has tended to establish for itself certain limits. For example, they usually don't think in terms of individual loans usually of more than \$5 million, and this has kept them to the smaller projects. It seems so far, as a practical matter, not to have created severe problems of competition. However, there is here particularly the danger of competition in reducing lending standards, because the Inter-American Bank is a bank dominated by the recipient countries. In the board of directors of the Inter-American Bank, the United States has an important vote, but the majority vote is held by the Latin-American countries as a group. Furthermore, they have a Latin-American president, and the staff is largely Latin American, with a considerable American ingredient.

On the other hand, the Inter-American Bank's capital is set up very much like the World Bank with a certain initial contribution from governments, but with the idea that after that the Bank should borrow. So far the Bank has been reasonably conservative in its transactions, no doubt reflecting the desire in their mind to build up their reputation as a banking institution and to establish their credit. And from our point of view it's a great safeguard that that sort of motivation exists.

On the other hand, things are moving very fast in Latin America, and we're just now witnessing the completion of the Montevideo conference in which the United States government has been promising money very freely and on a very large scale. And it may be that the U.S. government agencies and the Inter-American Development Bank will be placed under very great pressure to lower their lending standards, both in terms of credit worthiness and in terms of the selection of projects and in terms of the design and execution of projects. And, if so, this will be a source of embarrassment in our relations with these institutions.

One of the most recent interesting developments in connection with the Bank has been the organization of international consortia meetings, which the Bank has sponsored with respect to India and Pakistan to mobilize assistance for those two countries from various capital exporting countries on a bilateral basis to join their efforts with the Bank and IDA, and to build up a pattern of financing which can provide adequate

long-term assurance to the recipient country of the feasibility of their development programs. This involves not just fund-raising to meet determined targets; it also involves a discussion of the terms on which aid is to be provided, the limits of credit worthiness, and in particular, the need for providing a large part of the aid on nonconventional terms. It involves, to a certain extent, the discussion of conditions to be required from the recipient country, although actually in this respect the Bank has done a great deal more just on its own behalf than on behalf of the consortium. The discussion of conditions in the consortium meetings does not in general achieve very much. And, finally it's these consortia meetings and the follow-up work which the Bank staff does on them that has provided a certain opportunity for sorting out who is going to do what in terms of the allocation of different projects for financing by different sources, although also there are limitations on that. My own attitude on this subject always is that basically there's no substitute for adequate planning mechanisms in the country concerned to sort out projects and present them to the consortium for finance. In other words, the so-called coordination of aid from various external sources is certainly best achieved by having an organization within the country concerned that is capable of sorting and directing this aid rather than trying to have a creditor's club, so to speak, decide on priorities.

Now, these consortia meetings, as I say, started in India and Pakistan. We're now actively working on plans for expanding

such operations to other countries. The leading candidates at the moment are Iran, Nigeria and possibly in Latin America, Chile and Colombia. There is a serious question how far these consortia meetings can be carried in view of the very heavy staff work which they require, and we feel certainly at this time that it's going to have to be confined to selected cases, cases where a country has an adequate program as a basis for a consortia meeting, one which the Bank and/or IDA are prepared to support financially--one which, in other words, we can commend, at least in its general outlines, to the other consortia participants; and, of course, one in which we can attract the other participants. But by those tests, these countries that I mentioned seem to measure up pretty well. The real problem is: where do we stop? Because to a certain extent, when the Bank runs a consortium for a country, it does give a special impetus to that country. We can't do this for 60 or 70 underdeveloped countries. We're going to have to stop somewhere. And there are some unresolved problems here as to just how we allocate our efforts.

Also, we can't claim a monopoly on this field. There is probably room for other consortium activities. The OECD, or rather the Development Assistance Group, a subcommittee of the OECD, is interested in principle in sponsoring this sort of thing along the lines that we have done. This is an idea pushed in the development assistance group by the United States, which regards this as one device for making that particular body a more useful

and active and meaningful one. No plans have yet been formulated for DAG sponsoring a consortia meeting, and the question of what countries they may select, the basis of selection by them; the question of how far the Bank would participate in or even provide the staff work for DAG consortia: these still remain open questions.

I think all this is a very promising and interesting field, one which stems back to the case of India. Of course, India was far and away the most important undeveloped country; furthermore one of the most advanced, if not the most advanced, in terms of development programming and planning. So it's perhaps not surprising that India became the first case for a consortia application and consortia techniques. It is interesting, however, to look back and recall how this happened. There's no question but what the real impetus for this idea came from a resolution which was introduced in the Senate a couple of years ago--I won't pretend to date it--by Senator Kennedy and Senator Cooper. This resolution called upon the Administration to take the lead in organizing an international approach to the problem of financing the Indian third Five-Year Plan. And, although the resolution itself, as I recall it, did not mention the World Bank, the speeches that Senator Kennedy made proposed that this might best be organized under the aegis of the Bank.

This resolution passed the Senate. The U.S. Administration did take it up with the Bank as to whether we could organize this work. After taking soundings among other interested capital

exporting countries, we found that there was a good response to this idea, and we undertook to do so.

I spoke of this being organized to finance the third Five-Year Plan. That is not correct. The original Kennedy resolution and the original consortium activity was directed toward financing the balance of the Second Five-Year Plan, which was at that time threatened with serious stalling as a result of an unexpected drain on the Indian exchange reserves. And the first one or two meetings of the consortia had the earmarks of a salvage operation to provide money on a rather crash basis to keep the second Five-Year Plan from stalling. However, that moves right on into the stage of the last consortia meeting, which was addressed to the third Five-Year Plan.

Q: I was just going to ask whether you know whether Senator Kennedy or Senator Cooper had conversations with Mr. Black or other people in management about this; that is, to what extent was the Bank itself sort of actively promoting this kind of idea?

Knapp: Well, we certainly did not promote it. If there was any discussion between Senator Kennedy and Mr. Black, it was pretty casual--at that stage, prior to the introduction of the resolution. Kennedy, however, knew about our work. In fact, I went to see Kennedy myself on one occasion to brief him on the Bank's work in India and its views on prospects there. This was

all prior to the introduction of the resolution. But it was certainly nothing that we instigated in any way.

Now, we, as a first step toward laying the basis to an international approach to the Indian problem, organized what came to be known as the Three Wise Men Mission, which was a special commission named by Mr. Black consisting of three western bankers, Oliver Franks from the United Kingdom, Hermann Abs from Germany and Allan Sproul from the United States. This mission, each with a staff assistant, went to India and spent several weeks there and came home and rendered a report to Mr. Black in the form of a letter running to maybe a dozen pages, containing a general appreciation of the Indian development program and what they were doing and the importance of giving support. This was not really a technical appraisal of the Indian program, nor was it intended as such. The whole mission might be thought of as a very high-level public relations job to represent to India the interests being maintained by the West in their development problems, especially coming from three private Western citizens-- eminent citizens but nonetheless private people without public affiliation. And, on the other hand, the purpose of the mission was to educate these three outstanding citizens of the West, none of whom, as I recall, had ever been in India before, and who came back and have since been influential in public and private circles in forming opinion in regard to India.

That mission was followed up then with a Bank staff mission, headed by Mike Hoffman, the director of our Economic

Development Institute. That mission prepared an appraisal of the Third Five-Year Plan, which formed the basis for the last consortia meeting, in which there was in effect a successful underwriting of the anticipated foreign exchange requirements of the Plan during its first two years.

Now, the consortium on Pakistan has followed fairly closely, with a little delay, on the pattern of the Indian consortium meetings. The Pakistan program itself is, by no means, so far advanced, and at the meeting held two or three months ago on Pakistan, much less success was achieved in getting underwriting of foreign exchange expenditures for the period ahead. Reasonable assurances were obtained for the first year, but a meeting will have to be held again this fall to review what more needs to be done perhaps in the first year, and to consider the following year's program.

It's interesting, perhaps, to note the participation in these consortia meetings. Of course, we've been the sponsors. We chaired the meetings, and we've taken a very large hand in running them. The Monetary Fund appears as an observer. Aside from that we've had as regular participants the United States, the United Kingdom, Germany, Canada, and Japan.

Q: May I ask who represents the United States? Would it be something to do with the Development Loan Fund?

Knapp: No, this is usually done at the Assistant Secretary of State or the Assistant Secretary of Treasury level, with people like the president or vice-president of the Export-Import Bank and/or the chairman or vice-chairman of the Development Loan Fund in attendance as part of the delegation. It's been at the top civil servant level, you might say, with respect to the other countries, and with respect to the United States it's been perhaps higher--top civil service and going into the lower political level of appointment, the Assistant Secretary level.

Now, our problem in connection with these consortia meetings, or one of our important problems, has been to attract a wider participation. And, in general we have issued invitations for participation in these consortia meetings to any country which had become an important contributing country in IDA. This is more or less a self-elected group of capital exporting countries. The ones that we have particularly sought as members of the consortia meetings after the original five were the continental Europeans, such as France, Italy, Belgium, the Netherlands. We have been making progress in this respect. The pattern is a little complicated, and I don't have it in mind. At different meetings different countries have come. Also, there's been some difference between India and Pakistan. But, fundamentally, the picture today is that the French are in, the Italians are in, the Dutch are in. The Belgians are still lagging behind for very obvious reasons, their difficulties with the Congo and so on. But, we hope it won't end there, and we

hope this group can continue to be expanded despite the fact that adding more countries makes meetings unwieldy. It's obviously desirable to pass the hat to the widest possible circle.

The meetings did provide not only a place for the discussion of particular country problems, but in the early stages in a way they anticipated the creation of the Development Assistance Group. They were a place where countries could begin talking about the whole across-the-board problems of policies and procedures on the administration of development assistance. They always will have some of that quality, especially in the India consortium, because of the sheer magnitude of the Indian aid program in relation to the others. It's obvious that once you make decisions on India, that assumes a lot of weight with respect to other programs.

One question very much in our minds at the moment is the question of how this type of meeting might be run in Latin America in view of the fact that the Montevideo conference has just been completed and launched a new program of Inter-American action on all these fronts, and the Inter-American Bank has in mind the idea of running consortia meetings for Latin-American countries, extending not only to the administration of their own funds and that of the United States government agencies, but also inviting European participation. I mentioned earlier that we are ourselves considering Chile and Colombia. It remains to be sorted out as to who does what between us and the Inter-American Bank in Latin America, with the ad hoc solution at the beginning

probably being that again there's room for everybody; it's a very burdensome business, and we have to divide up the territory in accordance not with any agreement that we had made between the two institutions but in accordance with the expressed wish of the countries concerned. Some will come to us. Chile and Colombia are pressing us at the moment to take the lead. There will be other countries that will prefer for one reason or another to present their case for handling to the Inter-American Bank.

Q: The members of the consortium other than the Bank, I take it, are getting to make funds available on a grant basis.

Knapp: Oh, no. No, not at all. As a matter of fact, this is a fundamental problem. Take the Indian case. The Bank is on a hard loan basis. IDA is on a soft and very lenient loan basis. The United States program on the whole is on a very lenient basis, although there's some admixture of financing with the Export-Import Bank. The P.L. 480 program is practically on a grant basis, with some repayments of a nominal kind in local currency. The D.L.F. program is now shifting to the IDA type terms, very long-range amortization and a nominal interest rate. The Canadians are on an outright grant basis. They just don't believe in lending for development assistance. But--and this is a very important but--the rest of the membership of the consortium is very largely on a hard loan basis, and until recently tended to provide money on 10- to 15-year terms. We

have been in the lead naturally, with the Indians in pressing the European countries, including also the United Kingdom, and Japan--let's say pressing other consortium members to extend the terms of their loans and to shift gradually toward the admixture of a substantial amount of soft money or what is called an unconventional loan. This has been quite a struggle, and only modest success has been achieved. I should say in general what we have done is get these countries for the most part up to the 15- to 20-year level instead of the ten-year idea, but there's still very little to show in the way of outright grants or really lenient and unconventional terms.

This, I might say, has created a very serious problem for the Bank, and we've made no secret of this. In fact, we have rather bluntly stated at the consortium meetings that already the amount of hard lending being done by other members of the consortium had given serious concern to the Bank. Indeed we practically notified them that if they continued in subsequent years of the Indian third Five-Year Plan to continue to put hard loans out on the scale that they had recently, that the Bank would have to withdraw. In general, what we have urged is that they shift toward providing IDA type money for India, and we have taken the opportunity to say that one of the ways they can provide IDA type money is to build up IDA itself, either by way of supplementary contributions to IDA or by way of across-the-board increases.

Now, one of the questions that came up in that connection was whether the management of the Bank and in IDA, we would welcome contributions to IDA earmarked for a particular country, such as India. Well, we certainly felt that we would prefer to get contributions that were not earmarked for a particular country, such as India, that is contributions that were not earmarked and allocated in advance. Secondly, we certainly felt that if they were to be allocated in advance by the contributing country, it should stop at the level of allocations to the country and not continue by way of allocating to the project. But, we have somewhat reluctantly accepted the idea that we would be prepared to accept supplementary contributions to IDA earmarked for a particular country. Now, this raises some problems of administration, because obviously the Indians do not budget if the Germans, for example, make a supplementary contribution to IDA earmarked for India, but then we, in the administration of our regular IDA funds, cut down on India correspondingly. In other words, the pure theory of this thing is that IDA should go ahead providing India what it would have provided, with the German contribution being truly supplementary. That's a fine theory, and we might loyally try to observe that policy, but I think it has obvious practical difficulties simply due to the fact that what we otherwise would have done for India is a pretty theoretical matter, since it never has been determined.

Q: I should think there would be a problem also in that some of the members of IDA would allege that the Indians, let's say, were receiving special consideration, that IDA was not being operated in a true international way.

Knapp: Yes, that's right. That's a danger. All we can say is: "Well, it isn't really that. We're simply undertaking a multilateral administration of funds which otherwise would occur on a bilateral basis. We, as management of the Bank and IDA, are not the judges of the amount of aid. We only in these circumstances provide the management of the Fund and try to devote it to the best purposes. The country that's been selected by the contributor is the preferred recipient of these funds". But I think you're right, that it does smack a little of favoritism; and for that reason it may well be that the capital exporting company will in the end decide not to use that as a device. They may feel that by putting money up to IDA earmarked for India, while they might thereby achieve some favor with India, there'd be too many countries left out who would take offense at it.

Q: Also coming back to my question about the grants or loans in the case of the other participants in the consortium, if the member countries were making hard loans, then I should think that the questions would come up: Why doesn't the Bank itself do it? If they're making lenient loans, then the question is: why

doesn't IDA do it? And certainly the ultimate question is: What's the point of having them participate except on a grant basis at all? Because there are organizations already in existence that make the sort of loans that they're prepared to make.

Knapp: Well, that's quite right. But the fact is that countries have not reached the essentially political decision to pool all of their development assistance. They pool parts of it. The portion that is pooled on a multilateral basis is increasing, but countries still have their own bilateral lending agencies and are likely to continue to.

Q: I'm just not quite clear what the advantage of this consortium approach is over what can be done anyway.

Knapp: Well, the consortium approach as such...You mean you're not clear what the advantages are of bilateral administration of aid?

Once you have that, once you have big bilateral programs, the consortia meetings do serve in ways that I've described earlier as one of the coordinating mechanisms. But, you're right, perhaps, in thinking that perhaps the most effective coordination could be achieved if all the funds were pooled for administration through the multilateral agency.

Q: I guess what I'm really asking is does this approach end up by providing a greater total amount of overall foreign assistance than would be the case if there was no consortium approach?

Knapp: Well, I think there's no doubt that it does. And this gets back to the problem I mentioned earlier about favoritism; the favoritism that the Bank might be accused of, if it agrees to sponsor certain countries for consortium meetings and not others. I think there's no doubt that the fact that the Bank sponsors a country for a consortium does give a special impetus to the aid to that country, partly just because it focuses on people's attention on it. This would be more obvious if we picked out some less conspicuous country like Chile. And this is partly because, after all, the other capital exporting countries are more prepared to loosen up the purse strings if they receive assurance that the money is going to be used effectively. There is more assurance that the money will be used effectively if it's a case of a development program that's been vetted by the Bank and endorsed by the Bank in a general way. We never commit ourselves to the endorsement of all the details for a particular program--even the Indian program, which I've described earlier, and which is probably one of the best prepared and organized programs in the underdeveloped countries in the world. Nonetheless, it suffers from severe defects, we feel, in structure and in some of the projects. The development of nuclear energy, for example, in India we feel is being pushed excessively on essentially prestige grounds, though, on the other

hand, one must consider that even if it isn't an economic proposition today in the narrow sense, nuclear energy development in India builds up technology in a broad sense not only in power production but also in other fields, not to mention its military attributes.

We've also been critical, for example, of the Indian policies with respect to industrial development and have deplored the fact that they haven't done more to attract private capital in that field and have earmarked a very significant part of public capital funds for purposes which perhaps could have been satisfied by resort to imported private capital.

Q: Has the Bank's experience as a joint lender with private investors provided a precedent in some way for this sort of thing? Does the fact that the Bank had done joint operations before make it easier to fall into this consortium approach?

Knapp: I wouldn't say so particularly. The participation with the private markets are, generally, quite differently motivated. The great bulk of them, which are participations in the short maturities of our loans, are motivated more by the interests of private banks who have established their position in the country concerned for commercial purposes, to get accounts, get letters of credit business, and otherwise establish their public relations position in the country concerned. We've had a few cases which have extended into a real long-term investment

interest by a participant. On the whole, they've been rather few. I'd say that the sort of thing that has come closer to the consortia meetings has been special international intergovernmental deals which we've entered into for the joint-financing of selected large projects.

The one great example of this at one stage was the Aswan Dam transaction which fell through. We've had some joint operations with the British, with the CDC. It's in effect an official institution in British Commonwealth areas. But the two most recent examples which illustrate the consortium technique applied to a particular project are the Roseires project in the Sudan, which we recently financed through a triangular operation, the Bank, IDA and the German Kreditanstalt. This was a special case in which we obtained a large-scale participation by a German government institution. And the second one, which we're currently working on, is a somewhat more elaborate one, which brings together as partners in a loan operation the World Bank, the Export-Import Bank, the Development Loan Fund, and the British Export Credit Guaranty Department, which means the British Treasury would put up a loan through its export credit guarantees mechanisms. The project I am here referring to is the Volta River project, which will come to conclusion within the next two to three weeks.

Q: All of these operations suggest the Bank feeling that the amount of capital funds, external capital funds which can be

usefully used in many countries at least, are considerably in excess of the funds that the Bank can make available through its normal operations. I'm wondering how far back in the Bank's history this feeling goes or has this just sort of always been in the Bank?

Knapp: Well, there have always been these bilateral programs. I don't think we've ever taken the view that we were doing everything that could be done. We may have taken the view that we have been doing everything that could be done in a particular country, taking into account the loans it was getting from other sources. But it's also true--and I've mentioned it in the case of India--that we are very much concerned about the threat of an excessive degree of hard lending resulting from this international mobilization of funds. We may very well be overloading the credit worthiness of India if this goes on much longer.

Q: Well, just taking account of the grants by themselves, has it always been recognized, as far as you remember (of course, I know you weren't here in '47 and '48), that countries could usefully use more money than they could get on a grant basis, for example...?

Knapp: Let me make two statements. The first is: I have no doubt that the Bank in its early days--maybe in its later days,

too--has been pretty conservative in appraising the capacity of countries to absorb assistance. But also there has been a tremendous evolution in the capacity of countries to absorb assistance. Go back to 1947, say: in a 15-year period there has been quite a transformation in the case of many countries. And, for this transformation the Bank can claim its share of the credit. There's a great deal of credit to be awarded here: first of all to the countries themselves that have set about developing their plans for projects. But, if you want to measure absorptive capacity in terms of the capacity of countries to mount a physical investment program that makes sense and is productive, there have been very great strides made in the underdeveloped countries themselves which have opened up opportunities for lending and for grants that simply didn't exist before.

Of course, we still feel today that there are serious bottlenecks, and we still today feel that the Bank is making inadequate efforts to break those bottlenecks, helping countries to design development programs both at the general level and at the project level which will satisfy the needs and to use the phrase I've just used, that will create the opportunities for the productive supply of development assistance. In several different ways we are thinking of--and not only thinking of--we are expanding our technical assistance activities to help prepare the seedbed. And, of course, we are only one of the agencies that are doing that. This is being greatly accelerated through the United Nations, through the United Nations Special Fund,

through the Inter-American system. In fact, the whole Kennedy new look on foreign aid is very much characterized by an emphasis on self-help of the recipient countries: self-help in general, which has reference to their broad financial and economic policies, their social policies, etc., but also very specifically self-help supplemented by external technical assistance in the field of drawing up integrated, long-range, productive programs for investment.

Q: I take it that you're suggesting that there has been almost a revolution in people's understanding of the problems of economic development in the last 15 years and particularly in the techniques of programming and planning.

Knapp: Yes, I think that's true. Perhaps the revolution is not so much in techniques as in the application of the techniques. That is to say, techniques may have developed in that period of time, but the techniques have been taken out of the laboratories and the academic halls and been put to work in public life. There's been recognition at the political level in these countries that this was important and needed doing and needed doing professionally. There's been recognition that haphazard political manipulation of development projects to satisfy local regional groups or to build monuments to the incumbent Minister of Public Works was extremely shortsighted and fruitless, even fruitless in the narrowest political terms. The clamor of the

people in these countries for tangible and concrete advance in living standards has finally convinced people that political survival itself needs a different approach. I should say it's convinced the politicians that political survival itself depends on their doing a more solid job, and this has meant the organization or reorganization or creation of agencies and institutions to do the planning and to carry out an effective execution of public investment programs.

Q: I suppose just to conclude this general discussion, it would be fair to say that the Bank's assistance early in the game on the use of its funds for productive, directly productive, purposes is a fairly important part of the story as to why people's thinking on these subjects has changed somewhat.

Knapp: Yes, I think it is. I really think that the demonstration effect of Bank-financed projects in countries has been very, very important. And I think, perhaps, I referred in earlier discussions we had to the fact that when we first began talking about development programs there was great skepticism in the countries concerned, who felt that this was an excuse by the Bank to delay providing the financing of a particular project, when we said that we wanted to see this project within the framework of a particular program; secondly, they thought it was in extreme cases an infringement upon their sovereignty for the Bank to look beyond the particular project that we'd been asked

to finance. But what has emerged, we hope--I don't want to be too complacent about this--is an increasing realization in countries with whom we deal of the identification of interest between them and the Bank; that the Bank's narrow interest even as a creditor, wanting to get its money back, is identical with theirs. We want to see maximum economic growth in countries with whom we deal--firstly because we're a development institution and that's our mission, but also in the sense that we want to get our money back. This identification of interest has been perhaps one of the most effective ways to convince countries to adopt some of these planning and project preparation techniques.