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Transcript of interview with

SUMAN K. BERY

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By: Richard Webb and Davesh Kapur

FOREWORD

The following is a transcript of an oral interview conducted by the authors of the World Bank's fiftieth anniversary history: John P. Lewis, Richard Webb and Devesh Kapur, *The World Bank: Its First Half Century*, Washington, DC: Brookings Institution Press, 1997. It is not a formal oral history, and it is not a systematic overview of the work of the person interviewed. At times the authors discussed the planned publication itself and the sources that should be consulted; at other times they talked about persons and publications extraneous to the Bank. Some interview tapes and transcripts begin and end abruptly. Nevertheless, the World Bank Group Archives believes that this transcript may be of interest to researchers and makes it available for public use.

[Begin Tape 1, Side A][1]

WEBB: . . more fruitful for us, but Latin America in general.

BERY: What's the cut-off date? Is it going to be [both speaking at once] through to ‘95 itself, or . . .

WEBB: No, I think end of ‘93 is the most likely cut-off date.

BERY: Okay. So basically what's happening here and now is also of interest to you. It's not that it's all retrospective. I mean, what's current now will be history by the time the book comes out.

WEBB: That’s right.

BERY: I see.

Okay, well, two things: one is just a quick kind of delineation of what I've done in the twenty years. I mean, Ernie *[Ernest Stern]* called this generation “*[Robert S.]* McNamara yuppies” and I guess I'm one of those. And he also said that that was—that we were members of, you know, the baby boom of the Bank, as it were. That was the period of the Bank's biggest expansion ever--or yet. So, you know, I would say that both in life and in the Bank one has this familiar baby boom sense of, you know, people ahead of one having had a great time, an easy time of it, but one's own cohort being very crowded. But essentially I divide the twenty years into more or less four, five year segments. After coming in as a YP *[young professional]* my first five years were on research staff, and part of that was--three and a half or four--part of that was preparation for wanting to go back to Princeton actually on a leave to do my Ph.D. So that took me from ‘72 to about ‘77.

WEBB: Were you in DRC *[Development Research Center]* or DED *[Development Economics Department]*?

BERY: DED, in the Public Finance division.

WEBB: You know, I had forgotten that.

BERY: Yeah.

WEBB: So you were with Doug *[Douglas H.]* Keare.

BERY: Yeah, well, Oktay Yenal was the division chief at that point.

[1]Original transcript by the Brooking Institution World Bank history project; original insertions are in [ ]. Insertions added by the World Bank Group Archives are in *italics* in *[ ]*.

WEBB: Oh, I'm sorry; I'm getting confused. It was Oktay.

BERY: Yes. Doug was [both speaking at once] in Urban Finance. That was Public Finance division.

WEBB: It was a very small division, wasn't it?

BERY: Yeah.

WEBB: Well, not "very," but it was a bit smaller than the others.

BERY: Yeah. His immediate predecessor had been Stanley Please, and in Stanley Please's time it had been, you know, a major division, but then it got shrunk in the '72 reorganization. And let me say that the '72 reorganization was probably my second week in the Bank, so I'm very much a product of the post-'72 Bank, I mean that's the Bank between '72 and '87.

KAPUR: Was that the group after mid-'72 which then went and made up the fiscal affairs department at the Fund *[International Monetary Fund]*? There was this group which moved from the Bank to the Fund.

BERY: I didn't know that there was a large group. There were a couple of people, Dave *[David A.]* Dunn being one, who--except he wasn't—you know, you must remember my own consciousness and awareness in those days was pretty limited so I may not have known all that was going on.

But, yes, I mean I think two things happened. One was that there was some devolution of fiscal capacity to the newly formed regions at that time. And, secondly, was that also one of the moments of the Bank-Fund concordat, one of the continuous revisions of it? Because I think that, you know, that was one of the moments, as in '88, that again Bank-Fund collaboration got surfaced and some kind of division of labor and boundary lines were established. So it may have been that at that—those were the moments.

WEBB: Yes.

BERY: So there was that period.

Then after a year away I actually came back and was secretary of the research committee for the first year after I came back in '78-'79. I mentioned this to John *[Lewis]* when he and I talked, and that was interesting because that was when Arthur Lewis was commissioned to do a review of Bank research.

So, you know, if one had to shape the period '72 through '79, I would say that I was kind of witness to the whole *[Hollis B.]* Chenery build-up and its ratification by the Lewis panel and the whole kind of concretization of the role of research in the Bank which really got going I think only after Chenery arrived and after the '72 reorganization.

Then from '79 'til '84 that was really the first time I was in Bank operations as a country economist on Yugoslavia, and this book is relevant to that. And that was coincident with, of course--I mean, I had done a lot of country work from DPS *[Development Policy Staff]*, but this was the first time I was in the "belly of the beast," as it were. And that was coincident with the transition to adjustment preoccupations, if you will, and the Yugoslavia SAL *[structural adjustment loan]* was one of the early ones and not one of the very successful ones, I think, with hindsight. There was a lot of learning to be done. That went on 'til '84.

And from '84 to '88 was something of a time out, although it was for me a continuation of the kind of adjustment phase, because I was then recruited to EDI *[Economic Development Institute]* to try and, you know, design a curriculum and a set of offerings to reflect the evolution in the Bank from the "investment bank" of McNamara to the "policy bank" of the '80s. And basically EDI in the McNamara period had been the main purveyor of project evaluation. I mean, in the '70s post *[Ian M.D.]* Little- *[James A.]* Mirrlees, and *[inaudible]*, et cetera, project evaluation had become, you know, the accepted methodology. And all through the '70s project evaluation, the project cycle, project management, this was the way in which EDI tried to prepare the borrowers for interacting with the Bank and for the big expansion in project lending that McNamara attempted through the '70s. And then, of course, that all kind of came to a fairly shattering halt around 1980, '81 because of the debt crisis and stagnation in the West and high world interest rates and terms of trade and all of that hit simultaneously. And then EDI was reoriented to become more of a policy institution. I was on a task force headed by Shahid Husain that predicted a new role for EDI in the early '80s since I was recruited, as I say, to try and define and design the national economic management curriculum which was really the management and content of structural adjustment.

And I did that until '88 when I was recruited to this job, as COD *[Country Operations Division]* chief for the Southern Cone. And that meant that in, amongst other things, that I actually sat out the '87 reorganization in EDI, which was not touched per se. I mean, its location in the Bank got altered, but its internal structure was not altered because it had been through its own reorganization in '83-'84 when *[Christopher R.]* Willoughby took it over.

KAPUR: You arrived in COD here before or after that major battle with the Fund?

BERY: Again, literally the week of it. I started exactly four years ago tomorrow, July 1, 1988. I had a month of intensive Spanish training, and I was due to start proper work August 1, and I think August 7 the decision was taken for the Bank--or the Argentines launched the so-called Plan Primavera. Husain was recalled from Ecuador where he was on Spanish training, and he went down more or less the whole month of August to Argentina for the preparation of the big Argentine package.

So I guess just retroactively putting some shape on it, I would regard what I have to comment on in the ‘70s as being the development of the intellectual side of the Bank and the ‘80s as really being the adjustment story. What I'm not a very good commentator on is actually what was going on in investment lending in any one of these periods. I mean that's a side of the Bank's work that--in a sense slightly surprising if one’s been around as long as I have that I've had much more superficial involvement with *[inaudible]* than others of my contemporaries like Harinder Kohli or Malcolm Rowat. These are all people who cut their teeth in the ‘70s on the bread-and-butter project lending of the Bank. But that's an experience that I know at some distance and not intimately.

WEBB: Yeah. You know, one rather specific question, taking advantage of your public finance start, one of the things that strikes me is how little the Bank seems to have done to attract and, let's say, analyze in some ways public investment growth. Do you share that? Am I wrong on that? It's just an impression I have. It seems--one would think . .

BERY: In aggregate?

WEBB: Well, country by country, and also behavioral characteristics across countries. But I would think this would be, as it were, a central unit for analysis of relationships by the Bank. And I know there was a lot of talk about this in the ‘50s, ‘60s, of an investment program. People did go and look at investments all the time, but . . .

BERY: I think it's a theme. My sense is, Richard, it's a theme that kind of bobs up and down. It never quite disappears, but it never quite succeeds, either, because somehow the methodology and the staff resources for doing it always end up kind of exhausting the initiative of—I mean, I can think of at least three phases in which this has been, you know, central and current. One is, of course, that when there were these big kind of foundation missions to countries like the *[Bernard R.]* Bell mission to India and I think a similar mission to Indonesia--this was before you actually got to the so-called basic missions of Hollis’ time--but before that there were these kind of foundation development plan based reports by the Bank on countries. At that stage I think public investment was center stage. Then, I think, my sense is that interest kind of died down, and then in the late ‘70s again, stimulated in part by, you know, some work that Basil Kavalsky did, there were some articles on financing development, again I think it’s part of, maybe in the early days of the adjustment phase. Again, you know, people began to appreciate that there had been much both waste in public investment programs and that rationalizing public investment was necessary. So there was a wave of public investment reviews at that stage. I think there was one on Turkey that *[Bela]* Balassa headed with Jayanta Roy; I know that we on Yugoslavia were under pressure to do one.

But I would agree with you that, you know, coming up with a tight methodology for doing this in a way that allowed the Bank to make sensible cross-sectoral comments, we never quite got there. So a lot of the stuff tended to degenerate. I remember in the discussions on Yugoslavia to a rather anecdotal and propagandistic search for white elephants, everybody thought.

And, you know, I think that in the late ‘70s the Bank's interest in this, at least as I witnessed it, was motivated by the fact that people knew there had been wasteful spending coming out of the credit boom of the late '70s. You know, I mean it was obvious that the negative interest rate cum high liquidity combination of the late '70s was leading governments to kind of invest badly. And so since that whole situation turned around so suddenly, with the Polish crisis of, I guess, the fall of '81, the first temptation of a number of governments was to--and I'm using Yugoslavia as a model here—was, you know, just to stretch out investment programs, not make hard decisions to close or to abandon projects. And so that was part of the atmosphere in which people thought, "Hey, we have to look at the aggregate of investments." But that's a long . . .

I think that the Bank obviously started off interested in individual projects. I think the Bank is comfortable still and has been throughout, particularly in certain sectors like electric power and transport, in--it has methodologies for dealing with the integrity of a sectoral investment program. And, for example, most Bank sector loans for power, for transport—you know, there are well-defined sector programming methodologies that the client uses, and the Bank has a review clause. So I think up to the sector level we've done pretty well. Where we tend to fall down is some notion of the inter-sectoral balance and what that should be in a normative sense and how governments--and I guess the work that you had done in the '70s, the work that *[Marcelo]* Selowsky and Lerman *[phonetic]* did on public expenditure incidence which is, of course, not just investment but investment and expenditure--absorbing that to have a view of the relationship between public expenditure and certain developmental goals, there I don't think we quite pulled that one off ever. And by the same token I don't think academia helped us much really in thinking that through.

WEBB: Right.

KAPUR: When did the Bank shift? I mean, you had these PIRs *[public investment reviews]* in the '70s, and then as one gets into the '80s you begin to see these so-called PERs, public expenditures reviews. Do you sort of recollect when PERs became part of the . . .

BERY: I think your key resource on this is Basil Kavalsky. Have you talked to him?

KAPUR: No.

BERY: Okay. He lectured on this topic actually, even for EDI, at about that time, and he was the person out of the country policy department, I think, at that time who was most involved in thinking about what are the circumstances under which investment reviews were warranted, what were the circumstances under which expenditure reviews were warranted.

But also, you know, I think that the more the Bank has got into the human resource area and the poverty area, you know, the more people have begun to find that the distinction between capital expenditures and current expenditures starts to kind of fade away a little bit. But I think it's fair to say that the attention to public expenditure analysis has typically been motivated by the negative desire to identify waste and inefficiency rather than the positive desire to link expenditures to developmental goals, if I can draw that distinction.

WEBB: I remember in ‘83, ‘84, those were the years, ’82 even, when the roof was falling in and the floor was falling out from under us.

BERY: This was in Peru?

WEBB: Yes, in the government in Peru. And there was an “economic team,” quote unquote, a bunch of young guys straight from the Bank, and of course we all agreed with the IMF and the Bank and with ourselves that we had to drastically cut public investment. Okay. So somebody had to do that. So they asked one of us, and one of us said, “Okay, I'll do it. Where's the list? What are the cutting?” Well, there was no kind of list. And then how on earth do you begin? We didn't have an absolute clue what was involved in saying, “Here's this area in which a project’s started; we've spent so much this year. Do we stop it? Interrupt it for five years? Or cut it altogether? Or cut down the spending from 20 million to 10 million?” To try to find out what was involved, the contracts that were involved, a lot of expenditures are--that's a given, there are legal givens. I didn't know that. For a long time I didn’t know that. Then there are interrelationships between projects. There are things that make sense and that don’t, but technicians, the specialists, engineers, you talk to those people and they say, “Oh, no! You can't cut this! Impossible!” So you couldn't get any real information from those people. Well, we were totally ignorant, and we never got the slightest bit of help from the Fund and the Bank. It was kind of—it was one of the things that really amazed me. [both speaking at once]

BERY: Well, let me pursue the point you're making there [both speaking at once]

WEBB: I just wonder whether this was an odd--maybe because I didn't ask enough, or whether Peru was unusual.

BERY: Yeah, I think the larger issue is a different one.

WEBB: I wonder that the Bank has so little, general sense of this.

BERY: Well, I wasn't really addressing that issue. I was addressing, you know, the kind of basic design issues, whereas the question you're asking--which is difficult to disentangle; I accept that--is really, you know, what assistance does the Bank provide upon implementation of any of this stuff

WEBB: When you’re cutting back.

BERY: Yeah.

KAPUR: Especially adjustment, you know, when it became inevitable.

BERY: To me, that has been--well, look. There are two, you know, approaches that have been taken: the approach of the Fund--I'm talking now about the issue of implementation of policy actions rather than investment actions. And I think--as I say, I'm not that knowledgeable about investment lending per se, but as an observer and an outsider and also as a Young Professional I did go on some of these projects, project missions, the Bank in those days had some feel for a methodology of getting stuff done. I mean, you had workshops. You had action plans. And, of course, there was the whole business about the disbursement of funds being associated with physical execution. So implementation monitored through supervision was a vital concern of the Bank.

But when you got into the policy areas, the Fund, of course, has always taken the view that implementation is the government's responsibility. And it's taken that view in part because, as I see it, it started off as an institution for developed countries and you could make certain assumptions that the . .

[Interruption]

BERY: My criticism—so the Fund's attitude, as I say, on all this stuff has been very lofty. You and we agree on the targets, and then how you achieve it is your lookout. And they've adopted that view in part because, you know, they--it's a way of evading to some extent political responsibility. You know, "We aren't responsible for cutting the school feeding program; it's the government's choice." So that was the Fund approach since time immemorial.

I don't think the Bank's approach was quite as clear cut or well established as that, but I think that the Bank just did not invest the intellectual effort in discovering what is involved in implementing macro policy in countries, even when it got into the adjustment lending business. And this came across abundantly clearly to me in my EDI phase, you know, when all these guys said, "Okay, you've persuaded us on the 'what.' Now tell us the 'how.'" And there was damned little experience in the minds of people in the Bank, firstly, but damned little effort made by the Bank, you know, to tap what experience was accumulating in the world on these issues. And I think the Bank is culpable on that.

I think that—and as you possibly know, Richard, the little bit of academic literature on this associated with Merilee Grindle and Joan Nelson and these people tends to make the point that the failures of these programs is just as much because of inability to implement as it is because of backsliding in the, you know, sense of volition. And when you consider what the costs to countries of failure--failure as measured by conditionality not complied with, as measured by falling out of favor with the rules of, you know, the evolving rules of the game in Washington and the so-called Washington kind of census or cabal--I think that there is a real issue and story there about whether the Bank could have done more to educate itself and help countries on the implementation when it got to the adjustment phase.

Now, you approached the issue in a different way. I thought you were approaching the issue in terms of "Has the Bank had a considered view of what it wants done in public expenditure?” I see your preoccupations as more being in this other area, that when the emergency hit . .

WEBB: That's just an example, really, because it's a more general question. For instance, I'm amazed at *WDR [World Development Report]*, all these marvelous statistics, no figures on public investments. I would have thought that be the number one figure for a *WDR*, public investment. I mean, this is what it's all about. This is the Bank's business. This is, as it were, the Bank's market.

BERY: But in the structure of expenditure table, isn't that where they talk of public and private savings?

WEBB: That’s savings, yeah.

BERY: And the aggregate investment is not broken down?

KAPUR: No. In fact, the first source . .

BERY: Is DFS.

KAPUR: . . no, it’s actually--given the IFC *[International Finance Corporation]*. Guy *[Pfeffermann]* has been doing this private investment and public investment as annual things, and the Bank itself—you know, I mean, IBRD *[International Bank for Reconstruction and Development]*--the Bank was uses that to see public investment.

BERY: But surely in world tables, I mean . . .

KAPUR: Well, it's not there because I checked up, and then I saw in Johannes Linn's paper he uses Guy’s figures. You know, Johannes Linn’s thing on impact of *[inaudible]* IBRD lending in the ‘80s, the figures on public investment and everything he uses Guy’s figures. So I called up Guy to ask him, you know, and he said, “You know, it's never there in the Bank.”

WEBB: That's just an illustration, really, Suman, that prompted my question.

BERY: Okay. But . . .

WEBB: We could talk a little bit about the actual adjustment experiences.

BERY: Your—in a sense your starting point is--you're updating the story from *[Edward S.]* Mason-*[Robert E.]*Asher?

WEBB: No, no.

BERY: So you’re going back further than that.

WEBB: Yeah.

I mean, the Yugoslavia experience, did you see--were there interesting differences there with what you later saw in Latin America in the way things were handled? Was it—I mean, to me it's always fascinating how the Bank has dealt with socialist countries.

BERY: Well, you know, when I was there, if you like, over the transition from boom to bust, because the story was quite similar to, say, the Mexico story where you had--of course, they didn't have much oil of their own, so there wasn't the flush of ‘79 oil price increase as there was in a place like in Mexico. But nonetheless, I mean Yugoslavia--like most developing countries, I guess--didn't suffer that much from the ‘72 crisis because they kept borrowing, and borrowed at terms that seemed cheap because there was all this new *[inaudible]* around. And I think the first lesson I would draw is that it takes, given the Bank environment anyway, it takes a very clear-eyed person to say that the punchbowl should be taken away when the party is still going. I mean, I know that that’s the role that we ought to be playing. I know it is the role that we--I think we play it more now than we used to. But when countries are racking up seven, eight, ten percent growth, cries for caution by individual Bank staff tend not to be heard very well.

So, for example, you know, China today. I'm not close enough to know whether what is going on is sustainable or unsustainable. Let us argue that in some sense it's financially unsustainable. I think it would take an extraordinary act--just given the sociology of the institution--an extraordinary act of leadership and self-confidence for the lead economist on China or the director on China to say, “Hey, this thing can't go on. We've got to size it back.” That's just not the way the Bank is set up. The Fund is set up that way. But we are in that sense, I think, a naturally, you know, bullish and buoyant institution.

WEBB: It’s funny. I remember I was talking to Mr. *[Toyoo]* Gyoten at a lunch and remembering the early Bank support for Japan, and one of the points he was making was that the Bank has always been too cautious.

KAPUR: Same thing with Ray *[Raymond J.]* Goodman on Korea [both speaking at once] when we talked of *[Chung-Hee]* Park, and, you know, all the *[inaudible]* scheme and all those and the Bank would say, “No.” Park would always listen and then promptly do the opposite.

WEBB: Yeah, it's the same. Gyoten said, “Yeah, we listen, but we never paid any attention, fortunately.”

BERY: I see. So it goes both . .

KAPUR: But in the early days, in the ‘50s and ‘60s, it appeared the Bank was much more cautious.

WEBB: Yeah, you get this sense of the Bank being more “World Bankerly” in a way.

KAPUR: And then the McNamara sort of *[inaudible]* I mean, you're absolutely right, the optimism, bullishness, "we can do it," you know, that sort of became embedded in the whole institution.

BERY: Okay, but let me just step back here, let me summarize, give my summary judgment, and then try and amplify it, and that is that I think—I mean this comes back again to my time in public finance area--I don't think anybody in the late '70s appreciated that the warning signs were almost all in the fiscal area. I think people concentrated on the BOP *[balance of payments]*, concentrated on external financing with the notion that sustainability was really . .

[Interruption]

BERY: . . that sustainability really depended on the public finances and public solvency and that those were the lenses through which the viability of an economic strategy needed to be judged. I think that realization was absent in those periods.

WEBB: That's a very good point. Yeah.

BERY: And I think, you know, I'm seeing this now. I mean, I've seen this three places now. I mean, Yugoslavia, where you had this transition from seeing a problem as a--of course always the destabilization aspect because of inflation--seeing the problem as a trade problem and a balance of payments problem and only finally beginning to see how the public finances radiate through all of the solutions and how, you know, how central and how difficult the fiscal adjustment is. Then Argentina. And now India, where, you know, there are a couple of far-seeing people like the finance minister, Montek Ahluwalia, who do see the fiscal as central. But everybody else will go through a kind of a period of denial, thinking that you can mess around with exchange rates, that you can mess around with the trade, you know, solve the problem.

So I think that that realization was not there, either in the Bank or in the Fund. And I think we--what, I mean that was particularly obscured by the different institutional structure, you know, the fact that there were six republics, and there were all kinds of deals going back and forth, and that it was a foreign language. You know, these things matter when you're trying to make an economy transparent to you and you don't really speak the language, you're operating with translators and stuff like that. All this stuff does make it that much more difficult. I'm sure people working on China today have some of that sentiment as well.

I'm not sure that I've answered your question. Your question really was--the basic point I'd make about Yugoslavia versus Argentina was just that I think that collectively the Bank has moved to a much more crystalline view of the world of fiscal adjustment and the whole process. I think that that learning is now being applied in CIS *[Commonwealth of Independent States]*, for example. I think that people like Schroeder *[phonetic]* and Kemal *[Dervis]* and all these people have internalized how to think about inter-temporal sustainability of the public finances in a way that we just didn't know how to think about at the beginning of the ‘80s. I think that there was a process of collective learning. But to the Bank's credit I do think that this is an area of analysis in which the Bank exercised leadership and more or less wrote the book. I think there is the kind inter-temporal fiscal feasibility model associated with Schroeder and his work on Turkey, which has now become generalized . . .

WEBB: I'm sorry. What does that mean? Inter-temporal fiscal? What is that referring to?

BERY: Well, it's referring to, you know, what is the sustainability of the financing patterns of the government. I mean, to what extent do future tax revenues make it likely that the debt burden can be serviced. What is the implicit need for an inflation tax? The enclosing fiscal accounts . . .

WEBB: I mean, is this something more than . . .

BERY: Well, yes. I mean, it's all of those, but it's a question of seeing how--actually, it's no more than that. It's just that to the extent that the traditional mode of analysis in the Bank was balance of payments at two gap, this gives much greater primacy to fiscal projections and to the issue of the impact of certain other instruments, particularly the nominal exchange rate on the fiscal feasibility of—on the feasibility of a fiscal *[inaudible]* because particularly when you’ve have substantial foreign debt, as you know, the nominal exchange rate has a significant impact on the fiscal burden and measured in domestic--so it is a question of integrating fiscal concerns into economic management more than had been the case.

WEBB: One of the things that strikes me—I mean, I'm just amazed at how ignorant, I think, we've all been or we were in the early ‘80s when all this was beginning, at how grossly we underestimated the degree of recession that would be involved and the difficulty of bringing down inflation. But one of the . . .

BERY: It depends on the country. There is no inflation in Malaysia, virtually no inflation in Thailand, and yet they went through adjustments that were--I'm told; I haven’t looked at the, I don't have the comparative numbers at hand—but my understanding is that the nature and the work of Balassa and the *[inaudible]* that people did that I think the actual magnitude of the shocks that a lot of the East Asian countries suffered, Southeast Asian countries was no less.

WEBB: Well, to me that makes us even more ignorant because we don't really understand--I don't think--why the difference. But certainly, where there was substantial inflation sustained, no one was predicting that it--everyone was always saying it was going to come down in a couple of years, and it would be, you know, a lot easier than . . .

BERY: To me on this, apart from Schroeder's work, the other classic [both speaking at once]

WEBB: I’m sorry. The reason I brought this up was because one of the mechanisms that was very much a part of all this, I thought, was the relationship between recession and revenues, because the recession, the fiscal problem of underestimating, new taxes were being created but the economy is sinking, total revenues were going down. Did you have a sense of this going on at that time? Do you agree with that characterization?

BERY: Well, you know, this is of course the great criticism of the *Wall Street Journal* of the Fund *[inaudible]*

WEBB: The fiscal, yeah.

BERY: Well, not only fiscal, but it’s, you know, that these are recessionary strategies rather than growth.

WEBB: You know, I'm not saying that because I'm suggesting that the Bank and the Fund should have been less strict and therefore a little more *[inaudible]* or anything of the sort. Maybe they should have been stricter and you would have had less recessions. I don't know. I just have this feeling of ignorance, fumbling around crude ideas.

KAPUR: You were about to mention some of the classic works other than Schroeder’s?

BERY: Well, this little paper by Max Corden in the *[World Bank] Research Observer* about two or three years ago on internal investments and fiscal balance.

Really, all I'm saying, Richard, is it’s so . .

[End Tape 1, Side A]
[Begin Tape 1, Side B]

BERY: We all focus on the *[inaudible]* of external lending or borrowing as an external financing problem, okay? Because that is what the Bank's tradition of RMSM *[Revised Minimum Standard Model]* projections and what have you, that was where the searchlight was. And the searchlight was there because of, you know, two gap analysis, Chenery and *[Alan B.]* Strout, this kind of stuff.

What all of us were missing was that this stuff had become a very important part of below-the-line support for public finances because the entities that were borrowing--well, two stages, of course. The first stage is that a lot of the entities that were doing the borrowing were public sector entities, okay? And so if their financing was cut off, they were in any case the less flexible parts of their economies and so the financing had to be found somewhere else. So that was, if you like, the first round effect. The second round effect, particularly in Latin America--I don't think other countries did this to the same extent--was socialization of the private debt so that, you know, and this was much more--although it was also a phenomenon in Yugoslavia because, I think, the analog between Yugoslavia and the Latin American countries is that Yugoslavia by constitution and the Latin American countries by persuasion of the international financial community ended up putting all these obligations in the public finances by taking over the debt burden and took it off the burden of their private sectors and put it onto the burden of the public sectors. And so that is the way in which it became an even more acute fiscal problem. I mean, a number of countries--Mexico, Indonesia, Argentina, India--in any case had been using their public enterprises to be their borrowing vehicles. I remember Pemex. I remember Pertamina, in India ONGC *[Oil and Natural Gas Corporation of India]* and ICICI *[Industrial Credit and Investment Corporation of India]*. .

WEBB: In Peru it was that way, too.

BERY: . . in Argentina YPF *[Yacimientos Petrolíferos Fiscales]* and the big power companies or Intel, the telephone. So, I mean that was the configuration of public financing that got established in the period '73 to '80, you know, post the first oil shock, increase in liquidity, the negative real interest rates, and the growth of kind of the London syndications market. That was the '70s, right?

And then [snap] with *[Paul A. Jr.]* Volcker the party came to an end like that. And all of us started worrying about below the line, but we started worrying about balance of payments and trade adjustment. It took us longer to realize that another aspect of this was that this stuff that was actually going into public finances, so that there was a fiscal adjustment needed. And that fiscal adjustment, because all fiscal adjustments are--including in this country today--are intensely political acts, was not--it wasn't indulgence. It needed autonomous policy action every grinding inch of the way, and that's what has proven to be so hard. It proved to be hard in Yugoslavia, and I think that's one reason why the country split apart. It has proven to be hard in Latin America. And, you know, it basically took *[Augusto]* Pinochet in Chile to kind of pull it off, and it took the actual experience of hyperinflation in Peru and Argentina to create a climate within which people were willing to swallow the bitter pill, so I see the history of the '80s as being the fact that the trade adjustment happened quickly but that the fiscal adjustment was just, just painful.

WEBB: I'm curious. In Peru, the way I see it--I wrote an article on this--was that most of the adjustment occurred before the quote unquote "adjustment," in other words there was de facto adjustment. Did it happen that way in Argentina, or was it more because of *[Domingo F.]* Cavallo's measures?

BERY: That's a good question. No, no, no. Certainly not Cavallo's measures.

No, I mean I think there was a disorderly adjustment which meant that the share of public--what happened was the disorderly adjustment consisted of the following dynamic sequence: public expenditures being squeezed through inefficient means, cutbacks in investment and cutbacks in civil service salaries, an erosion in the level of services provided by the state, leading to a kind of breakdown in the implicit social contract between the state as provider of services and the state as tax authority, leading to in effect a tax strike by those who were due to pay their taxes because they couldn't see any benefit that they were getting out of it, leading to erosion then on the revenue side, leading to a hyperinflationary explosion and then, you know, the thing being put on a more orderly basis by various tricks like—well, through more genuine recognition of the expenditure erosion that had taken place, through kind of more structural measures.

Well, actually, what's made it possible in Argentina, let's be honest about it, is the sale of assets, okay, the sale of assets providing some credibility that the government in the future would have enough money to do two things: (a) collect taxes properly, i.e., that it would have the administrative capacity to collect taxes; and (b) although they haven't reached there yet, that a modicum of core public goods would be provided so that there would be some reason for paying taxes. But I regard this as still being, you know, to some extent on notice. I mean, if the system does not perform better with basic social services, public services, then I'm sure the tax strike—people will go on tax strike again.

WEBB: Argentina brings up another central question--I'm sorry to butt in, but--exchange rates. How have you seen Bank thinking about exchange rates over the '80s?

KAPUR: That it stopped growth at the Fund, almost.

WEBB: Why do you say that?

KAPUR: Well, I mean, the inflation rates one sees *[inaudible]* than in the '70s or '80s. And the Fund, you know, then in Africa particularly--you see that the Bank, because it's much more preoccupied with trade issues seems to be more hawkish. In fact, I was always amazed to see *[inaudible]* on India or in *[inaudible]* a lot of countries as much as they devalued, they always are below that: "Well, but they could devalue more." I almost never see the *[inaudible]* on a country in the '80s where the Bank would say, "Well, you know, this is about a reasonable amount."

BERY: Look, I don't think it's just the Bank. I think the whole profession is totally messed up on nominal exchange rate policy.

WEBB: Just one question on this, on the—I mean, it's pretty evident that the Bank have has different ideas on. Is this something there is a lot of debate about?

BERY: Well, certainly over here.

WEBB: Within the division? A lot of debate as to . .

BERY: The region, department, region--it's nonstop at the moment. I don't know . .

WEBB: Is this on record, some of this debate? Or does it tend to be highly confidential and therefore not written down much?

BERY: Well, I don't know about other departments, but over here there are papers like this floating around. *[seems to hand over a document]*

WEBB: Uh-huh. I see.

BERY: I mean, you know, obviously these things have to be embargoed to a certain extent, but there's a pretty lively internal debate.

WEBB: Probably more than anything else.

BERY: What? More reserved or more debate?

WEBB: More reserved, yeah. It's, well, I mean, so much potential speculation is involved.

BERY: I would put the matter slightly more broadly. I mean, for me the biggest learning of starting work on Argentina has been to try and grapple with macroeconomic policy.

[Interruption]

BERY: Yeah, I think this is an important point. I think that the Bank's whole thinking on macroeconomic policies has really not caught up with open capital accounts. And, you know, it's certainly been something I've had to teach myself in this job, that a lot of, you know, a lot of the knee-jerk reactions from the '70s about exchange rates, monetary policy, fiscal policy, they end up--as we've discovered with the developed countries--they end up having very different power and value. And with an open—I mean, this is basically the contribution of *[Michael J.]* Mandel, but it's still not--I mean, people at the Fund, because have to worry about these things more, but they are smarter about these things, I think, than at least the average Bank person or even Bank economist. Now, I think that at the leading edge some of the Bank's thinking on this topic is probably more sophisticated--or as sophisticated--as the staff in the Fund.

WEBB: Who is leading edge here on this?

BERY: Well, I think Jim *[James Q.]* Harrison is. I think Schroeder was or is. I think Homi Kharas, who now works on the Philippines, I mean I think he understands the stuff.

Actually, I don't want to underrate the Fund. I mean, obviously, people like *[Guillermo A.]* Calvo and *[Jeffrey A.]* Frankel when he was there and Mike *[Michael]* Mussa, these guys know this stuff cold. They've written the book on it.

KAPUR: Stan *[Stanley]* Fischer also has . .

BERY: Yeah, I mean, he's certainly written textbooks on the subject. But I would say that, you know, the kind of revolution in thinking--this comes back to, if you like, my '70s experience in the Bank rather than '80s—you know, the kind of obvious systematic effort that Bela launched to get people thinking in a certain way on trade policy and in a different area than Warren Baum and *[Christopher L.]* Hermans pursued to get people thinking in a certain way about projects and the projects cycle, the Bank has not really had that kind of champion on the macro--ever. And so there isn't therefore a consolidated

Bank view in thinking about these things as there is in those other areas.

And so, you know, I think a lot of the subtlety that's needed to think about exchange rate policy under a variety of macroeconomic circumstances and, you know, relationships between nominal exchange rates and real exchange rates and labor market preconditions and all this kind of stuff, which is quite complicated, I think it is not that well disseminated in the institution. And neither does the institution, I fear, have the quality control mechanisms to ensure that the advice that's going out to the countries--but I don't want to accuse just the Bank. I mean I think that the Bank in the early ‘80s when the Fund was providing exchange rate policy advice to Yugoslavia, we were a little bit, kind of—I mean, we were involved, but we were taking a backseat on the issue at that time. I think the Fund did give some erroneous advice that was far too responsible for the descent into hyperinflation in that country as well.

WEBB: Did they recommend devaluation?

BERY: No, they recommended, in effect, one of these kind of progressive indexations schemes that you should always depreciate to . . .

WEBB: *[inaudible]*

BERY: I mean, that was one aspect of it. I'm sure this was kind of public finance crisis was--but, you know, this is my point, that all these things get involved, and that's what I mean by *[inaudible]* that if you recommend that kind of policy as a trade or exchange rate measure, but you're insensitive to the fact that this might have an impact on the public finances because of the fact that there is foreign debt. That, then, has its impact on the need for an inflation tax. That, then, has its impact on the next round of the indexation. And whether you are in a converging or an explosive cycle depends on, I would imagine, on certain parameters and whether anybody actually models these things to know whether the cycle closed or exploded, those, I think, are some of the things that people are not sensitive to. Okay?

WEBB: Yeah.

[The last few minutes of this interview were a bit difficult to understand; the interviewee was trying to rush off to a meeting.]

[End Tape 1, Side B]
[End of interview]