Address by Mr. John J. McCloy, President, International Bank for Reconstruction and Development before the Thirty-Fifth National Foreign Trade Convention, Grand Ballroom, Waldorf-Astoria, New York City, at 3:00 P.M., Monday, November 8, 1948.

THE INTERNATIONAL BANK AND WORLD TRADE

I am very pleased to have the opportunity to be here with you at this 35th National Foreign Trade Convention. Apart from the immediately pressing political difficulties which seem to bedevil mankind in almost every corner of the globe, there are no problems more urgently in need of solution nor any whose solution would be more conducive to both political and economic stability, than the problems connected with foreign trade and international finance which you have assembled here to consider.

I believe that I can perhaps best contribute to your discussions by reviewing with you briefly what the International Bank has done and is trying to do to help solve those problems and by analyzing some of the difficulties we are confronted with in discharging our responsibilities. I would like, too, on the basis of that review and analysis to suggest some of the steps which I consider to be necessary if lasting progress is to be made towards the creation of a healthier world economy.

As most of you doubtless know, most of the loans granted by the Bank to date have been for purposes of European reconstruction. In the spring and summer of 1947, we made a series of four European loans — to France, the Netherlands, Denmark and Luxembourg — aggregating $497 million. These loans came at a time when European resources of dollar exchange had fallen to dangerously low levels and credits from the United States and other Western Hemisphere countries had largely been exhausted. They served, I believe, their intended purpose of helping to prevent a disastrous drop in the production of the borrowing countries and possible economic collapse.
We were fully aware, of course, that these loans, vital as they were, provided only a partial solution to Europe's problems. The physical devastation, the disruption of trade and the industrial and governmental dislocations caused by the war left a far wider crevice in Europe's economy than any but a very few had anticipated. Financial aid on a scale far beyond anything the Bank could conceivably afford was clearly necessary. Fortunately for Europe and for the world, the seriousness and urgency of Europe's situation was recognized by farsighted leaders of the United States and as a result of their efforts, combined with a really hopeful display of initiative and cooperation on the part of the Western European Countries themselves, the European Recovery Program was brought into being. That program, in my judgment, happily combines the best qualities of the American tradition -- generosity, daring and realism.

There is a misconception in some quarters that, with the enactment of ERP, the Bank is temporarily out of business in Western Europe. In every stage of the formulation and administration of ERP, participation by the Bank in the financing of European recovery, on a modest scale at least, has been recognized to be both necessary and desirable. Indeed, far from interfering with the Bank's operations, ERP should greatly facilitate them through improving the economic position of Western Europe and thereby increasing the security of Bank investments in that area. Furthermore, the very existence of the recovery program relieves the Bank of pressure to make general balance-of-payments loans and enables it to concentrate on its intended sphere of activity, the financing of specific productive projects. We are at present discussing with a number of ERP countries many different projects which they would like the Bank to finance -- projects which are an essential part of their long-range investment programs but which they could not afford to undertake unless they secured the benefit of Bank loans in addition to ERP aid.

The story in Eastern Europe is somewhat different. The Bank has four member countries in that area -- Poland, Czechoslovakia, Yugoslavia and Finland. To date, the Bank has not been able to grant loans to any of these countries because of the impact of the existing political tensions and uncertainties upon their economies and upon their credit. We are fully aware, however, of the importance to these countries of the development of their productive resources and of the importance to Europe as a whole of an increase in East-West trade. While the extension of long-term credits to Eastern Europe at the present time involves many hazards, the short-term financing of East-West trade on a quid pro quo basis affords some very constructive possibilities which we are actively exploring.

A case in point is the proposed timber loan, which is now in an advanced stage of negotiation. Finland, Poland, Czechoslovakia, Yugoslavia and Austria are all timber-exporting countries. They are badly in need of about $17 million of additional lumbering equipment, roughly half to be procured in the United States and half in Western Europe. If they get this equipment, it is estimated that they can expand their timber exports by about $60 million annually. Most of the Western European countries, on the other hand, are urgently in need of additional timber imports, and particularly imports from non-dollar areas. The deal we are now trying to work out contemplates that the Western European countries will
furnish to the Eastern European countries equipment worth about $8.5 million, which for the most part will be paid for by timber exports. The purchase of the equipment needed from the United States would be financed by the Bank, the loan to be repaid over a period of about two years, also from the proceeds of timber exports from East to West. The whole transaction would be based upon an agreement by the Eastern European countries to make available to the West the additional supplies of exportable timber resulting from use of the equipment.

I believe that if this financing eventuates, it may provide a hopeful pattern for other comparable operations and may thus contribute substantially towards increasing the volume of East-West trade.

The Bank's activities in the development field, mainly in areas outside of Europe, are not easy to generalize about because they vary so greatly from country to country. We are presently carrying on discussions concerning development projects in more than 20 of our member countries. These discussions cover a great many different types of proposed undertakings, such as power development, the construction of transportation and communication facilities, irrigation, reclamation and other agricultural projects, migration programs and industrial and mining development. As you can well imagine, the work involved in investigating all these projects, not only on their intrinsic merits but also in relation to the sound economic development of the particular countries concerned, is both immense and time-consuming.

We are faced with a great many obstacles in trying to bring this work to fruition. Although our underdeveloped member countries are impelled by a tremendous desire to improve their situation, they generally lack the technical knowledge as to how to go about it. Few of them, for example, have any well-formulated concept of the over-all lines along which their development is most likely to make progress. The projects they present to the Bank are all too often inadequately planned or prepared, reflecting in large part the severe shortage of technical personnel. Furthermore, many of the under-developed countries are suffering from chaotic monetary conditions which must be rectified if any investment in their further development is to be either productive or safe.

I mention these difficulties because of their importance to an understanding of the Bank's activities in the development field. In order for the Bank to assure that its resources are effectively used for development, we have to do more than merely pass upon loan applications as they are presented to us. Most of our underdeveloped members need technical assistance at least as much as they need financial assistance. They are coming more and more, therefore, to look to the Bank not only for loans but also for help in determining what projects they should put forward for financing, in mapping out an appropriate over-all pattern for their economic growth, and in formulating the economic and fiscal measures necessary to put their economies on a stronger and more stable basis. This imposes a heavy responsibility on the staff of the Bank, but it is one which I believe we must assume if we want to assure that our funds are wisely invested in practical, productive projects.
To date we have been able to grant only one loan for development purposes; we have made commitments to Chile, aggregating $16 million, for hydro-electric projects and for the importation of agricultural machinery. However, several other developmental loans are now in an advanced stage of negotiation and I am confident that, during the course of the coming year, we shall be able to make a number of additional such investments. In the long run, of course, the development field will be the Bank's principal sphere of activity.

I would like to turn now from this general review of the Bank's lending operations to consideration of some of the larger problems which I believe must be faced and solved if world trade is to be reestablished on a firm and lasting basis.

For one thing, there must clearly be some relaxation of the knife-edged political tensions which now pervade the whole world scene. The prevailing political uncertainties and unrest have undermined the confidence necessary for long-term productive investment and for monetary stability. They have disrupted normal trade relations and have necessitated a serious diversion of manpower and materials from productive pursuits to the maintenance of large military establishments. In the case of some of the Western European countries, for example, military expenditures are absorbing as much as 20 to 25 per cent of their entire national budgets. Politically-inspired strikes, such as those we have been witnessing in France, have seriously interfered with production in key sectors of the economy. Without some alleviation of these conditions, the most enlightened economic statesmanship will find it difficult to succeed.

It would be a mistake, however, to attribute all of our economic difficulties to the disturbed political scene. There are many steps of a predominantly economic character which urgently need to be taken irrespective of political developments.

So far as the under-developed areas of the world are concerned, there is need for a new attitude and a new atmosphere in relation to foreign financing. I have found in too many quarters a disinclination to take those measures necessary to attract private capital from abroad and, instead, an insistence that inter-governmental or International Bank credits should be made available in large amounts and should be allocated primarily on the basis of need, without too critical an analysis of the prospects for repayment.

That approach, in my judgment, is neither realistic nor sound. No amount of foreign loans will be of lasting benefit unless domestic conditions in the borrowing country provide both a firm economic base for development and reasonable prospects for repayment. Bad loans may serve temporary political ends or bring temporary relief, but in the end they leave behind only disillusionment, debt and ill will. Furthermore, although public sources may bear the burden of financing development for a time, sustained investment in the substantial amounts required can reasonably be expected only from the free flow of private capital, particularly equity capital. I would urge, therefore, that the under-developed countries place less emphasis on their need for extraordinary
types of public assistance from abroad and more on the necessity for creating an
environment attractive to the investment of private capital through balancing
their budgets, stabilizing their currencies, overhauling their tax systems and
conserving their foreign exchange resources. These measures involve hard work
and sacrifices, but the process of opening new economic frontiers is never easy.
I wish to make it clear, as I hope I have on previous occasions, that the Bank
is prepared to move concurrently with the development countries in this direction.
We do not demand that everything be put in such order that no loan becomes
necessary. We only demand that the environment be such as to make the loan
effective and we are prepared to match local progress with International Bank
aid.

Much the same is true of Europe. Financial assistance through ERP cannot
by itself bring European recovery. The most that it can do is to help the ERP
countries in their own efforts to effect a fundamental readjustment of their
productive and trade mechanisms. Self-help is the very essence of the program.

The ERP countries have already made substantial progress in the expansion
of their total production. They have established, through the recent intra-
European trade and payments agreement, a means of moving a substantially in-
creased amount of goods among themselves. However, these accomplishments, en-
couraging as they are, are just a beginning.

Perhaps the most urgent need in Europe today is for financial stability.
It is hard to over-emphasize the importance of this. Production, trade and in-
vestment plans, no matter how well conceived on the national or international
level, are worth little unless they are translated into action through the ef-
forts and initiative of millions of individuals. A pre-requisite for that is
confidence on the part of the business man, the farmer and the laborer in the value
of the money they receive for their goods or services. Given such confidence,
seeming miracles of production can be accomplished. Without it, true recovery
is impossible.

Equally important, financial stability is necessary for the free flow of
international trade which is the life-blood of the ERP countries' economy. It
profits little to produce more goods unless they can be freely sold in the mar-
kets of the world. Yet we can only progress from the refined barter techniques
which still characterize too much of intra-European trade and re-establish it
on a healthy multilateral basis if confidence is restored in the currencies in
which such trade is conducted.

The prevailing lack of confidence in European currencies is perhaps most
dramatically reflected in the flight of capital now going on. The causes, of
course, are both political and economic. There can be no financial stability
in the absence of sound financial policies, but there can also be no financial
stability without confidence on the part of the people in the political future
of their country. This explains why the problem of military guarantees, now so
widely discussed, has such direct and vital economic implications. It isn't
necessary, of course, that all political tensions be removed before we can
take firm constructive steps in the economic field. But the minimum we must have
is a situation in which there is not a common belief that war is inevitable.
The financial policies essential for stability are both simple and well understood. They involve a balanced governmental budget, or, preferably, even a surplus; credit controls to ensure that the banking system does not create excessive means of payment; and appropriate price and wage adjustments internally so that productive resources are not diverted into non-economic output as a result of price maladjustments.

In this connection, it is interesting to note the development of what has been called the "ashtray economy". With the price structure maladjusted and prices of essential items rigidly controlled in many countries, people frequently have more money to spend than they can use to buy rationed commodities. Two results flow from this. The first is that a premium is placed on the manufacture of ashtrays, knickknacks and other non-economic products which can be sold at free prices but which cause a diversion of labor, materials and power from the production of more essential items. The second result is that domestic demand for all goods, both essential and non-essential, is so strong that there is no incentive for the manufacturer to look to foreign markets for the sale of his products. This situation can only be remedied by creating conditions of monetary stability which permit of realistic price readjustments through the normal mechanisms of the market.

In short, restoration of financial stability will increase the over-all volume of production, will result in more production of essential goods, will increase the availability of goods for export and will put European trade on a firmer and more stable basis.

Another pre-requisite for European recovery which I should like to mention briefly — one which is perhaps less immediately urgent than financial stability but which in the long-run is equally essential — is greater integration of the economies of the various ERP countries. I mean by this the lowering of trade barriers among them and the planning of their investments in the expansion and modernization of their productive facilities on a regional and not solely on a national basis. In order to accomplish this, more is required than a reconciliation of conflicting national claims. The basic need is for a revamping of existing mechanisms so as to provide for unified thinking, planning and action in terms of the best interest of Western Europe as a whole.

It may well be that the ultimate answer is a complete economic union of the Western European countries. But such an economic union, involving as it does centralized control of such vital matters as currency, investment programs, wages, prices and foreign trade, cannot, in my judgment, be accomplished without political union as well. And in view of the historical and deep-rooted differences in language, customs, traditions and national habits and prejudices among the European countries, it is not realistic to expect that such a political union can be quickly achieved.

I believe, therefore, that it would be a serious mistake if, through undue emphasis on the ultimate objective of a political federated Europe, we should be led either to overlook the very real accomplishments already made in the
direction of European economic cooperation or the many additional measures of integration, short of complete union, which are possible of prompt realization. There is already apparent a new attitude of mind, a recognition of the essential interest of each ERP country in the common fate of all. There is also gradually developing in the OEEC, I believe, the type of integrated thinking and planning which is necessary. The gradual development of these trends, accomplished by a corresponding willingness to relinquish national sovereignty to the extent necessary to make integrated action possible, seems to me to hold the best hope for the achievement of our ultimate goal.

I want to turn now to one final subject -- the steps which the United States itself can, and in my judgment must take to supplement recovery and development efforts elsewhere. The United States may justifiably take pride in the financial assistance it has already made available and is proposing to make available to permit increased production in many areas of the world. But increased world production will contribute fully to a healthier world economy only if it results in a corresponding increase and a greater balance in international trade. Whether or not it will do so depends very largely on the trade policies of the United States.

The enormous export surplus of the United States today plainly cannot long continue, dependent as it is on emergency measures of extraordinary assistance and on the use of dwindling gold and dollar reserves. In the long-run, the other countries of the world will be able to purchase the volume of goods from the United States which they would like to buy here and which the United States would like to sell to them, and at the same time service their dollar obligations, only if the United States follows policies designed to encourage a great increase in American imports.

I refer not merely to government policies, important as these are. Certainly a further reduction of tariffs would be of substantial value. But at least equally important is the attitude of the American commercial community and consuming public. A joint British and American group of industrial and labor leaders was recently appointed, as you all know, to promote an exchange of information between the two countries with respect to the latest production techniques. It would be equally appropriate, I believe, if in the next few years similar means were developed so as to make available to producers and traders abroad information on how they might most effectively reach the American market.

Certainly there is no need to impress on a group such as this that foreign trade, far from being a one-way street, can flourish only as a vigorous two-way traffic. That means, in the case of the United States, that the maintenance of the present high level of exports depends very largely on the promotion of greater imports. Indeed, I think it is fair to say that the United States is rapidly approaching the cross-roads at which it must choose between the path of anarchy marked by such signposts as "Buy British" or "Buy American", which characterized the last depression, and that leading to a healthy era of international commercial cooperation. Given general acceptance in the United States that anarchy is inefficient and destructive, that a prosperous world is possible only if there is a goodly volume of international trade and that the prosperity of the United States is indivisible from that of its neighbors, the choice should not be difficult.