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Remarks

Prepared for Delivery by

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President

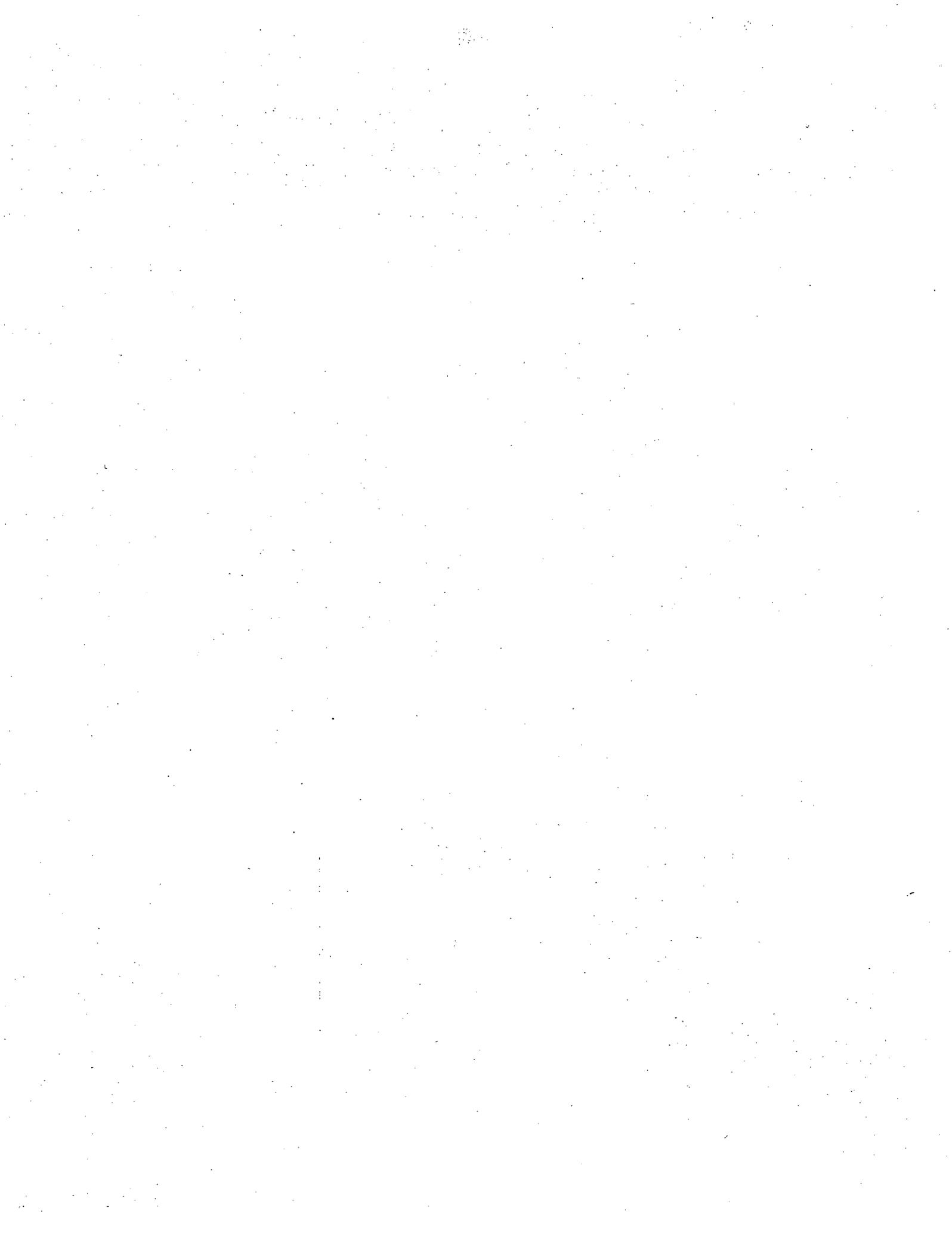
The World Bank

before the

Council on Foreign Relations

New York

September 23, 1982



Thank you, Mr. Peterson. a/ Good evening, ladies and gentlemen.

It is indeed an honor to appear before the Council on Foreign Relations. Over the years, this group has repeatedly helped to encourage the United States to provide positive leadership in international affairs.

Right now, the world economy very much needs positive leadership from the United States. This is a time for vision. We must all rise above the immediate short-term pressures we confront, and look ahead to the longer-term effects of actions we take in response to pressing problems.

America's destiny is deeply entwined in the broad political and economic trends of our planet, and our world is bound to become yet more inextricably interdependent in the years ahead. So I am troubled that many Americans do not yet sufficiently appreciate how much their own interests are served when the U.S. provides strong, generous leadership in international economic affairs.

a/ Mr. Peter G. Peterson, Chairman, Lehman Brothers Kuhn Loeb, is to introduce Mr. Clausen.

We've just come back from the Annual Meetings of the Governors of The World Bank and the International Monetary Fund in Toronto. Although we've seen some encouraging economic signs lately, those meetings were sobered by Mexico's financial troubles, and by the frustrations which finance ministers from all around the world expressed.

In these introductory remarks, let me report to you that we reached a convergence of views at Toronto. We found general international agreement on three broad lines of action to help us recover non-inflationary growth. These are: disciplined economic management by national governments, liberal international trade, and reliable flows of financing to the developing countries.

Now, over the next few months, is the time for follow-up action! And successful international action toward economic recovery will depend, more than anything else, on positive leadership by this country.

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The current situation clearly calls, first of all, for disciplined economic policy management by governments.

The industrial countries still account for two-thirds of global production. The U.S. alone accounts for roughly a quarter of everything produced in the world. So global levels of inflation and growth depend mainly on the policies of the U.S. and other industrial countries.

The industrial countries have relied heavily on monetary policy to fight inflation, while their fiscal deficits have remained quite high. And this has made the struggle to recover non-inflationary growth unnecessarily long and painful.

We all hope for a new surge of investment, which is, after all, the main engine of growth. But private investment has been stalled by high interest rates, and securing stable, low rates of interest demands a better balance between fiscal and monetary policies.

Disciplined economic management is no less essential for the developing countries during these difficult times, and The World Bank is increasingly stressing sound economic policies in its dialogue with our borrowing countries. We aim to help them reduce their balance-of-payments deficits without unnecessarily restraining growth.

This often calls for fiscal discipline to control inflation. As a group, the developing countries are putting more of their income into investment than the industrial countries are, but we often suggest how they can make more efficient use of their investment -- by giving better incentives for efficiency in agriculture and industry, for example, or by channelling more investment into the conservation and domestic production of energy.

Sound economic policies are always good tonic, but during these years of adjustment, they have become essential medicine. That's the message we're giving our borrowing countries, and the health of the global economy depends even more on disciplined economic management in the U.S. and the other industrial countries.

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At the same time, we need to recreate dynamic conditions at the global level to support the efforts national governments make toward economic recovery. So let me turn next, then, to the issue of liberal international trade. On the trade front, we've got a big opportunity coming up this November -- the GATT Ministerial meeting.

The upcoming GATT Ministerial will be the first such high-level conference organized by the General Agreement on Tariffs and Trade since the Tokyo Round began in 1973. The U.S. was imaginative and forceful in bringing the Tokyo Round negotiations to a successful conclusion. But noisy disputes just now among the U.S., Europe, and Japan threaten to divert attention away from the common business of preparing for a new round of negotiations.

Nowadays, nearly a fourth of everything produced in the world is traded internationally. That proportion doubled during the Seventies. And because of the increased integration of the world economy, bowing to protectionist pressures now is even more dangerous and disruptive than in the past.

The GATT meeting in November could be a historic event! If the ministers can get beyond a general reaffirmation of the principle of liberal trade to specific progress on trade issues which still need to be resolved, this meeting could -- together with falling price levels and interest rates -- help to mark the end of our economic disarray.

One of the most important breakthroughs the ministers might achieve would be defining a process toward free trade with the developing countries. More than any other factor, trade has contributed to the economic dynamism of many developing countries. And, as a result of such dynamism, the United States, for example, now exports 60 percent more to the developing countries than to Western Europe.

On the other hand, many of the developing countries still retain high barriers to trade, and both we and they have lost tremendous potential benefits because of it. So the Ministerial should start discussions about how to focus more attention on trade items that are important to the developing countries.

The GATT Ministerial could also plow new ground on the possibility of agreed rules for private international investment. Such rules would stimulate more foreign direct investment, especially in the developing countries.

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This brings me to the third and final broad line of action -- in addition to disciplined economic management and liberal trade -- on which we discovered general agreement in Toronto: reliable flows of financing to the developing countries.

The net flow of capital to the developing countries has more than tripled -- in real terms -- over the last two decades. In the early Sixties, about a third of this financing was from private sources, and considerably more than half was development assistance. Primarily because of the dramatic growth of commercial bank lending, those proportions have just about been reversed. More than half the new financing developing countries now receive comes from private sources, and only a third is development assistance.

It is essential, both for the developing countries and for the stability of the international financial system, that net levels of financing, both commercial and official, be -- at the very least -- maintained in real terms.

It is, therefore, imperative that the commercial banks continue to play their crucial role in providing funds to nations with payments deficits. This is a moment for prudence by commercial banks, but certainly not for retreat.

The World Bank, too, has weighty responsibilities for maintaining capital flows to the developing countries.

Allow me to explain that The World Bank consists of the International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA), and the International Finance Corporation (IFC).

IBRD borrows the bulk of its funds in the world's financial markets -- including, starting soon, the U.S. short-term markets. IBRD bonds are fully backed by the guarantees of its member governments; it lends no more than the equivalent of its capital plus reserves. IBRD makes a profit. And IBRD lends only to creditworthy countries; it has never faced a default, despite the fact that it has a firmly applied policy against rescheduling loans.

IDA is our concessional finance affiliate. Its approach to project appraisal and supervision is just as tough as that of the IBRD. But IDA extends credit to the poorest of the poor countries of our planet (for 50 years at zero percent interest), and IDA is funded mainly by contributions from donor governments.

IFC is an affiliate of The World Bank that deals primarily with the private sector. IFC can make loans without any government guarantee, and it also takes equity positions in commercial corporations in the developing countries.

The World Bank, together with other official financial institutions and aid programs, provides an essential complement to commercial investment in the developing countries. Our lending is long-term, and we advise borrowing governments in ways that private lenders cannot.

On the whole, the credit record of the developing countries is a sound one. But the swiftness with which Mexico recently fell into financial difficulties again demonstrates how essential it is that we strengthen the short-term and long-term support which the International Monetary Fund and official development agencies like The World Bank provide.

When The World Bank was founded, back in the Forties, its architects expected that its main activity would be supporting private investment, not lending its own funds. It seems the time is now ripe to expand the Bank's collaboration with private investors.

We are doing this in a variety of ways. We built \$1.8 billion worth of private co-financing into projects approved by the Bank in fiscal year 1981, we raised that to \$3.3 billion in private co-financing in fiscal year 1982, and in the next few months we will be introducing new co-financing techniques. We're also examining the possibility of a multilateral insurance scheme for private investment. Meanwhile, IFC completed more project agreements last fiscal year than ever before, and it has a record number of projects under preparation.

In addition to contributing to the stability of the global economy, official financing (and particularly concessional financing) also reaches countries that would otherwise be excluded from the international financial system. Seventy percent of commercial lending to developing nations, for example, is concentrated in just 13 countries. Most developing countries aren't able to meet their legitimate needs for foreign exchange in the capital markets.

Roughly half the world's population lives in countries which are too poor to qualify for IBRD lending, let alone commercial lending. IDA is the major source of concessional finance for these poorest of the poor countries. So it is distressing that we had to amputate 35 percent of our fiscal year 1982 IDA program, primarily because the U.S. failed to meet its previously agreed IDA commitments.

The decision of the U.S. administration to fund the U.S. commitment to IDA's sixth replenishment in four years instead of three, as originally planned, provoked a crisis in IDA funding. At the Toronto meetings, most of the donor nations except the U.S. agreed to pay in their commitments to IDA6 in three years, despite the U.S. shortfall. And they agreed to provide an additional \$2 billion in fiscal year 1984, while the U.S. is finishing up its commitment to IDA6.

The world recession has hit many of the low-income IDA countries hardest, and the other donor nations are coping with difficult budget problems in these years, too. The generosity of the other donors is a triumph for international understanding. It is based, however, on the clear commitment of the U.S. administration to work to complete its IDA6 contributions within about the next 18 months.

The donor nations also agreed in Toronto that they will begin negotiations for the seventh replenishment of IDA this November. If these negotiations are to be creative and successful, we will need leadership -- not indifference -- from the United States.

Finally, in this connection allow me to comment briefly on the acceleration of military spending that is currently underway in this country. I appreciate the arguments that are made for substantial defense budgets, but the very rapid rise in military spending has crowded out development assistance programs such as IDA. And is it unreasonable to assert that an increase of a few hundred million dollars in U.S. contributions to IDA would do more for international security than a similar amount added to the U.S. military budget, which already runs into the hundreds of billions of dollars?

The World Bank is innovating in a number of ways to make maximum use of the resources entrusted to us in maintaining the flow of financing, both commercial and official, to the developing countries. But we need support from the major economic powers to do our job.

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To sum up graphically, the nations of the world find themselves together in something of an economic swamp. We know, in general, some directions we should be moving to get out. But we need strong, generous leadership to get the nations of the world moving together toward economic recovery.

It is clear that disciplined economic management, liberal trade, and adequate financing for the developing countries will help us toward economic recovery. And we can take giant steps in those directions, in the next few months, at the GATT Ministerial and the IDA7 negotiations.

Pete Peterson wrote in a recent article that people in this country need to "come to grips with our ignorance, apathy, despair, and cynicism toward the Third World." Well, we've got to find ways to help people bust out of these negative attitudes, and to wake up to the possibilities of positive U.S. leadership within the world economy.

With these general remarks as background, then, let me welcome specific questions or comments. In particular, I'm expecting to get some good advice for our work at The World Bank from our discussion together.

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