Address

By

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to the
EXIMBANK Annual Seminar

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Thank you, John, for inviting me to be with you today at your annual Seminar.

I am happy to have the chance to meet with such a large and distinguished group of commercial bankers.

Walter Winchell used to define an optimist as a man who gets treed by a lion but enjoys the scenery.

There may be a feeling around that the whole global economic jungle is about to be populated by bankers treed by the lion of the Latin American debt crisis, and that the scenery viewed from the upper branches is going to be anything but enjoyable.

Before clawing our way up the bark, we must ask ourselves whether the situation calls for a flight to the top branches in the uncertain hope of self-preservation, or for the foresight of Androcles who saw what pained the lion and pulled the thorn from his paw.

The paw is hurting, and has been for some time. The adjustment effort that the highly-indebted countries have been undertaking has proven costly and protracted.

There are no simple solutions.

The plan outlined by Secretary Baker to assist the highly-indebted nations remains both the most constructive and most viable initiative. It calls for strong cooperation between borrowers and creditors. It demands that all involved in the debt crisis -- the nations themselves, the World Bank, export credit agencies and commercial banks -- participate in the search for solutions. It is in the interest of none to opt out of this joint venture.

The Baker Plan recognizes that the revival of trade and investment is essential for the restoration of creditworthiness of the highly-indebted nations. Today I want to talk about the scope of that challenge and the need for you to work with us in ensuring success.

From the start, adjustment had to be carried out under very unfavorable external conditions:

- sky-high interest rates until 1985;
- recession in the OECD countries slowing down international trade;
- primary commodity prices on a seemingly endless decline;
and, since the second half of 1982,

- the virtual disappearance of all voluntary lending by commercial banks, which, despite IMF-led efforts to organize rescue packages to help the most heavily indebted meet their commitments, led net capital inflows to Latin America to plunge from $38 Billion to $7 Billion in most recent years.

Large increases in interest payments, and from some countries the flight of vast amounts of capital, added to the misery.

Net payments of interest and profits hit a record $39 Billion in 1982, then levelled off at $35 Billion.

The old problem of capital flight persisted. Ten Latin American countries accounted, as best we can calculate, for well over $100 Billion of capital flight between 1976 and 1985 while accumulating $270 Billion of additional foreign debt. The $30 Billion that fled Venezuela actually exceeded the country’s new debt.

The sorry result was that, having received net medium and long-term resources from abroad in 1982 of about $25 Billion, Latin America found itself transferring around $20 Billion per year to the rest of the world in recent years.

That is over 4 percent of the region’s gross domestic product, which is twice the percentage that Germany was paying in post-World War I reparations to the victors between 1925 and 1932.

Despite all this, the region cut its current account deficit from over $40 Billion in 1981-1982 to less than $200 Million in 1984. They did it by achieving an astonishing turnaround in the trade balance, turning a $2 Billion deficit in 1981 into a $39 Billion surplus in 1984.

The turnaround was achieved, however, because expenditure fell, imports were fiercely compressed and growth was halted.

Such was the cost of closing the current account deficit: falling output, falling investment, falling employment and falling living standards.

It was not that the switching of policies failed to increase exports. Despite the world recession, the volume of Latin America’s exports rose by 30 percent in 1980-1985. The twist was that the dollar value of them rose only 3.5 percent, reflecting the region’s still heavy dependence on primary products for its export earnings, and the drastic fall in their prices.
As a result, the entire burden of correcting the huge imbalance had to be shouldered by imports. They plunged from over $90 Billion in 1981 to $56 Billion in 1983, before stabilizing at around $60 Billion in 1984-1986.

This contraction went much deeper than just the trimming of some fat on the earlier import bills. It hit inputs indispensable to growth.

Between 1980 and 1986, Latin America's total import volume fell by almost one-quarter, and on a per capita basis by one-third.

Mexico was importing $6 Billion worth of investment goods from the United States in 1981, but less than $3 Billion in 1983. It was importing $14 Billion in American manufactures in 1981, and only $6 Billion in 1983. From Alaska to Alabama, American exporters have been hurting.

This massive contraction of imports naturally had strong recessionary effects. In 1982 and again in 1983, the region's GDP fell for the first time since World War II. Per capital income was down by 14 percent.

Consumption fell almost 10 percent on the average, often cutting into critical expenditures on health, nutrition and education. The adjustment came at the expense of growth.

I am not for a moment suggesting that the region's present troubles are all imposed from the outside. Far from it. There have been policy short-comings as well. A capacity for the self-inflicted wound is all too noticeable in a number of countries. Fits of profligacy when things have started to look a little better, untimely stimulus of domestic demand, blind eyes to continuing capital flight -- each has taken its toll somewhere.

However one apportions the blame, the fact remains that Latin America's declining ability to import is crippling its chances of an early return to sustained growth and social progress.

It is not enough to say that better export performance will finance a higher level of imports. There is an obvious Catch-22. Further import compression will deny the exporters the materials and machinery they need to do the job.

While exports are the prerequisite for an increase in imports vital to growth, imports are a prerequisite for an expanded capacity to export.
As the massive import compression and the scale of policy changes in Latin America clearly show, the nations of the region have been bold in instituting reforms. Much more must be done, however.

Given current conditions, Latin America must be assisted from the outside in its struggle to revive creditworthiness. Bankers and businessmen in this country have a vital interest in such a revival and in seeing Latin American imports bounce back strongly.

For this to happen, the region must boost its earnings from exports. What are the prospects?

Commodity sales are part of the equation and here the outlook is not bright. Global non-oil commodity prices are desperately low and a further decline could well occur in 1987.

Prospects for a significant expansion in Third World export earnings this year are dimmed by what appears will be only lackluster economic growth in the biggest industrial nations. The U.S. growth rate could be as low as 2 percent. Growth in Japan and in the major European countries may be only a notch above the sluggish rates of last year.

At the same time, the pressure is on in OECD nations to curb trade. Hanging like the sword of Damocles is the threat of increasing protectionism. The markets of the industrial nations must remain open if trade liberalization is to be pursued in the developing world and if, for example, Latin America is to increase earnings from exports.

Latin America's net earning capacity is, of course, further hampered by the high level of debt service, with a total external debt-to-export ratio of about 310 percent.

External debt is up 60 percent since 1980, and we expect it will have reached $390.5 Billion at the end of 1986, 86 percent of which is long-term debt. Service on that will have been about $38.1 Billion.

Given the broad economic outlook and current estimates, there can be no doubt that there has to be a major increase in net external capital flows to Latin America to secure growth.

Bilateral aid to the region is mostly going to the Caribbean and Central America and is unlikely to increase. Private direct investment has fallen sharply in recent years to very low levels. This certainly is one area for great development.

The World Bank, through the International Finance Corporation and shortly through the new Multilateral Investment Guaranty Agency, is fostering such investment. The governments of the debtor nations must
consider actions to bring back flight capital for direct investment purposes.

We should have no illusions, however, about a great expansion of private investment flows taking place without evidence of support by commercial banks for these nations. And what are they doing?

Sixteen Latin American and Caribbean countries owed $260 Billion to all commercial banks at the end of 1985. $81 Billion, or about 31 percent, was owed to U.S. banks -- this represented a 5.5 percent decline from the previous year. This trend must be reversed.

The restoration of Latin American creditworthiness has to be a product, in part, of resumed bank participation, not a precondition for it.

Participation by commercial banks might be eased somewhat by regulatory changes, but I do not want to get into those details here today. I do want to stress, however, that the goods of your U.S. clients and the strength of your long-term relations with Latin American nations depend heavily on the restoration of growth in these nations.

Bankers must appreciate the full scale of policy reform that these nations have, and are, implementing. Adjustment demands popular support over time, and it can be sustained better in an environment of growth than in one of import compression and declining incomes.

The World Bank accepts its obligation to put together adjustment packages, the value of which will be apparent to participating commercial banks. Cooperation is necessary; the key players cannot stand on the sidelines.

The World Bank has been responding with increasing lending on its own account: commitments to the region in FY86 were up 29 percent on the previous year. Loans supporting policy reform amounted to $1.5 Billion, or 32 percent of our lending to the region. This marks a major increase in the Bank’s support for the adjustment effort.

Another group assisting in growth is the export credit agencies. Export credit is one of the three main sources for our co-financing operations. We want to see the ECAs do more. A projected net decline in ECA exposure should not be acceptable in a concerted effort to expand resource flows. For some major debtors, export credits have been cut in recent years.

There is wide agreement on the need for ECA support for the adjustment process, for the early resumption of cover, for ECA discrimination in the selection of projects they finance and for increased consultations and exchanges of views with both the Bank and the IMF.
The Eximbank ranks second only to Japan in export credit co-financing of Bank operations. In all our consultations with the ECAs, the Eximbank has been a key contributor. We place great value on our continuing dialogue with Eximbank on a range of general issues, as well as on our relationship at the project level.

There is no banker or businessman in this country who does not want to see Latin America's creditworthiness restored, and its progress down the path to sustained development assured.

When that happens, we are all winners.

Sustained growth in the industrialized world and an open trading system are crucial prerequisites.

Yet, without a vigorous effort to close the financing gap, the indebted countries' opportunity to exploit an improved global economic environment will be lost. Many highly-indebted countries have made substantial progress toward achieving sustained development by undertaking major difficult structural reforms. Without timely financing support, however, these efforts will be stopped in their tracks.

I find the scenery from my perch in the upper foliage anything but discouraging.

Like "Papa" Hemingway, who no doubt got treed from time to time, I find the earth in his words "a fine place, worth fighting for."

We have to fight this battle together. No bystanders.

The international financial system is durable. It can take and has taken some serious buffeting. It is foolish to underestimate its strength, and worse to excuse inaction on the grounds that it cannot cope.

Our ability to cope depends on our willingness to cooperate with each other. We're all in this together.

Thank you.