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Transcript of interview with

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Interview with Mr. Aron Broches by Prof. H. Oliver on July 11, 1961

Q: Now, you are Mr. Aron Broches.

Broches: Yes, I am a Dutch citizen. I came to the Bank in 1946 as an attorney in the Legal Department and I'm now the General Counsel, - since 1959.

Before coming to the Bank, I served in the Netherlands Embassy in Washington and while serving there I'd gone to the Bretton Woods Conference as secretary of the Dutch delegation, and that's how I got interested in the general field of activity of the Bank.

Q: At what point did you become a member of the staff of the Bank?

Broches: In September of 1946 I joined the Legal Department, where we had then, I believe, five lawyers -- we now have sixteen. I became Assistant General Counsel in '51 and head of the Legal Department in '56 and also got the title of General Counsel, in addition to being head of the Legal Department, in 1959.

Q: Who was the chief General Counsel at the time that you came?

Broches: Chester A. McLain, a New York lawyer. He had been a partner in Cravath, Swaine & Moore New York. When he came to the Bank, that is, before he came, in August of '46, the legal staff was headed by Ansel F. Luxford. Luxford had been the chief legal advisor of the U.S. delegation at Bretton Wood and joined the legal staff of the Bank and

was acting General Counsel until McLain came.

Q: Was Mr. McLain acquainted with Mr. Meyer?

Broches: I think he was, either personally or through his partner, Swathland. By the way, Mr. Demuth would be able to give you the background on that.

Mr. McLain had been in general practice. He was particularly concerned with Bethlehem Steel: he was their outside general counsel. He was also counsel for Kuhn, Loeb, and during the war he had become involved in labor problems for Bethlehem Steel, but before then he had done a general corporate practice. He had some international experience in France and Italy and he considered this quite an adventure, something that was new.

He did everything himself once. He always said, I'm not going to ask anybody to do what I haven't done once myself. He actually ran the legal department as a sort of school for himself and his staff for the first year or so, which was an unusual thing. The work was regarded as new and everybody was trying out and trying to see how the work should be done.

Q: I take it that he was a rather influential member of the Bank's staff.

Broches: He was very influential. Of course, the senior--type Wall Street lawyer is used to having his advice sought and listened to by his clients, and that was very much the attitude he brought to the

Bank. He had a great loyalty to his client, and I think he considered the President of the Bank as his primary client, at first Mr. Meyer and later Mr. McCloy. Now, Mr. McCloy had been his junior in his law firm, and I am told McLain took McCloy along as a junior in the late '20s, when they were working on financial deals in Italy and in France. There was a very close relationship there. And I ascribe McLain's leaving when McCloy left in July of '49, very much to a sense of personal loyalty, and possibly due also--McLain is no longer alive so you can't check it--to a feeling that "the boy" needed him. McLain had that feeling.

He was very much concerned that the Bank shouldn't go off the rails long before there were rails, and he tended to keep things pretty close--that's not a very good way of putting it--but he was conservative and extremely careful in his tactics, although I think he had in mind that once he knew where we were going he would open up. But really before that stage came about he had left along with McCloy in '49. In any event, he was greatly respected by the other department heads and he was definitely in a senior position.

During the interregnum, between the Meyer resignation and the McCloy appointment, he practically ran the Bank. The Bank didn't do any business during those days, but administratively and trying to hold things together, he was very much the man on whom everybody relied.

Q: Do you suppose that he was influential in asking Mr. McCloy to become President?

Broches: I don't know. I don't know. As a matter of fact, I was away

during the four weeks immediately preceding the solution of that crisis. I was away during February of '47 when all this happened.

Q: I wonder if we may talk just a little bit about Bretton Woods itself. You are one of the few people who is still with the Bank and who was actually at Bretton woods. Can you tell us something about the anticipations at Bretton Woods or at Savannah, for that matter, with respect to the amount of loans the Bank might expect to make or the role it could play in reconstruction?

Broches: Well, I don't think that quantitatively people had any very firm ideas either at Bretton Woods or in Savannah, which took place a year and a half later. The Bank, of course, as you know, always played second fiddle to the Fund in the minds of people. Technically, it was much less complex. As a concept it was fairly simple. Most of the time and energy of people was spent discussing the Fund. On the other hand, I consulted a report, which I wrote at the time for the Dutch delegation, and I found there a statement that notwithstanding the fact that there had been so little preparation for the Bank--conclusions were reached and an agreement was drafted in a very short period of time. One of the reasons that was assigned for that was the realization that the Bank was necessary as an adjust to the Fund and that if there were no bank, that the Fund would be driven into long-term financing. It was something that I don't remember having been said but I just read it this morning in my own report.

Another thing that has often been said and one that I verified, at least as to what we in the Dutch delegation thought at the time, was

the expectation that the Bank would do two things: it would make loans out of its paid-up capital, but the principal activity would be to guarantee loans made, to guarantee bonds issues offered in public markets by borrowing governments. In other words, there was no idea, I believe, at the time that the Bank would supplement its paid-in capital by borrowing in the market so much as by guaranteeing loans made by others.

I found no explicit discussion of it, but, for instance, the Dutch delegation took the lead at the conference in trying to make the Bank a solid and sound institution. This came up in the discussion of the limit to which the Bank might lend or guarantee. As you know, the Articles now say that loans and guarantees may not be increased beyond 100 percent of capital and reserves. Well, the original proposal was that it could not be extended beyond x-times capital and reserve. A lot of time was spent at the conference deciding what that "x" should be. As I recall, the Norwegians wanted to go to 300 percent, as certainly did the Poles. In the U.S. delegation there was a split. Harry White wanted 150 percent. The Dutch delegation made a computation and it came to 75 percent on the ground that the money to make good on the Bank's obligations as a borrower or guarantee would have to come from the unpaid 80 percent of the Bank's subscribed capital, and that the unpaid 80 percent would have been subscribed certainly in part by countries which had defaulted on loans and thereby made calls on the 80 percent necessary. If they were unable to pay back the loans, they would be unable to meet their 80 percent. Finally, the issue was compromised at 100 percent of capital and reserves. The way it was done was rather funny because the Dutch held

out for 75 percent and some other people for 150 and the chairman said, "Let's split the difference. We'll add one third to one and we'll deduct one third from the other, and we'll come to 100 percent."

Now, the reason why the Dutch were so keen on keeping the limit low was that unless this was done the Bank's guarantee wouldn't be worth a thing. You find constant references to it: if the Bank's guarantee wouldn't be highly regarded, and if people weren't able to borrow in New York with the Bank's guarantee, the Bank would be a failure. And I think that was very much the feeling of the way we would operate, that is by means of guarantees. As you know, in fact, we have never done a straight guarantee transaction.

Q: Do you recall anything about the British position on this subject at Bretton Woods?

Broches: The British tended to agree with the Dutch and the Canadians. And in the U.S. delegation it was Mr. Brown who was a very colorful figure--Ned Brown of the First National of Chicago. He was the only banker, the only Wall Streeter, although he came from Chicago, in the delegation. And he was in favor of the more conservative approach. The conservative approach on the Dutch side and on the others was purely motivated by the fact that otherwise the Bank would be a failure because you couldn't force people to accept the guarantee of the Bank.

Q: Just to jump ahead, sort of out of context, I wonder if you could comment on why the Bank has not guaranteed private loans and has floated its own bond issue?

Broches: In the beginning, when we thought of increasing our resources to assist European reconstruction, we felt it would be simpler to borrow than to do a guarantee transaction, especially since our own credit wasn't established at that time. I'm now talking about 1947. Our own credit wasn't established and the only market open to us at the time was the United States market. The United States market isn't particularly fond of guarantees, and at that time it wasn't fond of the European credit either--it was regarded with great suspicion--not in a moral sense but because of the situation. So that to try a guarantee operation at that time would have been just to complicate the picture that was already very complicated. So, we issued our own bonds. We went on with that and we found that was a way that suited us very well.

From time to time suggestions have been made --no formal proposals--to do a guarantee transaction, a direct guarantee, where a country would borrow publicly with our guarantee, and we found that the difficulty was that the investors would rate the paper according to the primary borrower. In other words, they would charge more for a loan by an inexperienced borrower, guaranteed by us, than for a loan, say, by a Western European government, guaranteed by us, which would have been confusing in the opinion of Black and the others who knew the market; they felt it would be confusing to the public if a loan which was fully guaranteed by us would sell at a different yield, depending on who the primary borrower was.

In addition, of course, for any borrower, except with the very best credit, it would have been more expensive to borrow that way. As a result, it was never done.

I'd like to point out some qualifications. In the first place, in

our early days we did sell some parts of loans that we had made with our guarantee, sort of a test. What we sold was mostly short-term paper, and that was maybe also significant. But in one instance, the Belgians in 1949 were looking for money. They had talked to their New York bankers, Morgan Stanley and Smith Barney, and I can't remember exactly how close they were to doing an issue, but in the end what was decided was that we would make a loan--it happened to be a loan for 16 million dollars, which was signed in March of '49--and concurrently with the loan negotiations there were negotiations with these two banking houses, which tried to sell portions of the loan to institutional investors with the Bank's guarantee. And that transaction came about and it was one where we, I think, signed the loan on March 1, 1949 and on March 11, we sold the entire loan to five or six institutional investors savings banks and I believe New York Life was also one of the purchasers. So that comes pretty close to doing a guarantee transaction, although we haven't had cases like that since then.

Q: Would it be correct to infer that had there been more investment bankers, particularly in the American delegation, at Bretton Wood that they would have foreseen that the Bank would have floated its own bond issues in preference to guaranteeing private issues?

Broches: I couldn't really say. I don't remember that in contemporary discussions in magazines, in articles, that this was ever discussed at great length. I just don't know. But it was certainly a typical case of miscalculation of what was going to happen.

Q: Was there any particular discussion at Bretton Woods concerning the reconstruction requirements of Europe?

Broches: No. I think there was at most a tacit assumption that with the Allied armies' aid plus UNRRA, the basic damage would have been repaired and that the assets or the resources, which were available to the Bank, might go some way towards meeting the need. Of course, by 1947 it was quite clear that that was not so, and then you have the Marshall Plan which demonstrated how much was needed to set things right.

There was some discussion, some considerable discussion at Bretton Woods, about the dual purposes of reconstruction and development. There was a split, as you can imagine. The European countries felt that reconstruction should have priority. The underdeveloped countries, led by Latin America and India, felt that development merited special attention. At one time, there was a proposal to split the Bank in two parts, with one half of the resources available for reconstruction and other half for development. There were any numbers of drafts during the conference until we finally came out with the text which says that both purposes will receive equitable consideration, which, in practice, of course has meant that in the early days the main attempt went to the reconstruction side of the Bank and since then we've been concentrating on development.

Q: I wonder if it's pertinent to say something about the anticipated role of the executive directors at Bretton Woods. Was it thought that they'd provide some management themselves?

Broches: I can say quite a few things about the role of the executive directors, but not in the Bank but in the Fund. There was extensive discussion always dealing with the Fund about the role of the executive directors, or rather the type of executive directors we wanted to have. There was a big split. The U.S. delegation had in mind a board such as the fund now has: officials who would be permanently at the seat of the institution and who would be more or less in continuous session. There was another group, led by the British, the Canadians--and the Dutch at that time were also of that opinion--which said, no, what you need at the Fund are people who are in daily touch with the monetary affairs of their countries. And if you have people sitting around a table, it tends to become a gathering of professors rather than of monetary practitioners, and they would tend to lose contact with the communities from which they came. The matter was compromised by a sentence which is now in our charter and which talks of their being at the headquarters in continuous session and that they shall meet as often as is required, which was more or less a compromise between the two positions.

In conjunction with the Bank, nothing was said about the directors. The provisions of the Fund charter were just copied. This battle flared up again in Savanna, when in the by-laws the salary of the executive directors had to be determined. Those who wanted permanent officials were in favor of high salaries, and those on the other side--led in that case by the Canadians--were in favor of low salaries, which would discourage people from coming there. And, of course, the Canadians announced that they would not take any salary, that they would feel free to send a man, say, every quarter, rather

than have their principal director here all the time. And that is the practice, which the Canadians have followed both at the Fund and at the bank. Louis Rasminsky who has been a director most, if not all of the time, comes only on special occasions.

Q: The meetings at Savannah were in March, were they?

Broches: March '46.

Q: And it was not until May of '46 that the Bank found its first president at all. This was, of course, before you came to the Bank. Could you say anything about this period? What sort of things were happening?

Broches: Not much, except that nobody got killed in the rush trying to get the job, and there were various stories in the press about people who had been approached. I can't remember their names now; although I think at the time Lewis Douglas was mentioned as one candidate. There was also a story that Mr. Eugene Meyer was prevailed upon at a luncheon by Mr. Byrnes to take the job more or less with an assurance that it wouldn't take very much of his time. I don't know how authentic this is.

Q: But the executive directors have conducted meetings during this period?

Broches: They conducted meetings. They dealt a little bit with

everything. There were a number of questions of interpretation that had come up. One, I think, was referred to the directors by the U.S. director under instructions from Congress, because, as you know, the Bretton Woods Agreements Act required the U.S. to seek an interpretation of the powers of the Bank to make stabilization loans.

And I would like to recall on that--and I checked that this morning--that the British made a number of attempts at Bretton Woods to have the Bank's charter make explicit the Bank's power to make stabilization loans. The U.S. said that was entirely unacceptable, and as a result we have somewhat vague language. In the meantime--of course, after the agreements were signed, when the opposition against the Fund developed--the U.S. said it would seek clarification of the Bank's provisions to see whether they permitted stabilization loans, and the U.S. Administration was also under instruction to seek amendment of the charter in case the directors decided that the Bank had no power to make stabilization loans. The Bank decided that it had the power.

Then they dealt with such questions as the opening of accounts, arrangements with depositories, administration, calling up the initial subscriptions. There were quite a number of meetings. I wasn't there, of course, during the first four months, but I've had occasion go back over the records. There were quite a lot of things to be done. Of course, there was no thought of starting operations at that time.

Q: What sort of things did Mr. Meyer begin to do when he arrived on the scene? Was there a discussion of lending policy?

Broches: I think one of the first things that Mr. Meyer--there I refer

you again to Mr. Demuth, who was his personal assistant and would know--I think he was concerned with two things. On the loan side I think he was considering what could be done for France. That was the first thing that he started thinking about. And the other thing he did was to take up contacts in New York. He went to New York quite frequently to sound out the financial community.

Q: What particular people in New York would he be likely to see?

Broches: I think mostly his old friends, but I'm not sure. I happen to know that the first Dutch director, Mr. Beyen, reported quite extensively on this early period and about Mr. Meyer's discussions in New York. And if we look at all of his reports and got permission to use them. I think we might find some very interesting contemporary reactions or reports on what Mr. Meyer reported.

Q: Yes. Mr. J.W. Beyen was director in what period?

Broches: He was director from '46 to '52. He is one of the leading directors because of his background. He had been president of the Bank for International Settlements in Basle from '36 to '39. He was a fairly young man. He was one of the leading members of the board.

Q: He is now the Dutch ambassador to France?

Broches: Yes. And, in the meantime, he was Netherlands Foreign Minister. He was very much interested in the Bretton Woods

institutions and while he didn't have much to do, as he always said, I know that during the first period he thought a lot about these problems, and I should hope that there exist somewhere some pretty good contemporary reactions to the period about which everybody now is somewhat vague.

Q: So that in his personal files there is likely to be considerable memoranda on this early period.

Broches: Yes, I would think so.

Q: Now, after you arrived on the scene, in September?

Broches: September 23.

Q: What sort of things were happening at that time?

Broches: Well, we had then received a few applications, or at least approaches. I know that we considered Denmark and Chile. Those are two that I distinctly remember. We used to have working parties, at which more or less the entire staff of the Bank was present, which was very small.

Q: Excuse me, but at these staff meetings did the Executive Director representing the applicant country sometimes join in the discussions?

Broches: No. But we didn't have a loan director at the time. This man

Beyen, whom I've mentioned, was asked to act as loan director for two or three months, so he actually presided at some of these meetings, at which such department heads as we had at the time would attend along with one or two of their staff. Mr. Meyer was not at those meetings, as I recall, not in these larger meetings where we had maybe 15 to 20 people.

Denmark and Chile were projects that were discussed in the fall of 1946. Of course, on the side of the legal department we had a whole list of questions of interpretation or implementation of the charter, mostly having to do, at that time, with payments of subscriptions, which were still in process. And Mr. McLain, and, of course, all of us lawyers tried to look to the time when answers to certain questions would have to be given. We were then engaged in listing the questions. In the next stage we tried to work on the answers. But since we didn't do our first loan operation until May of 1947, we had quite a bit of time; but I must say that we were all terribly busy.

Q: In other words, it's doubtful that the loan could have been made any faster than it was.

Broches: I don't know. If we hadn't had the interruption in management, I think it might have been a bit faster. I think that most of the raw materials for the evaluation had been gathered pretty much by the beginning of the year, but then, of course, Mr. Meyer resigned-- I think on December 18--in a new management didn't come in until March 15. So, we lost three months right there.

Q: Did you know anything about why Mr. Meyer resigned at that juncture?

Broches: No. There is, of course, somewhere a record of his own statement, which if I remember correctly, said that he had carried the Bank through its organization stage and he felt that it was time for somebody else to come in. There was some feeling that he was discouraged. He found it a much more baffling assignment than he had thought. Maybe there was some friction between him and the U.S. director, Emilio G. Collado, who is now the Treasurer and a director of Standard Oil, but who was then very much a State Department man. It may also have been that he felt that while he could lend his name and his efforts to the organizational stage he was now not at an age where he wanted to start operating it.

Q: It then took two and a half months to find a second president. Can you tell anything about this search and what was going on at the Bank at that time?

Broches: Well, of those two and a half months I was in the Bank for the first one and a half months, being away in Europe during February 1947. Immediately after Mr. Meyer's resignation, the then vice president, Mr. Smith, who had been director of the U.S. budget, became acting president. I assume that he had some hopes of becoming president, but he, of course, had had no experience at all in this field and my recollection was that among the directors certainly there was no thought that he should become the president.

Mr. Smith died. I don't know exactly when, but it was during that period.

As you know, under the charter the president is chairman of the executive directors. A question arose who would preside at the meetings of the executive directors, after Mr. Meyer's resignation. The suggestion was made by the U.S. director that he should preside. Mr. McLain, the general counsel, thought that that was unconstitutional under our charter. More importantly, of course, he felt that this would bring the directors too much into management and it would make it impossible for the Bank to operate as a non-political organization. After having argued that on the merits, he also took the position that as a formal matter, as a legal matter, it couldn't be done. He told Mr. Collado that if he wanted to preside over the meetings, he would resign, that is, he, McLain, would resign.

I recall very vividly being called to McLain's room and he said, "Well, you've probably heard. I'm going to resign. I've offered my resignation. Here are some books" (articles of mine that I sent in connection with my application), "I'm just giving things back, and I'm packing up, and this is it."

I know that then David E. Sommers, who had joined the Bank only six weeks before, told McLain that he thought he would resign as well. We talked about it, and I had the same feeling and I said I would resign.

McLain was very emotional. He said no, that was all wrong; he was going, but we had to stay there, we shouldn't leave the ship, and we had to carry on. And then, I believe, over the weekend Collado caved in and McLain was back in his office. So, then we had lost a president

and we had lost a U.S. executive director. Well, he hadn't resigned but the situation was not good. Then, of course, when the new team came in, and it was really a team, with McCloy, Garner and Black, Collado resigned and Black, then as U.S. executive director, assumed office on March 15, 1947.

Q: Have you any idea what the attitude of the United States Government was at this time? Were they aware of the fact that it was necessary to act in such a way that the New York investment bankers would get behind the Bank? Do you think that they were looking for people who had had banking experience?

Broches: Yes. And, of course, the choice of Meyer, although he may have been too old for this particular job, was to look for a man who would be respected in Wall Street. I think they just had difficulty finding anybody, and there must have been a great deal of controversy in the U.S. administration. There, again, I hope that we can find something in the reports of Beyen, who was one of the spokesmen for the directors who went to see--who was it at the time? Snyder, I suppose--Snyder to ask when the nomination for a successor was going to be put forth. As you know, there was an understanding that the U.S. would nominate the Bank president, who would then be selected by the executive directors. The directors were very much concerned because the absence of a management didn't do the Bank any good. All sorts of stories came up and the press tried to magnify the problems that existed. They conjured up--at least I thought it was without justification, so I use that expression--visions of a board dominated by

borrowers who would control the Bank and just take the money out. There were all sorts of rumors flying. It was a very bad situation. And the great merit of Mr. McCloy was that through his personality and his reputation he managed to quiet all this down. The moment he came in people began to take the Bank seriously.

Q: Mr. McCloy, Mr. Garner and Mr. Black all came as part of a team. How did they divide up their responsibilities?

Broches: Yes. Well, I understand--but this is all hearsay--that Mr. McCloy, when he was approached, made it quite clear--probably after having taken advice--to the U.S. administration that he wanted to run the Bank, if he took the job, without interference from the executive directors. I think that what he had in mind was the position of a president and chairman of the board in an American corporation. And I understand that he also made it clear to the U.S. administration that that included--this wish not to be interfered with--freedom from interference by the American director, and that he wanted to at least approve, if not propose, the American director.

Now, I must say that during this process Mr. McCloy was quoted as speaking in a somewhat uncomplimentary fashion about the directors. I don't know whether he really did but I remember returning from Europe on the 28th of February 1947 and reading the London Financial Times, where an announcement was that McCloy had accepted the job and in which he was quoted as having referred to the directors as "a bunch of chatterboxes."

This leads to another anecdote. When I came back here my Dutch

friend, Mr. Beyen, asked me whether I had seen that. I said yes. He said, well, our Belgian colleague--who has now left--Mr. Basyn--he was a very soft-spoken gentleman--had come to him and said, "You know, this is very unfair. Nobody can say that I'm a chatterbox." In fact, he never spoke.

But there was a lot of bad feeling generated, and, as I recall, there was definitely not a happy atmosphere when McCloy took over, something of an occupying army coming in. McCloy came in knowing that he would have a very difficult time, so he was very reserved. Gradually, of course, people got to know each other and relationships improved. But in the beginning, of course, he and Garner came in as people who were going to salvage this institution, which, I suppose, from the directors' point of view was not such a pleasant thing to happen, if the directors had the feeling that it wasn't their fault that the institution was in need of being salvaged in the first place. So, the first few months were not very happy.

I think Mr. Black, although he was U.S. executive director, was not expected so much to represent the United States on the board, although that was his official function, as to advise and help and assist in establishing a market for the Bank's bonds, in which field of course he is a past master, and he was even then.

The three of them, without distinction, whether it was management or board, went all over the country trying to familiarize people with the Bank and trying to make it look respectable. And from the very fact that we did an enormously successful issue on July 15, 1947, which was only four months after they came in, you can see that enormous amount of work was done, in which, I'm sure, nobody paid any attention

to the fact that the one was president and the other was a member of the board representing one of the member countries. I think all three of them worked on this job, with Mr. Garner assuming the function of a general manager.

Q: So, he was more responsible for dealing directly with the staff, I would take it.

Broches: That's right.

Q: We'll come back to development of loan policy under Mr. McCloy's regime but I wonder if you could say just a few words about Mr. McCloy's resignation. When did this take place?

Broches: His resignation was effective July 1, 1949. It was announced quite a bit earlier, - sometime in May, I think. So, he accepted the position of High Commissioner of Germany about two years after he came to the Bank. He was put under some considerable pressure. I happened to be at dinner at his house while Bedell Smith phoned and apparently went to work on him, except that I didn't have the faintest idea at the time what it was he couldn't say yes to quite yet. Then I heard from McLain that this was going on and McLain hoped very much that McCloy wouldn't go. But, as I told you, when McCloy went McLain went too. As I say, I think it was out of personal loyalty to McCloy and a feeling that McCloy could well use his services as a general adviser. McCloy leaned very heavily on McLain; they had a very good relationship.

If you want another sidelight on McLain, his protective attitude--

I think this is typical of some of the Wall Street lawyers--at one time at an annual meeting in London the Poles had indicated to us that they might make an attack on the Bank--I've forgotten what the point was-- and the management had held a strategy meeting and it was decided that McCloy would not be provoked into answering it. Well, a meeting took place, and the Pole made a statement--McCloy was at the table; McLain was sitting in back and I was sitting next to him--and McCloy was provoked and did get into a discussion and answered, whereupon McLain poked me in the ribs and said, "That boy is certainly a great help to me." A typical lawyer's attitude; he had to take care of everybody.

Q: Did McCloy's resignation indicate in any way that he was dissatisfied with the way the Bank was going?

Broches: I don't think so. I think McCloy, who has always been tremendously interested in Germany and very hopeful about Germany, was just seduced by the challenge of that job. Some people have felt that he shouldn't have taken that decision; others think that he was right. I don't think there was anything negative as far as the Bank was concerned. I think this was just a challenge that looked very, very attractive to him.

In the Bank he had given evidence of being very much interested in the German question. He had considered making a loan to a Ruhr authority--this was long before Germany became a member. I think it's just that this was very glamorous to him and he took it.

Q: Are there any contrasts or similarities that should be mentioned

between the McCloy and Black periods, or was it pretty much one continuous--

Broches: Oh, no, I wouldn't say so. No, I think there is a difference. There may not have been a sudden break, but the personalities are so utterly different. I think McCloy was a statesman who became a banker--I don't think he even became quite that because he wasn't there long enough; he may have later when he went to Chase--and Black was a banker who became a statesman. So they came to the job in an entirely different way. Then, of course, Black's personal attitude made for much easier relationships with the board and the borrowers. He's a more outgoing person, or at least he strikes people as such, than McCloy. Then, in part, it may be a natural development that after the first half year with Meyer and then the two and a quarter years of the McCloy administration we had finally done enough spade work to be ready to develop and start doing business, which was in about 1950. The year after Black came and we were in full swing.

Q: Mr. Black's personal relationships with the Board have always been very good.

Broches: They've been excellent, excellent. Of course, he had been their colleague for a while, and even though little was known about Mr. Black beyond his capabilities in the strictly financial field, the board was quite happy when he was selected, or nominated by the U.S. to be president. You see, there was another succession problem when Mr. McCloy left.

Q: But that was resolved rather quickly, wasn't it?

Broches: Yes, that was resolved quickly. At that time the board did take a position because there was again the question of the vice president, Mr. Garner, and the board at that time did, as I am informed, tell the U.S. that they did not think he should be nominated; they wanted somebody else. Then the U.S. came forward with Mr. Black. I don't think any other names were mentioned.

Q: Were there any important legal interpretations required during Mr. McCloy's regime that we should put on the record, or that we will perhaps discuss somewhere else in connection with lending policies?

Broches: No, the interpretations that we had at the time--the two most important ones were one dealing with the obligations of members to make good on the guarantee embodied in the 80 percent unpaid portion of the Bank's capital, and the other one dealt with the maintenance of value of currency. So that was a question of loan policy, but the first one came up as one of the issues that had to be resolved before we put out our first bond issue.

This issue was going to be offered in the American market. The American investors, if they were going to buy the issue at all, would buy it relying on the U.S. guarantee, the U.S. indirect guarantee through the U.S. obligation to make payments to the Bank on account of the 80 percent unpaid portion. In that connection a number of questions were raised by the bankers; they wanted to be sure that the U.S. couldn't get out of its obligation. For instance, one question

that was asked was, well, if the Bank needs money in order to pay off these bonds and makes a call on its members--and these calls have to be proportioned--and a number of members don't pay, does that afford an excuse to the U.S. not to pay? Then, even if it doesn't, if the U.S. has paid and more money is needed, can another call be made on the U.S., if the U.S. should be the only country that hasn't defaulted? Of course, all these questions were answered the right way. The answer wasn't really in doubt. But it was felt desirable that authoritative answers to these questions would be on record to assure investors. That was an interpretation, I think, in May of 1947.

Q: It was pretty clear at that time, I take it, that the guarantee of the U.S. was the guarantee, which made it possible to sell the bonds.

Broches: There was no doubt at all. As a matter of fact, at that time we were advised by bankers in New York to insert a clause in our bonds agreeing never to borrow more than an amount corresponding to the U.S. unpaid part of the 80 percent portion of the capital. It was something that was considered but that we fortunately turned down.

The other interpretation, which was either at the end of the McCloy or at the beginning of the Black regime, was really an important and interesting question of loan policy. Under the articles the paid-in capital, to the extent that it's paid in local currency, the so-called 18 percent, is guaranteed against devaluation in terms of gold by a provision of the Articles which requires each member concerned to maintain the value, to maintain the value of currency derived from its 18 percent and held by the Bank. Well, then the question came up: what

happens if the money has been loaned? While it's out on loan it depreciates and when it comes back it's worth less. Is then the member, whose currency was loaned, required to make good the loss? The Articles are not very clear about this. This was a problem that was recognized very early and we worked on it for about a year and a half. Finally we answered the question in the affirmative.

But you've got two perfectly good arguments. The one is that the member agrees to make available a certain quantity in terms of purchasing power in his own currency, and that like any other creditor who has loaned his own currency, if his own currency devalues, then he gets back less in the end. That was one sound argument. Looking at the members of the Bank as creditors, looking upon them as entities, which advanced money, loaned money through the Bank as a channel.

The other argument was that the borrowers had received a certain value and why should they have a windfall? Why shouldn't they be required to pay back to the Bank the same in purchasing power, at least as that can be measured in terms of par values, as they received.

Legally, that second point of view is somewhat more easily reconcilable with the Articles than the first, although the Articles don't exclude the other. But the practical objections to putting the exchange burden on the borrower were very great because our loanable resources consist in part of 18 percent funds and in the other part, a larger part, of borrowed funds. Now, when we borrow funds, we don't take an exchange risk. If we borrow Swiss francs, we repay Swiss francs. If we borrow dollars, we repay dollars. They are not gold dollars; they're paper dollars and paper Swiss francs. So, there's no need to protect against any risk because there isn't any risk. On the

other hand, the 18 percent, our capital is stated in gold, and if you want to protect the value of the capital, you would have to put a gold clause or possibly a dollar clause in your loan agreements. But whether or not you would have such a clause would depend on the source of funds. You can easily see that everybody would want to have funds that don't require protection rather than the other funds where a gold clause or a dollar clause would have to be put in.

So that unless we interpreted the Articles to mean that the members were required to maintain the value of their currency even while out on loan, we would have had great difficulties in operation. So, the problem was submitted on exactly that basis, saying that legally you could go either one way or the other but in the interest of the operations of the Bank as a whole, the thing to do was to interpret the Articles so as to impose on members the obligations to make good any devaluation loss, which was accepted.

But while the thing was still in doubt, we had to do something because we had started making loans in 1947. Then we put in a dollar clause saying, in effect, that if any currency other than dollars was loaned to a borrower, then he would pay back the same dollar equivalent in that currency as he had borrowed. So that temporarily our loan agreements carried a dollar clause. Then, when the interpretation was adopted, that provision became inoperative.

That's more easily told than done. I mean, all this took a great deal of time, as you can understand.

Q: This particular interpretation would have been about what time?

Broches: I think it was 1950.

Q: I'd like to begin talking about the Bank's lending policies per se, but before I do I wonder if there are any other last things that we should mention in connection with this early period.

Broches: No, I can't think of anything.

Q: Well, we're getting close to the end of the tape, and I wonder if it wouldn't be wise instead of talking about the French loan, which may occupy quite a bit of time, if you could talk a little bit about the Polish and Czech loan applications.

Broches: I have no good recollection about the Czech loan application. The only thing that I found out when I asked around was that there was a letter--I saw the acknowledgement by Mr. Meyer--for a loan of \$350 million dollars with the statement, "The Ambassador will be happy to give you some further information, if you want it." I assume that since nothing came of that loan and nothing came of the Polish loan that those files must be in the penthouse or in another warehouse. They don't seem to be available in our archives here, but of course, they are available somewhere in the Bank.

The Czech loan didn't go very far. The Polish loan did. After the second annual meeting of the Bank in London in '47, Mr. McCloy went to Poland, and the thought was then, as I recall it, that the loan would be for the rehabilitation of the coal mines. And this was believed to be a good project and one that would pay out because Europe

was short of coal and Poland, through its coal exports, would get the foreign exchange to service the loan. Of course, this loan never came to fruition, and that led to the first instance where the question of politically motivated decisions came up, because when Poland did not join the Marshall group and it looked as if it wouldn't trade with the West, that was one of the reasons--not the only stated reason--for saying that we didn't think we could make the loan.

Q: In other words, the very fact that they wouldn't be trading coal with the West made the loan look much less good.

Broches: That's right. And, of course, McCloy was asked: Why was this? Because the U.S. government doesn't want to make the loan to Poland? Is this a political decision?

There is a statement, which must be in the files somewhere--I think it was a press release--in which McCloy said substantially this, that political factors have to be taken into account and political events may influence economics. And to that extend politics had a lot to do with the decision not to move forward with the loan. That was not to say that it was politically motivated. I'm nearly sure that's a press release that ought to be in our files.

Q: Were you aware of any discussions about this that went on between the management of the Bank and the United States Government, for example?

Broches: Oh, there was of course constant discussion about a lot of

things and this must have figured quite prominently in it.

Q: Was this one of the things that caused the Polish delegation at the London meeting to make the violent statement that you referred to earlier?

Broches: No, I forget what that was. It was after the meeting that Mr. McCloy went to Poland. I can't recall what the occasion. It was after the discussions started in earnest, and I can't recall exactly when the Paris group was formed, the European counterpart of the Marshall Plan.

Q: I think it was in early '49.

Broches: No, early '48, I believe.

It looked for a while as if Poland would participate, but then, of course, they decided they couldn't or weren't permitted to.

And the Czech loan ran into difficulties around '49, when Czechoslovakia was taken over by the Communists, and there you have the same problem of orientation of trade. I'm much less clear--I think that thing had been dragging on possibly for other reasons. A lot of serious work was being done on it when the thing suddenly died.

Of course, you know the Poles withdrew in March 1950.

Q: The Czechs never completed their gold payment, their two percent payment.

Broches: No. The war devastated countries had five years to pay the last one-half percent of their two-percent gold payment, and Czechoslovakia, after the five years had expired, said they couldn't pay or they wouldn't pay because the U.S. was illegally withholding certain gold or other assets from them. And we said that was too bad and they should complain to the U.S., but that we had no connection with that and there was no reason not to pay us. If they wanted to put it on the basis of impossibility, if they were willing to come forward with, well, a balance sheet, as it were, and say we can't pay, that would be one thing. But if they placed it on the basis that certain of their assets were being illegally withheld, that was an argument that we couldn't accept. It was quite possible that assets were being illegally withheld from them, and they should do something about it, and take redress from the governments that they thought were illegally withholding their assets, but they shouldn't take it out on us.

Q: Were they the only members who said they were unable to pay the two percent?

Broches: No, the Chinese as well. And, of course, the Chinese didn't ever pay the full amount until through a reduction of their capital their default was cured, in a sense. That happened only last year or a year and a half ago. The Chinese never denied their obligation to pay; they said they were unable to pay.

Q: I take it they satisfied the Bank that in some way this was in fact the case.

Broches: Yes.

Q: Well, I think now is perhaps a good time to stop this particular tape, or else we'll get into another subject which may take us beyond the tape we have available.

Interview No. 2

July 24. 1961

Q: Now, Mr. Broches, we finished our first session with a discussion of the Czech application and something about the Polish application, and I wonder if you wouldn't like to just tell us, in general, about some of the early loans and early policy discussions that went along with them.

Broches: Well, one of the problems that we ran into after we got through with the first batch of reconstruction loans, that is, the loans to France, Holland, Luxemburg, Denmark, was presented in a loan request by Belgium. Belgium was, at that time, and this was 1949, well provided with dollars, but in its own reconstruction program it was short of capital and came to the Bank with suggestions that the Bank should lend for local expenditures--that the Bank should make available foreign exchange for local expenditures. In the event that particular loan never materialized, but in the process of thinking about the loan application or the suggestion for a loan, the question was discussed in the staff and also in the Board of where the Bank stood on this problem of financing local expenditures, a subject which the Articles seemed to have a bias against.

As I say, the matter was discussed with the staff and later with the Board, and where we came out was that, while one had to exercise great caution in financing local expenditures with foreign exchange, and while countries should be wary of trying to follow that course of financing unless it was the right thing - on the other hand if a good case were presented -, then there was no reason why the Bank couldn't

finance local expenditures. And a good case would be presented if a country had enough credit worthiness and if the particular needs that were priority needs happened to be ones that did not require the immediate expenditure of foreign exchange.

So, that actually, you could say that at that time the Bank decided that in any appropriate case local expenditures could be financed.

The first case, in which it really happened, to my recollection, was a year later, 1950, in Italy. Italy had then recently embarked on the development program for the South. The actual goods and services required for the projects to be carried out there could be provided by the North, by the industrial north. On the other hand, the program itself and the payments of wages to a population that before then had been at the very bottom of the money economy, would lead, so it was argued by the economists or reasoned by the economists, to increased imports of cotton and of food grains. And that led to the theory of the indirect foreign exchange impact and that what we were financing there was the impact.

Our loans for that plan were calculated on the basis of a certain percentage of total expenditures on the plan by Italy and were calculated to furnish Italy with the amount of foreign exchange more or less equivalent to the additional foreign exchange expenditure resulting from the carrying out of the plan.

Later, since that time, as you've known, we've made many local expenditure loans. We've not tried to quantify in that manner and have simply said that where a country is short of capital but not short of capital goods which have to be imported, and where a country has ample

credit worthiness, that we would make loans for financing local expenditures.

Japan has been an example in more recent times.

On the other hand, there have been no instances where we've done this directly in the case of the very underdeveloped countries.

Q: I just want to make clear what is meant by local currency loans. The currency actually loaned by the Bank was not local currency, was it?

Broches: No. I used the expression "local expenditures." What we were financing were local expenditures with a foreign-exchange loan.

Q: So, in the case of the Italian loan, for example, the Central Bank of Italy wound up with dollars of whatever the foreign exchange was and the Bank made no effort to supervise the use of those particular dollars.

Broches: No. On the other hand, maybe not in the first loan but in a later loan, we did tie the use of the local currency to particular project. So instead of supervising the money we disbursed, we supervised the counterpart.

Q: Yes, exactly.

I'm curious as to the origin of the word "impact loan." To me, impact implies that you're taking account of sort of the income multiplier effects of a given loan, which is a little bit different

thing; it seems to me, from actually making available local currency for purchases within the country as a consequence of the foreign exchange.

Broches: Well, I think that Professor P. N. Rosenstein-Rodan, who worked on that loan and who developed this theory, which, as I said, was later abandoned or at least simplified, what he took as the basis was the impact on the balance of payments of the carrying out of the Italian development program. He thought you could, in a fairly simple economy like the Italian South, where many people were, say, at the lower limit or below the lower limit of a reasonable standard of living, that you could predict there what would happen with the additional money incomes--that none of it would be saved and that x-percentage would be spent on clothing, y-percentage on food, and that you could then go and calculate how much of those expenditures would be in foreign exchange.

Q: Well, that's what I would have thought was meant by impact loans, but it sounds like it turned out a little differently from that.

Broches: Well, that was the way the first loans to Italy were calculated.

Q: I see. So that the Bank did not lend a foreign exchange equivalent of the total local currency expenditures.

Broches: Oh, certainly not. I forget what the percentage was but it

was very small.

Q: You were at Bretton Woods. I wonder if you remember from your experience at that conference any discussion about this issue.

Broches: There were a number of people in Bretton Woods under the impact--to use the word in another sense--of the happenings of the '20s and '30s. There was a lot of talk about the unsoundness of borrowing for local expenditures, of borrowing abroad to finance local expenditures. And the examples were generally the borrowing by Germany in the '20s for such public amenities and facilities as swimming pools and sports parks, borrowings by municipalities, and so forth. Even then, I think, some of the more discriminating people said that the bad thing was not necessarily that it was to finance local expenditures but that it was to finance unproductive local expenditures.

But there was a general wave of revulsion against that sort of thing which, we think, is reflected in the charter. Now, the charter does provide that in exceptional circumstances, when a project gives rise indirectly to an increased foreign exchange need; the Bank can in such a case provide the borrower with foreign exchange not to exceed the local expenditures. And, as I say, in the case of Italy the foreign exchange, which we provided, was a small fraction of the local expenditures.

And the two examples that were given at the Bretton Woods conference were those of a country, which diverts industrial capacity to reconstruction, thereby lessening its export package, reducing its exports, which, of course, was the Belgium argument after the war.

They had a steel industry but instead of exporting steel, as they had been doing traditionally, they had to use a much greater proportion at home.

The other example that was given at Bretton Woods was that of an agricultural economy, and presumably one with fairly full employment, where people would be diverted to industry and, as a result, the country would become a food importer or a smaller food exporter.

That is about as far as people went at Bretton Woods.

Q: My reading of the minutes of the Bretton Woods meetings, insofar as they're available in the two volumes, a Department of State publication, suggests that the New Zealand delegation brought up the balance of payments impact argument at that time, in much the same way I now understand Dr. Rosenstein-Rodan brought it up at the Bank. Do you recall?

Broches: No, I don't.

Q: Indeed I've heard that the New Zealanders refrained from joining the Bank, initially at least, because they still had reservations as to whether the Bank was prepared to give this type of impact loan.

Broches: I'm not aware of that. I am aware of the fact that New Zealand, along with Australia, had great doubts about the wisdom of joining the Fund because of the stress on exchange stability. Of course, Australia joined not immediately but very shortly after the institutions came into being, and New Zealand is now just about to join

after much soul-searching; they've now decided to put it at least to their legislature.

Q: Well, could you say anything about the people involved in the discussions in the Bank on this particular issue?

Broches: No, this was not really an issue on which there was much controversy. It was regarded as a new departure, as indeed was another loan, which we made in 1950, a loan to Australia, in August 1950. This was a loan not for a specific project but for a program of imports of capital goods by private importers. What we financed there was the foreign exchange requirements, and particularly the U.S. and Canadian dollar exchange of Australia in particular sectors. But the importers were in most cases private individuals, so that you couldn't talk of a project in the sense in which project was, at that time, understood by the Bank. That was a departure. That was in 1950. And, of course, the loan has often been held up to us by other countries that said it's so hard to find projects or to develop projects and get them in shape. Why don't you give us money for a general import program? It's something that we have resisted.

Let me say, since you said that you wouldn't be adverse to having some examples by way of anecdotes, that Mr. Crena de Iongh, whom you are going to see--you might remind him of this and check whether it isn't true--came back from one of his trips to Europe in probably '48 or '49, when the Bank had regained the respect of the financial community. On his way back to Washington he had lunch with a New York banker, whom he might be able to identify. This banker said to him,

"Crena, you fellows now have a reputation for being very sound. When are you going to do something that will shock us? You now have the reputation to go ahead and do something new."

I think that around that time we began to do some new things.

Q: I've heard that there was some controversy in the Bank in these early days, particularly between the loan department and the economics department, or the research department as I guess it was called in the beginnings, on some of these issues.

Broches: Well, there was quite a bit of interchange of personnel, as I recall, and I'm not sure I would know how the lines were drawn, because you know that until '52 we had a loan department--one loan department--and a research department and that in the reorganization of '52 the area departments were set up which combined so-called operations officers and the economists. And then the economics staff, as a more either consultative or ivory tower, less involved group.

Q: Can you tell anything about the background of this particular reorganization?

Broches: Nothing that you couldn't guess from other reorganizations. It was felt that the situation up to that time wasn't very good and--I think it was right--that for operational purpose there should be a unified direction of the economists and the operations officers. Of course, the distinction between an economists and an operations officer is an artificial one; I think it's one of emphasis. And that is best

proved if you would go through our personnel statistics; you will see how people have moved from one position to the other.

Then the Bank created the economics staff, which was not immediately involved in operations, and could be a sort of watchdog in seeing how the economics of the Bank were developing, which they're doing in consultation with the economic advisers of the various area departments through the staff economic committee, which has the confusing name of SEC. And then they occupy themselves with general economic problems, commodity studies, foreign investment, and a number of those problems, which don't fall into any particular area. I think it has worked well.

Q: It would be appropriate, I suppose, for me to ask you about various important legal decisions which had been made, but I understand that you have already done a paper on this subject. I wonder if you could just cite it for the tape.

Broches: Well, the paper I am referring to deals with the legal character of our agreements which is a matter of considerable importance and on which we did a lot of thinking and finally came out with a particular legal solution, namely, that of regarding these agreements as international agreements. I lectured on that subject in somewhat wider context in 1959 at the Academy of International Law in The Hague. And my paper is published in the Proceedings, Vol. 3, of the year 1959, of the Academy for International Law.

Q: Since we don't need to cover that subject, perhaps we could talk a

bit about the development of the market for the Bank's bonds, both in the United States and abroad. Could you tell about some of your experiences in connection with some of the earlier bond issues?

Broches: Yes. Our first two bond issues were made in the United States in 1947, and they crowned a three-months' sustained effort by Messrs. McCloy and Black and Garner trying to familiarize the investors and to convince them that this was a good investment.

I must ask you one question. Didn't I refer to interpretations of the articles in that connection?

Q. I think you did.

Broches: Yes I think I did.

Another element in connection with our marketing in the United States was to search for an appropriate method. I don't know how much material you have on that.

Q. Very little. I wonder if before you talk about the method though, you will perhaps say a little about the attitude of the bond market toward the Bank at the time Mr. McCloy became president. There had been much exploratory work done?

Broches: I can't say. I believe that before that time there had been a number of talks with the New York market, but how conclusive they had been, I don't know. In another way, quite a lot of preparatory work had been done, and that was in the legislative field, because in this

country most of the institutional investors are limited in the choice of their investments either by federal or by state law, or the laws of the District of Columbia. And at a very early time--I'm not so sure that it didn't start before the Bank started operations--the U.S. Treasury and later the Bank's own staff tried to get legislation approved in important states which would permit institutional investors, such as savings banks and insurance companies, to invest in the Bank's bonds, because with the legal structure as it was, in the absence of such legislation, we couldn't have really started out selling bonds. The Bank was an institution, which was not foreseen in the legislation in force; it didn't seem to fit the usual categories, so that even in states or jurisdictions where the legislation was liberal, the description of the Bank frequently just didn't fit any category of issues that were named in those statutes. So that New York, Massachusetts, New Jersey, I think Connecticut, and Pennsylvania were the first round of states that were attacked to see whether we couldn't get legislation to at least permit some important groups of institutional investors to buy our bonds.

Q: And this was done even before Mr. McCloy became president.

Broches: Oh, certainly. I think it was done before Mr. Meyer was president. I think it was either the U.S. Treasury or the State Department--more likely the Treasury--that started doing this work of preparation, after the Articles of Agreement became effective which was the end of '45. We didn't get organized as an operating unit until the middle of '46. I think some of the work was done even before the

middle of '46.

Q: You don't happen to know the names of any people in the Treasury Department at the time, who would have been working on this question, do you?

Broches: No. I know that Luxford, Ansel Luxford, whom you have talked to, must have been involved in this; he was the moving force on the legal side in the Treasury. It seems to me that Jack Corbett--but he was in the State Department--went out on speaking tours and talks with state regulatory agencies to investigate the problems.

Q: I remember one incident in this early period that was reported in the press, an occasion when Mr. Beyen, the Dutch executive director, gave a speech about what the Bank was doing in preparing the way for the bond market. And he had no sooner given his speech than the management of the Bank issued a statement that things were not progressing in quite the way that had been said. Do you recall this particular incident?

Broches: No.

Q: Well, at any rate, after Mr. McCloy became president he and Mr. Garner and Mr. Black, I take it, were involved in trying to clear the road . . .

Broches: Yes, all three of them. And then when they had the feeling that things were ready, then the question arose--or it had arisen

before--how do you market these bonds? In this country there is a variety of ways in which you can do it. You can have ordinary underwriting, the classical form of underwriting, or you can have an agency deal in which the people to whom you sell, are really not buying for their own account but as agents, and there's competitive bidding, and there are combinations. The big question was which method to select. The method of underwriting involved, of course, a choice, a selection of bankers, which was something that the Bank was not prepared to do at that time. You would have an enormous fight on your hands.

One other method that might have been available was competitive bidding, but we chose a third method, and that was an agency deal. Of course, even in an agency transaction you have to decide who will be your agents. There, again, in order to avoid criticism, we invited all members of the NASD--National Association of Security Dealers--to be agents, and I believe we ended up with 1600 of them, which didn't make for a very well organized issue, as you can see. And the allotment problem was something awful.

First, the issue seemed to be sticky but then a short time before it came out it was considered a success. That meant that everybody subscribed to more than he wanted to get in order to get what he expected to get, and there was free riding and a very disorderly market for a while. So that this method was abandoned.

Q: Before you talk about other methods, could you say a little bit more about that first bond issue. Didn't the bonds all get sold, in effect, in a couple of minutes after the stroke of 12 when they were

supposed to go on sale?

Broches: Well, they were sold. They were heavily over-subscribed. I forget what the factor of over-subscription was. And that gave the terrible problem of allotment, because you had to try and determine which subscriptions had been serious and which subscriptions really came from speculators. And it isn't very easy when subscriptions come in through 1600 firms. There was quite an organization set up in the Fed in New York--that's just the locale of the organization--and a number of houses--Morgan, Stanley and I think there were also others; I know there were others--had made available some of their partners or officers to help in running the books and organizing it. I know that Mr. Francis T. Ward, who is now semi-retired, a partner of Morgan, Stanley, and Dudley Schoales, a partner of Morgan, Stanley, who was then not yet a partner, they were very active in it. There was a big volunteer organization to run this transaction in New York.

The bonds did go to a premium, and then later they dropped below par, and at that time the insurance companies, which I believe had at first been somewhat disgusted since they couldn't get what they wanted with this enormous number of participants, then started to buy quietly and acquired their holdings at a decent price. And after that the market has been very stable.

Q: They went down as far as 95 at one point, didn't they?

Broches: I thought it was 96, but it was thereabouts. Certainly it was much too far down and they had gone up to between 103 and 104,

which was too far up. There was altogether too much fluctuation, which was ascribed to the poor distribution.

Q: So, you decided to abandon the agency approach.

Broches: That was abandoned, and then we went to, in 1950, when we refunded one of the two issues that we had done in 1947--we refunded the 10-year, two-and-a-quarters, and we replaced those by serial bonds of 1950 due '53 to '62. And then we did that on the basis of competitive bidding, and three or four groups were formed, one of them under the leadership of Halsey Stuart, who were the great propagandists for competitive bidding.

Well, the bids came in and they had to be filed in New York at the Fed, and I believe it was half an hour before the bids would be opened when Halsey Stuart came in and wanted its envelope back and substituted another one. When the bids were opened it turned out that Halsey Stuart was the low bidder, or high bidder from our point of view, and had been all along and that they needn't have improved their bid. They were way below, or above, the three other groups, which didn't make a very good impression. The other three had been fairly close, and this one was very out of line. We borrowed at a very low cost, I think it was 1.92 and the other bids were over 2 percent. The feeling of many people was that Halsey Stuart wanted to prove to us that this was the way to do it, and they wanted to be sure to get the bid. But they couldn't sell the bonds, and for years they held on to the bonds; they were unwilling to sell them at a loss and they were able to hold on to them. But for many years our prospectuses had a statement that some of

the underwriters of the issue to which the prospectus related had been in an earlier issue and might still be holding some of the bonds. So that wasn't considered a success.

We then went to a third method in 1951.

Q: Was there any other explanation as to why Halsey Stuart had made what turned out to be an error?

Broches: As I recall, the market also had changed in an unfavorable sense shortly after the offering.

Q: You mean, interest rates in general went up.

Broches: Went up. But certainly as compared to the other three groups they showed that they had an entirely different judgment of the market.

Q: It was purely clearly a case that they had just misinterpreted the market at that time.

Broches: Well, it was certainly a case of their wanting to make sure that they got this issue, and they were eager to prove to us that this was an inexpensive way of financing. And their desire to prove that may have influenced their judgment. I think that's the best way of putting it.

Q: From the Bank's point of view, though, it is not clear to me why this was thought to be an undesirable situation.

Broches: Well, it isn't very good when the person to whom you've sold bonds is stuck with them, and a block of bonds is overhanging the market. I think it was over 20 million dollars out of a 100-million-dollar issue. It may have been even more than that.

Q: Did you feel that if you had tried another time with competitive bids that you would have had very poor bids from the Bank's standpoint because of this experience?

Broches: Frankly, I don't know what made Mr. Black decide--in the meantime, Mr. Black had become president --in any event, Mr. Black's judgment was relied on to a great extent in all these marketing matters even before he was president--to go on the third method, which was a very strange one. I mean, strange in merely a technical sense. We called that, I think, a sponsorship transaction, in which a number of the old bidding groups of the competitive bidding of 1950 took turns, or were supposed to take turns, in heading a syndicate for the Bank's bonds. And we sold the bonds to them outright, but they placed them before we sold them to them. So that, legally, as I recall--I really should have checked this--this was a sale, not a commission transaction. They first got subscriptions and then bought from us, so that economically they were agents rather than principals, although legally they were principals.

Q: Was the commission, in effect, agreed upon in advance?

Broches: Oh, yes, that was agreed upon in advance. And the cost, as

far as that was concerned, was exactly the same. We did that a couple of times and that was not considered very satisfactory, and the reason why it wasn't satisfactory is because there was not one single group that was both expert in this particular field of selling Bank bonds, which had two features, which I'll mention in a second, and that had a sense of continuity and considered this as its baby, as its responsibility, in which they would have a continuing interest even though there were no issue at a particular time. There was no one group, before we went to the present system, that would try and follow the market and make a market in the Bank's bonds, and try to interest investors in buying these bonds also in between issues.

And the two features of the Bank's bonds that I referred to are, in the first place, that they are like government paper in one sense, and secondly, that they're international. And those two features seemed to make--no let me take that back.

In 1952 we decided that there was one group that seemed especially capable of making the best of those features, of best handling an issue which had those features, and that was the group consisting of Morgan, Stanley and The First Boston Corporation. In '52 the decision to pick up two houses to head the syndicate was not as hard as it would have been in 1946 because we had had experience. I don't think that Mr. Black felt that this was a difficult decision to make. He was, as I recall, convinced that this was the combination that was best for us, that it was best to go back to traditional underwriting and to have a syndicate headed by two firms that were capable of doing this work and with going on with the same syndicate and the same managers as long as thing went satisfactorily. So that from '52 on, for our issues in the

United States, we have been on a straight underwriting basis. And these two firms have always headed the syndicates, with the only variation being that at one time Morgan, Stanley heads the syndicate jointly with First Boston, and the next time First Boston heads the syndicate jointly with Morgan, Stanley. That only involves the listing of the names on the prospectus and the people with whom we have our negotiations.

Q: Have any of the other underwriters, such as Halsey Stuart, ever objected to this, felt they were squeezed out of the market, so to speak?

Broches: I can't say for sure, but somebody must have complained. People always complain. In the securities business in every country in the world that I have seen the securities business in, there are always jealousies and the question of how high you are on the list and whose name is printed on the left side of the prospectus. There's no doubt about it that there must be people who feel that they are more important than they are regarded by others. No doubt about that.

Q: Is there any story that needs to be told about the decision as to the interest rate the Bank would offer on the bonds in the United States?

Broches: No, that was in each case decided in consultation with bankers when we--in underwriting it's negotiated with the underwriters. In the sponsoring group arrangements, which chronologically were just

before the underwriting, it was done with the sponsoring group. In competitive bidding, of course, it was decided by the bids. And in the very first offering it was done by taking a sounding of opinion, market opinion.

Q: Has the bank rate been related in some consistent manner to the rate paid by the United States Government on its bonds?

Broches: It has always been higher, of course, than the United States Government's rate. The premium over the U.S. rate has not, I believe, always been the same; that has depended in part on the technical market for the Bank's bonds. But our first borrowing, long-term bonds, was at 3 percent in 1947.

Q: At what point was it decided to add the special features such as the feature that the Bank would not call in for redemption the bonds before a certain period of time?

Broches: That must have been in '56 or '57, when the market was not very good, and when that feature and the feature of the purchase fund were regarded as additional attractions for institutional investors. The question of so-called delayed delivery sales also came up because there were a good many institutional investors who were loaned up, who had put out a lot of mortgages or in other ways. On the other hand, they knew that they had money coming in, premiums or savings or whatever it was, and found the bonds attractive and were willing to make a commitment to buy them at a later time.

We were very liquid, so that this suited us too. We thought that the rate was all right for us. We didn't need the money immediately, and this actually saved us some money, because instead of paying interest over the whole period for the entire amount, we only paid a commitment charge to those people who called for later delivery. It was always clear that orders for delayed delivery would only be taken from institutional investors because, obviously, it involves a question of credit and responsibility, if you have a commitment which may run as much as three years.

Q: There is some maximum time they can delay their purchase, I take it.

Broches: Yes, and I think it has varied from issue to issue.

Now, in some issues we had another feature. Fortunately, it was only in two, I believe. That's the so-called purchase fund. In those issues the Bank undertook an obligation during a certain number of years to spend up to a certain amount per year to buy bonds up to par, so that if the bonds went below par--it may have been up to and including par--that then the Bank would spend over a year a specified amount to buy in bonds and cancel them. That was intended as a price support, but we've never regarded it as a very happy feature. We've had it in two issues.

Q: I wonder if there's a story to be told in the case of the federal legislation that was necessary to make the Bank's bonds acceptable to federal corporations.

Borches: No, there isn't much of a story on that. I don't think there was any difficulty on the federal side. We've had considerable difficulty in some states, in some isolated cases, where legislators after having heard some of our American staff or top officers speak complimented them on their patriotism, on their soundness, and said you're fine people, very fine Americans, but we don't think we'll do anything; we just don't like foreigners. I think Sommers can tell you some stories about that.

There is a story, which may or may not be true, of our savings banks legislation in Massachusetts, where we were in trouble and then sought the support of Representative McCormack, and he said he would help. He sent a message to either the leader--anyway the person who was dealing with that legislation in the Massachusetts legislature. The story goes that this man, who was an Irish-American, was just engaged in making a long speech against the proposal, pointing out that this meant giving money to the British, who were terrorizing the Irish, and this is a very bad thing. At which moment, a page handed him a piece of paper and he looked at it--this was a telegram from McCormack--urging him to support the bill. At that he put down the piece of paper, looked at this fellow members, and said, "Well, gentlemen, this much for the arguments against the bill," and he turned around and set forth the arguments for the bill. So, we got the savings banks legislation.

Q: I had heard that there was some delay for a year or so in getting proper Congressional committee to take the necessary federal legislative action.

Broches: Could you be referring to another legislative development I should mention, and that was our exemption from certain provisions of the Securities Acts?

Q: That may well be, yes.

Broches: Because in 1947, when we did our first issue, we were regarded as subject to the provisions of the 1933 and 1934 Acts. That means that we are registered with the SEC and that the offering couldn't be made until the registration statement had become effective. That is the moment that is commonly referred to as the moment when the SEC "approved" the issue, although the SEC does not approve issues and the prospectus says that it's a criminal offense to state that the SEC approves or disapproves issues. The technical term, then, is "when the registration statement becomes effective."

There is a story to be told in connection with that, because, as I mentioned, we had an undetermined number, which would certainly run into the hundreds and which turned out to be 1600--people involved as agents in the distribution of our securities. Now, you couldn't possibly approach the whole list of the NASD at the moment when the registration statement became effective, which is normally just before the offering. That would have been the time at which we normally could have approached these people. On the other hand, we had another problem, and that is that under the Act underwriters have specific liabilities. We knew that most of the members of the NASD who deal in government bonds and who are exempt--I mean, the government bonds are exempt--didn't like the idea of getting involved in liabilities under

the Securities Act. So we asked for a ruling to the effect that these people would not be underwriters, within the meaning of the Act, for that purpose. And we stated why we wanted the ruling.

However, that created another technical problem, because until a registration statement has become effective, you're not permitted to discuss the issue with potential takers other than underwriters. And now these 1600 people had been ruled to be not underwriters for certain purposes. And we sent out telegrams to all the members of the NASD, and the SEC got very excited and said, "Wait a second. You violated the Securities Act because you've offered, or you have at least solicited, offers to buy from people who are not underwriters. You came to us and said they weren't underwriters, and we so decided." There was great excitement about that. Mr. McCloy and Mr. McLain were summoned to the SEC--of course, it was all a misunderstanding and nothing happened. But what it did show us was that it was wrong for the Bank to be subject to the provisions of the Act. We didn't know how future marketing would go but we did know that much of our dealings, or many of our dealings, would be with people who are not used to being under the Act because they're dealers in government and municipal bonds. And then with this point of the U.S. administration we went to Congress--or rather the U.S. administration went to Congress--for an act exempting us from certain requirements of the '33 and '34 acts. And that act was passed--the amendment was passed in 1949.

I don't know when the first steps were taken, probably soon after our first offering in July '47. But that was very important to us.

Q: I'm very hazy about a story that somebody told me. I wonder if it might have been you in our first conversation. It was about somebody in the Bank's having to appear before a Congressional committee to say that he was saying something in behalf of or for the Secretary of the Treasury and was quoting from the Congressional Record on some issue. And something had happened wrong in the Congressional Record reporting, and as a consequence somebody in the Bank got a call from the Secretary of the Treasury's office saying that he was being misquoted in some way. This would have been not from you?

Broches: No, I don't recall that. I do know on the SEC issue one thing was important. We could have made an argument that we were not subject to the Securities Acts, but during the deliberations on the Bretton Woods Agreements Act, that is on the joining by the United States of the Bank and Fund, the administration witnesses in answer questions said, of course, the Bank would be fully subject to the Acts. So, we decided that it would not be a very good thing to take a contrary position under the existing legislation. But then later, as I say, we asked for and the U.S. administration asked Congress to amend the Act so as to provide an exemption for us.

Q: What, do you suppose, has been mainly responsible for the high rating which the Bank's bonds have now attained?

Broches: I think it's a combination of factors. In part, it has been the famous 80 percent that I've talked to you about before, the unpaid portion of the Bank's capital, which, of course, in the meantime after

the capital increase has become 90 percent, which constitutes a very large amount in relation to any foreseeable borrowing, and on which the United States is independently liable for an amount now in excess of five billion dollars. First it was two-and-a-half billion dollars. That in itself was, of course, a source of great financial strength, the two-and-a-half billion.

I still think that if the rating services hadn't liked the management and the general way in which things were done, I don't know what they would have done, but I do know that they've taken this very much into account and that that has helped in giving us a high rating.

Now, until our capital was increased we didn't have the highest rating, the triple-A or its equivalent, and I supposed that the reason for that was that people said, "Well, two-and-a-half billion, that is something that the Bank could reach." There was no prohibition either in our charter or in our bond issues against our going or trying to go beyond the figure that would be the equivalent of the U.S. obligation. That may have caused them not to go all the way in calling the triple-A, but after we doubled our capital that was done.

In the meantime, of course, we also established a good financial record; we had no defaults, our reputation had grown generally, people became more interested in the developmental functions of the Bank, which maybe in the beginning would have been regarded with some suspicion but now are generally acclaimed. The financial community, and I'm not only talking about New York--I found very little difference between New York and Zurich and Amsterdam and Brussels and London; investment bankers tend to think the same way--and now when we get into some new ventures, such as an economic development institute or

something else, our survey missions, all of that is regarded as very important and very useful. Generally, the Bank has an all around, good reputation, plus five billion dollars obligation of the United States, plus additional huge amounts of other countries, which are now regarded as pretty good obligations too.

Q: Do you think that there are some types of loans, some types of projects say, which it would have been questionable if the Bank should have financed or which in the course of its history, if it wanted to maintain the highest sort of relationship with the market?

Broches: No, I don't think there's anything we've done that has been criticized in the market. I know that in our early years there was much talk that the market wouldn't like this and the market would like that. There's much less of that now. That has some relevance to that story I told you about Crena de Iongh, who was asked by the banker, "When would you start making a mistake?" What he really meant is: You shouldn't only be guided by what you think the market would want. Once you've become experts you should lead, and if you feel something is a good thing, you ought to do it. I think we've done that repeatedly. I don't think we shocked the market; it just accepted our judgment. So that nowadays--of course, Mr. Black has his finger on the market's pulse--I don't think that there's any feeling that the market would take a very strong view on any of the things that we have in mind.

Q: If a loan like the Italian had been made in '47 instead of '50, or whenever it was made, might this have shocked the market then, do you

think?

Broches: I just don't know. I mean, the market could have been shocked at our reconstruction loans because when we made them, it was quite clear that the countries involved, the rest of the European countries, needed a lot more money than we could possibly provide. So the market might have been shocked at our optimism in investing 500 million dollars in a month and a half in that very risky area of the world. I don't think there was any shock; I think those loans were welcomed by the market, because the names were good, the people were in poor shape at the time but they were responsible countries with a long, good financial record.

Q: I wonder if you could tell us something about the development of the market abroad.

Broches: That's been a slow and gradual process, but a very interesting one. We had our eye on other markets and the first market in which we did something was Switzerland. It was in 1948. In 1948 the Bank for International Settlements, which is not a Swiss institution, indicated that it would like to do something with us. And they loaned us 17 million francs. We turned around and loaned those 17 million francs to the Dutch, under their general reconstruction loan. Up to that time we had been lending only dollars but we asked the Dutch whether they would be willing to take Swiss francs for a part, so we amended the Dutch loan agreement to provide for a Swiss-franc tranche.

The BIS gave this to us at what they regarded as a somewhat

subsidized rate because they wanted to do business with us and they liked to cooperate. They later sold some of this paper to Swiss Commercial banks. Then in 1950 we had reached the point where some of the Swiss banks, or the three big Swiss banks with whom we are still working--the Swiss Bank Corporation, the Credit Suisse, and the Union Bank of Switzerland--were found willing to buy some short-term or medium-term bonds from us. The BIS was in the picture to help; they were willing to accept a somewhat lower interest rate to make the transaction possible. So, we dealt with those four institutions, the three Swiss banks plus the BIS. That was in 1950. We did that with the hope that the next stage would come soon in which we could make a public issue in Switzerland. That was one front.

Then we started talking to the Dutch. There was nothing doing there, except that the Dutch were willing to permit us to issue Dutch certificates for our 1947, 3-percent U.S. dollar bonds in a limited amount which could be bought by Dutchmen who had dollars arising out of liquidation of American securities. So that all that happened was a shift in the composition of Dutch investments; it didn't mean that any new dollar investments could be made, but somebody might sell, say, American shares and then he was credited with investment dollars, and those could be brought by somebody else or used by the same man and used to buy our bonds. To make that attractive the Dutch government agreed that those bonds wouldn't be requisitioned. At that time there was still the danger that the government would be forced to requisition dollar assets or foreign-exchange assets generally. That was a second step.

In 1951 we moved on two fronts. In 1951 the British let us do an

issue of five million pounds sterling, and we had our first public issue in Switzerland. By that time, we had also obtained--the Swiss were very much interested in having us borrow in their country; they had not joined the Bank and they still haven't because they don't want to join the Fund (it's an old story)--but they wanted to cooperate with us. And we had had many contacts with them. Mr. McCloy and Mr. Black had many talks with them and in the spring of '50--this was completed in '51--the Swiss entered into an agreement with us by which they gave us a number of tax advantages and immunities to give us a status which was very much like the legal status that we enjoy in the territories of our members, in return for which we agreed to consult with them and get their consent before we did market operations.

But the idea was that Switzerland wanted, without becoming a member of the Bank, to give us about the same as what a member could provide. And they said we would be a welcome borrower in their market. I spent about a year working on that agreement; it was quite interesting to see--they are very tough to negotiate with, but they admitted that they were extremely eager to get this close connection with us.

Ever since '51 we've returned to the Swiss market very regularly. Soon we'll do our tenth issue there.

In England we didn't return to the market because the British didn't feel they could let us go there until 1954. Then we did a third issue in 1959. The '54 issue was once again for five million and the '59 issue was for 10 million pounds.

In Holland we were constantly in touch with the authorities and it was there also in '54 that we were permitted to go to the market with a

public issue. We did another one in '55. Then things changed and we didn't return to the market until 1961.

We had two issues in Canada. Those are the only ones that I didn't personally work on. I don't know the dates. I think the first one was in 1952.

Very much more recently, of course, we've borrowed in Germany, in '59, and in Belgium also in '59. Those were public offerings.

But in the meantime--and these were offerings in the currencies of those markets--as dollars became available Europeans and other non-Americans bought parts of our American issues, of our dollar issues, that were publicly offered here.

Q: They were paid for in dollars.

Broches: And they were paid for in dollars.

In addition, for a number of years we have been offering short, medium-term loans in dollars to non-American investors, mostly central banks, exchange stabilization funds and other institutional investors. Those have been offerings entirely outside the United States but of dollar bonds.

Then, in Germany, of course, we have been borrowing on a very large scale from the German central bank, the Deutsche Bundesbank.

If you take it altogether, a majority of our borrowed funds have now come from sources outside the United States, although the bulk of our borrowing has been expressed in United States dollars.

Q: Well, once again we've come to the end of the tape.