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ORAL HISTORY PROGRAM

Transcript of interview with

Richard H. Demuth

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Interview with Mr. Richard Demuth

By Robert Oliver August 10, 1961

Interview # 1

Q: Now, sir, will you give your name?

Demuth: My name is Richard Demuth. I joined the Bank in July, 1946, in the very early days. My training was as a lawyer. I had been in private practice and with the government before the war. I went into war service. I first had international experience with the Allied Control Council in Germany. When I came back, I decided I wanted to stay in the international field, and a good friend of mine, General Swatland, of Cravath, Swaine and Moore, I discovered had recommended my name through Mr. McCloy to Mr. Meyer, who had just become president of the World Bank. Mr. Meyer asked me to come down and see him, and eventually offered me a job as his assistant. Without knowing very much about the organization, but intrigued by the job, I came down to work for the Bank.

Q: This law firm you mentioned is Cravath, Swaine—

Demuth: And Moore. That’s where Mr. McCloy was a partner, and Chester McLain the first general counsel. Meyer at first asked McCloy to become general counsel of the Bank. McCloy had been unable to accept it but recommended Swatland. Swatland, having been unable to accept, had recommended McLain. McLain was coming in and they suggested that I come in with McLain as part of his legal staff.

Q: Was this firm later changed to Cravath, Swathmore and something?

Demuth: It was then Cravath, Swaine, Moore, something like that. It's now Cravath and Moore. It's, I guess, the largest law firm in New York.

Well, I came in as a general assistant to Mr. Meyer, when there were practically no other members of the staff. Floyd Harrison, who was Mr. Meyer's personal investment advisor, was down here helping him. There was practically nobody except in the administrative services. McLain came on board shortly afterward. Luxford was already here, and gradually over the course of the summer, a number of people came who are still with the Bank—Rist, who was alternate to whoever was director for France, came on as the head of the economics department. Crena de Iongh, who'd been the Dutch Alternate Executive Director, came on as the treasurer. Dave Sommers came on early in the fall—gradually we built up a working staff.

In those very early days, we had a full time board of directors. They were terribly anxious to do something, and they sat around and created committees and decided all different kinds of policy issues, and the staff was kept terribly busy trying to write papers for these board committees. We never did have much time to really get to work, because we were attending committee meetings.

Very early on, the issue which subsequently became of major importance, the board-staff relationship, came to a head, not in a very clear form, but in an important way, even as early as the summer of ’46. The US director at that time, Pete Collado, was a very ambitious young man, and he was determined to run the Bank from the US director’s seat, and he had 33 or 35 percent of the votes. The US was putting up most of the money, and he felt the US had the right to take the lead in running the Bank.

Collado had a lot of connections in the State Department, with whom he was in constant contact, and I think one of Mr. Meyer’s difficulties was that he found himself fighting with the major supporter, the major stockholder of the Bank, the US, fighting with Collado for the initiative in running the Bank, rather than being supported by the US in what he was doing. Although Mr. Meyer never told me directly why he resigned, my own feeling is that he woke up one morning and realized he wasn’t happy. He’d had a number of very important jobs in his life, accomplished a great deal, had taken this job on at the urgent request of the President, and he found he wasn’t enjoying himself. The reason he wasn’t enjoying himself was that instead of running his ship, he was having to battle with the executive directors led by Collado all the time, and he just decided that he’d had enough.

He resigned with two weeks’ notice, not dependent on finding his successor, but simply gave notice of resignation that he was leaving two weeks later, the idea being that this would put a great deal of pressure on the directors to select his successor. Where were we going to find a successor that quickly? The company sort of . . . .

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Q: I wonder if you could say anything about some of the things that were at issue between Mr. Meyer and the board?

Demuth: Well, I don't think there was any very specific issue. It was more the question of the approach the Bank should take. Collado in particular was very anxious that the Bank should invest a lot of money and lend a lot of money very quickly. I think the first approach we had from an underdeveloped country was from Chile. Chile asked for 40 million dollars, for a completely undigested list of projects. Collado told Mr. Meyer that the Bank was darned well going to make this loan by December of 1946 or he'd know the reason why. Meyer pointed out that we knew nothing about Chile's economy or anything about the projects. Collado said he knew Chile, he'd known them for a long time, and they were good for 40 million dollars and the Bank was darned well going to make the loan. And it was this kind of approach, whether the Bank was just going to be an institution to hand out money to governments or whether it was going to be a real investment banking institution on an international scale, that underlay the issues. I don't recall now the specific points of policy or whether there were in fact any specific points of policy on which there were disagreements. Oh, Collado also wanted the Bank to go out and issue bonds on the market very quickly, and I don't think he believed Mr. Meyer’s appreciation of the bond situation, that there had to be a great deal of educational work done before the Bank could sell any bonds. It was that kind of general issue, as I recollect.

Q: There was a newspaper report about October of ’46, I think, that Mr. Beyen, the Dutch executive director, had made a speech somewhere in Canada announcing that the World Bank, the International Bank of course, was considering borrowing something like a billion and a half dollars, selling bonds to that extent. About a week later this was repudiated by the management of the Bank. Do you recall anything about that?

Demuth: I don’t have any recollection of that at all. I don’t recall that Beyen was any particular problem. In fact, Beyen was borrowed from the Board then to become an interim first loan director, before we had a loan director, so he was on both sides of the fence. He was acting as a staff man as well as an executive director. I think our major difficulties then were with the US and the UK directors, as I recall. But we were all terribly inexperienced. I remember going to my first loan working party on a French loan application. Nobody knew where to begin. We were inexperienced. We didn’t know what kinds of questions to ask, what kind of investigation to make. We hadn’t developed the kind of project approach that we worked out later. Our European problems were very different from our development problems at that time, of course, and the whole idea in fact of making national and creditworthiness studies hadn’t yet been developed. Just like any other new institution in a new field, at that time we were trying to struggle along finding our way, and we had all these pressures to operate very quickly and make a lot of loans very quickly.

Well, Mr. Meyer resigned. Mr. Smith, who was the vice president at that time, was in terrible odor with the board. They didn't like him at all, didn't get along with him. He had no appreciation of this. He wasn't aware of the hostility with which the board viewed this. This, I think, was more a personality issue than anything else, although Smith was not a man of any particular competence in this field, or of imagination, which made it particularly difficult, because Meyer just disregarded Smith as a member of the management, and used to send things through me that should have been sent through the vice president, which made my relationships with the department heads very difficult. So when Meyer resigned, Smith was nominally head of the Bank, but he couldn't get anywhere. He thought the directors were going to elect him president. They had no notion whatever of electing him president. And so the Bank sat without a president for some time.

Q: Have you any knowledge about the attitude of the United States government, the Advisory Council, at this time? Were they prepared to back Mr. Meyer, or were they listening to Mr. Collado?

Demuth: I don't think that Mr. Meyer ever brought this to an issue where the National Advisory Council was called upon. I may be wrong about that, but my feeling is that Meyer just—these things hadn't come to an issue at that point. Meyer did talk to Will Clayton and a few other people and complained about Collado, but there wasn't any specific issue that could be brought to a head. I doubt that the US government was aware of what was going to happen. I think they were taken quite by surprise by Meyer's resignation.

Well, then the question came up of finding a successor, and then quite a game was played. Every time the board decided to approach anybody, this fact was leaked to the papers, and the papers would then carry stories about how Mr. X was going to be approached and he was going to turn it down because the job was an impossible job, because there couldn't possibly be harmony between the executive directors and the staff of the Bank. The whole issue that we talked about, between the directors and Meyer, wasn't as much of an issue in fact, or at least hadn't been brought to the surface in fact, to the extent that it was brought out in the newspapers. The newspapers contained detailed accounts of the impossibility of running the job, and it became quite apparent after a while that this was a deliberate campaign to dissuade anybody from taking the presidency of the Bank.

Q: Do you know whether Mr. Meyer himself talked this over with prospective candidates, and in a sense helped to dissuade them by pointing out how difficult the situation was?

Demuth: No. I think Mr. Meyer—I think the job was first offered to McCloy, and I think McCloy probably talked to Mr. Meyer and talked to Mr. McLain, the general counsel, who, then on Smith's death came to be the strong man and leader of the staff, and undoubtedly the conditions which he asked the US to accept as a condition of his accepting the post of president were worked out after consultations with Meyer and McLain. McCloy's conditions were turned down, and McCloy then turned down the job.

It was then offered, I believe, to Graham Towers of Canada, and to others, but the campaign to tear the Bank down by proving how impossible the job was, dissuading anybody from taking it, was conducted from within the board. The British director, as an unwitting accomplice of the American director, was the channel through which this stuff was leaked, and the purpose of it being—this is my interpretation, but I'm practically sure that this was what it was—the desire being to have the situation get so bad that there would be no alternative but to turn to the American director and ask him to be temporary president, the idea then being that the Bank would make some loans and would issue some bonds, and the US director, even though a young man, would be asked to become permanent president.

This campaign came within about a day of being successful. The US was told by Collado that the board of directors was agreeable to electing him on a temporary basis, and that would create no problem within the staff and the staff was prepared to back it. In fact, it was violently opposed by the staff. McLain made it perfectly clear to Collado that he would resign if this went through. One or two others of us made it clear that we would resign if it went through. This had never been relayed to the US government. About a day before—exactly a day before—a meeting of the Executive Directors was scheduled to be held to elect Collado as temporary president. The US State Department was made aware of the situation, and the night before the morning of the meeting they directed Collado to ask for a delay of the meeting.

Subsequently, the State Department called up McCloy and asked him to reconsider, and told him they would accept his conditions, and McCloy did accept.

This obviously didn't leave a very good taste in anybody's mouth, and caused McCloy to come down appearing as though he were trying to dictate to the Bank and ride roughshod over the executive directors. This issue clouded his whole administration of the Bank, because there were raw feelings left as a result of this battle and Collado's subsequent resignation, and McCloy had to keep a pretty tight rein in order to assure the management's position. The word "management" came into the jargon of the Bank after McCloy came in. This was McCloy's contribution to the Bank—establishment of the tradition that the initiative in running the institution was to be left to the management. Although, I think, McCloy on the whole got good cooperation from the board, it was always somewhat grudging cooperation, but by the time he left the position of the management had been so firmly established that Mr. Black, an easier, pleasant man with the board, could loosen the reins without impairing the position of the president. So McCloy was wonderful for his era, and Black was fine for his era. In many ways, and I think Black would probably agree, he reaped the benefits of what McCloy sowed, and in the nature of things, things were easier for Black than they had been for McCloy. (Let's stop for a while)

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Demuth: I have skipped over rather hastily Mr. Meyer's six months in office, because I can't really remember very distinctly when particular policies of the Bank were established. In any event, during that period policy questions were being explored rather than decisions being made, and a great deal of the time was devoted to just setting up the Bank's structure and getting some people to staff it. If I had to mention the one major contribution, the largest contribution I think Meyer made to the Bank, it was the number of people that were recruited during his time of office that rose to senior positions and are still with the Bank. It was really quite an amazing recruitment job in a short period of time.

Meyer's selection as president of course was in part dictated by his reputation as a very successful investment banker, and as a successful head of the RFC, and one of his major preoccupations was sounding out the private capital market on raising money for the Bank. I accompanied him on his first trip to New York, when we had a meeting of investment bankers in the Federal Reserve Bank up there, and he was most cordially received. The bankers were very ready to hear his story. They were however, thoroughly unenthusiastic about giving any financial support for the Bank. There was an amazing discrepancy between the attitude of the bankers and the expectations of Bretton Woods, where it was believed that the Bank could easily borrow up to the total amount of its subscribed capital, reserves and surplus. There were many reasons for the complete disinterest of the bankers in buying our bonds. In part it was due to legal limitations. I think the legal limitations were quite severe, but even more, it was the attitude of the market towards an institution that was completely unknown, and that smacked of having to do with foreign lending, which at that time was in very bad repute. The Bank had a lot of members whose credit was undoubtedly non-existent. In general, it was thought of as a do-good institution, as a wild idea, without any respectable support. Some people understood the value of its securities, but they were few and far between. When we finally did come to make an issue, we had to undertake a tremendous campaign of education, changing laws, particularly getting boards of directors and investment committees to understand what the Bank was, because anything called the World Bank or the International Bank in those days just smacked of something that investment committees didn't want to have anything to do with. So we organized a terrific sales group, Black and McCloy did, when they set up the first issue. Their presence and the support that they got from their friends in the investment banking community in New York, the underwriting group they finally were able to put together, insured the success of the issue. If it had been done with any less careful preparation, I'm afraid it might have been a very substantial flop.

You want me to talk about Mr. McCloy's term of office? One really can't talk about McCloy without talking about the triumvirate of McCloy, Garner and Black. They worked as a remarkably good team, Black out selling the Bank to the market, McCloy helping greatly in that effort but also selling the Bank to the world, the public at large, Garner the able chief of staff who really got the Bank into operation as an effective banking institution. I don't think one could speak too highly of Garner's contribution in those days, not only in terms of tremendous work but tremendous toughness, his insistence that we operate not as a public institution, accepting less than the best standards, but as a business institution. Our staff had to be the best staff that could be gotten together, and we did not compromise because of the political nature of our constitution and our structure.

I know this created conflicts with governments at times, governments that were pushing people—for example, he refused to pay any attention to the political pressures that were put on to employ certain individuals. While he was sometimes impatient with the economists, with the "long hairs" in the Bank, his approach was a very broad approach, and he was willing to stick his neck out to make decisions. All those policy issues that had been discussed for a long time in committees were brought up to the management of the Bank for decision, and they were quickly decided, sometimes rightly, mostly rightly, sometimes wrongly, but at least they were decided and enacted.

Q: You are speaking of Mr. Garner in this?

Demuth: Yes, Mr. Garner. Mr. McCloy gave the Bank a broad vision and incisive approach that was extremely salutary, and I think he probably made the most, the boldest moves the Bank has ever made in terms of its European reconstruction loans. He realized that the Bank's reputation was at a low ebb and action had to be taken, so he both organized the marketing campaign I have mentioned and he decided to proceed rapidly with a number of European loans. Nobody at that time had any assurance that our loans to Europe would be repaid, but there was a desperate situation there, when Lend-Lease was cut off and the Marshall Plan had not yet been conceived, and the European economy was threatened with a stoppage of fuel and food imports, raw material imports, and McCloy decided that action had to be taken, and we made 500 million dollars of European reconstruction loans, on faith to a very large extent, without reasonable prospects of repayment that could be documented, but in the knowledge that if Europe wasn't held together, the rest of the Bank's job was not going to be very effective.

Then, you must remember, shortly after those loans were made, the idea of the Marshall Plan was first mentioned by Dean Acheson in his Louisiana speech, I think it was, and Marshall made his speech at Harvard which was taken up by the Europeans. The Bank spent a great deal of time in the summer of 1947 in helping work out the Marshall Plan, helping the United States and helping some of the Europeans work out the presentation of the Marshall Plan. McCloy testified for the Marshall Plan, in full knowledge that this would put us out of business in the main area in which we were attempting to do business, but with thorough recognition that the job was so much beyond the Bank's resources that we shouldn't take a narrow jurisdiction stand and that the Marshall Plan was a necessity. And I think his testimony assistance and the Bank's position were of considerable assistance in getting the Marshall Plan through Congress. Then we turned to the problem of development.

Q: Before you go into development, I wonder if you could say something about the policy issues that had to be decided in the case of the first loan in particular and the reconstruction loans in general.

Demuth: My memory isn't good enough for that. Among the problems I remember was the question of how we were going to supervise the loans. These were large loans that could be disbursed for a wide variety of goods. They were not the kind of project loans that the Bank was set up to do. We had to pretend they were project loans, or decide they were all exceptions, exceptional situations. But I don't remember with any definiteness, what the particular issues were.

Q: What sorts of things were you doing in those days, the first days of McCloy's tenure?

Demuth: Oh, I was working on all kinds of things—for example, the question of board-management relations. We finally got some kind of a memorandum agreed to by the board as to how we would go about processing loans, how we would take them to the board, what kinds of initiative they would leave to the management. Then there were all kinds of recruitment problems still. I did a lot of speech writing for McCloy. I did a lot of work on the Marshall Plan. We had a large number of policy issues that came up to Garner, and I was acting as his assistant, trying to get some of those policy issues resolved. We had organizational problems. As a matter of fact, I was general assistant to both Garner and McCloy at the time.

Q: You had been a special assistant to Mr. Meyer.

Demuth: Well, he had two assistants and I was one of them. The other was a Collado man who left more or less with Collado. Before Garner came in, I recommended to McCloy that my job be switched to being assistant to the vice president rather than assistant to the president, so that we wouldn't have the same situation that we'd had with Smith, where things were going through me to other people instead of going through the vice president, and since McCloy had brought Garner in and had confidence in him and was going to use him as chief of staff, it seemed to me that the kind of job I was doing would be more appropriately put on the level of assistant to the vice president. I had suggested that it be changed to that level, but I, in fact, acted as assistant to both of them.

Q: Was the name of the fellow, who was the other assistant, John Ferguson?

Demuth: Yes.

Q: When did he leave?

Demuth: Almost immediately after McCloy came in. He was of the school that believed the US executive director ought to run the Bank, and at the time of the interregnum, he was the staff man. Who'd go to the directors and keep them informed what was going on in the staff. When Collado left and McCloy and Garner came in, Ferguson decided to leave too.

Q: Was the staff divided in camps, or was Ferguson alone?

Demuth: Ferguson was almost alone. I was in the unhappy position of not being able to be invited to staff meetings in those days because if I was invited, Ferguson had to be invited, and Ferguson would take everything the staff said to Collado. This was an unhappy situation.

Well, the other job I had at that time, which brings up a whole new subject, involved our relationship with the United Nations. In the very early days of the Bank, when it was under Mr. Meyer, the UN people came down and approached us and said that they wanted to enter into a liaison arrangement with us, a relationship agreement, and they gave us copies of relationship agreements that they'd entered into with some of the other specialized agencies, which made the other agencies very definitely subordinate to them. We said we didn't know enough about our business to enter into any kind of formal contract with them, that we were quite willing to cooperate in a lot of fields where we thought we could be mutually useful, but that entering into a contractual relationship was something we wanted to defer for a year or so until we knew more about our business and what our relationship should be. In any case, we said that we couldn't enter into the kind of contract that the other agencies had entered into because it would appear to the public that we were in effect an agency of the United Nations, and if it seemed that we were an agency of a political instrumentality, our market position would be impaired.

This was reluctantly accepted for a while, and then on review at the UN, their lawyers said that it was—the Charter required that the United Nations enter into a contractual relationship, that this required a written contract agreed to by both sides, and they raised again with a good deal of insistence the need for a written document.

Well, we said, all right, if they really wanted a written document we'd submit a draft that we could accept but they wouldn't like it and we wouldn't recommend that they accept it. Their lawyers said, "Let's see what you can do," so we wrote a draft agreement that was in effect a declaration of independence, starting out with—"The United Nations is an independent international agency with its own governing body, and the International Bank is an independent international agency with its own governing bodies, each responsible for its own policies."

This was a document that if we had been the United Nations, we wouldn't have been glad to sign, and we didn't urge them to do it at all, but we said if they needed a contract, this was the only kind of contract we could accept.

Q: I suppose this is still in the files somewhere?

Demuth: Oh, yes. This contained also a statement that the United Nations would not make any—as a matter of policy - the United Nations Economic and Social Council would not make any recommendations to the Bank with respect to a particular loan or with respect to the terms of financing, something like that.

Well, this caused a lot of—the UN people wanted to go ahead with it, the international organization people in the State Department were very anxious that it go through, and there was a very strong, vigorous negotiating session between a committee of the Economic and Social Council and Mr. McCloy, which went on for a day at the United Nations, in which our draft was reviewed, and we took out a few of our declarations of independence but not very many. The agreement, as it presently exists, was agreed on and accepted by the Economic and Social Council with a certain amount of bad grace.

I don't think anybody's ever looked at it since. It's been misconstrued. There's nothing in this agreement that prevents the Economic and Social Council from making general policy recommendations to us, but the ECOSOC has been so cowed that they feel that it prevents them from making any recommendations on policy to us, which it doesn't at all.

Q: I take it that what you were trying to make clear primarily was that even if they did make recommendations, you weren't obliged to accept them.

Demuth: Well, we wanted to make it clear that the Economic and Social Council would not attempt to dictate particular loans to us, that we were making the loans on a businesslike basis and without regard to political considerations, that we wouldn't want a political body to be standing over us and telling us what loans to make or on what terms to make them, but if they wanted to make a policy recommendation, for example that we should give thought to industry or to agriculture, or if they wanted us to give more emphasis to Africa than to Latin America, there was nothing in the agreement that would stop general recommendations of that sort. We wouldn't necessarily adopt them but we didn't say that it was appropriate to make them. We had agreed in this agreement that we would submit a report to the Economic and Social Council once a year, but unlike the other agencies we did not agree to prepare a separate report for the purpose. We told them that we would send our annual report and that we would appear before the Economic and Social Council and present it, and each year the President does go up and present it to the Economic and Social Council which gets publicity. They make a few speeches back, and that's the relationship with the Council. It's extraordinary how differently the governments react in their discussions, at the Annual Meetings, for example, where the finance ministers are representatives and at the Economic and Social Council where the representatives come from foreign offices, and are more politically motivated. This is one of the difficulties in the relationship.

Our relationship also became very difficult on a staff basis. The UN at that time had some pretty ambitious characters who were trying to build the UN up into a top agency and wanted the Bank to be a tool that they could use, but they never really had the ability or stature that went with their pretensions. The United Nations, for example, wanted to undertake all the general survey missions. They wanted the Bank to supply experts to their missions, and we should just do the financing in accordance with the recommendations made by their missions, done by the UN. We said, “Send out any kind of missions you want, but we’re going to send them out too, if we’re asked to by the governments, and we don’t feel we should participate in anybody else’s missions because that would bind us, make us participate in a mission we didn’t control and might put us in an embarrassing position, if we couldn’t finance the program that was recommended.”

This was a subject of very bitter dispute between Mr. McCloy and David Owen. It ended up with our saying, “You just go on your own way and we’ll go on our way,” and in the end the requests came to us rather than to the UN and so we did this sort of business and they didn’t. But with David Owen then running the Economic Affairs Department and David Weintraub as his ambitious second in command, it was a very rough relationship, which still hasn’t been wholly smoothed over. It’s a very difficult relationship at best, because in the hierarchy of things the UN is the top agency. They’re the central global body, and they feel they ought to be able to exercise authority over all the other international agencies. On the other hand, the Bank has the money. It has many more people of real stature on its staff than the UN has. The UN’s a little jealous of us, and on the other hand we're very impatient with any kind of UN interference. Also, our management has from the beginning been very loath to get involved with the UN in any way for fear of contamination because for the most part we didn't have much respect for the people, and this kind of attitude gets felt, so the job of keeping relationships happy in that kind of a milieu is not an easy one. I think it has become considerably better, though now it's beginning to get aggravated again as the UN is once again engaged in a desire to become the top development authority in the world and use the Bank as an instrumentality, and the Bank itself wants to be the top development agency. This is where the conflict is beginning to make its appearance in a few ways.

Q: Has the development of a Special Fund in the UN complicated matters?

Demuth: No, I don't think so. The Special Fund, you know, was created because the US wanted to buy time on SUNFED, and they thought with this 100 million dollar a year fund—50 million dollars a year originally—they could direct the persons—for a capital investment fund for a few years.

We felt that the Special Fund might have a very real role to play, and Mr. Black has been very anxious that the Bank cooperate with the Special Fund, and in fact we've cooperated with them quite effectively. We are one of the executing agencies—some of the other agencies have many more projects, but I think we've probably got more completed and under way than most of the others, and on the whole I think this has worked out very well. We've been able to put things to them which they've financed, and others we've carried out with the help of their financing. The difficulty is that Mr. Hoffman, Paul Hoffman, has greater ambitions for the UN, and he wants the UN to get more actively into development work and to serve as a world development authority. To do this he is now about to use his money to try to build up UN field offices to serve as central coordination points for all development efforts in the poor countries, and to that extent there is some conflict, maybe. But on the whole he has not been active in supporting a UN capital fund, which was always the one threat that has been hanging over us. Once a UN capital fund has been created, the confusion between that sort of fund and the Bank would have been tremendous, and whether the creation of IDA, which was designed in very large part to hold that development off, will succeed in doing so, has yet to be seen. But with IDA getting into many more fields, and the Special Fund active in fields in which we're interested, our relationships necessarily become closer.

Q: Are they closer?

Demuth: Much closer, and I would say that for the last five or six years they have been pretty good, quite good—that is, a fairly close relationship, and both Mr. Black and Mr. Hammarskjold are very much interested in the Near Eastern problems. They have a mutuality of interest there, so that ever since Mr. Hammarskjold came in and Dr.

Seynes came in on the economic side, things have been considerably better.

Q: I’ve heard that the real beginning of good relations between the UN and the Bank began with Suez and Mr. Black’s work there.

Demuth: Well, that has certainly had a good deal to do with it. That’s where Black and Hammarskjold really came together. I think in fact—well, that’s where the management of the Bank began to have some respect for the UN. Staff relationships have gotten considerably better since that time. I think with the advent of Dr. Seynes as the top economic man at the UN - to a certain extent with the departure from the Bank of Mr. Garner, who had no use for the UN - things have gotten better.

Q: How does the Bank decide how to coordinate with the Special Fund?

Demuth: Well, we get all the Special Fund projects. They send them to us for examination and advice, and to get our views on what should be done, and we’re in close touch with what they’re doing.

Q: While we’re on the subject of coordination with other lending agencies, could you say something about the Bank’s relations with ICA and the Development Loan Fund and Export-Import Bank?

Demuth: Oh, the Export-Import Bank relationship has a whole history in itself, but I can't begin to remember all of it. For a long time our position was that the Export-Import Bank get out of our business, that the United States shouldn't do any international financing and should leave this entirely to the International Bank, and for a while it almost succeeded. When the Eisenhower Administration came in, Mr. Humphrey strongly supported this view as Secretary of Treasury, but it never was adopted. Of course the US program, instead of being out back, has grown immensely. We never had good relations with the Ex-Im Bank, I think largely because of its competition. People at the head of the Ex-Im Bank always seemed to be good fellows before they went over there and became devils as soon as they became president of the Ex-Im Bank. The advent of the DLF made things somewhat better, because the need to coordinate became even more evident, obviously, and there were three agencies, DLF under its statute not being allowed to finance if the Ex-Im Bank or we were willing to finance. It forced some kind of coordination. Our relationship with the DLF from the beginning was better than with the Export-Import Bank. I don't know quite what the reason for this was. Maybe the fact that they were giving soft loans and therefore strengthening the credit of our borrowers.

Q: In a sense their activities increased the creditworthiness of the countries that the Bank was interested in but the activities of the Ex-Im Bank decreased the creditworthiness.

Demuth: The first part would be fair to say. I think the second would have to be documented. I would hope that the Ex-Im Bank's loans on the whole were for sound enough projects so that in fact they did not weaken a country's economy and thus decrease its creditworthiness.

Q: In any case they were not development loans, isn't that true?

Demuth: Well, the only things we were worried about were the development loans.

Q: But if the foreign debt of a country is increased as the consequence of an Ex-Im Bank loan, and the money has been used to finance current consumption, for example, then in a sense the country is less likely to qualify for a World Bank Loan.

Demuth: Well, that's right, but very few of the Ex-Im Bank loans were for current consumption. Now, what we were worried about and what we are worried about in the USA program is that when we try to impose conditions on our loans designed to improve the credit of the country, if it can just run around to the State Department and the Export-Import Bank and get a loan without these conditions—it weakens our position. The US frequently has to give loans for political reasons, but we think they would be better made if certain conditions were first fulfilled, and it's that kind of thing rather than decreasing the creditworthiness that concerns us.

Q: I understand that this was quite an issue with Brazil. Was it an issue before Brazil also?

Demuth: Oh, yes. There was a case where McCloy went on a campaign on this during his tenure in office, which was long before the Brazilian crisis came to a head, and it was very difficult from the beginning, because there was just no rational basis on which you could decide whether something should be financed by an Export-Import Bank loan or a Bank loan. We wanted some guidelines put down, and we were quite willing to leave the political loans to the Export-Import Bank if they didn't undercut us on our normal loans. But the US was quite understandably reluctant to say, "We'll only do extraordinary political loans in the Export-Import Bank," because this meant, if they'd adopted that rule, that anything the Export-Import Bank did would immediately be labeled as a political loan. So they wanted to do a wide variety of loans, including political loans in those. And they also felt, and I think quite justifiably, that it would be unfortunate to give a monopoly role in international finance to any one institution. We were likely to do more, and more money was likely to go out overall if there were two agencies operating than if there were only one. But this was a long hard fight, this relationship between the two agencies.

Q: Speaking of Mr. McCloy, somebody told me that when Mr. McCloy got back to the Chase Bank after his period in Germany, he suddenly decided that the Ex-Im Bank was pretty good after all. Did you hear this?

Demuth: Well, I think probably that what your informant had in mind was that the Chase Bank set up the Chase International Investment Company in which they tried to take over, with Export-Import Bank backing, some of the export financing—this was export financing, not development financing, that the Ex-Im Bank was doing. Whether this was a misconceived idea or whether there were some other reasons for it, it never worked out, and I know before the end of that experiment the Chase Bank was very browned off with the Export-Import Bank.

Q: How about the relationship between the Bank and the Fund?

Demuth: The International Monetary Fund. They haven't been good. They've been good at the working level. They've never been very good at the higher levels. In the early days of the Bank, the Monetary Fund was a fairly inactive institution. It was dominated by its board of directors, and regarded as a very much more political institution than we were. Its management was not as strong as the Bank's management, and the Bank's management didn't have very much to do with it. The reason we're in this building today rather than in a beautiful building down on Constitution Avenue—what we were offered was a magnificent plot of land, by the US government—was because the Bank didn't want to have a permanent building alongside, share a permanent building with the Fund. Now, all kinds of things that might have been expected to have been done jointly never could work out—joint missions, for example. I finally succeeded in borrowing one or two Fund people for some of the Bank's missions, but this took a terrific amount of effort. There has been a feeling of intense competition between the top people at the Fund and those at the Bank. I think personality conflicts rather than any issues of substance were at the root of the trouble — the top management relationships were bad. I think the working relationships were good, and I think as the Fund gets more active and acquires a more reputable place in the world and more inspired leadership things will be considerably better.

Tape 2

Q: I wonder if you'd say a little more about how the Bank was organized under Mr. McCloy, particularly before 1952, under the general reorganization.

Demuth: Well, the two major departments of the Bank under Mr. McCloy were the loan department and the economic department.

The economic department had in it all the functions that are now performed by the economic staff, general studies, a lot of these studies, and all the creditworthiness studies now performed by the area departments. The loan department was the loan negotiating department, and it had an engineering staff under General Wheeler which in effect did what the whole technical operations department now does. They were the project analysts.

Q: That didn’t begin right away, did it? Wasn’t it not til about ’49 that the Bank really had engineers on its permanent staff?

Demuth: No, my recollection is that Spec Wheeler came over in ’47. ’48 at the latest but I think it was ’47. It was a very small staff, as we didn’t feel very many engineers were needed. Then the supervision of loans was done by the Treasurer’s Department. There were many problems involved in this organization, and people got shoved around from country to country and there never was any continuity in Bank staff working on a particular country. In part there was difficulty because the economist was working on a country and reported to one man, and the loan officer who was trying to work out a program for the country reported to another man, and they never came together except at top management levels. Then, of course, the end use work was being done by a group that had nothing to do with the original negotiation of the loan, or at least no responsibility for it.

Nonetheless, the organization was not inherently bad. There were normal bureaucratic jealousies between the two operating departments. Oh, I should add that somewhere about that time, in ’50 or ’51, I was charged with the responsibility for technical assistance, and that was then an operating responsibility, and I was in charge as a direct operator rather than as a staff officer.

Q: Was this in a department, or was this a separate technical assistance department per se?

Demuth: Well, this was in my capacity as assistant to the vice president. I was also in charge of technical assistance.

Q: Did you have staff working for you on technical assistance problems?

Demuth: One or two people. This was in the early days of technical assistance. We had a discussion around 1950 as to whether the Bank was appropriately organized, whether it should be reorganized. This was shortly after Mr. Black came in. It must have been before 1950. We had a long discussion of the organization of the Bank, and at that time we decided that there was no urgency about reorganization, that the organization we had was as appropriate as any other and it was a question of making it work. But a few years later, we reviewed the problem again. A working party was set up under Mr. Iliff of which I was a member, to consider how to improve the organization. There was a general feeling that if we had a group of economists and loan officers working on the same country, they would come up with a more consistent approach, and it would be an easier operation. There was a general feeling that project work should be separated out from the rest, and that it should be done not just by engineers, but by engineers, economists, and financial experts. I think the major thing that came out of that reorganization was the technical operations department. Then we created the economic staff to do the general economic work. The technical assistance work then became, on my recommendation or certainly with my affirmative concurrence, a staff service, because the difficulty we had with technical assistance was that the loan department regarded it as outside its jurisdiction. It was something that was Demuth's specialty and the loan offices felt that they had nothing to do with it. I felt, on the other hand, that the Bank shouldn't build up a technical assistance staff, large staff, to conduct separate relationships on technical assistance operations. We were an important technical assistance agency largely because we were a financial agency. The two had to be integrated. It was therefore very important to make the people who were in charge of a country program feel that technical assistance was part of their responsibility. So technical assistance was made an operating responsibility of the area departments, with my office retaining a responsibility for recruiting personnel and for generally advising the area departments, thus bringing in the experience that we had in various areas to bear on any new problems that might arise in an area in which we hadn't operated before.

The one great danger in this reorganization was that the economist would lose his independence, and that, if a loan officer wanted to make a loan, he would more or less direct his economist to come up with a report that indicated that a country had enough creditworthiness to justify the loan. We were quite anxious to avoid the subservience of the economist and to maintain his independence. We tried to do that in two ways. One was by creating an economic adviser in each department, who was supposed to be the man to whom the economists in the department could come if they were being pushed around, so that at management level within the department they would have a supporter. The economic adviser was also supposed to review the work of the economist, to be sure that it was kept up to scratch.

Then we also created the economic committee consisting of all the economic advisers, who would review all the economic reports and make sure that there was consistency in the reports among the areas. I don't think we—we have really achieved the latter. I think we are acquiring quite different creditworthiness standards in fact in the different areas. But there are people working on it. Perhaps this is inevitable anyway. You can't have standard criteria in a vague field. Probably you have different judgments with different economists working on different countries anyway.

The other essential coordinating factor in the organization is the working party, which on the whole has worked pretty well. It works well in keeping everybody informed. There's one basic difficulty with the working party, and that is that the loan officer is the chairman. This is inherent in the idea that the area department coordinates everything. In fact, the loan officer is frequently a man of less stature than the technical man who is working on the report or than the technical assistance person, if it's a technical assistance problem. Particularly if the loan officer is a young man without too much to do and the working party is the instrument through which his own satisfactions come, because this is where he's boss, he only has a few countries and he wants to concentrate on them—he can waste an awful lot of time at working party meetings which could well be spent otherwise. And it makes the technical operations people in particular feel as though they're subservient to the loan officers, and this is a difficult kind of relationship. The technical operations people, who often have considerable professional competence, don't like always to be second to the loan officer in a subservient position.

Q: Does this imply that the loan officer, being an area department person, is rather more likely to push for a given loan than the technical operations person in a working party?

Demuth: Probably yes, and that's probably sound. I think the best loan officers are the people who are trying to push loans, although not trying to push them over sound technical objections. But I think you need some kind of a balance, because your technical people are always looking for flaws and should be, and you need to compensate for that with someone whose primary interest is to get loans through, and I think that's an appropriate role for the loan officer. But the relationship is not an easy one and never will be an easy one, however we may be organized. We've had trouble with it and I think we'll continue to have trouble with it, but I think that's inherent in an organization where you try to put together as many different talents as you do in this organization.

Q: I've heard that in the early days before the reorganization of '52 that there was some conflict as to whether the economists even in the loan committee should be primarily in charge of a given study, and also that the economists were rather more ambitious about trying to push loans and had rather broad standards of creditworthiness, more than was true of the loan committee.

Demuth: The second part of this doesn't ring true at all. I would not have thought the economists were trying to push loans. I do think that the economists took a broader view of the situation. They saw a country needed capital and they were anxious for the Bank to make capital available and had perhaps more impatience than they should have had with the loan department which took the project approach, and because the—until the project had been worked out, there wasn't any capital to be made available. I think they were impatient with the project approach and wanted to see the Bank take more of a balance of payments or program approach, and in that sense I think they probably were anxious to push ahead.

On the other hand, I suppose, since there were two coordinate departments, sometimes the economist was considerably senior to the loan officer. I suppose there probably were conflicts as to who should be in charge of a mission. In fact, I think in those days sometimes the economists were in charge of the mission.

The present organization has a different difficulty which is not easy to work out. Because the area departments are basically administrative loan-making departments, the directors have to be operating types. They have to be administrators. And that means that the Bank hierarchy gets filled up with people who come up through the operational channels rather than through the economist channels. The staff members who stay in economic positions feel that they can't get ahead very far, about as far as they can go is to become an economic adviser or head of the economic staff or of EDI perhaps. They have little chance, as economists, to become a department head or assistant department head. And that leads a lot of economists to feel that the economists aren't appreciated at the Bank and that one has to be an operator in order to get ahead. And this is one of the reasons, I think, that we decided to create this new Development Advisory Service, as a separate unit of the Bank, so that we could get away from this administrative structure. In the Development Advisory Service we have a whole group of senior level economists who are recognized simply by their inclusion in the service to be senior level people, without regard to whether they're called a department head assistant or department head. It's like the foreign service. There are class 1 and class 2 officers, without regard to an hierarchical arrangement.

But this problem of keeping top level economists happy at the Bank in that situation is difficult in the present organization.

Q: Well, some people who were in the economics department have in fact become senior operating officers in the Bank.

Demuth: Oh, there are a number of economists who have gotten ahead in the Bank by becoming operators, including one of the vice presidents, but this is by becoming operators, rather than by staying economists.

I think the difficulty is that the tendency is all for the economists who are ambitious and want to get ahead hierarchically, they say, “Well, we can’t do this thing as economists. We have to become operators.”

Now, I think frequently economic training is the best training one can have to become an operator in the Bank. But there are some economists who want to remain economists and work in that capacity. They’re very much needed in the Bank. Yet if they want to stay economists, as thinking analysts, their chance for advancement is much less. That’s what I meant.

Now, you asked me what my own job is. My own office in the Bank has always been a hodgepodge of things that just didn’t fit anywhere else. In the very early days, it was largely just greasing the wheels. For a time I was the interpreter of the economics department to Mr. Garner, or vice versa, so that there would be some communications between the two. I’ve always had a certain number of special policy problems thrown at me; through historical accident I’ve been responsible for our liaison with the UN and other international agencies. I have this technical assistance program. And I’ve had the job of really creating and getting under way most of the new programs the Bank has gone into. For example, I was responsible for getting the Economic Development Institutes started. The idea for an International Finance Corporation was worked out between Mr. Garner’s office and my office. I did all the preliminary work on getting IFC started, and spent the first year of IFC helping Mr. Garner to get it going, similarly with the IDA, I helped work out that charter and get it through the Board, and I chaired the committee which formulated first policies of the IDA. I also helped work out the concept of the

Development Advisory Service which has just been started and various other new approaches to technical assistance. I also coordinated the Bank's work on and was the channel of communication for all the Special Fund projects that we have.

Beyond that, I was responsible for a long time for the entrepreneurial work in connection with the development banks, and to a degree responsible for developing the Bank policy on the establishment of such banks. This was a rather vague assignment, because the area departments were all interested in this. The technical operations department was administering our development bank loans. I was the fellow that was supposed to be solving new ones, working out our policy on development banks, which was rather an administrative monstrosity. IFC is also concerned with this, and I think I'll be relieved of this responsibility in the future.

Q: I'd like to hear you say something about development banks but before you do there's one quick question. You say that in the early days you were liaison, interpreter or something like that between Mr. Garner and the economics staff. I don't quite understand.

Demuth: Well, this is really a personality question more than anything else. Leonard Rist, head of the economic staff, and his deputy Paul Rosenstein-Rodan, on the one hand, and Mr. Garner, on the other, just didn't understand each other's language, and they also got on each other's nerves. Nevertheless the economics department had a great deal to add to Bank policy making and the policy being made,

made a great deal more sense than it sounded to the economists. So I was to a certain extent the spokesman for policies being advocated by the economics staff, explaining it in terms that Garner would understand and then translating Garner's policy decisions into terms that the economists would go along with, rather than the way they might misunderstand him.

Q: I wonder if in this connection you and others were responsible for the Fifth Annual Report which contains perhaps one of the earliest systematic statements of what the Bank's lending policy was?

Demuth: Well, I was responsible for that. I just felt that it was time to establish the policy and explain it to the world. I guess I forgot to say, through the Fifth, my job was to write the annual report, and at the time of the Fifth Annual Report I thought it was time we had a systematic statement. We also wanted to make policy. That report made some policy, not all but some of it was made in that.

Q: Would you say something about the evolution of policy?

Demuth: Oh, I think I'd rather talk about development banks. Well, development banks—this is an almost necessary mechanism for industrial financing, and when we talk about development banks, in this case, we're talking about industrial investment institutions. It's just impossible for any global institution to assist the great many industries in a country. You just can't go through the investigation.

You don't know the promoters and the people involved. Beyond that, we had a charter limitation that required a government guarantee, and it was very difficult for most industrialists to get or even accept a government guarantee. So financing development banks was a way in which we could get money into the private sector, the investment sector, and we felt that it was terribly important to get some kind of investment banking tradition established. Garner, I think, was the originator of the idea. There'd been a number of development banks, but most of them before we got into operation, at least in the underdeveloped countries, were government run. Garner's feeling was that we should establish these under private commercial control, so as to get them away from political control that had them invest their money according to political considerations, and in order to establish some kind of a real investment banking tradition in the country.

This is a very difficult field, because no development bank in an underdeveloped country, is likely to be successful without some kind of subsidy. The cost of investing money and investigating projects, also of engaging in promotional activities is so heavy that if you have to take private money and pay your overhead costs, then you can't get a return that is sufficient to satisfy the investors. This is particularly true in most underdeveloped countries where the market is small and you have to give a great deal of technical assistance, where you probably have to wait a long time for returns on some of your money, and where the alternative opportunities are many and higher returns can be realized through loans and other investments. So the development bank is just not going to be able to attract private money unless it has enough subsidy money to make it a—to give it some leverage. Even then it’s not attractive as a pure investment matter. Most of the local stockholders in these development banks are people who are public-spirited or who are interested in the industrialization of the country for other reasons, and expect to benefit as industrialists and bankers, rather than from their development bank shares as a pure investment. So institutionally the banks are of a very mixed character. They are in private ownership, but basically some government support is necessary to make them go, and the private ownership is frequently motivated by other than investment considerations.

Nonetheless, despite the unorthodox character of these institutions, their record on the whole has been pretty good. They have been able for the most part to stay out of political lending; because they have to account to their stockholders for profit, they have to make dividends, they’ve been following much more businesslike practices than most of the government banks. And gradually, all of these banks have had great difficulty, but gradually they’re—the early ones are coming out of the woods and making a very substantial contribution. The difficulty with our position is that we will assist only the privately-owned development bank, and the number of economies in which this kind of development bank is either feasible or appropriate is very limited. We’ve done the obvious things, like India and Pakistan and Turkey. Latin America is probably the only big untapped place that has room for this kind of institution, and there there are already some public institutions in this work, which makes it harder to promote private ones. So everybody recognizes that development banks are a good thing, but since our ideology prevents us from helping a government owned one, we've operated within a much more limited sphere than we might otherwise have.

There's a current of opinion that we've been rather rigid in only helping privately owned ones. I think Mr. Black recognizes that privately owned development banks are not appropriate in many places, but since there are a lot of other financing institutions around, he'd rather have somebody else finance the government-owned development banks because he feels that they're not likely to be very successful.

In at least one instance, I saw the value of this. We've been trying to promote a private bank in Colombia. We haven't been successful in this for various reasons. In Colombia a private bank would be a fine thing, a very good thing, but, if we had been willing to follow the policy of promoting a government bank, we wouldn't have had a chance in the world of getting a private bank there because the government wouldn't have had any conceivable interest in its creation and would much rather have us support their government institution, which hasn't been very effective. Our only chance there, and we may sometime succeed in getting it, was because we said we wouldn't support a government institution and if they wanted this money that we were anxious to put into their industry, it would have to be through a private bank. Maybe the rigidity of these rules, although it may offend in some places, has been justified in a number of other places. Rather than taking the easy road, we've taken the harder but perhaps better road.

Interview with Mr. Richard Demuth

By Robert Oliver August 16, 1961

Interview # 2

Q: Now, if you'd say a word about the background of the International Finance Corporation, in the light of the Bank's interest in private enterprise as such.

Demuth: Well, the same considerations that caused our interest in development banks were responsible for our initiative in connection with IFC, namely, we thought it was important to develop the private sector of the economy. We were prevented from doing it to a large extent because of the requirement of obtaining a guarantee and because we didn't have available any equity money, and many of the private industrial projects that we saw needed venture capital rather than fixed loan capital.

So way back—I don't know what the dates are, my memory for dates is pretty bad anyway—way back, before IFC started, we gave a good deal of consideration to the possibility of creating an arm of the Bank, but with separate funds, that could do something about this.

This was way back in McCloy's day, as a matter of fact. I recall that when Truman made his Point Four speech in '48, the State Department was caught completely unawares. They had no idea he was going to do this, and they had no idea of how they were going to draw up the development program that was announced in his Point Four. There hadn't been any thinking about the concepts—nothing. At that time Willard Thorp was Assistant Secretary of State for Economic Affairs, and McCloy was asked to go over and see him. I went over with McCloy. We tried to sell him the concept of IFC as part of the content of the Point Four program. So the thinking was way back as early as that.

What we were thinking about was a fund that could be made available to private enterprises, without government guarantees, and in the form of equity as well as in the form of obligations.

We drafted some memoranda on this. Dave Gordon and I did most of the work on it. Bob Garner was the most enthusiastic on the management side. Again, this was a subject which had the staff divided down the middle. Most of the people were very worried about it. They thought the IFC was a very dangerous experiment for the Bank to go into. Even Dave Sommers was very negative. But McCloy and Garner were interested, and as I say we proposed this to Willard Thorp and took it up very actively.

Eventually we made this proposal. Well, what happened was, that Nelson Rockefeller was named head of an advisory council to the President to write a report that eventually was called Partners in Progress. He had Stacy May doing most of the work on that one, and they were looking around for ideas to put in the report, something concrete and new. They came down and talked to us and we sold them on the IFC idea, and this first saw the light of day in Rockefeller's report, Partners in Progress.

It was then picked up in the United Nations somehow, in the Economic and Social Council, and we devised the strategy of having this debated in the United Nations, to begin to bring pressure on governments to take some action about it. So, we stimulated it and accepted a request from the Economic and Social Council to make a report on the whole subject. For several years in a row we made reports to the Economic and Social Council on this proposal. And this gradually generated more interest and more and more pressure.

The underdeveloped countries on the whole were very favorable to the IFC idea. The opposition came from the United States, which regarded it as pretty socialistic, the idea that money would be provided by a public institution for private enterprise, particularly in the form of equity investment. This was regarded as public ownership of private property and that was socialism. The NAC voted against it.

Gradually the pressures built up, however. There were two subjects on which the various United Nations bodies continued to harp. One was Sunfed, the international capital development fund which was to make grants and long term low-interest loans on that basis. The other was the International Finance Corporation idea. And Latin American countries in particular, who didn't see that they were going to get very much out of grants or long term low interest loans, were particularly enthusiastic about the International Finance Corporation. The pressure continued to build, and finally the US felt it had to give way on some front if it was to buy time on the creation of the International Capital development fund. The US also had to go down to a meeting in Brazil of the Latin American countries and had to say something, give them something to relieve the pressures.

This came right after an annual meeting of the Bank in which a great many speeches had been made in favor of the International Finance Corporation. So they began to reconsider their position on that, and they had some meetings with the management of the Bank.

Q: Could you say who “they” is?

Demuth: Humphrey was the Secretary of the treasury at that time, and Garner and Black were the Bank representatives, with Sommers and myself participating. Two things happened to make it more acceptable for the United States. One, Black cut down the proposal size from 450 million dollars to 100 million dollars. He said, “I don’t want 450 million dollars. I want to try this out on a pilot basis, let’s make it 100 million dollars,” and this made it a great deal more acceptable to Humphrey. Burgess, Randy Burgess was the other man in the US that was in on these discussions.

And the second thing was a suggestion I think made by Dave Sommers that we should cut out the equity idea, and get venture capital through things like profit participation options and convertible debentures instead of direct equity ownership and that last proposal, which I fought, finally put the thing over. But I think the pressures were such that it would have gone over even without it.

Both of these concessions, as a matter of fact, have had an unfortunate effect on IFC. I don't know that they necessarily follow, but historically they did have this effect. As for cutting the size down from 450 to 100 million dollars, that probably would have been a wise thing, if the 100 million fund had been operated as though it were the first part of a 500 million dollar fund. Instead, it was administered as though it were the only resources IFC would ever get, and so it led to a great dispersion of funds among very small industries. Every time a 10 million dollar project came along, this was thought of in terms of "this is 10 percent of our total resources," which made it appear quite different than if it had been a 500 million dollar fund, and in my opinion the result of that was to drive away or turn away the very business for which IFC was primarily designed, namely, the large enterprises that needed mobilization of foreign capital. Foreign capital is often reluctant to put that much money in underdeveloped countries without some kind of umbrella which the IFC was designed to provide. So for many years I have seen it suffer under this handicap of operating with 100 million dollars instead of a 500 million dollar fund.

And the second obstacle created all kind of problems which are now being removed through amendment of the charter. I don't know that they were inherent either but they led to unorthodox types of financing which confused people. They probably induced confused thinking on the part of IFC's management too, which consistently tried to get both a creditor's position and a venture capital position. The result was that the terms proposed were considered excessive by some of the people that they were doing business with. If they had been making direct investment they wouldn’t have thought of trying to get a creditor’s position for the same money for which they were getting an equity position. So I think the novelty of it, the fact that it didn’t fit in with existing patterns, caused confusion to the borrowers, and I think it caused confused thinking on the part of IFC, because in order to provide real venture capital IFC would have had to do something that really would have looked pretty silly to orthodox financial circles, something like taking perpetual bonds without any fixed interest with income dependent on dividends and fully convertible. Well, this sort of thing is unorthodox, and the thinking was, well, let’s think about this sort of thing but let’s make it 50 years instead of perpetual, or better still let’s make it 20 years, let’s have some fixed interest as well as participation in profits, and so on. And when you began to add all these things together, you got a package that wasn’t anywhere near as attractive to people as a straight loan and equity investment would be.

But in any event the US finally changed its mind about the creation of IFC, and once it changed its mind the proposal moved rapidly, because then the US took the initiative in pushing it. It was decided to ask the executive directors to draw up a charter, and then the whole thing went into a drafting session with the executive directors which worked out pretty well. I think subject to the limitation, of no equity investment, it turned out to be a pretty good charter and it’s probably as good as one could expect. I think that’s about all.

Q: It strikes me as very ironic that Mr. Garner, one of the leading advocates of private enterprise in the Bank, should be in favor of a plan that the US government or some people in it like Mr. Humphrey would think of as being socialistic.

Demuth: Well, there were two great ironies. One was, the charge of socialism against a Garner-advocated plan. Nobody's less socialistic than he. And secondly, the vital and almost essential role that the United Nations played in getting this adopted. Mr. Garner is one of the people around here who has least respect for the United Nations and has always been derogatory about it, and if it had not been for the discussions in the United Nations, the public opinion pressures that were created by the UN, IFC would not have been here today. In fact, for a long time the UN emphasized that IFC was its own brainchild and creature.

* * *

Demuth: I think when I last talked to you in connection with the very early days of the Bank and Mr. Meyer's regime and Mr. McCloy's regime, because what dominates my memory is the interregnum between the two and the personality difficulties. I may have understated or under-emphasized the amount of actual policy work that went on during the first six months of the Bank's existence when Mr. Meyer was president. As I think I stated, there were all kinds of committees of the board reviewing policy questions, and some of the Bank's policies that are so established that one doesn't think of them as issues of policy anymore were in fact debated and established at that time, or at least the groundwork was done so that they were established immediately afterwards.

I'm thinking of such things as the decision that we would charge the same interest rate to every borrower irrespective of its particular creditworthiness, and the decision not to take security for loans in the normal cases except where we are financing private enterprise. In the case of private enterprise financing, there are various factors which may make security advisable. But generally no security for a public authority.

Q: The negative pledge clause?

Demuth: The negative pledge clause was also very much debated at that time. The whole form of contract was beginning to be worked out at that time -- the issue of whether we would operate through loans or through guarantees, because at Bretton Woods, as I understand it, there was a strong feeling that the Bank would be primarily a guarantee operation. The whole question of looking intensely into projects, rather than simply making money available in the form of a loan or line of credit holding off all financing until the project is ready to receive it. The notion that we really would follow disbursements to make sure that we only financed those things for which payments had actually been made. So that I think I may have given the wrong impression, that there wasn't a great deal of work being done. We take these things for granted now because they are so well established, but at the very beginning we had to think all of these things through.

Q: Well, there was no sharp division claimed between Mr. Meyer's period and Mr. McCloy's period.

Demuth: Well, there was a sharp division between Mr. Meyer's period, when all these things were being debated in committees of the directors, with the staff so occupied attending these meetings that it was very hard to get decisions made, and the period when McCloy and Garner came in. The initiative was then taken over by management and decisions were made very much more rapidly than they had been before. But certainly the McCloy-Garner team utilized all the groundwork that had been done during the Meyer regime. A great many of the personnel, Dave Sommers and to a certain degree I myself, were all involved in the same process right through.

Q: Would you say a bit more about the discussions as to whether or not the Bank would give lines of credit loans or whether they'd finance specific projects? I take it this has been sort of a running discussion almost throughout its history.

Demuth: Well, there are a lot of aspects to this. In the early days there was some feeling that, if we just knew the general purposes for which a country needed money we ought to make a loan to the government and let them spend the money within certain categories. This was to a large extent Collado's view. He pounded the table and said, "You have to make 40 million dollars available to Chile within the next few months. I know them, they're good people, they need money."

Well, that disappeared very quickly, and it was generally recognized at a very early stage that we had to be satisfied with the soundness of the program for which the money was needed.

Then there was the question of definition, of "what is a project?" Should a project be considered primarily a factory or a power plant or a distribution system, or could you make a project out of a specified expenditure? In other words, suppose there was an import program for a lot of spare parts and other miscellaneous imports needed for the economy of a country, for private industry as well as governmental efforts—could you take that kind of a program and call that a project?

The way we evolved, this is not a project now, not considered a project, although if you read the Fifth Annual Report you will see that we say there that the whole specific project approach was designed simply to insure that we knew what our money was being used for and that it would be used for high priority purposes, and that definition would include loans for a program.

I think the general feeling here in the Bank has been that while countries that were well managed would use the proceeds of a program loan effectively and that for them, a program loan would be just as good as a project loan. For other countries, less well managed, we'd never be able to tell whether the imports were well used or not, and therefore it was better to look at a specific project in the terms which we use now.

Then there were all kinds of debates as to how far we ought to go with projects. We've gradually gone deeper and deeper into getting into the details of projects. Some of us think that sometimes we go into too much detail. But this is something that's a matter of degree and it's hard to pose this as a policy issue.

Another issue that was discussed in the early days—the question of whether you should say to a country, "We'll make you a line credit of say, 20 million dollars to be utilized for projects that you work up, and when you work them up we'll examine them and if we're satisfied with them then we'll let you draw on this line of credit against them"—this is the device which the Export-Import Bank used very extensively and still uses, and DLF has used, and it's got the great advantage that if the borrowing country has an immediate political need for money, you can assure the country that they're going to get money if they get sound projects and stimulate project preparation. And you give them great assurance in their planning. It has the added advantage for institutions like the Export-Import Bank that they make double capital out of it. They make capital out of the time they grant the line of credit, and then they again make capital in publicity terms at the time they approve the drawing on the line of credit.

The basic difficulty, and the reason why we didn't adopt it, is that it puts terrific pressure on the lending institution to approve projects, because once it grants the line of credit, then if it never finds a project that is satisfactory, the pressures build up and the government will say, “Maybe you didn’t mean this line of credit, you give the line of credit but you haven’t approved a single loan on it.”

We thought we would be in a better position to make sure that the country did the things necessary to absorb the money effectively if we didn’t extend the credit until the project was ready to receive the money. Now, we’ve had a different policy of course in connection with development banks, where we’re simply putting a development bank in a position to make commitments which they have to work out afterwards.

But I think on the whole our policy in this respect has been sound, although it puts us sometimes under criticism that we don’t function as generously as some of the other institutions.

Q: I think you left the impression that Mr. Collado was inclined to want to give lines of credit or more general balance of payment loans. Is that correct? Or was it the board of directors, for example?

Demuth: The Chileans had come up with a loan request and mentioned a number of projects, but none of these projects had been worked out to the point where they were ready for financing. Our first development loan was in fact to Chile. I think about two years later, and I think it was for one of the projects included in the original request. I suspect some of the projects that were in that 40 million dollar loan request have never gone through yet. So I suppose some of them were good and some of them weren’t. You’d actually have to go back to the records to see on that.

Q: I wonder if you'd like to say a bit more about the whole technical assistance operation.

Demuth: Yes. That's a big subject. We started in this technical assistance field as the result of a realization that although we were being very careful to see that our money was used effectively for priority projects, all the care that we were using in connection with our own money wasn't going to have very much effect on the development of the country if they were using the resources released by our loan and all the other resources for silly projects, wasting the money. Basically we weren't a bank just in terms of wanting to lend money and get repaid with interest, but we were interested in the effects of our operations on the development of the country, and that development was going to be very much more affected by what the country did with the 90 percent of the resources that came from domestic sources or other financing agencies than by what it did with just the small percent, the small fraction, that came from us.

In part this was also due to the fact that in order to determine the priorities of projects presented for Bank financing, we had to look at the whole program of a country to determine whether a power project or another project had priority. So we had to look at what they were doing in the whole field of industry and agriculture, so that our people were gradually getting a good deal of knowledge about the economies of some of our countries. And we realized that very few of those countries had effective programs of any sort.

So we felt that—we had a number of discussions internally before we ever took any outside action—that if we could effectively help these countries program the use of their own resources, using bank loans as both a carrot and a stick, we might be doing very much more than just finding a few projects to finance ourselves.

There was a good deal of opposition to this approach within the Bank. People were saying, "Well, if we help the countries draw up a program, then we will be committed to finance a portion of that program. Do we want to take this commitment?"

And to their credit, the management of the Bank said, "Yes, there is a moral commitment, and we recognize it and we want it. We're anxious to make loans for sound programs. We think we can make more loans where a country has a good program and uses its own money effectively. We can accomplish more of the Bank's objectives. So we're not worried about the moral commitment."

Q: Is this a particular period or time in the Bank's history?

Demuth: Well, this was I think around 1950, '51, because—

Q: Shortly after Mr. Black became president?

Demuth: I don't know if Black or McCloy was president at this time.

Q: Black became president in '49.

Demuth: It must have been after Black became president. Well, we did a lot of talking about this and there are internal Bank documents on this subject, as to what we should do. At that point Mr. Garner got very interested in Colombia, got very close to some of the leaders of the government in Colombia, and we had more or less decided that we were going to make Colombia somewhat of a showcase, show what we could do in one country in Latin America, and this might have a stimulating effect on other Latin American countries around.

Somewhere along this time, the Colombians came in, or some of the Colombians came in—I think it was Emilio Toro, who was then the Colombian director at the Bank—and said, “We’re having a hard time making decisions on our investment program because we’re divided into five separate regions, and we’ve got more regional loyalties than we have national loyalties. Everybody thinks first of his region and second of Colombia as a nation. So all our decisions are made on the basis of balancing all of the regional and political influences against other regional and political influences, and nobody’s looking at the problem on a national basis—won’t you send a commission down here and recommend a development program to us?”

To what extent this was an original idea of Toro’s or initiated by Toro and to what extent it was implanted in Toro by Garner, I don’t know. I think he had a good deal to do with stimulating the request, because it was something we were anxious to try out.

Q: Toro was what?

Demuth: He was the Colombian executive director of the Bank and an important influence in the Colombian government at that time.

At any rate, we did get the request, we agreed to accede to it, and then we went about trying to organize a mission. We spent months getting the first head of the mission. We got Lauchlin Currie. That's a story in itself but I won't go into it at this time.

Q: Was he already in Colombia?

Demuth: No, he was at that time a business consultant in New York, an economic consultant in New York. And we got about a 14 or 15 man mission that went down to Colombia and spent three or four months there and came back and spent a year writing a report. And that report has since been extremely influential in helping shape the development program of Colombia.

After the report was written, we were faced with the problem of how to translate a report for a—into a Colombia program. We suggested to the Colombians that they set up a non-partisan citizens' committee to review the report, and to make recommendations to the government as to the action the government should take on the report. They did. They set up the Economic Development Committee. This was the first time in years the two parties had worked with one another. And they sat for months, with help and encouragement from the chief economists on the mission, considered various aspects of the report, made their own reports to government, and a great deal of action followed from that. At the same time we published the report here and I think they published it in Spanish. And we had a good enough view of this report that we decided the technique should be extended to other countries.

Then I think Turkey asked for this kind of mission, and we sent the wrong kind of mission to Turkey—personalities who'd made their way in the business world but had no idea what economic development consisted of. That mission was headed by a man who'd come up through Sears Roebuck, who went out to Turkey on a preliminary visit and came back and recommended a mission—a mission composition on which there was no economist. Well, unfortunately we still employed him to run this job, and the mission was a terrible mess and we finally had to pick up the pieces and write the report ourselves. We wasted—

Q: --why did the Bank decide to go outside of its own staff to do these reports in the first place?

Demuth: Necessity, because it takes—oh, it's a year's report writing job at a minimum, and although we always put some people from our staff on the mission, we couldn't even put all the economists on, to say nothing of all the specialists. Some of the specialists required were in fields where we had no experts on the staff, and even where we did, our people were very busy operationally and we felt that particularly in the specialist group, we could effectively go outside. And this is a pattern that's developed really over the years. We always put on these missions with a few exceptions – it's our policy always to put on these missions from the staff either the mission chief or the chief economist or both and usually one other economist.

This way you get the experience we've had in this field translated from one mission to another. Then we usually get one or two economists from outside, and then some of the specialists from outside. Sometimes we have a transport man from the Bank or a power man or an industry man, but usually the Bank's staff is so busy we have to go outside. And this is a field where you can, because on these specialists' jobs it's only a four to six months assignment and people are very anxious to get them. We've been able to get some very high caliber people that way that we couldn't ever have hoped to attract to the permanent staff of the Bank.

Q: Was there also a consideration of the sort that you were talking about before, that the Bank did not want to get too closely involved in the missions because this would imply that the Bank was going to finance the program the survey developed?

Demuth: Well, this is kind of a fuzzy area. Our legal posture is that these reports are the reports of the missions, in fact they're the reports of the mission chief who's responsible for the report, and all the Bank does is approve the report in the sense of certifying that it's a piece of work done by a serious and competent group that should be given very careful consideration by the government. The Bank doesn't approve the individual recommendations. Nonetheless we recognize that in the country those are regarded as International Bank reports. We reserve our legal position, but it doesn't really affect our moral responsibility, and we know this, and because of this we very carefully review those reports, and we have in many instances pressed for substantial revisions in the reports simply because we didn’t think that they were reports that we wanted to live with. We’ve had many hot discussions and many very very difficult sessions, where we had to get reports rewritten because they weren’t something that we were going to stand back of. On the whole, however, I think the end results of these reports, in almost every instance—there was one case that we weren’t very proud of and some others that weren’t quite as good, but for the most part these reports have been something that we were quite ready to stand behind. And surprisingly enough, they have never really embarrassed us as one would have expected with the very substantial number of recommendations that go into these reports and the large number of countries, that we would have been embarrassed and subjected to substantial criticism for erroneous or incompetent reports and recommendations. This has happened in individual cases but nothing of any serious nature at all, and to the contrary, the reports have had a much larger influence than I expected. I’m always pretty cautious about this because it’s terribly hard to tell what the effect of a report is. You never know how much would have been done if there’d been no report. You never know how much actually is attributable to the report, or the training, which some local official has obtained through his contacts with the missions. I’ve been pretty cautious in assessing the value of these things. I remember once I gave a lecture at EDI about this and was being very cautious, and I got very strongly attacked by three members of the EDI who came from countries to which we had sent missions, and each of them said that I was badly understating the effect of those missions, that the organized development effort in his country had really started from the time the Bank's missions went in. Which was very encouraging to hear.

The one thing I think it would be wrong to conceive of these missions as thinking up of brand new development programs, or come up with bright new ideas that have never been thought of before. Basically what they do in most instances, is to give support to the people in a country who are trying to do the right thing but frequently don't have enough power or political influence to do that, and having the Bank report to rely on, they can do what they wanted to do anyway. The missions also provide a longer-term perspective, of a kind that a day to day operating official of a government can't easily get. The missions go out and stand away from the day to day problems and take a longer view than the government would normally take.

Q: I suppose the fact that the Bank is in charge of the report, so to speak, if not legally committed to its conclusions makes the report much more useful from the standpoint of the borrowing country than if the report had been done say by a center of international studies at MIT or any given outside organization.

Demuth: Well, I think, Number 1, the Bank has a reputation that most of the other organizations don't have, so that when the finance minister or the prime minister gets up and says, "We must do this because the Bank says we must," this has a great deal more political importance than if they say, "We must do this because Max Millikan says we must." So that's Number 1.

Number 2, they help to get financing, which is extremely important. Number 3, and this to me is very important, the program usually must include not only use of domestic resources but use of resources that can be reasonably expected from the outside. That means you have to make an estimate as to what people expect to get from our Bank, the Export-Import Bank and whatnot. It has to be a pretty realistic assessment of what outside resources are likely to be obtainable. And when other bodies send out missions, they're not responsible for financing, and they're liable to take the needs and say, "Here's what needs to be done, this is a reasonable objective, this is the amount of money that will be required," without thinking too deeply about, can that money be repaid? Is it likely to be forthcoming in a form that doesn't have to be repaid? And so forth. So you find in most cases in reports written by UN groups or FAO groups or others that used to be in this business at one time, an unrealistically high program is presented, which never can find the finance, and which has the result that when it isn't carried out it causes disillusionment and discontent, worse than if the report hadn't been done.

I think our reports on the whole have been inclined to be more realistic, without being too bankerish in the sense of trying to cut it down to a minimum. We try to give alternative programs, depending on the amount of money the country will find available.

Q: Did the Bank coordinate its missions in any way with these of other organizations like FAO?

Demuth: Oh, yes, we’d always go to FAO for example in picking out agricultural exports. We’d have them briefed by FAO on the way out, and debriefed by FAO on the way back, and we’d send the pertinent parts of the report to them in draft form for comment. Similarly with WHO and UNESCO. In these countries like Libya where the UN has had a big program, our whole report is submitted to them for review. The mission retains the right to reject the comments of the other agencies and in some cases there are fundamental disagreements on some points that never do get resolved. These are the exceptions. We work very closely with the other agencies and they have told me that they find it very useful to have these reports.

One of the most interesting things about these general survey missions has been the fact that several colonial powers have asked the Bank to send missions to their colonies. This has been particularly the case with the U.K. Not that the UK couldn’t organize a mission that was just as good as any we could organize, but if they did it and sent it out, the local government was likely to think the report of the mission was made for the benefit of the UK rather than for the benefit of the colony. So the U.K. decided that they would like to have these developing country missions come from the Bank, even though that meant that the colonial office in the UK lost control of what the report said. The missions had a great deal more acceptability coming from an independent institution. And the UK colonial office has in fact been our biggest client for this type of mission. I think it's been a very useful relationship.

Q: What did the Bank itself do with these survey mission reports? How does it use them?

Demuth: Well, I think we use them as background material. I think in the early days the operating people were inclined to slough off these reports if they didn't like them and this is one of the changes we were seeking to accomplish by putting technical assistance responsibility in the area departments so that these reports would be made by missions for which they, rather than some other department of the Bank were responsible.

The views of the operating departments vary considerably. I think some of the reports are used very religiously as guides for their own actions, others they're likely to be skeptical about. But I think on the whole they're quite useful, and I think they're being more useful.

Q: Has the Bank ever considered using these survey missions as a sort of a starting point for continuous advisory service to a number of governments for helping them plan development programs?

Demuth: Well, this is the idea from the beginning, that the survey mission would be the first step, and we would then maintain a continuing relationship with the government, helping them to translate the mission report into a national development program, and then helping them to carry it out. It's never worked quite this way, but taking that Colombian survey mission, in the beginning, we first sent the mission down, then we sent people down to help them consider the mission report and decide what was to be done and eventually we sent some advisers down to work with what was then their planning office and start implementation.

Q: Were these advisers people from the Bank's staff?

Demuth: Yes. It turned out that some of them left the Bank and got plush jobs with the Colombian government, to our annoyance. But I mention this as the archetype of what we ideally wanted to do in our relationships. The difficulty, of course, in all of these exercises was the lack of people. It's terribly hard to find the very high level people that are necessary for this sort of job, who are willing to live abroad for a long period of time. The people who were best were the people that the Bank wanted to keep in its operation, and the demand for this sort of thing was tremendous. All during the last ten years, the realization of the need for programs, the desire for programs has been growing, and development economists have been more and more in demand, so that we just didn't have the people to carry out the kind of relationship that we would like to have.

A number of us have been wrestling with this problem for years. We've suggested that the Bank should have additional people available for this kind of work, and we advocated what we called the fat man policy. The fat man policy was that we should have some fat on our bones to be available to be stripped off and made available to the countries for advisory services. And it was agreed some time back that it would be very proper that the area departments should have one or two "fat men." But what happened was what almost inevitably would happen. The people that were any good were very quickly absorbed in operational work, and there never was additional personnel. That overstates the fact. Every once in a while we manage to pry somebody loose to take a technical assistance requirement; we've had a resident mission in Pakistan and a number of resident missions in South America, and now Nigeria—but we never were really able to build up the kind of extra people we needed for this sort of work. And there were a number of reasons for that. One of them, I think, was the fact that department heads were quite naturally reluctant to take on people when they didn't see exactly what job they'd fit into. Secondly, this requires a pretty high level type of person, and to get that kind of person into an organization already established is likely to disrupt morale. Because they have to be brought in at a higher level than many of the existing staff. Because we have a necessarily pyramidal organization it would disrupt the hierarchy to get these people in at high level kinds of positions. And I think there was also probably opposition by some of the operational heads who were very much more interested in making loans than in looking at development in a broad way and considering their responsibility for development, as a developmental, a broad developmental responsibility in which financing was a major tool, rather than just a financing responsibility. It varied considerably and does still vary from department to department, depending on the personality of the department head.

At the same time that we were unsuccessfully trying to add to the economic talent available for this sort of work, the demand grew and grew, because not only were there more and more countries, as new countries became independent and needed economic talent, but some countries that had done a lot of planning in the past began to get into high gear in their development efforts and needed more people to be sure they were doing the right things, and there was generally much greater awareness of the importance of some kind of programming, as evidenced by the US Foreign Aid Bill, for example, where now the great emphasis is on the kinds of things that we've been preaching for a long time.

Well, up til now, our technical assistance program has been concentrated, simply because of the lack of personnel, and we didn't want to overstep our bounds and get in the way of other organizations. We've been concentrating on short term experts, short term missions, survey missions, and similar kinds of advisers going out for short periods of time. We've always known that this wasn't the whole answer or even a major part of the answer, but it's become apparent that there's a tremendous gap in people who are available to do resident advisory jobs, that the ICA personnel is very spotty for the most part, not terribly good for this sort of thing. The UN has never been able to acquire them. In a few instances some good people have gone out under contracts, like Ford Foundation contracts, to Pakistan and

Iran, but there just is a tremendous need for more people available on a full time basis, particularly for long term resident assignments.

When we tried to find these people outside the Bank, we ran into the problem that nobody wants to leave his occupation and career for two years with no assurance of re-employment, with everything in the process of going ahead rapidly throughout this part of the world and not knowing what's going to happen to them when they come back, and if we really wanted to get the kind of people we wanted we had to offer a career service.

Well, we decided first to take these people on in area departments, the fat man policy and so forth, but that didn't work out, and this summer finally we have decided to establish, partly as an administrative technique, a new foreign service which we are calling the Development Advisory Service, which is largely an administrative gimmick designed to enable us to get in high level people without their worrying what their position is vis-à-vis the economic adviser and the area department director, etc., and with their positions and salaries and so forth depending on their professional qualifications, not on their particular positions in the administrative hierarchy.

This was decided on after consideration of very much more drastic approaches—that we should sponsor an institution that would be independent of the Bank, and although the Bank should run it in the sense of naming its head and lending it the authority of its prestige, it should be entirely independent of Bank policies and should go out without the supervision of the Bank. We felt that we couldn't do this because we couldn't give the Bank name without being sure that the people were going to follow the general lines of Bank policy, and it could really disrupt things, to have advisers go out from an institution that we sponsored while we at the same time keep on with our normal activities of giving advice and reviewing the plans.

We didn't have enough people available for any of that to happen. An independent outfit going out meant that the Bank would have to review everything that was done and perhaps come to a different conclusion. So although we saw some advantages in the suggestion, we thought the disadvantages were greater, and we set this thing up as an integral part of the Bank.

Q: These will be full time people?

Demuth: These will be full time people that will be available for a variety of things—resident assignments abroad, being chief or chief economist on a survey mission, short-term assignments abroad, and then in between assignments abroad doing operational work, teaching, doing research, working at the Economic Development Institute. What we want to do is give a satisfying career in the whole field of development with perhaps two thirds of the total time spent in resident assignments abroad. Now, whether we'll be able to get the people to do this sort of work is the great question. We have presented it to the board. We have presented it as an experiment. But we're sure the demand is there. If we can get the kind of people we need, I'm sure they will be immediately absorbed, and this thing will grow into a very large operation. But it won't grow rapidly because it's going to be so hard to get the people. What we eventually want to do is to build this up in such a way that it becomes the capstone in the career of a Bank economist. From the most part we'll recruit people from the operational staff of the Bank, after they've been trained in the operational side of the Bank, who gravitate towards development. In the beginning I hope, as I said, in the course of developing the advisory service, some of the senior Bank people will be transferred to it.

Q: Is this a brand new departure for the Bank?

Demuth: Yes, the organization questions haven't been fully settled. The only thing that's been settled now is, it's an administrative service within the Bank, headed by somebody with the rank of a department head. Exactly how it will be set up, I don't know. There was considerable thought given to setting it up more elaborately as a development center, including the Economic Development Institute, the technical assistance program, advisory service, all within a center. We decided not to do this initially. Whether it will eventually come to it or get to something like it through other mechanisms hasn't yet been decided.

Q: Maybe you'd care to say something about the Economic Development Institute as such, in its relationship to technical assistance.

Demuth: The Economic Development Institute idea was first stimulated by Paul Rosenstein-Rodan when he was on the Bank staff, although I think he had in mind something that was considerably more advanced in theory. Eventually for my sins I was put in charge of trying to work something out of the idea, developing it. Mr. Black was enthusiastic about it, as something to do—nobody'd ever gotten down to seeing what we could effectively do. And my staff and I did some scouting around in the United States, talking to a lot of people. There was a lot of academic doctrine, theology, that was very foreign to us—the question of whether we would give a degree or not give a degree. We had in mind at one time asking Harvard to do this for us, but to do it in Washington where we could make our people available, and they refused to do that. They said the whole idea of a university was to be concentrated on a campus, not outside. We talked to MIT, the same way, and they didn't want to do it. Finally we discovered we were getting over our heads. We were getting involved with educational matters we didn't know very much about. We decided to ask Alec Cairncross to spend a summer here and work out a program, and Alec agreed to do that. He came over and spent a summer and wrote a report. What he very much had in mind was the Merrill Center in Southhampton—the idea of a group living together and working together for a year, six months, and great mind-stretching exercises between the people. We generally approved what Alec proposed, and then we talked Alec into agreeing to head the thing for the first 18 months.

Then came the problem of trying to find a Merrill Center in the midst of Washington, or close enough to Washington that staff could be made available, not so far out that people would feel isolated, and this proved just about impossible. Eventually we got a great big old mansion through Mr. Meyer, that he owned, his own home. We then went through the problem of decorating it, and found that we didn't really know very much about how to run boarding schools, but we got the place decorated and we got our first group in, and we ran into all kinds of trouble. A Pakistani came in—I think it was a Pakistani—and said he'd never shared a bathroom even with his wife, and why should he share it with his Indian colleague across the hall? An Indian wanted tea served in bed. He'd always had tea served in bed, why shouldn't he have it? They were a miserable and unhappy bunch because they weren't getting the kinds of facilities they were used to, and they were thrown on top of one another. So the first year was a very difficult year.

Alec was very interested in the intellectual aspects of the year and very impatient with these administrative housekeeping details. The net result was that they had an exciting time intellectually and a miserable time in their personal relationships, and we had to do a lot of rethinking about that.

Alec really gave the Institute a very distinctive character, through his own personality, and the persons who were part of his first faculty were among the best people at the Bank. They worked up a pretty good curriculum. My goal then was merely one of making contact with the Bank and I worked with them to a certain extent on revising their curriculum. Alec left the middle of the second year, and Mike Hoffman came on. Mike considered his job quite differently from Alec. He considered his job to be more that of the executive director, getting other people in to do the substance, not trying to do as much of it himself as Alec did. At the same time, he was a much neater administrator. The calibre of the participants has been very good. This was our great worry at the beginning, could we get people who were good enough to warrant the expenditure of money? On the whole the calibre has been very good. I think the discussions have remained lively.

I’ve been disappointed in two aspects. One is that we don’t in the Bank get as much of the benefit of these discussions and criticisms of the Bank’s policies or suggestions of new Bank policies as we should. There’s no a two way interchange there. The Bank people go teach at the EDI, but there’s never been the mechanism through which the value of what goes on in the discussions at EDI comes back to the Bank. And perhaps related to this, I’ve been disappointed that EDI hasn’t published more. I had hoped that as a result of these discussions, preparations of lectures and preparations of teaching materials, we’d be able to get out some teaching material on economic development that would be useful, and get more people knowing more about development which would redound to the benefit of the Bank, and that we’d get more books published of the kind that Bill Diamond wrote on development banks, which was stimulated there. We’ve had a few, Bill Diamond’s book, and the Tinbergen pamphlet was really done on Rist’s initiative for the EDI. Now Al Waterston is working on something, organization for development planning. But there hasn’t been as much thinking and writing on the Bank as I really think there can be and should be and maybe in the future will be.

Q: I've heard that initially there was hope that the EDI could make considerable use of the experience of the Bank itself in the development field, but one of the difficulties was that loan negotiations and working party reports and so on in the Bank couldn't be made fully available, for reasons of the confidential nature of the material involved.

Demuth: Well, that puzzled me, because one of the early decisions that was made was that we were going to treat the EDI participants as Bank staff members and we would make available confidential material, with agreement by them not to reveal it. I was under the impression that they utilized Bank materials very freely in teaching courses. I'm surprised at this—if it's true, something ought to be done about it—I didn't realize it was so. I also think—we're not talking history now, but of the future—but I do think EDI should and probably will experiment. I think we need a great many more training courses. For example, I think we need a course, a training course for development bank people. I think we ought to have a training course in project appraisal for programming people. This may require different kinds of facilities, different kinds of staff, but there seems to me no reason why you can't or shouldn't take advantage of our experience in the Bank to have short as well as long courses on specific subjects as well as on the whole broad spectrum of the problem.

Q: I think you said, didn’t you, that you’re hoping to have some sort of a coordination between this new advisory service and EDI?

Demuth: Well, I think there has to be. I think the members of the advisory service should be available from time to time for teaching. It seems to me that a great deal that’s being done at the EDI would be of value to these people in the advisory service. What Waterston is doing, I mentioned, on organization and development of programming, certainly ought to be useful to most of these advisors. So I would think there has to be a pretty close relationship. Training is just one aspect.

Q: There’s about five minutes left on this tape. I wonder if you’d like to use it to talk about development banks, or is there something else that you’d rather deal with?

Demuth: Well, development banks—that’s another big subject. I guess Garner again was the one most responsible for getting us into this field. It started out when he perceived the necessity for establishing some kind of an effective long term industrial financing mechanism in Turkey, wanted to get it out of state control, and proposed the establishment of some kind of a private investment institution that the banks would own, and gradually get investors in.

This is a very difficult field, because we’re aware all the time—our bank policy has been that we will support only privately owned development banks, but we know that privately owned development banks in most underdeveloped countries can't exist without some kind of subsidy, and the only place that subsidy could come from is government. So we set up private banks with government support and government subsidy, and then try to make—try to get every assurance that the government won't have anything to do with the operation of the banks. This is a pretty difficult road to follow, because it takes a far-seeing government to say, "We'll give half of the resources or guarantee loans and so forth for these institutions, but we will have nothing to say about them," when they are prime agencies, prime instruments, for pushing a major sector of the economy.

On the other hand, many governments have recognized that government-owned instrumentalities are apt to get their resources frozen through making political loans, and this is an ineffective way of carrying out development.

All of these institutions are sort of anomalous. They're privately owned, with a certain amount of public funds, a certain amount of public influence. But on the whole I think the record has been pretty good. The two biggest banks, the Indian and Pakistani banks, Mr. George Woods of the First Boston Corporation set up as a consultant to us; both of them have had tremendous troubles, troubles in part caused by the necessity of having a foreign manager, as there was no local investment banking experience, but a foreign manager brings problems with him, no matter how good he is—in some cases foreign managers have not been as tactful or as good as they should have been. The board sometimes necessarily represented the industrialists of a country, because they were the people with the money, but where they had an interest in either promoting or preventing projects going forward—and practically everything that came up in India for a while, there was somebody, usually a number of people on the board, that had an interest either in promoting or in stopping it.

The fact is that in most of these institutions, the motive of the private people that come in isn't an investment motive, because these institutions have such a large overhead that you can't develop an institution that—they can't be very profitable, and investors of any sense don't go in to make money. They go in either out of patriotic motives or because they see that the institution would be good for their own banks, industries or whatnot.

Q: What is the role of the World Bank in getting these started?

Demuth: Well, we have been a motivating force, in Turkey, India, in Pakistan, they saw the Indian one and they said they wanted one like it, and then we promoted it. In Iran, the actual lead there was taken at the request of the government by Lazard Freres and Chase International. We participated in the discussions, and were an almost necessary intermediary between the government and Lazard Freres and Chase. In Ceylon the bank was set up at the suggestion of a survey mission, and again as the result of a bank mission that went out there and promoted it. Similarly, we provided either technical assistance or actually suggested the idea in Thailand and Taiwan, where they have a very good little development corporation. The history of that was that they sent a bankers' mission over here, and we talked to them about some of the things we'd done in development banks elsewhere, and they went back and recommended that a development bank be set up. We sent out a mission. They actually beat the gun, because they set up their development corporation before our mission reported. There've been various ways we've given encouragement, advice and assistance. Sometimes we've put people out for a period as advisers. Bill Diamond was out in India for a year.

Q: Do you make loans to these?

Demuth: Yes, we've made—most of the development banks, we've used as an intermediary through which we can make loans to private enterprises. We can't make direct loans to anything but big private enterprises, because they're the only ones in a position to get government guarantees or which can afford to accept a government guarantee. But in terms of processing the medium and smaller sized industry, industrial projects, the development bank knows the people, is in a position to process their loans, and they don't have to have a government guarantee for their sub-lendings of our loan. There's a pretty full discussion of all this in the two books that we put out on development banks, so I'm not sure it makes much sense for me to go into it more fully here.