LENDING POLICIES OF THE WORLD BANK:

A THIRD WORLD PERSPECTIVE

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Lending policies of the World Bank: a Third World perspective

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Introduction

"Do you believe the World Bank will play an important role in Peru during the next decade?"

"Yes, because I believe there has been an important evolution in the World Bank's policy; it is now participating in sectors in which it did not participate before, and these are precisely the key sectors for Peru during the coming years." (1)

This was the answer given by Manuel Ulloa, Peru's designated Prime Minister and Minister of Economy and Finance, in an interview in June 1980, several weeks before the recently elected government was to assume power. During 20 months in office, the new Peruvian administration has begun to work very closely with the World Bank.

Two basic areas of cooperation seem to exist. First, the government expects to become a major recipient of concessional loans from the World Bank, aiming to borrow between US $300 and $350 million annually (2). Second, the Bank seems to be strongly increasing its influence over the new administration on economic and policy issues. So far, the Bank has prepared an important report, PERU: Major Development Policy Issues and Recommendations, in which it outlines economic priorities in the macroeconomic development planning process. The Bank has also worked
with the government in the selection of 88 specific projects, known as the Investment Plan 1981-85, that would require public and private international financing. This work culminated with a meeting held in Paris in May 1981 of the Consultative Group of International Financing, in which these 88 projects were offered for financing to the representatives of 26 bilateral agencies and officials of all the multilateral financing institutions (3). It seems clear, therefore, that the Bank will play an important role in Peruvian development during the years to come.

This paper focuses on some of the organizational, political and economic issues involved in the World Bank's lending policies to the Less Developed Countries (LDC's) in general and to Peru, as a case of study, in particular. Although much has been written about the World Bank as an institution, often considered interventionist and neoimperialist (4), and about how it functions, little is known on how the Bank works in specific countries from a historical perspective and from an outsider's viewpoint. To understand the policy issues involved in World Bank lending programs it is indispensable to see how the institution works and to understand what its initial objectives were and how these goals have evolved over time. Therefore, the first part of this study will attempt to explain the general operations and activities of the Bank. The second part will analyse
the role of the World Bank in Peruvian development. Some of the issues I will discuss include the extent to which the Bank has been a successful source of financing, the criteria used by the Bank to approve Peruvian requests for economic assistance, and the degree of leverage, if any, the Bank has in Peruvian internal affairs.

I would like to stress one final idea that, although not explicitly developed in this paper, will underly many of the things that will be said and, in a sense, is a general framework to what I shall study. It is the idea of how theories of development have changed during the last 20 years, especially during the last 10 years.

What some authors (5) call the "first generation" of development theories were mainly concerned with the problems of economic growth and accumulation. The main goal of development was understood to be the need for a substantial increment in productive investment. The magic formula was, therefore, the rate of growth of the Gross National Product (GNP). Since the industrial sector was the most important engine of growth, the efforts of most governments and international organizations were concentrated in promoting industrialization, while the traditional agricultural sector was relatively neglected. The additional investment needed to create an additional unit of
output, the incremental capital/output ratio, became a basic question in economic discussion.

But as Herni points out (6), this conception of the development process seemed to be mistaken in several of its assumptions and had not taken into account other, often non-economical factors. Some of the wrong assumptions, experience had demonstrated, were the idea of perfect competition in an integrated national market and the idea of capital accumulation within a steady growth path. First generation theories failed to consider the fact that in many poor countries, especially in Latin America during the 1960's, the recycling of surplus capital by entrepreneurs was not usually reinvested in productive areas in order to accelerate growth but, on the contrary, was often spent in unproductive activities. No consideration was given as well to the fact that in the poor countries agriculture was not sufficiently highly developed to constitute a basis for industrialization, as had been the case in Europe during the Industrial Revolution.

"Second generation" development theories were more concerned with problems of allocation of resources than with problems of accumulation. More importance was given to income distribution and to the quality rather than the quantity of investment. The importance of the agricultural sector was dis-
covered, with its great potential for employment generation. As a result, most international development banks reoriented their lending policies from highly capital-intensive projects to more labor-intensive projects and programs.

As Mahbub ul Haq points out (7), the thinking of economic development had undergone a quiet revolution in the 1970's. The essence of this revolution was quite simple: economists had finally graduated from a fascination with the intermediate means of development to a consideration of its ultimate ends. They finally recognized that although the growth of Gross National Product (GNP) is absolutely necessary, it must be directed intelligently toward the problems of mass poverty. While development theories still need to consider how to increase production, they have finally added the more fundamental question: for whose benefit?
I) The Bretton Woods system

During the final months of World War II, the allied countries, particularly the United States and the United Kingdom, were already concerned with the post-war economic situation. The war had left a great part of Europe destroyed, and many countries that were suppliers of raw materials during the war period had suddenly become aware of their strategic importance and of the disparity between their importance and their situation of poverty and marginality. The planners and negotiators of the allied countries, aware of this situation, had three objectives in mind for the post-war years: external resources for the reconstruction of the European countries; financing economic development in the poor regions of the world, particularly in areas that supplied raw materials; and expansion of trade and investment abroad, especially to prevent a post-war economic crisis in the United States (8).

Although informal conversations had already begun before the war had ended, the allies did not officially agree upon structures to accomplish these three goals until the Bretton Woods conference in July 1944. Three international organizations were to be established: the International Monetary Fund (IMF), the International Trade Organization (ITO) and the International Bank for Reconstruction and Development (IBRD). The
IMF would repair the disintegration that had befallen the international monetary system prior to the war and would regulate monetary policies in order to prevent international monetary crises in the future. As the years have passed, the IMF has increasingly played a "confidence building" role. Its approval of a nation's economic policies allow that nation to more readily obtain financial assistance from capital-exporting countries.

The ITO would work to liberalize trade, to reverse the protectionist and discriminatory trade practices that had multiplied during the pre-war depression years. The ITO was never created because of the opposition of the United States Congress, but the basic idea was crystallized in the General Agreement on Tariffs and Trade (GATT). The third institution, the International Bank for Reconstruction and Development, would stimulate and support foreign investment, which had declined to insignificant amounts during the war.

The initial proposal for the IBRD was made by the United States Treasury in November 1943 in a document known as "Preliminary Draft Outline of a Proposal for a Bank for Reconstruction and Development of the United and Associated Nations" (9). The emphasis of this proposal was that investment capital should be provided to LDC's and Europe primarily by private
investors. Thus, it would be necessary, particularly in the immediate postwar period, to encourage private investment by sharing the risks and providing actual funds from the Bank as a supplement (10). Some of the major issues of the proposal were as follows: the Bank should grant loans to or through government or political subdivisions of the member countries on an untied basis; the Bank should be a "lender of last resort" (11), that is, the Bank should grant a loan only after commercial banks or other financial institutions demonstrated that they were not interested in the project (12); the Bank would have a certain amount of control over the feasibility and execution of the project or program, although it was clearly understood that the Bank would not interfere in internal political aspects of the borrowing country and that only economic considerations should be evaluated when approving or rejecting a loan petition; and, finally, the IBRD would only lend under special terms: concessional loans with low interest rates and long periods of repayment.

Although most of the countries participating in the Bretton Woods Conference were in agreement regarding basic considerations, there were two related areas in which participating countries maintained opposing views and which have played a key role in the lending policies of the Bank. One of these areas was the controversy over the purpose or destiny of the
World Bank's loans. Under the initial United States proposal, financing would be provided to specific projects under the understanding that loans would only be granted to help increase the productivity of the borrowing country (13). This approach gave the Bank much more leverage, since it could directly control the use of the money being lent. Article I of the final Charter of the Bank indicates that its purpose is to "facilitate the investment of capital for productive purposes". In June 1944, the United Kingdom proposed alternatively that the Bank not only lend for specific projects but, in addition, should make loans "of gold or foreign exchange to a member country" to help it in critical balance-of-payments situations (14). This later became a very important issue since the US Congress, adopting a different view from that of the Executive branch, wanted the Bank's functions to be enlarged so as to permit it to make long-term stabilization loans (15).

A compromise solution was finally reached. The Charter of the Bank stated that loans would be made for specific projects "except in special circumstances" (16). This was interpreted by the Executive Directors as permitting loans other than for specific purposes (17), and, in practice, has been the "legal window" through which the Bank was able to shift the emphasis of its loans during the 1970's from highly capital-
intensive projects to more general "structural adjustment" loans.

The other related are in which no consensus was initially reached was that of the emphasis that should be given to the Bank's operations: development vis-a-vis reconstruction. Although the issue lost some importance with time, as European countries turned from borrowers during the reconstruction period to lenders as their economies prospered, it is nevertheless important to see how countries or regions of the world understood the role of the Bank and to comprehend what their expectations towards the Bank were. On the one hand, the European countries stressed the importance of loans for reconstruction purposes. Some of them were particularly interested in obtaining loans for restocking their raw materials inventories or for purchasing gold reserves for their currencies (18). This attitude was only natural since the war had totally destroyed the productive sectors of most European countries. Substantial investment, either private or through multilateral aid organizations, was needed to restore their economies. On the other hand, the less developed countries worried that if too much emphasis was placed on reconstruction, the Bank would never participate in development projects (19). The situation of Latin American countries was very special. As a consequence of their important role as raw material suppliers, they had
greatly increased their monetary reserves during the war years. However, they had been unable to purchase capital goods and other manufactured goods because of war-time restrictions (20). Thus, Latin American countries saw the IBRD as the institution that would provide the capital needed to develop the major economic sectors.

The Charter provisions left the question of priority of purposes entirely to the discretion of the Bank. Article III, Section 1 (a) of the Articles of Agreement, provides:

(a) The resources and facilities of the Bank shall be used exclusively for the benefit of members with equitable consideration to projects for development and projects for reconstruction alike.

The other two institutions that comprise the World Bank Group are the International Development Association (IDA) and the International Finance Corporation (IFC). The IDA, to which we will only refer incidentally because of the similarity in standards and policy issues to the IBRD, was established in 1960 to assist the poorest less-developed countries by providing development capital on very favorable financial terms (21). Its development credits are for a period of 50 years, interest free, and have a service charge of 3/4 of 1% on amounts due to be repaid (22).
The International Finance Corporation (IFC) was formed in 1956 to assist the growth of the private economic sectors in less-developed member countries. The IFC gives risk capital for productive private enterprises in conjunction with additional private investment. Investments are made in the form of share subscriptions and long-term loans. The IFC also provides financial and technical assistance to privately-owned development finance companies. In particular, it supports joint ventures which provide opportunities to combine domestic sponsorship with capital and managerial experience available in the industrialized nations (23). We will not study the IFC because it has not changed its strict private-oriented policies and has no socially oriented lending criteria.
II) The World Bank Structure

II.a. Membership

Membership in the World Bank Group is tied up with membership in the International Monetary Fund (IMF). Article II, Section 1 (a) of the IBRD Charter indicates that membership in the IMF is a precondition to membership in the IBRD and that IBRD membership is, in turn, a prerequisite to membership in the IFC (IFC Charter Article II, Section 1) and in the IDA (IDA Charter Article II, Section 1). Why has membership in the IMF been so important a World Bank membership criterion? The basic reason seems to be that the drafters of the Articles of Agreement were concerned about continuous monetary instability and considered acceptance of the monetary discipline imposed by the IMF as necessary for eligibility for long term loans (24).

Since World Bank Group membership requires IMF membership, one must look at the provisions of the IMF Agreement regarding membership in order to discover the required status of the members of the World Bank Group. Article II of the IMF Agreement refers to "countries" whose "governments" accept membership before December 1945 as original members and those who accept membership after December 1945 as admitted members. This unusual terminology, which in international law usually refers
to "states", raises two general questions (25). The first question concerns the effect to be derived from an agreement that refers to "governments" in the context of membership. To what extent are national institutions, e.g., legislative, judicial, private corporations, bound by the provisions of the agreement? Does "governments" mean only the executive bodies or does it include other national entities that are part of a state? By examining the IMF as a whole, one can see that many member obligations imply actions that go beyond the jurisdiction of the executive and they have been so understood. Two examples will illustrate this point.

(1) Among the obligations for membership is the requirement that members assign large amounts of money to be used by the Fund in its general operations. In most countries, this appropriation cannot be made solely by Executive agreements, but requires special legislation. Therefore, although the negotiation process to become a member can be performed exclusively by the Executive, there will necessarily be legislative intervention when it comes to the assignment of funds.

(2) Article VIII 2 (b) of the IMF Agreement provides that exchange control contracts that involve the currency of a particular member shall be unenforceable in territories of any member if contrary to that particular member's exchange control
regulations. Some judicial decisions from member countries indicate that courts consider themselves bound by this provision of the Agreement (26).

Apparently, then, one can conclude that the reference to "governments" as members in the IMF Agreement, and thereby in the World Bank Group, was not intended to have a meaning different from that which would have resulted had the members been referred to as "states".

The other question that the unusual terminology in Article II of the IMF Agreement raises is whether the drafters, by using the word "countries", were considering entities other than states to be eligible for IMF membership. If a functional interpretation of the Agreement were the basis for membership, it would have been necessary to admit to membership those entities that had control over the currency in circulation in particular territories: states, dependent territories or colonies, and monetary unions. But according to Article XXXI, Section 2 (g), separate membership for dependent territories is not permitted. IMF and World Bank Group practices reinforce the "state" interpretation; no entities other than states have been admitted to membership (27).
II.b. Sources of funds and voting powers

In order to become an independent institution for economic development, the IBRD first had to become a Bank; that is, the IBRD had to become a strong, reliable financial institution, not only with respect to the member countries that had formed it, but also, particularly in its initial years, within the international financial community. Otherwise, it would not have been able to borrow money from private sources. This turned out to be a difficult task in light of the world economic situation in which the Bank opened for business on June 25, 1946.

Before entering into an analysis of the sources of funds through which the Bank operates, we will examine how IBRD subscriptions were determined and how these subscriptions are related to the voting power of each country. Discussions concerning IMF quotas and IBRD subscriptions were carried out at Bretton Woods on the basis of a formula originally devised with regard to IMF quotas, proposed by the US Treasury Department. The main considerations expressed in the formula were as follows: the ability of the member to pay its quota; the frequency with which a country would have to make use of drawing rights to alleviate balance of payment problems and the amounts needed to be drawn; and the long-term impact of
international trade on national income (28).

While IMF quotas established a member's limit on the use of drawing rights and member countries, therefore, wanted a large quota in the Fund (29), there is no necessary relation between a member's IBRD subscription and the amount that the member can borrow. The correspondence between IMF quotas and IBRD subscriptions of member countries is not uniform and initially had been the cause of some disagreement among countries. After several days of discussion at Bretton Woods, the impasse was broken by the United States, which accepted an obligation to subscribe $3,175 million, although its Fund quota was $2,750 million. China, Canada and France also accepted subscriptions to the Bank that were larger than their IMF quotas, thus making it possible to reduce LDC subscriptions by approximately $200 million when compared to their IMF quota (30). Latin American countries, having initially proposed for themselves IBRD subscriptions of 60% of each country's IMF quota, finally agreed on 70%, except for Ecuador and Paraguay which subscribed 64% and 40% of their IMF quotas respectively.

The Bank, therefore, was initially formed with authorized capital of $10 billion US dollars, divided into 100,000 shares with a par value of $100,000 each. During the IBRD's first year, only 80,245 shares were subscribed to by the 44 original
members. As a result, the Bank initiated its operations with a subscribed capital of $8,024,5000,000.

The voting procedures rule is that each country has 250 votes plus one additional vote for each share of stock held (31). The 250 minimum votes per member provision was established in order to weigh the votes in favor of smaller, economically weaker countries. In practice, however, these minimum votes, even when added to the votes entitled by subscriptions, do not give small shareholders any significant control over Bank operations. And as we shall study later, the limitations imposed in the way Executive Directors are elected makes the formation of regional groups very difficult. These regional groups could otherwise vote together, increasing their power over Bank operations.

Because of its large subscription, especially during the Bank's first years, the United States by itself cast 34% of the total votes. Together with the voting power of the United Kingdom (14.17%) and France (5.88%), these three countries enjoyed a total voting power of 54.28% in 1947. Since Bank decisions are made by a simple majority of votes (32), they had absolute control over the Bank. It is interesting to compare the differences in voting power between Latin American countries and the five largest IBRD contributors:
### IMF quotas, IBRD subscriptions and IBRD voting power

(as of August 1947)

<table>
<thead>
<tr>
<th></th>
<th>IMF quotas (a)</th>
<th>IBRD Subscriptions (a)</th>
<th>IBRD Shares</th>
<th>Number of votes (b)</th>
<th>% Total IBRD votes</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Latin America</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bolivia</td>
<td>10</td>
<td>7</td>
<td>70</td>
<td>320</td>
<td>.34</td>
</tr>
<tr>
<td>Brazil</td>
<td>150</td>
<td>105</td>
<td>1,050</td>
<td>1,300</td>
<td>1.39</td>
</tr>
<tr>
<td>Chile</td>
<td>50</td>
<td>35</td>
<td>350</td>
<td>600</td>
<td>.64</td>
</tr>
<tr>
<td>Colombia</td>
<td>50</td>
<td>35</td>
<td>350</td>
<td>600</td>
<td>.64</td>
</tr>
<tr>
<td>Ecuador</td>
<td>5</td>
<td>3.2</td>
<td>32</td>
<td>282</td>
<td>.30</td>
</tr>
<tr>
<td>Paraguay</td>
<td>2</td>
<td>0.8</td>
<td>8</td>
<td>258</td>
<td>.28</td>
</tr>
<tr>
<td>Peru</td>
<td>25</td>
<td>17.5</td>
<td>175</td>
<td>425</td>
<td>.45</td>
</tr>
<tr>
<td>Uruguay</td>
<td>15</td>
<td>10.5</td>
<td>105</td>
<td>355</td>
<td>.38</td>
</tr>
<tr>
<td>Venezuela</td>
<td>15</td>
<td>10.5</td>
<td>105</td>
<td>355</td>
<td>.38</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>322</td>
<td>225.5</td>
<td>2,245</td>
<td>4,495</td>
<td>4.80</td>
</tr>
</tbody>
</table>

**5 largest subscribers**

<table>
<thead>
<tr>
<th></th>
<th>IMF quotas (a)</th>
<th>IBRD Subscriptions (a)</th>
<th>IBRD Shares</th>
<th>Number of votes (b)</th>
<th>% Total IBRD votes</th>
</tr>
</thead>
<tbody>
<tr>
<td>US</td>
<td>2,750</td>
<td>3,175</td>
<td>31,750</td>
<td>32,000</td>
<td>34.23</td>
</tr>
<tr>
<td>UK</td>
<td>1,300</td>
<td>1,300</td>
<td>13,000</td>
<td>13,250</td>
<td>14.17</td>
</tr>
<tr>
<td>China</td>
<td>550</td>
<td>600</td>
<td>6,000</td>
<td>6,250</td>
<td>6.68</td>
</tr>
<tr>
<td>France</td>
<td>450</td>
<td>525</td>
<td>5,250</td>
<td>5,500</td>
<td>5.88</td>
</tr>
<tr>
<td>India</td>
<td>400</td>
<td>400</td>
<td>4,000</td>
<td>4,250</td>
<td>4.55</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>5,450</td>
<td>6,000</td>
<td>60,000</td>
<td>61,250</td>
<td>65.51</td>
</tr>
</tbody>
</table>

(a) In US million dollars  
(b) Number of votes are determined by adding 250 plus 1 vote per each share held (Article V, Section 3 (a) of IBRD Agreement)

Source: IMF Charter provisions  
IBRD Charter provisions and Second Annual Report, 1947
Since 1947, subscriptions and voting powers have tended to change, mainly because new members have been incorporated into the IBRD, principally newly independent African nations. By the end of 1981, a total of 139 countries were members of the World Bank Group. As a result, the US subscription to the Bank has relatively decreased, although its influence over the World Bank has by no means declined. The industrialized Western nations still maintain total control over Bank operations. The voting power of South American countries, however, has remained without significant variation. In 1981, South America, including Argentina which joined the Bank in 194, had a total voting power of 5.40%. The evolution of the voting power by regions can be discerned from the following table:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number of members</td>
<td>% votes</td>
<td>Number of members</td>
</tr>
<tr>
<td>Africa</td>
<td>2</td>
<td>1.64</td>
<td>34</td>
</tr>
<tr>
<td>Asia</td>
<td>3</td>
<td>11.66</td>
<td>17</td>
</tr>
<tr>
<td>Australasia</td>
<td>1</td>
<td>2.41</td>
<td>2</td>
</tr>
<tr>
<td>Central/South America</td>
<td>18</td>
<td>8.39</td>
<td>22</td>
</tr>
<tr>
<td>Europe</td>
<td>14</td>
<td>35.72</td>
<td>20</td>
</tr>
<tr>
<td>Middle East</td>
<td>5</td>
<td>2.21</td>
<td>9</td>
</tr>
<tr>
<td>North America</td>
<td>2</td>
<td>37.97</td>
<td>2</td>
</tr>
<tr>
<td>Total</td>
<td>45</td>
<td>100.00</td>
<td>106</td>
</tr>
</tbody>
</table>

Source: IBRD Annual Reports
We will examine how each country exercises its voting rights at a later point, when we study the organization of the Board of Governors and of the Executive Directors of the Bank. But let us first complete our discussion of how the IBRD formed its initial capital and how the Bank has thereafter become the largest borrower institution in private financial markets.

IBRD loanable funds basically come from four different sources: capital subscriptions; earnings from Bank operations; borrowings in the international capital market; and participations and portfolio sales (33). Let us examine each source in detail.

1. **Capital subscriptions.** According to the IBRD Charter, capitalization structure is determined in the following way: (34)

   a. 2% of each country's total subscription must be paid either in gold or US dollars;

   b. 18% is to be paid in each country's own currency;

   c. the remaining 80% is not expected to be paid unless some contingencies occur; it is a guarantee fund held by the respective governments as "callable capital".
The two percent to be paid by each country in gold or US dollars has never presented a collection problem. Article II, Section 8 (a) indicates that this two percent payment should be made within 60 days from the date the Bank begins operations. By September 1947, the time of the First Annual Meeting of Bank governors, $143 million had been paid out of a possible total of $153 (35). The only countries which did not make their payments had been temporarily excused because their metropolitain territories had suffered from enemy occupation or hostilities during the war (36). As of 1981, the two percent payment in gold or US dollars had grown to $399,589,000 from 139 countries.

The 18% subscription, however, did present some problems, which arose not in connection with its collection, but from the fact that it could not be freely used by the Bank for loans. Article IV, Section 2 (a) of the IBRD Charter, which deals with the 18% subscription in members' own currencies, states:

Section 2. Availability and transferability of currencies

(a) Currencies paid into the Bank under Article II, Section 7 (i), shall be loaned only with the approval in each case of the member whose currency is involved...

Furthermore, if approval is granted and a member's currency is
thereby loaned by the Bank, Section 2 (b) of Article IV indicates that the currencies received in repayment shall be exchanged for the currencies of other members or reloaned only with the approval in each case of the member whose currencies are involved.

These provisions, then, represented a serious limitation on IBRD loan operations during its first decade. By mid-1947, only the United States had released its entire 18% subscription. As a result, the Bank had to commence operations with very serious financial limitations. During its first 15 months of operations the Bank could use without restriction only the 2% paid in gold or US dollars (approximately $150 million) and the $571 million 18% US subscription. By 1949 a few other countries had authorized the use of their currencies. Belgium had released $2 million (of its 18% subscription of $40.5 million), Canada $8 million (of $58.5 million), Denmark $0.1 million (of $12.24 million) and the United Kingdom $1.9 million (of $234 million).(37)

As individual countries improved their overall economic condition, especially their balance of payments situation, they authorized the Bank either to directly use their currencies for loan operations or to convert their currencies into US dollars. The advantage of the conversion to US dollars is that amounts
repaid can again be freely used by the Bank in any of its operations. US dollar repayments, then, are not subject to the restriction imposed by Article IV, Section 2 (b).

In 1981, the 18% capital subscription paid in member currencies totaled $3,596,304,000. Out of this total, $2,289,419,000 was used with member consent and $147,349,000 was subsequently converted by members into US dollars (38). The remaining $1,159,536,000 was held in non-dollar currencies and was not loaned because authorization for use had not been granted or because there was no need for those currencies.

The 80% remainder in each country's subscription is the guarantee fund. Article II, Section 5 (ii), declares:

**Section 5.** Divisions and calls of subscribed capital

... (ii) the remaining eighty percent shall be subject to call by the Bank only when required to meet obligations of the Bank created under Article IV, Sections 1 (a) (ii) and (iii).

Article IV, Section 1 (a) (ii) concerns funds raised by the Bank as a borrower in the capital market of a member and (iii) concerns the guarantees made by the Bank to private investors for loans made to member countries. This guarantee fund, which has never been used and will likely never be used, constitutes a
large reserve that gives the Bank a high rating for its borrowwing in world financial markets (39).

In September 1959, the Bank's capital was more than doubled, from the original $ 10 billion authorized in the Articles of Agreement to $ 21 billion. Ten billion US dollars was to come from a doubling of the capital subscriptions of existing members, while the additional $ 1 billion was to be provided by the admission of new members and from further increases in the subscriptions of some existing members. In this process, the 18% subscription became 9% and the 2% subscription became 1% (40). Since 1959, there have been several additional capital increases, mainly as a result of the admission of new members. The total subscribed capital as of June 1981 was $ 36,614,508,000 out of which $ 32,953,057,000 (that is, 90%) was the uncalled portion of subscriptions.

2. Earnings from Bank operations. The Bank's yearly income comes from three sources: a) interest on loans made by the Bank either from its own resources (Article IV, Section 1 (a) (i)) or from money it has borrowed in financial markets (Article IV, Section 1 (a) (ii)); b) commissions or commitment charges due in connection with loans or guarantee made by the Bank (Article IV, Section 4 (a) for loans, and Section 5 (a) for guarantees); and c) investment made with money the Bank
has not yet loaned or would otherwise hold in its reserves.

The important issue raised in connection with the Bank's earnings is their use or destiny. Two reserves exist in the Bank's financial structure into which net income has always been allocated: the Special Reserve created by Article IV, Section 6 of the Articles of the Agreement; and the General Reserve created by the Board of Governors in 1950.

The drafters of the IBRD Charter believed a Special Reserve should be created that would be held as a guarantee against possible defaults on loans. All commissions would be allocated into this Special Reserve. Article IV, Section 6, states:

Section 6. Special Reserve

The amount of commissions received by the Bank under Sections 4 and 5 of this Article shall be set aside as a special reserve, which shall be kept available for meeting liabilities of the Bank in accordance with Section 7 of this Article. The special reserve shall be held in such liquid form, permitted under this Agreement, as the Executive Directors may decide.

Section 7 (b), which deals with the preference in meeting the liabilities of the Bank in case of default, provides:

Section 7. Methods of meeting liabilities of the Bank in case of default
...(b) The payments in discharge of the Bank's liabilities on borrowings or guarantees under Section 1 (a) (ii) and (iii) of this article shall be charged:

(1) first, against the special reserve provided in Section 6 of this Article;

(ii) then to the extent necessary and at the discretion of the Bank, against the other resources, surplus and capital available to the Bank.

These provisions created a very solid reserve that could be used only in case of default. The drafters, however, did not foresee that the Bank would be a very profitable institution and that no default would occur in the Bank's first 35 years as a lending institution. As a result, the Special Reserve grew continuously from incoming commissions on loans but was never used for the purposes for which it was created. In response, the Bank's Executive Directors froze the Special Reserve in 1964.

Net income (41) began increasing very rapidly after 1949, even after commissions allocated to the Special Reserve. Consequently, Bank executives had to decide whether dividends were to be distributed to member governments or were to be kept in the Bank. In 1950, Poland withdrew from membership in the Bank, and the Executive Directors agreed to pay Poland its share of net earnings in addition to returning its 2% contri-
bution (42). After this episode, however, the Executive Directors decided that the Bank would no longer distribute dividends among member countries. As a result, the Bank created a General Reserve in July 1950 into which all Bank profits would be allocated.

In 1964, loan commissions allocated to the Special Reserve amounted to $33.18 million, and the net income allocated to the General Reserve was $97.43 million. At that time, the cumulative Special Reserve totaled $288.13 million (including the $33.18 million earned during 1964), and the General Reserve totaled $560.46 million (excluding 1964 profits). Total reserves, then, were $848 million (43). The Bank's Executive Directors feared that reserves approaching $1 billion would be subject to political attack. The Bank's objective, after all, is to use its money for development purposes and not to keep a huge reserve, especially since it has a very significant "guarantee fund" formed with the 90% "callable" subscriptions. Among the proposals that worried Bank executives was the suggestion made by some members of the US Congress that the World Bank should assume certain deficits of the United Nations system (44). In response, the Executive Directors made two very important decisions. First, the Executive Directors decided not to allocate any more funds to the Special Reserve; that is, all income from loan operations would be allocated directly to the
General Reserve, which was not subject to any Charter restrictions but was subject to the discretion of the Bank's Executive Directors. Second, they decided that the Bank would make yearly loan transfers to the International Development Association (IDA), provided that the Bank's financial situation permitted them.

The decisions made in 1950 and 1964 allow several conclusions to be drawn. First, the Bank firmly established that it would not distribute dividends among its members. Second, the Special Reserve created by Article IV, Section 6 was to remain at the 1964 level unless a default occurred. Third, income earnings from Bank operations either were to be allocated to the General Reserve, to be used for whatever purposes the Executive Directors stipulated, or were to be loaned to the IDA. In 1981, the Executive Directors allocated $509,103,000 of the $610,103,000 net income earned in the fiscal year ending June 30, 1981, to the General Reserve, and recommended that the Board of Governors approve the transfer by loan of the remaining $101,000,000 to the IDA. (45)

3. Borrowing money from the world financial markets. The World Bank's principal source of funds for financing its operations is borrowings in the international capital markets through the issuance of securities. As we have already seen, these borrowings are supplemented by paid-in capital, accumulated earnings,
and loan repayments (46). Article IV, Section 8 deals with the authority granted to the IBRD to issue, guarantee or invest in securities, and says:

**Section 8. Miscellaneous operations**

In addition to the operations specified elsewhere in this agreement, the Bank shall have the power:

(i) To buy and sell securities it has issued and to buy and sell securities which it has guaranteed or in which it has invested, provided that the Bank shall obtain the approval of the member in whose territories the securities are to be bought or sold...

IBRD bonds and securities offerings have been a successful source of funds for several reasons. Most important is the Bank's solid capital structure. Not only does the Bank have a very large reserve ($2,566,731,000 as of June 30, 1981), but "callable" capital constitutes the most important guarantee in any international development bank ($32,953,057,000 as of June 30, 1981). Also important are the related factors that the Bank has never experienced a default and that very strict criteria are used in most of its economic and financial decisions. As a result, the Bank has become one of the most creditworthy borrower institutions and has been able to gain investor confidence. For example, IBRD bonds are rated "AAA" in the United States capital market, which means that they are considered risk-free, gelt-edged investments. (47)
In general, there seem to be two problems regarding the collection of resources through the public issuance of securities. First, there is the problem of qualifying the Bank's securities for sale or underwriting by governmentally regulated investment organizations, a process which requires legislative action in most of the important capital-exporting countries. This process was initially a complicated and long one for IBRD securities (48). This problem became the primary difficulty Bank executives faced when securities were first offered in the US capital market. As Asher and Mason point out (49), the US market initially viewed the IBRD as a peculiar institution whose securities did not fit into any of the categories under state laws that made securities automatically eligible for purchase by investors. But after the relative success of the initial securities issue and through the lobbying efforts of the Investment Bankers Association of America, several state legislatures passed bills authorizing investment organizations to buy IBRD securities. Bank securities were soon considered such a solid investment in the US capital market that Bank officials started to offer securities in other markets, thereby raising currencies other than US dollars.

The second securities-related problem is the determination of the methods to be used for securities marketing. The Bank sells securities in two types of markets. First, the Bank may
place Bonds and other documents on member countries through central banks and other governmental institutions. This kind of bond does not present any marketing problems. Second, the Bank may offer issues to investors; in a public capital market, this offer is made through investment-banking firms, merchant banks and commercial banks (50). Prior to 1952, the IBRD usually sold securities on the basis of agency agreements with up to 1,700 security dealers. In 1950, the Bank sold an issue on the basis of competitive bidding, and in 1951 it sold two issues under sponsorship arrangements. Since 1952, however, all issues have been sold by negotiated underwriting (51).

During the 1960's the Bank greatly diversified the markets for its obligations in order to avoid undue dependance on one particular market. This diversification has become a basic Bank borrowing policy. During 1981 the Bank borrowed in Deutsche marks (DM 2,601.8 million), Swiss francs (SF 1,731.8 million), Japanese yen (¥ 234,000 million), Dutch guider (G 600 million), British pounds sterling (£ 100 million) and US dollars ($ 1,111 million) (52).

4. Participations and portfolio sales. Since participations and portfolio sales seek to attract investors to participate in the loan operation, they are substitutes for securities issues. Participations take place when the Bank sells
some part of a particular loan to different investors after the negotiation process of the particular loan has concluded (53). The Bank and the participant enter into a Participation Agreement, according to which the participant agrees to remit the negotiated-for currencies to the Bank either at the time the borrower becomes entitled to withdraw those currencies or on agreed upon dates. In return for these payments by the participant, the Bank agrees to give the participant certain amounts of the principal and interest payments received from the borrower. The participant is usually required to agree that the IBRD shall have the sole right to administer the loan and to enforce the obligations of the borrower (54).

Portfolio sales can be distinguished from participations in some important aspects. As the name suggests, portfolio sales are sales to investors of parts of already made loans from the Bank's established portfolio; that is, they arise after the IBRD has disbursed the money loaned but before repayment has been concluded. In return for the purchase price, the IBRD transfers the notes issued in accordance with the loan agreement to the investor. The borrower pays the principal and interest directly to the purchaser of the obligation in proportion to the purchased amount. The only rights assigned by the transfer are those that entitle the lender (the IBRD) to receive payment. The other rights and obligations between the IBRD and the borrower remain
unaffected (55).

Participations and, especially, portfolio sales have represented only a small amount of total funds raised when compared to funds raised from the other three sources of funds. During 1981 fiscal year, the total amount of portfolio sales added up to $25,470,000. As Asher and Mason point out (56), this relatively small amount of portfolio sales seems to be a result of the Bank's shift in lending policy away from loans to developed countries and concentrating its loans in the less developed world. In the eyes of the capital markets of the world, the quality of the portfolio has declined. The guarantees of the governments of most less developed countries are not regarded with the respect given the guarantees of most Western European governments, even though the Bank has never experienced a default.
II.c. Organization of the World Bank

The purpose of this section is to study some of the organizational aspects of the World Bank: how the drafters of the agreement distributed the powers over the institution and its operations, and how these powers have evolved over time. We will also review the relationship the World Bank has with the United Nations system.

II.c.1. Board of Governors and Executive Directors.

The Board of Governors (Article V, Section 2 (a)) is the highest body in the World Bank organization. Each member of the Bank has the right to appoint, in the way its national laws or administrative regulations determine, one representative to the Board of Governors, a "governor", as well as one alternate. The appointment, according to Charter provisions, is for a period of five years, and the appointee may be reappointed as many times as the member country may wish. As a result, state's representation on the Board may, in theory, be very stable over time. In practice, however, this stability is only apparent. Since most representatives are high government officials, usually ministers or Presidents of central banks or other financial institutions, they are subject to national political changes. Governors and alternates, then, will not always remain on the
Board of Governors for the five year period. As we will see, the heterogeneous nature of this "conglomerate" of representatives raises several questions regarding the policies of the World Bank. But we shall first turn to the functions and powers of the Board of Governors.

One of the basic links between the three institutions that comprise the World Bank Group is that the representatives to the IBRD Board of Governors are, at the same time, the members of the Board of Governors of the International Finance Corporation and the International Development Association. The Charter provisions of both the IFC (Article IV, Section 2 (b)) and the IDA (Article IV, Section 2) indicate that IBRD Governors serve *ex officio* on the IFC and IDA Boards. Thus, although the three institutions serve different purposes and, therefore, carry out different specific policies in their lending operations, they nevertheless are supervised by the same collective entity.

The organizational scheme planned by the drafters of the IBRD is a hierarchical one that resembles that of a private business corporation (57). All powers of the Bank are vested in the Board of Governors, but they can be delegated, with some exceptions, to the Executive Directors. The reserved powers of the Board are as follows: the power to admit new members and
determine the conditions of their admission; the power to increase or decrease Bank capital; the power to suspend a member; the power to decide appeals from the interpretations of Charter provisions made by the Executive Directors; the power to make formal agreements to cooperate with other international organizations; the power to permanently suspend the operations of the Bank; and the power to determine the distribution of the net income of the Bank. (58)

The Board of Governors holds one regular annual meeting to review the year's operations and to decide upon matters that may not be delegated (59). Special meetings may be called at any time either by the Board of Governors upon the request of five members of the Bank or members of the Bank having together one-fourth of the total voting power or by the Executive Directors (60). These special meetings, however, have rarely taken place, primarily because the Board has delegated broad powers to the Executive Directors and because the Board of Governors can make decisions without formally meeting under special circumstances. The latter is the case when the Executive Directors feel that a decision must be made that should not be postponed until the next regular meeting of the Board but that does not require the calling of a special meeting. Governors, therefore, are requested to vote without formally meeting within a period determined by the Executive Directors.
The quorum needed for any meeting of the Board is a majority of Governors that at least exercises two-thirds of the total voting power (61). Once the meeting is formally convened, decisions are made by a simple majority of votes. There has seldom been a formal voting procedure; the By-laws contemplate the possible request of a formal vote by a member but one has rarely been requested. Instead, the President of the Board usually ascertains the general opinion of the meeting.

An important division one can observe at the Board of Governors meetings is the participation of less developed countries and the frequent opposition of interests between LDC's and developed countries. This conflict, however, does not usually appear in the form of open criticism to the institution, but most often appears as a petition for additional help, as a request to Bank members to pay attention to the more basic needs of LDC's development problems. Speeches delivered by LDC governors are usually made in representation of a group of countries, and each governor concentrates on the general needs of the group or region on whose behalf he is speaking. For example, at the 1971 annual meeting of the Board of Governors, on behalf of 22 Latin American countries and the Philippines, General Morales Bermudez, Minister of Economy and Finance of the Peruvian military government that had taken office in 1969, stated: (62)
The amount of the loans directed toward relatively new sectors for the World Bank (agriculture, education, industry, public social services, tourism, town planning and others) reached a total of $814 million, or around 30 percent of the overall total. This trend is a positive one and in expressing our pleasure we recognize the definite beginning of a favorable trend that gives growing support to our efforts. However, we would reaffirm the need for a larger volume of resources to be channeled to the priority sectors of our economies, where a major impact on productivity levels can be achieved through a real improvement in the living conditions of the majority groups of the population, since in economic development, an objective we are all working toward, the human aspect is and must be the main concern.

We will return to this policy issue when we analyze in detail the role of the World Bank in Peruvian development.

The general day-to-day operations of the Bank are carried out by the Executive Directors, who perform their functions on a full-time basis. Although the Executive Directory is usually referred to as the "executive organ", this term is not sufficiently broad to describe the sui generis nature of the body. The Executive Directors are something more than just an executive body because their decisions formulate Bank policy. (63) Although all powers are vested ultimately in the Board of Governors, the Board basically performs a supervisory function. The burden of policy decisions rests in the body of Executive Directors. Thus, it is important to analyze its formation,
function and operation.

The articles of Agreement stipulated that there initially would be twelve Executive Directors (64). Five of these twelve Directors would be directly appointed by the five members that have the largest number of shares in the Bank, and the remaining seven would be elected by the countries not entitled to appoint directors and would represent the countries that had cast votes for them. Since the drafters of the agreement had anticipated that new members would continually join the Bank, the agreement provided that the Board of Governors could increase the number of elected directors without modifying the agreement provisions. The Bank currently has 21 Executive Directors; five Directors are appointed and sixteen are elected.

To elect executive directors, each country, represented by its governor, casts all of its votes for one candidate. The sixteen nominees receiving the greatest number of votes will be elected executive directors but each nominee must first receive a minimum per cent of the total votes. If the votes cast for a nominee are less than the lower limit, he is not elected a Director (at least on that ballot). If, on the other hand, a nominee’s votes reach the required minimum, only those member countries whose votes were necessary to reach the minimum limit will be represented by the nominee. The mechanism to determine
which members' votes elect a director is established in Schedule B of the Articles of Agreement, which declares:

In determining whether the votes cast by a governor are to be deemed to have raised the total of any person above (...) per cent of the eligible votes, the (...) per cent shall be deemed to include, first the votes of the governor casting the largest number of votes for such person, then the votes of the governor casting the next largest number, and so on until (...) per cent is reached.

That is, the total number of votes cast for a particular nominee will be reduced, first by excluding the votes of the country that voted for that nominee which has the smallest number of votes, and continuing with the next smallest and so forth until no further reductions are possible without reducing a nominee's total votes below the minimum limit (65). These excluded votes can then be cast for other nominees.

This election mechanism presents two serious problems. First, it is clear that the mechanism favors the larger subscribers over the smaller ones, since the former are more likely to be represented by their first choice director. Smaller subscribers usually have to cast their votes several times before their votes are finally valid in the election of a representative. Second, the election mechanism makes the joint representation of sub-regional groups difficult though not impossible. If,
for example, there were a number of countries that formed a sub-regional group with voting power sufficient to elect an Executive Director, their intention could be frustrated by another member from a different region that wanted to elect the same representative. If the votes held by the country that is not part of the sub-regional group are less than that held by each of the sub-regional countries, then the sub-regional group could still elect their own candidate. But if the non-sub-regional member possesses more votes than any of the other countries wanting the same Executive Director, its votes would be included, while those of the sub-regional countries with the fewest votes would be eliminated (up to the point where the minimum percentage is reached).

This voting procedure explains why many regional groups have not been able to be represented by the same executive directors. For example, the five members of the Andean Pact (Peru, Ecuador, Colombia, Venezuela and Bolivia) are represented by three different directors. Peru casts its votes together with Argentina, Chile, Paraguay, Uruguay and Bolivia. I do not necessarily regard this as a disadvantage, but I want to show the possible diversity in the countries represented by one Executive Director.

The quorum needed for a meeting of the Executive Directors
is the majority of Directors that exercises at least one-half of the total voting power (66). Each appointed director is entitled to cast the number of votes held by the member that appointed him, and each elected director casts the total number of votes of the countries whose votes were required for his election. All votes of an Executive Director must be cast as a unit; votes cannot be divided (67). Decisions, as in the case of the Board of Governors, are reached by a simple majority of votes.

The Bank's policies are formulated by the Executive Directors within the framework of the Articles of Agreement. There are certain powers expressly granted to the Executive Directors, while others have been delegated to them by the Board of Governors. The Articles of the Agreement expressly empower the Executive Directors to:

(1) elect the President of the Bank and accept his resignation (68);

(2) temporarily suspend operations in emergency situations (69);

(3) negotiate arrangements to see that direct and contingent claimants are paid off (70);

(4) distribute the assets of the Bank to members until all assets have been distributed (71);

(5) value assets to be distributed (72);

(6) interpret the provisions of the agreement (73).
(7) convene the Board of Governors for its regular annual meeting (74) and, in special circumstances, for special meetings (75);

(8) prepare the annual report to be presented at the annual meeting of the Board of Governors (76).

The general policy of the Bank is carried out by the Executive Directors through decisions made regarding the use of loanable funds. We will discuss some of the policy issues of the World Bank in more detail when we study the loan operations and lending criteria of the Bank. But simply with reference to the organizational structure of the Bank, we can conclude that the composition of the Executive Body is of such a nature that large subscribers have direct control over the Bank's activities, mainly through their voting power reflected in the five appointed directors. The following table shows the percentage of votes cast by the appointed and elected directors as of June 30, 1981:

A) Appointed Executive Directors

<table>
<thead>
<tr>
<th>Country</th>
<th>Per cent of votes</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>20.84</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>7.44</td>
</tr>
<tr>
<td>Germany</td>
<td>5.06</td>
</tr>
<tr>
<td>France</td>
<td>5.05</td>
</tr>
<tr>
<td>Japan</td>
<td>5.04</td>
</tr>
</tbody>
</table>

-44-
B) **Elected Executive Directors**

<table>
<thead>
<tr>
<th>Country/Region</th>
<th>Per cent of votes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Maldives, Pakistan, Qatar, Saudi Arabia, Syria, United Arab Emirates, Yemen</td>
<td>5.25</td>
</tr>
<tr>
<td>Bahamas, Barbados, Canada, Dominica, Grenada, Guayana, Ireland, Jamaica, St. Lucia</td>
<td>4.44</td>
</tr>
<tr>
<td>Bangladesh, India, Sri Lanka</td>
<td>4.04</td>
</tr>
<tr>
<td>Greece, Italy, Portugal</td>
<td>3.73</td>
</tr>
<tr>
<td>Cyprus, Israel, Netherlands, Romania, Yugoslavia</td>
<td>3.71</td>
</tr>
<tr>
<td>Austria, Belgium, Luxembourg, Turkey</td>
<td>3.56</td>
</tr>
<tr>
<td>Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Spain, Surinam, Venezuela</td>
<td>3.47</td>
</tr>
<tr>
<td>China</td>
<td>3.47</td>
</tr>
<tr>
<td>Denmark, Finland, Iceland, Norway, Sweden</td>
<td>3.46</td>
</tr>
<tr>
<td>Burma, Fiji, Indonesia, Laos, Malaysia, Nepal, Singapore</td>
<td>2.55</td>
</tr>
<tr>
<td>Australia, Korea, New Zealand, Papua New Guinea, Solomon Islands, Western Samoa</td>
<td>3.26</td>
</tr>
<tr>
<td>Botswana, Burundi, Equatorial Guinea, Ethiopia, Gambia, Guinea, Kenya, Lesotho, Liberia, Malawi, Nigeria, Seychelles, Sierra Leone, Sudan, Swaziland, Tanzania, Trinidad and Tobago, Uganda, Zambia, Zambabwe</td>
<td>3.12</td>
</tr>
<tr>
<td>Brazil, Colombia, Dominican Republic, Ecuador, Haiti, Philippines</td>
<td>2.97</td>
</tr>
<tr>
<td>Benin, Cameroon, Cape Verde, Central African Republic, Chad, Comoros, Congo, Djibouti, Gabon, Guinea-Bissau, Ivory Coast, Madagascar, Mali, Mauritania, Mauritius, Niger, Rwanda, Sao Tome and Principe, Senegal, Somalia, Togo, Upper Volta, Zaire</td>
<td>2.71</td>
</tr>
</tbody>
</table>
15. Argentina, Bolivia, Chile, Paraguay, Peru, Uruguay.............................. 2.59
16. Afghanistan, Algeria, Ghana, Iran, Libya, Morocco, Oman, Tunisia, Yemen (Peoples Democratic Republic)................................. 2.34


II.c.2. Relationship with other organizations and the governments of member countries

When we studied requirements for World Bank membership, we saw that membership in the three institutions that comprise the World Bank Group is tied up to membership in the IMF; that is, in order to become a member of the IBRD, IMF membership is a prerequisite, and membership in the IBRD is a further prerequisite both for membership in the IFC and the IDA. This relationship between the World Bank Group and the IMF is established in the Articles of Agreement of each of the three institutions and can be regarded as a basic institutional relationship. We shall now examine in a more detailed way how the World Bank interacts with other international organizations, particularly the United Nations system. We will then try to point out some important issues concerning the relations the World Bank has with some of its member countries, especially the United States.

The basic authority the IBRD has to enter into either formal
or informal agreements with other international organizations is established by the IBRD Charter in Article V, Section 8 (a), which states:

Section 8. Relationship to other international organizations.

(a) The Bank, within the terms of this agreement shall cooperate with any general international organization and with public international organizations having specialized responsibilities in related fields...

On November 15, 1947, the Bank entered into a Specialized Agency Agreement with the United Nations (77), by which the Bank acquired the status of a specialized agency within the terms of Article 57 of the United Nations Charter. Bank officials initially had been reluctant to enter into an agreement with the UN. They feared that the Bank could be subject to political control and influence if it became a specialized agency, and that this would endanger its credit rating in the world capital markets (78). Consequently, when both institutions finally agreed to formalize their relationship the drafters of the IBRD-UN agreement, particularly those working for the Bank, were very careful in establishing a formal relationship that would secure the Bank's autonomy from the United Nations. Some of the important provisions of the IBRD-UN agreement provide as follows (emphasis added):
Article I. General.

........................

Sec. 2. The Bank is a specialized agency established by agreement among its member governments and having wide international responsibilities, as defined in its Articles of Agreement, in economic and related fields within the meaning of Article 57 of the Charter of the United Nations. By reason of the nature of its international responsibilities, and the terms of its Articles of Agreement, the Bank is, and is required to function as, an independent international organization...

Article IV. Consultation and Recommendations.

........................

Sec. 3. The United Nations recognizes that the action to be taken by the Bank on any loan is a matter to be determined by the independent exercise of the Bank's own judgment in accordance with the Bank's Articles of Agreement. The United Nations recognizes, therefore, that it would be sound policy to refrain from making recommendations to the Bank with respect to particular loans or with respect to terms or conditions of financing by the Bank...

Article X. Administrative relationship

Sec. 3.................

The United Nations agrees that, in the interpretation of paragraph 3 of Article 17 of the United Nations Charter, it will take into consideration that the Bank does not rely for its annual budget upon contributions from its members, and that the appropriate authorities of the Bank enjoy full autonomy in deciding the form and content of such budget...

Thus, the UN-IBRD agreement explicitly recognizes the Bank's autonomy in three crucial areas: institutional (Article I, Section 2), policy decisions (Article IV, Section 3) and budget
approval (Article X, Section 3). It is not surprising, then, that the agreement was subject to serious criticisms in the United Nations. The basic argument against the agreement was that it would undermine UN authority over specialized agencies, especially since the UN was then negotiating similar agency agreements with other organizations. But in the end, and not without political pressures from some members, the agreement was finally approved by the Economic and Social Council and then by the General Assembly. Today, this agreement still remains the basis for the relationship between the UN and the IBRD.

New relational problems between the two organizations arose as UN operations and functions diversified. Until the creation of the Expanded Program of Technical Assistance (EPTA) in 1950, World Bank officials believed that while Bank's activities were operational (granting loans), the principal function of the UN and other specialized agencies was merely to convene conferences, collect figures and set standards (79). The EPTA gave the entire UN system an operational role, since its basic function was to grant loans for technical assistance. Several years later, with the creation of the UN Special Fund in 1957, the United Nations further expanded its activities by providing loans for pre-investment projects. As a result, a shift took place in World Bank relations with the UN: from a very
general, often unfriendly and critical relationship with the UN and its Economic and Social Council, to a more specific, nearly complementary relationship with the Special Fund. The World Bank, in encouraging the creation of the Fund, made certain that the Fund would not participate directly in the operational phase of projects. The Fund would provide technical assistance; it would carry out project identification and preparation, leaving room for the Bank to finance the project at a later stage. The World Bank, like other international organizations, became an executing agency of the Special Fund, but it remained independent in its formulation of policy.

In 1966, the merger of the UN Special Fund and the EPTA created the United Nations Development Program (UNDP) (80). Since then, the World Bank and the UNDP have worked together in a series of specific projects, complementing each other's activities and operations. Robert McNamara, the former President of the World Bank, commented on the Bank's relationship with the UN Development Program in a 1970 speech as follows: (81)

Since the establishment of the Special Fund a principal function of the UNDP has been the financing of preinvestment studies. The principal function of the World Bank Group is the financing of investment projects. Preinvestment and investment are, of course, two stages of a single economic process. UNDP feasibility studies, for example, even when their findings are favorable, are fully useful only if the projects
studied can ultimately be financed; and, conversely, investment projects proposed to the Bank can be properly appraised and funded only if satisfactory feasibility studies of these projects have previously been made.

During the last fifteen years, the World Bank's relationship with other UN organizations concerned with development, including those that specialize in particular sector or geographical areas, have become more extensive and varied. As Asher and Mason point out (82), the Bank moved from an isolated and peripheral position in the UN system to a more central role, while the UN system itself moved from research, discussion and small-scale technical assistance to active participation in promoting development at local, national and regional levels.

In the early 1960's, the World Bank decided to expand its operations into agriculture and education, and further decided to collaborate closely with the appropriate functional agencies instead of relying exclusively on its own staff. In 1964, the Bank formally agreed for the first time to establish Cooperative Programs (CP's) with the Food and Agricultural Organization (FAO) and the United Nations Educational, Scientific and Cultural Organization (UNESCO). Pursuant to these agreements, FAO and UNESCO became executing agencies for the World Bank in
project identification and preparation. CP's assist governments in the identification and preparation of projects in sector surveys. The World Bank finances approximately 75% of these projects. (83).

Let us now examine very broadly some of the CP's which are currently in effect between the Bank and UN agencies (84):

(a) CP initiated in 1964 with FAO primarily funds missions to study agricultural and rural development problems. In Fiscal 1981, this program helped prepare more than 25% of all agriculture and rural development projects approved for financing by the Bank;

(b) CP initiated in 1964 with the UNESCO to provide assistance in preparing education projects and in analyzing educational problems in developing countries;

(c) CP begun in 1971 with the World Health Organization (WHO) concentrates on project preparation and subsector work, such as tariff studies and manpower-development programs. It also develops project preparation guidelines for the use of governments and multilateral and bilateral agencies;

(d) CP with the United Nations Industrial Development Organization (UNIDO) emphasizes the support of employment-intensive artisanal activities and small-scale enterprises in manufacturing and construction;

(e) CP with the UNDP provides financing for energy-sector project evaluation. (As already mentioned, the World Bank acts as executing agency for preinvestment projects);

(f) CP with the International Fund for Agricultural Development (IFAD) provides for Bank assistance
in preparing agricultural and rural development projects for financing by the IFAD or by IFAD and the Bank together.

These CP's are basically oriented toward pre-investment activities: project study and preparation. They do not involve project financing because the World Bank, fearing political interference in its decisions, always has been very careful to maintain its hegemony and independence in the provision of funds. This is related to the structural differences between the World Bank and the UN system, to which I would now like to refer.

Several organizational and functional differences exist between the World Bank and the UN (85). First, as recognized in the UN-IBRD agreement, the Bank maintains total economic independence. Second, the voting system in the World Bank is based on the subscribed capital of each member, while most UN institutions vote on the basis of a "one country one vote" principle. This is a crucial difference from the World Bank's viewpoint, since a "one country one vote" principle would immediately give the Bank a political character, thereby endangering its prestige in world capital markets and making it very difficult to carry out its operations under strict economic criteria. Third, very few communist countries are members of the World Bank; therefore, a further potential source of World Bank
politization is avoided. A fourth difference is more related to the day-to-day administrative operations and negotiations carried on by each institution. While the UN basically deals with foreign ministries and other sectorial ministries (e.g. labor, agriculture), the World Bank deals mainly with economic ministries and central banks. This can have two contrary effects. On the one hand, this day-to-day contact facilitates economic analysis under strict productivity and profitability criteria. On the other hand, it may foster an exclusive focus on economic considerations that inappropriately disregards the social and cultural dimensions of some decisions. Related to the administrative issue is another crucial problem: the hiring of personnel with reference to their country of origin. The UN has to distribute jobs equitably among country members. World Bank selection of personnel, however, is to some extent "less politicized". The Bank has traditionally tried to hire a very efficient group of professionals for its staff. The Bank considers the origin of the person to be hired, but efficiency criteria guide its decisions.
II.d. Member governments and World Bank decisions

One of the crucial dimensions surrounding World Bank activities is its relations with member governments, especially with the United States. Our study will focus on the United States influence over the Bank for several reasons. First, the US is by far the biggest contributor to the Bank. The US has played an important role in the Bank's administration and operations since its creation. Second, as indicated by a Congressional Office Budget report (86), the US influence extends beyond its calculated voting share. Frequently, the US takes the lead in advocating positions in which it is then joined by other members. Third, the US is probably one of the few countries that has enacted legislation that seems to be inconsistent with the Bank's Charter provisions, seeking to restrict the use of loanable funds under certain special circumstances. We will first give a general overview of the types of foreign aid given by the United States, their rationale and their effect on the economies of the recipient countries. Then, we can see the US has, in practice, tried to influence World Bank decisions.

II.d.1. Overview of the US foreign aid system

There are basically two ways in which official American aid is channelled to developing countries (87). Three bilateral aid
programs extend aid directly to the recipient country. The US also extends aid indirectly through contributions to multilateral development banks, the largest of which is the World Bank. These two types of aid programs serve different political and economic interests (88). The last decade has witnessed a great debate concerning which form of economic aid most directly serves US foreign policy objectives and, therefore, which form of aid should be primarily extended. It is not surprising that opposing views have been defended by different recent administrations.

Before entering into a detailed explanation of these aid programs, I would like to comment on some of the broad strategic and ideological issues involved in US economic aid. In an uncharacteristically lucid global analysis of American foreign policy, particularly with regard to Latin America, Richard Nixon, early in his second term, presented a foreign policy report to Congress, in which he stated the basic objectives of American aid to developing countries (89). A relevant part of this document states:

Basic humanitarian considerations call on us to assist these countries in improving the lives of their people. But we also have a major economic and political interest in the growth and stability of these countries and in their active cooperation.
Many of these countries have energy resources and raw materials that we will need in significantly increasing amounts. Some of them have become fast-growing markets for our exports. Almost one-third of US exports went to developing countries in 1972 and the future growth of these countries will expand our markets.

Underlying the President's speech, although not explicitly mentioned, is the growing military importance of less developing countries, not only for their strategic import and their raw materials, but also as a great market for military purchases, which became significant in the case of Latin American countries in the 1970's.

The substantial private American interests in a great number of developing countries is another area of concern in American aid programs. As Smith indicates (90), despite the fact that most less developed countries remain financially tied to industrialized lender countries, it is also true that industrialized nations are becoming financially tied to developing countries. In 1976, US private direct investment in developing countries had a book value of more than $30 billion and a market value perhaps double that amount.

This is the general framework in which US aid programs operate. Let us now examine the forms by which this aid is granted.
The US provides direct bilateral assistance to LDC's through three different channels: the Development Assistance Program, the Food Aid Program and the Economic Support Fund. Bilateral aid represents nearly 80% of total US foreign assistance. The remaining 20% has been allocated to multilateral development banks (the World Bank, the Interamerican Development Bank, the Asian Development Bank and the African Development Bank).

i) The Development Assistance Program, created in 1961, is administered by the Agency for International Development (AID), which had been created that same year to coordinate aid programs. During its first years, the Development Assistance Program was basically oriented toward infrastructure projects, aiding the construction of dams, roads and power plants under a relatively unequal, concentrated distribution of benefits among countries. In 1973, however, the program was reorganized by Congress with the enactment of the New Directions Act. Pursuant to this new legislation, development assistance under the program was shifted to the agricultural, rural development and nutritional sectors, to the poorer nations of the world, and to countries attempting to satisfy basic human needs. In 1979, 68 countries received development assistance through AID. Until 1972, the primary recipients of Development Assistance Program funds had been India (21% of total 1970 aid), Pakistan (11% of
total 1970 aid) and Brazil (8% of total 1970 aid). As a result of the New Directions Act, however, their share of aid declined substantially. In 1979, India received 9% of total funds, Pakistan 1% and Brazil no aid under the program. Bolivia became a major recipient of AID funds after the 1973 New Directions Act.

In the Latin American region the primary recent recipients have been Colombia, Chile and Bolivia. Two significant cases involving US development assistance to Latin America deserve mention. First, the case of Peru and the International Petroleum Company (IPC), and second, the case of US aid to Chile between 1970 and 1973.

In the 1960's the Peruvian government was confronted with the decision whether or not to nationalize IPC oilfields, and if nationalization was to be undertaken, how to arrange compensation. During the government of President Belaunde (1963-1968), the US government, in varying degrees, conditioned the availability and volume of development funds to the settlement of the IPC nationalization issue, even though no part of IPC's operations was physically expropriated during Belaunde's term in office (91). This situation created much political debate in Peru and was one of the major causes for the coup that overthrew Belaunde in October 1968. During the entire Belaunde adminis-
tration, Development Assistance Program aid to Peru totaled only US $ 90 million. When compared to the aid received during these years by Brazil (US $ 1,067 million), Chile (US $ 346 million) and Colombia (US $ 354 million), one can observe how aid had been purposely kept at low levels in order to pressure the Peruvian government to settle the IPC issue under terms favorable for the company.

The case of Chile, although a much more extreme case than that of Peru, also illustrates the way in which US aid has been conditioned. Until 1970, when the leftist government of Salvador Allende assumed office, the Development Assistance aid granted to Chile had been significant. During the Allende administration (1970-1973), grants were substantially reduced. After the military coup that overthrew Allende, US economic assistance began to be granted once more to Chile. But as the right-wing military government continously violated human rights within Chile, US aid again decreased to symbolic levels.

The following chart shows the evolution of US Development Assistance in four Latin American countries:
Disbursements of US Bilateral Development Assistance Funds, fiscal years 1968-1979 (million US dollars)

<table>
<thead>
<tr>
<th>Year</th>
<th>Chile</th>
<th>Colombia</th>
<th>Brazil</th>
<th>Bolivia</th>
</tr>
</thead>
<tbody>
<tr>
<td>1968</td>
<td>58</td>
<td>78</td>
<td>194</td>
<td>4</td>
</tr>
<tr>
<td>1969</td>
<td>35</td>
<td>101</td>
<td>12</td>
<td>11</td>
</tr>
<tr>
<td>1970</td>
<td>18</td>
<td>76</td>
<td>88</td>
<td>3</td>
</tr>
<tr>
<td>1971</td>
<td>2</td>
<td>84</td>
<td>79</td>
<td>4</td>
</tr>
<tr>
<td>1972</td>
<td>1</td>
<td>93</td>
<td>12</td>
<td>54</td>
</tr>
<tr>
<td>1973</td>
<td>1</td>
<td>77</td>
<td>41</td>
<td>17</td>
</tr>
<tr>
<td>1974</td>
<td>5</td>
<td>40</td>
<td>5</td>
<td>39</td>
</tr>
<tr>
<td>1975</td>
<td>31</td>
<td>14</td>
<td>3</td>
<td>20</td>
</tr>
<tr>
<td>1976</td>
<td>21</td>
<td>14</td>
<td>1</td>
<td>22</td>
</tr>
<tr>
<td>1977</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>36</td>
</tr>
<tr>
<td>1978</td>
<td>0.5</td>
<td>-</td>
<td>-</td>
<td>35</td>
</tr>
<tr>
<td>1979</td>
<td>0.5</td>
<td>0.5</td>
<td>-</td>
<td>29</td>
</tr>
</tbody>
</table>

Source: Assisting the Developing Countries: Foreign Aid and Trade Policies of the United States (Congressional Budget Office, September 1980), pp. 98-99

ii) The Economic Support Fund is in a sense the continuation of the post-war Marshall Plan and has been formally reorganized several times (92). ESF funds are directly allocated "to promote economic or political stability" in countries important for US interests (93). ESF aid, therefore, is granted primarily for international security reasons. ESF funds have usually been granted not for specific projects, but for general government purchases, mainly in the US market. More than 40% of ESF funds committed between 1975 and 1979 were used for commodity-import financing, approximately 20% for cash grants and around 30% for specific project aid.
In the early 1970's, approximately 85% of Economic Support Fund aid was allocated to South Vietnam. Since the end of the Vietnam War, a similar percentage has been targeted for the Middle East, particularly Egypt and Israel, reflecting a change in US security interests. A relatively small amount of ESF assistance is directed toward Latin American countries and Africa.

Although ESF aid is oriented primarily toward specific countries of special US interest, this program does not include direct military aid. Funds for defense purposes and military training are covered by other security assistance programs, which include (1) the Military Assistance Program, (2) the International Military Education and Training Program, and (3) the Foreign Military Sales Financing Program.

The following table shows the amount and percentage of total ESF assistance given to the four major recipients over a period of ten years:
### Amount and percentage of ESF aid to South Vietnam, Israel, Egypt and Jordan (million US dollars)

<table>
<thead>
<tr>
<th></th>
<th>South Vietnam</th>
<th>Israel</th>
<th>Egypt</th>
<th>Jordan</th>
</tr>
</thead>
<tbody>
<tr>
<td>1969</td>
<td>299 (67%)</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1970</td>
<td>361 (71%)</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1971</td>
<td>384 (67%)</td>
<td>0</td>
<td>0</td>
<td>5 (0.8%)</td>
</tr>
<tr>
<td>1972</td>
<td>385 (62%)</td>
<td>50 (8%)</td>
<td>0</td>
<td>55 (8%)</td>
</tr>
<tr>
<td>1973</td>
<td>312 (50%)</td>
<td>50 (8%)</td>
<td>0</td>
<td>50 (8%)</td>
</tr>
<tr>
<td>1974</td>
<td>333 (52%)</td>
<td>50 (7%)</td>
<td>9 (0.1%)</td>
<td>45 (7%)</td>
</tr>
<tr>
<td>1975</td>
<td>188 (14%)</td>
<td>325 (25%)</td>
<td>253 (19%)</td>
<td>88 (6%)</td>
</tr>
<tr>
<td>1976</td>
<td>2 (0.1%)</td>
<td>700 (62%)</td>
<td>253 (22%)</td>
<td>46 (4%)</td>
</tr>
<tr>
<td>1977</td>
<td>-</td>
<td>735 (41%)</td>
<td>700 (39%)</td>
<td>70 (3.9%)</td>
</tr>
<tr>
<td>1978</td>
<td>-</td>
<td>785 (35%)</td>
<td>751 (33%)</td>
<td>93 (4%)</td>
</tr>
<tr>
<td>1979</td>
<td>-</td>
<td>785 (39%)</td>
<td>835 (42%)</td>
<td>93 (4%)</td>
</tr>
</tbody>
</table>

**Source:** Assisting the Developing Countries: Foreign Aid and Trade Policies of the United States (Congressional Budget Office, September 1980) pp. 100-101

During the last ten years, therefore, most ESF aid has been granted to two regions of the world which historically have played a key role in US foreign policy.

iii) The Food Aid Program was established in the Agricultural Trade Development and Assistance Act of 1954, and is known as Public Law 480. The program's purpose is to dispose of surplus US agricultural goods and to foster agricultural price stability in the US. There have been several attempts to shift the program's focus from the disposal of US surplus goods to the alleviation of hunger through agricultural development. But as one Congres-
sional report recognizes, "establishing and maintaining commercial markets for US products remains an underlying objective of the Food Aid program" (94). Furthermore, this report says that the inherent conflict among the multiple goals is compounded by the inclusion of political considerations in the selection of recipients.

Food Aid pursuant to Public Law 480 is granted for donation or resale under three titles of the Act:

**Title I: Concessional Loans for Food Purchases** provides for concessional loans to finance the purchase of American agricultural commodities. Loans are granted over a period of up to 40 years with a grace period of up to 10 years.

**Title II: Donation and Disaster Relief** calls for the donation of food by the US for nutritionally vulnerable groups, such as young children and mothers.

**Title III: Food for Development** provides that at least 15% of repayments received under Title I shall instead be reinvested by LDC's in projects, which have to be approved by the US government, directed to increase their food supply.

The only major Latin American recipients of Food Aid Pro-
gram assistance are Chile and Brazil. As with AID economic assistance, the Chilean political situation has been a key conditioning factor in US food aid to Chile. Food aid declined dramatically during the Allende regime (1971-1973), increased a short period after the military government took over (1974-1977), and again declined when human rights considerations were introduced by the Carter administration.

**Food Aid (Public Law 480) from 1968-79**

(million US dollars)

<table>
<thead>
<tr>
<th>Year</th>
<th>Chile</th>
<th>Brazil</th>
</tr>
</thead>
<tbody>
<tr>
<td>1968</td>
<td>23</td>
<td>22</td>
</tr>
<tr>
<td>1969</td>
<td>15</td>
<td>10</td>
</tr>
<tr>
<td>1970</td>
<td>7</td>
<td>62</td>
</tr>
<tr>
<td>1971</td>
<td>6</td>
<td>35</td>
</tr>
<tr>
<td>1972</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>1973</td>
<td>3</td>
<td>10</td>
</tr>
<tr>
<td>1974</td>
<td>3</td>
<td>6</td>
</tr>
<tr>
<td>1975</td>
<td>62</td>
<td>8</td>
</tr>
<tr>
<td>1976</td>
<td>59</td>
<td>1</td>
</tr>
<tr>
<td>1977</td>
<td>32</td>
<td>1</td>
</tr>
<tr>
<td>1978</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>1979</td>
<td>9</td>
<td>9</td>
</tr>
</tbody>
</table>

*Source: Assisting the Developing Countries: Foreign Aid and Trade Policies of the United States (Congressional Budget Office, September 1980), pp. 100-101*
II.d.2. US influence over World Bank policies

The mutual influence member countries and the World Bank have on each other can be examined from two related perspectives. We can study the Bank as a purportedly neutral institution that is prohibited from interfering in the political affairs of its members and that makes impartial decisions through its Executive Directors. We can also study member countries' compliance with the prohibition against influencing the Bank's decisions on the basis of national policy considerations. The common denominators for these two perspectives are the Executive Directors. The five largest subscribers each appoint one Executive Director who is thereby subject to national political pressure. Elected Directors also are subject to political pressure from the countries they represent. But at the same time, Executive Directors are Bank representatives, obliged to carry out their functions pursuant to the Articles of Agreement.

This sub-chapter will first examine the Charter provisions under which Bank operations proceed and how these provisions have been interpreted by Bank officials. Then we will review some of the specific attempts made by the US to influence World Bank decisions under national policy considerations.

Article IV, Section 10 of the Articles of Agreement, en-
titled "Political Activity prohibited", provides:

The Bank and its officers shall not interfere in the political affairs of any member; nor shall they be influenced in their decisions by the political character of the member or members concerned. Only economic considerations shall be relevant to their decisions, and these decisions shall be weighed impartially in order to achieve the purposes stated in Article I.

Although any analysis or interpretation of this section can turn out to be merely casuistic, it is nevertheless important to try to understand its meaning and implications, that is, to understand the intention of the drafters and its real-world application.

The section's first sentence, prohibiting the Bank from interfering in a member's political affairs, raises the question of to what extent the Bank can condition a loan grant to certain economic performance by the borrowing country without interfering in the borrower's political matters. It is evident that there is no clearcut distinction between economic considerations and political interference.

The Bank usually tries to influence member country economic performance directly, by conditioning loan grants on the implementation of specific economic measures it wants the bor-
rowing country to pursue, or indirectly, by changing the volume of its lending with the behavior of development indicators so as to induce the borrowing country to improve its economic indicators (95). These conscious efforts by Bank officials to induce a change in borrowing country economic policies seems to contravene Article IV, Section 10 (96). The overall economic performance conditions that the Bank imposed on the Peruvian government during 1966-1967 illustrate this point (97).

Until 1965, the IBRD had been a consistent but relatively unimportant lender to Peru, and it had never shown any significant interest in Peru's performance. From its first loan to Peru on January 23 1953, to the date it sent a major economic mission to Peru in 1965 (98), the Bank made 20 project-loans to Peru totaling $ 197 million (See Appendix). The 1965 mission concluded that Peru deserved a substantial external support "provided the government pursued suitable fiscal policies." In January 1966, the Loan Committee accepted recommendations for a lending program of US $ 130 million for the years 1966-1967. The Committee report admitted that "the possibility of lending such a substantial amount over a sufficiently long-time period gave the Bank the required leverage to ensure that the Peruvian government would adopt the recent Bank Economic Missions' recommendations, which had already been accepted in principle" (99).
The Peruvian government urgently needed economic aid agreed to undertake some specific measures to improve economic performance in a "Memorandum of Understanding on the Financial Policies of the Government of Peru". This memorandum stated, in very general terms, the government's intention to modify the tax structure in order to make it less dependent on indirect domestic taxes vis-a-vis direct taxation, which basically meant the enactment of a new Income Tax Law; to control and reduce governmental borrowing from the Central Bank, which had increased significantly during 1965; and to limit commitments for short-term suppliers credit. Thus, the World Bank lending program was conditioned on the degree to which the measures indicated in the Memorandum of Understanding would be implemented.

Unfortunately, the Peruvian government was then confronting a serious internal political crisis. The causes were several and cannot be attributed exclusively to the performance of the Belaunde administration. The two main problems in Peruvian politics had been unresolved for at least 20 years. On the international front, the main problem was settling the controversy with the International Petroleum Company (IPC), an American oil company. Briefly stated, the controversy was whether or not the IPC oil fields should be nationalized, and if they were to be nationalized, how would compensation be arranged.
This problem required an immediate solution which would create the broader issue of whether oil activities should be carried-out by state enterprises or by private corporations. On the internal front, the Belaunde administration was unable to overcome the political strength of land-owners who opposed the agrarian reform that had been promised by Belaunde during the presidential election campaign (100).

In early 1966, in negotiations between the World Bank and Peruvian authorities and between the United States government and Peru, sufficient progress was made toward an agreement on international economic aid to justify the formation of a Consultative Group, which held its first and, for several years, last meeting in Paris in July 1966. Shortly after this meeting, internal political problems made the economic measures that already had been agreed upon and that had been presented to the international capital market representatives at the Paris meeting, impossible to implement. The Peruvian economy progressively disintegrated. The central government continued to borrow heavily from the Central Bank to pay large deficits and, therefore, the inflation rate continued to increase (101).

The following table shows the Central Government deficit and its main source of financing from 1964 to 1967:
### Central Government Deficit and Source of Financing
(million US dollars)

<table>
<thead>
<tr>
<th>Year</th>
<th>1964</th>
<th>1965</th>
<th>1966</th>
<th>1967</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Current revenue</td>
<td>15,843</td>
<td>19,669</td>
<td>23,231</td>
<td>25,967</td>
</tr>
<tr>
<td>2. Total expenditure</td>
<td>17,672</td>
<td>22,914</td>
<td>27,563</td>
<td>32,656</td>
</tr>
<tr>
<td>3. Deficits</td>
<td>(1,829)</td>
<td>(3,245)</td>
<td>(4,332)</td>
<td>(6,689)</td>
</tr>
</tbody>
</table>

### Financing

a) Long-term external development loans (mainly IBRD and IDB)  
   - 400  
   - 550  
   - 955  
   - 1,059

b) Other foreign loans  
   - 209  
   - 410  
   - 1,295  
   - 1,861

c) Borrowing from Central Bank  
   - 1,225  
   - 97  
   - 2,055  
   - 966

Source: Kuczynski, Peruvian Democracy Under Economic Stress,  

This table demonstrates some obvious changes in Peruvian economy. First, borrowing from international development banks (the IBRD and the IDB) increased dramatically in the mid-1960's but did not keep up with the needs of Peruvian economy. Indeed, development assistance decreased relative to the increase of "other
foreign loans", basically money borrowed from private capital markets. Second, Peru substantially increased its borrowing from private banks and other financial institutions under "harder" terms ("other foreign loans" in 1966 increased 300% over the 1965 level). Third, nearly all government deficits were covered with money lent by the Peruvian Central Bank, especially in 1964 and 1966. The immediate result of this particular method of financing was increased inflation.

Tax structure modifications in order to increase government revenues, another of the points agreed upon in the Memorandum of Understanding, were not implemented by the Belaunde government, mainly because of parliamentary opposition. The Peruvian Parliament was controlled by a two party coalition, APRA (Alianza Popular Revolucionaria Americana) and UNO (Union Nacional Odrista), that opposed tax increases. Haya de la Torre, leader of APRA and probably the most influential politician at this time, was emphatic in his negative answer to any proposed tax increase. His party slogan was "No mas impuestos" (No more taxes!) (102).

Meanwhile, the Peruvian government's purchase of 16 Mirage supersonic fighter planes from France at a total cost of US $20 million prompted the US Congress, upset that Peru did not purchase American planes, to cancel a $40 million AID program loan to Peru.
All these circumstances led the World Bank to freeze its lending to Peru and to call-off the second meeting of the Consultative Group.

This has been a very brief account of a very complex political and economic situation at a time when the Peruvian government, desperately needing money, was not only negotiating with the World Bank and the AID, but also with the IMF, the IDB and other international economic organizations. The main point I have sought to illustrate is that the World Bank decision to increase lending to Peru was conditioned on the implementation of certain changes in Peruvian economic policies. When these changes were in fact not realized, the Bank did not lend Peru what it had initially offered: US $ 130 million over 2 years.

The first part of Article IV, Section 10 establishes that the Bank shall not interfere in the political affairs of any prospective borrower. It seems clear that conditioning loan grants upon the implementation of recommended economic policies has clear political and social effects. Can this be considered political interference? The answer is not clear. Other countries to which the World Bank has granted loans contingent upon certain economic performance are Chile, Pakistan and India (103).
The second part of Article IV, Section 10, prohibits Bank decisions from being influenced by a member's political character. This clause can be distinguished from Section 10's first part in that this second clause refers to the political character of the borrower independently of its economic performance, while the first clause focuses more on conditional loans contingent on the implementation of specific sectorial measures with obvious political impact. When discussing the World Bank interpretation of this second clause in Article IV, Section 10, most authors (104) refer to the loans made to Portugal and the Republic of South Africa in 1966. These cases were important primarily because the United Nations was then making efforts to penalize Portugal and South Africa respectively for their colonial and apartheid policies. Therefore, the Bank had to consider not only Article IV, Section 10, but also its relationship agreement with the United Nations.

Since the early 1960's, the United Nations, with a new and large African membership, had been attempting to impose pressure upon South Africa to change its "apartheid" policy and upon Portugal to grant independence to Angola and Mozambique. The United Nations had adopted several resolutions calling upon its members and specialized agencies to cooperate in the effort to discourage South Africa and Portugal from continuing their repressive policies. Nevertheless, the Bank
continued its economic assistance to these countries. In response, the UN adopted specific resolutions calling upon the Bank to refrain from making any further loans to South Africa and Portugal. General Assembly Res. No. 2054 (XX) adopted December 15, 1965 and Res. No. 2107 (XX) adopted December 21, 1965, appealed "to all specialized agencies, in particular to the IBRD... to refrain from granting" financial, economic or technical assistance to Portugal and South Africa so long as they fail to implement earlier UN resolutions.

After having been notified of these resolutions, the President of the World Bank made the following statement to explain the Bank's position: (105)

The Bank's articles provide that the Bank and its officers shall not interfere in the political affairs of any member and that they shall not be influenced in their decisions by the political character of the member or members concerned. Only economic considerations are to be relevant to their decisions. Therefore, I propose to continue to treat requests for loans from these countries in the same manner as applications from other members... I am aware that the situation in Africa could affect the economic development, foreign trade and finances of Portugal and South Africa. It will therefore be necessary, in reviewing the economic condition and prospects of these countries, to take account of the situation as it develops.

Accordingly, in June 1966, the World Bank approved a $10 million loan to Portugal, raising total Bank loans approved for that country to $57.5 million. In September 1966, the Bank approved
a $20 million loan to South Africa, thereby raising Bank's total lending to South Africa to $241.8 million, of which $196.8 million were pre-1960 loans that already had been paid (106).

UN and World Bank legal opinions concerning Article IV, Section 10 differed sharply and have never been reconciled. The UN analysis maintained that Article IV, Section 10 is intended to prohibit Bank interference in the "internal" political affairs of its members and to prevent the Bank from carrying out discriminatory policies against any member country because of the political character of that member's government. But the UN asserted that the Article did not oblige the Bank to disregard the "international" conduct of a member country and the repercussions of such conduct on international peace and security.

The World Bank, however, condemned the UN's internal-external distinction. A Memorandum of the Legal Department of the Bank, dated May 4, 1967, declared (107):

There is no justification for imparting to the term "political", as the Secretariat memorandum does, the qualification "internal". The prohibition against interference "in the political affairs of any member", is not limited to interference in the member's internal political affairs but extends as well to the relations of a member with other states, i.e., its external political affairs. Just as the Bank is precluded in making decisions on loans or guarantees from
interfering in the domestic political activities of a member government, so it is precluded from interfering or attempting to interfere with the foreign policy of that government.

The Bank clearly stressed a "functionalist" approach to the problem. This "functionalist" strategy of the World Bank as an international organization is defended by Samuel Bleicher and is built upon four basic assumptions: (108)

(1) Cooperation between states for specific economic, welfare-oriented benefits is possible in situations in which political cooperation is impossible.

(2) Successful cooperation on a non-political basis through functional international organizations will develop habits of cooperation leading to the expansion of a functional machinery.

(3) The satisfaction of basic human needs by these organizations will produce a gradual transfer of loyalties away from "chauvinisms" to international organizational cooperation.

(4) The growing effectiveness of the functional agencies will ultimately lead to an integrated world community.

Despite the Bank's "functionalist" interpretation, its self-proclaimed political neutrality has been recently challenged with regard to its financial assistance to certain military governments. The Chilean experience is a case in point, which to some degree runs parallel to the already mentioned AID policies toward Chile.
In 1970, when the leftist government of Salvador Allende assumed office, Chile nationalized the copper industry, which was mostly owned by American investors. The Bank, in applying a policy regarding nationalizations advocated by the US (Public Law 92-247), indefinitely postponed negotiations for three proposed loan-projects and made no new loans to Chile during the Allende administration. In September 1973, General Pinochet took over power and quickly moved to settle the disputes which had arisen from the nationalizations; a final agreement between Chile and the expropriated American mining companies was soon reached. Shortly thereafter, the World Bank initiated loan negotiations with Chile. In February 1974, the Bank approved two supplementary loans and one technical assistance loan (109).

As Yokota points out (110), the significant aspect of the Chilean case is that while Allende's socialist government was in power, the Bank did not grant any loans to Chile, and that only half a year after the military government took power, the Bank quickly approved several loans. Under these circumstances, it is hard to believe that loan approval was decided exclusively on economic grounds. The economic performance of a country cannot change from unacceptable to acceptable so suddenly.

Some conclusions can be drawn from these case studies. First, the World Bank has frequently exercised strong leverage
over member countries' economic policy decisions. Conditional loans that require borrowers to carry out certain economic measures will usually have political impact. But can the imposition of these economic requirements, necessary for Bank approval of loans under seemingly strict economic criteria, be considered political interference? The degree of political interference can only be evaluated in a case-by-case study. But what does seem clear is that the Bank will always take into account the political situation of the borrowing country.

Second, the Bank has adopted a functionalist approach toward pressures applied over Bank policy decisions toward certain countries. In recent years, this "neutral" approach has been challenged where the Bank has dealt with certain leftist and military governments.

A second provision in the IBRD Articles of Agreement shifts our analysis to the flip side of the IBRD-member mutual influence issue: to member country efforts to influence World Bank policies. As we have earlier studied, World Bank decisions are generally made and carried out by Executive Directors representing member countries. Article I, Section 5 (c) states:

Section 5. President and staff

The President, officers and staff of the Bank, in discharge of their offices, owe their duty
entirely to the Bank and to no other authority. Each member of the Bank shall respect the international character of this duty and shall refrain from all attempts to influence any of them in the discharge of their duties.

The United States has enacted two laws, Public Laws 92-247 and 95-118, that are apparently contrary to this provision, since they seek to prevent US Executive Directors from approving loans under certain circumstances. Although the unavailability of official Bank voting records on specific loan proposals makes it difficult to link these laws directly with loan restrictions by the World Bank, certain Bank policies seem to be their direct consequences.

Public Law No. 92-247 was enacted on March 10, 1972 during a period of time in which nationalistic government movements arising in many developing countries expropriated many corporations with significant American capital participation. President Nixon made clear his administration's intention to condition the use of economic aid, both bilateral and multilateral, on the resolution of expropriation problems. In a speech before Congress, Nixon declared (111):

All these factors - the legitimate protection of American businesses abroad, the requirements of international law, the preservation of a reasonable and mutually beneficial atmosphere for foreign investment - led us in early 1972 to define our policy toward expropriations. We

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have made it clear that if an American firm were seized without reasonable efforts to make effective payment, we would provide no new bilateral economic assistance to the expropriating country. ... Nor would we support applications for loans by such countries in international development institutions. [Emphasis added]

Pursuant to this policy objective, the US exercised its power in development banks to settle American expropriation problems. Although expropriations generally had taken place during the late 1960's, Public Law 92-247 was intended to officially direct the President to place indirect pressure on developing countries through international development banks. The relevant parts of the law provide:

The President shall instruct the United States Executive Director of the International Bank for Reconstruction and Development and the International Development Association to vote against any loan or other utilization of funds of the Bank and the Association for the benefit of any country which has:

(1) nationalized or expropriated or seized ownership or control of property owned by any United States citizen or by any corporation, partnership, or association not less than 50 per centum of which is beneficially owned by United States citizens ...

Public Law 95-118, enacted on October 3, 1977, seeks to use international development banks for national policy purposes. This law was a part of the Carter administration foreign policy that heavily emphasized human rights considerations. Once again,
political considerations were introduced into World Bank operations. The relevant parts of Public Law 95-118 state:

**Human rights and the United States assistance policies with international financial institutions.**

(a) The United States Government, in connection with its voice and vote in the International Bank for Reconstruction and Development... shall advance the cause of human rights, including by seeking to channel assistance toward countries other than those whose governments engage in:

(1) a consistent pattern of gross violations of internationally recognized human rights...

(f) The United States Executive Directors of the institutions listed in subsection (a) of this section are authorized and instructed to oppose any loan, any extension of financial assistance, or any technical assistance to any country described in subsection (a) (1) or (2) of this section, unless such assistance is directed specifically to programs which serve the basic human needs of the citizens of such country.

The current US administration is shifting its focus on what role the World Bank and other development banks should play in economic assistance. More emphasis has been placed on private investment vis-a-vis assistance through international organizations. President Reagan, in a speech delivered before the IMF and World Bank Boards of Governors in November 1981, stated (112):

The International Finance Corporation plays the leading role in the Bank family in support of [private] investment. Given the importance of this role, we hope it can be enhanced. We believe
all facets of the Bank can play a more active role in generating private resources and stimulating individual initiative in the development effort.

Can anything be done to restrict member governments from influencing World Bank loan operations? It seems unlikely for two main reasons. First, many governments seek to use development banks to advance their foreign policy aims, as the US demonstrated through Public Law's 92-247 and 95-118. Second, capital-exporting countries have a two-fold interest in using development banks. These countries have an ideological interest in establishing free-market societies in the borrowing countries. They also have the related interest of increasing borrower purchasing power in order to increase sales of their products. Most purchases made with Bank loans are of products manufactured in those countries that are the largest contributors to the Bank.
II.e. Loan operations and lending criteria

Until now, we have conducted our study of the World Bank from two perspectives. First, we have examined the institutional aspects of the Bank: how the Bank raises funds to loan to borrowing countries; how the Executive Directors make Bank decisions under the general supervision of the Board of Governors; and what the relationships are between the Bank and other international organizations that to some extent serve similar objectives. Second, we have seen how the policy decisions taken by the World Bank, like those taken in most international development institutions, influence member country internal policies and are often influenced by member countries seeking to advance foreign policy objectives. In this section, however, we will review, in general terms, the basic loan operations and policies carried out by the Bank. We will examine the criteria the Bank applies in loan operations, either pursuant to the Articles of Agreement or as a result of policies the Bank has itself adopted. It will not be necessary to enter into a detailed analysis of the characteristics of each type of loan, that is, specific financial provisions, amortization schedules, interest and commitment charges, because these are usually a result of individual project economic analysis and do not reflect the institutional policies of the Bank.
The most important distinction involved in World Bank lending policies is the distinction between project-loans and program-loans. Related to both kinds of loans is the use the borrowing country must make of the loan proceeds, whether import financing or local expenditure financing. Before entering into an analysis of the project-program distinction, let us review very broadly some of the conservative, market-oriented principles that guide Bank lending policies (113).

The first criterion a prospective borrower must meet is that funds must be unavailable elsewhere since the Bank is a "lender of last resort" (114); the borrower must first see if it can borrow the money from private capital sources. Only when funds cannot be raised elsewhere, either because of high cost or because private sources lack interest, will the World Bank be willing to consider the loan request (115).

A second criterion, usually applicable only to project financing, is a high rate of return. The Bank will only agree to finance projects that have a very high rate of return. Only under special circumstances will the IBRD finance projects with a rate of return less than 10%.

The third criterion is that the country seeking to obtain a loan must be considered creditworthy according to the country-
evaluation made by Bank officials. This criterion, then, raises the issue of conditionality in loan operations, which leads to the more general question of whether or not the Bank is thereby interfering in internal political matters of member countries.

We will begin the study of project and program loans by tracing the distinction to IBRD Charter provisions. Article III, Section 4 (vii) provides that the IBRD can only lend money for specific projects except in special circumstances. Neither the term "specific project" nor the "special circumstances" that would permit exceptions to the specific project rule (program loans) was defined in the Charter provisions.

The distinction between project and program loans, more economic than legal, has been subject to several interpretations since 1947. One of the first interpretations was given in the Bank's Fifth Annual Report in 1950: (116)

The objective of this provision is simply to assure that the Bank loans will be used for productive purposes. In effect, the only requirement which it imposes is that before the loan is granted, there shall be a clear agreement both as to the types of goods and services for which the proceeds of the loan are to be expended and the uses to which these goods and services are to be put.

During the Bank's first 20 years, most development loans were
project-oriented; that is, most loans were limited to financing specific and independent productive installations. The Bank was very conservative in its project selection and sought to finance only highly-productive, capital-intensive projects.

A program loan can be generally defined as a loan made to finance the importation of raw materials, intermediate products or capital goods for use in a national development program (117). Thus, although the Bank usually mandates a certain degree of specificity as to the use of loan proceeds, its decision whether or not to grant the loan is based more on an evaluation of the development program presented by the borrower.

The distinction between project and program loans has very important consequences for the control and leverage the Bank has with the borrowing country. If the Bank not only wants to specify the imports that will be financed, but also wants to trace them through to their final use, it will usually directly finance the foreign exchange cost of identifiable projects (118). In, on the other hand, the Bank wants to provide foreign exchange to the borrower for imports that are usually specified in advance but over whose ultimate destiny the Bank does not wish to exercise control, it will usually grant a program loan. But the issue is not only "project or program", since Bank loans also depend on the needs of the borrowing country and country's "absorptive capacity".
The project cycle undertaken by the Bank before a loan is granted has three basic stages. The first stage is project identification: determining which projects should have priority for financing. During this stage, Bank missions are sent to possible borrowing countries to evaluate their overall economic performance (creditworthiness) and to determine possible specific projects to be financed.

The second stage is project preparation, which involves a determination of the technical feasibility of a specific project and an evaluation of its proposed management and organization. This latter consideration is very important in the Bank's final decision regarding economic assistance. Loans often have been conditioned on the improvement of management and on the creation of special project-executing agencies.

The third stage is project appraisal, which focuses primarily on the rate of return of the project under study and its economic-financial characteristics. During the initial years of Bank operations, most Bank-finance projects were for public services, i.e., hydroelectric projects, water supply projects, and road construction projects. The Bank, then, was mostly concerned with determining the rates and fees that should be charged to consumers in order to make the projects sufficiently profitable to meet operating expenses, to repay loans and to
create a surplus for future reinvestments. This process should be regarded as an advantage for some LDC's, especially in Latin America, because the agencies in charge of the public service were obliged to make the projects economically rentable; that is, these agencies would not require central government subsidies, as is the most often the case with public services.

The last ten years have seen the World Bank significantly shift its lending policies toward less developed countries. Ten years ago, nearly 55% of World Bank loans were targeted for traditional infrastructure projects to improve communications, power production and transportation. This proportion declined to 30% by 1977. Meanwhile, between 1971 and 1981, the percentage of IBRD project loans targeted for agriculture and rural development more than doubled to nearly 30%. As Hurni points out (119), the new global goal in development lending is perceived as "growth with equity", normally understood as initial growth to generate resources for later distribution. This does not mean that the more traditional projects have been dropped; rather, the new emphasis is on "making the poor more productive".

The Bank's new lending policies concentrate more on rural development, on establishing small-scale industries, on developing educational infrastructure, and on resolving nutritional and urbanizational problems. One of the important consequences
of this shift is that a greater local expenditures component is usually required. This constitutes a key factor in any national development plan, since the use of locally produced goods and local human skills has the effect of improving employment conditions and helping the development of local industries. We will discuss the issue of financing local expenditure through World Bank loans in more detail later.

Program loans are intended to meet the foreign exchange requirements of a development program. The borrowing country usually prepares a five or ten year Development Plan that requires a significant amount of foreign currency for imports. The Bank evaluates this Development Plan and, if it believes the Plan will improve the member's overall economic performance, as opposed to specific project performance, the program-loan is granted. During recent years, new international economic problems have made the Bank consider a new kind of program-loan: the structural-adjustment loan.

For the last decade, efforts to improve the economic situation of LDC's have been greatly affected by international economic conditions. The spiralling inflation in energy prices, the recessionary conditions prevailing over much of the industrialized world, exchange rate instability, worldwide inflation and the price decline of many minerals all have been factors contributing to the
critical economic and social situation faced by LDC's. Although this economic situation has had different effects in different countries (120), it is clear that LDC economies have been generally affected by Balance of Payments deficits. In order to correct this deficit situation, these countries will have to undergo important structural changes that will require a period of adjustment (121). The situation of the oil-importing countries is particularly critical; these countries are handicapped by an immediate shortage of foreign exchange that endangers their level of imports.

As Wright points out (122), the period of adjustment through which LDC's must pass is likely to take place in two phases: first, external deficits, understood as more borrowing, will rise in order to maintain a minimum level of imports; second, adjustment must be made to the patterns of production and trade in order to reduce the deficits to sustainable levels. LDC's may finance this adjustments in two basic ways: borrowing in private capital markets or requesting economic assistance from international development banks. Private capital market borrowing presents the problem that LDC's may be approaching their borrowing limits as LDC borrowing on commercial terms has risen sharply in recent years and as lenders perceive the economic situation in developing countries unfavorably. Loans from international development banks present the problem, from the lender's viewpoint, of uncertainty as to
the way the money will be used. We should not forget that according to the Articles of Agreement, the Bank lending policies are basically oriented toward financing "productive" projects. The Bank has been willing to finance program-loans only in "special circumstances". Nevertheless, since 1980, the World Bank has made an effort to help some LDC's overcome their shortage of foreign currency through special loans, called structural-adjustment loans (123).

A structural-adjustment loan is designed to support major changes in the policies and institutions of developing countries in order to reduce their current-account deficits to more manageable proportions in the medium-term while maintaining the maximum feasible development effort (124). The impact of foreign currency shortage is softened so as to permit the member country to maintain its level of imports. As of June 1981, only 18 structural adjustment loans had been granted. Since this kind of loan is still relatively new and since its implementation is still in progress, it is too soon to evaluate its effects.

One of the crucial issues raised by World Bank policies, applicable both to project and program lending, is the amount of local expenditure to be financed by a loan. We will first examine why this is such an important issue and, thereafter, we will study
the World Bank Charter provisions and policies concerning local expenditure.

Any capital investment will usually require imported equipment, materials and intermediate goods that will have to be financed through the expenditure of foreign currency. Any investment will also require the use of local labor and the procurement of certain locally made goods that can be financed in local currency. The less developed a country is, the larger the foreign exchange component of any capital investment is likely to be. As a country reaches higher stages of development, especially as its industrial sector tends to be more competitive in international markets, a country will soon be able to produce some of the capital goods it previously imported. Consequently, the percentage of total foreign currency needed to finance a particular project or program will tend to decrease overtime. With time, then, some part of the capital transfers made through loan agreements may be used for needed imports not necessarily related to specific projects or programs. As a result, this provision of funds has been called "free money", since it provides basically untied foreign currency to borrowing countries under highly concessional terms.

These untied imports can be financed through loan agreements in two ways. First, they can be financed by receiving a requested amount of foreign currency in project loans in excess of the import
requirements of the project itself and, therefore, "freely" available for general imports. Second, they may be financed through program loans covering the exchange costs of a given volume of imports specified in more or less detail and related to a Development Program.

The local expenditure issue is important because developing countries prefer using locally manufactured goods and local human capital (professional and technical) that can be financed with local currency. Local expenditure, then, permits LDC's to use "freely" the foreign currency provided in a loan. On the other hand, the World Bank, an international institution controlled by the capital-exporting countries, has traditionally preferred that Bank loan proceeds be used in the import of goods, often manufactured in the capital-exporting countries.

Article IV, Section 3 of the Articles of Agreement establishes the general provisions for the use of currencies from IBRD loans. Section 3 (a) establishes the general rule: the World Bank lends foreign currency only for imports.

Section 3. Provision of currencies for direct loans

(a) The Bank shall furnish the borrower with such currencies of members, other than the member in whose territories the project is located, as are needed by the borrower for expenditures to be made in the territories of such other members to carry out the purposes of the loan.
Section 3 (c) establishes the exception to the general rule, under which the Bank may provide foreign currency in "exceptional circumstances" for local expenditure. Section 3 (c) states:

The Bank, if the project gives rise indirectly to an increased need for foreign exchange by the member in whose territories the project is located, may in exceptional circumstances provide the borrower as part of the loan with an appropriate amount of gold or foreign exchange not in excess of the borrower's local expenditure in connection with the purpose of the loan.

With the general shift in World Bank policies away from the normally import-intensive infrastructure projects to more socially-oriented, small-scale agricultural and industrial projects, and human and rural development programs, all of which rely more heavily on local resources, it should be clear that the Bank has also changed its initial strict interpretation of Section 3 (a), a "foreign currency only for imports" view, to a more flexible interpretation of the special circumstances under which it may grant foreign currency for local expenditure. Nevertheless, critics of the World Bank policies still consider that the Bank very strict in the provision of foreign currency for local purchases and expenditures.
III. World Bank policy toward Peru in light of the political, economic and social changes in Peru since 1968

The World Bank's policies toward Peru since 1968 present an important case-example for the analysis of World Bank policies generally. Two very important, unrelated series of events came together to make this period interesting to study. First, as already developed, the World Bank shifted the emphasis of its loan policies from large infrastructure projects, whose impact on the poor was difficult to evaluate, to more socially-oriented, small-scale projects that more directly assist the poorer groups in particular borrowing countries. The Bank also started to assist specific sectors to which it had traditionally been reluctant to lend: tourism, housing and, more recently, oil activities. Further, the World Bank increased its program-loans and commenced a structural-adjustment loan program to help offset balance-of-payments deficits. The issue we will examine in this chapter is whether these new policies have been implemented in Peru; more specifically we will study the types of loans granted Peru and the economic sectors that have benefited from them.

The internal political developments of Peru are the second important factor in recent World Bank policies toward Peru. In 1968, a military coup deposed President Belaunde from office, thereby ending the democratic regime that had existed just five
years. In the following years, the military governments implemented very important social and economic measures. The World Bank completely cut off economic assistance to Peru for more than five years (125) as a direct consequence of US influence over the Bank. The American government successfully conditioned World Bank economic assistance to Peru to the compensation of shareholders of the nationalized International Petroleum Company (126). This episode clearly raises the issue of World Bank political neutrality and independence.

Our examination will begin with a general introduction to the political and social transformations that were effected by the military government. Then we will analyze Bank policies during that period.

During the Belaunde administration (1963-1968), the two major long-standing problems in Peruvian politics, the possible nationalization of the International Petroleum Company (IPC) and the agrarian reform, became critical. However, due to the circumstances in Peruvian politics, both issues remained unresolved. On October 3, 1968, a military coup deposed President Belaunde. Within a week, the new military government expropriated all IPC assets and militarily occupied the company's installations in Talara, the northern Peruvian region where the company's main operations were located.
Although these actions seemed to resolve the problem from the Peruvian standpoint, they triggered a long, and often tense and unfriendly process of negotiations, not only with IPC representatives, but also with US government officials. These negotiations ended in 1973 with an agreement between the two governments that settled the compensation issues concerning all American companies that had been nationalized or expatriated by the military government.

During this five-year negotiation period, the American government, through its Executive Director in the World Bank, exercised its power in the Bank to cut off all economic aid to Peru in order to pressure the Peruvian government to compensate American shareholders adequately. The only World Bank loan granted to Peru between September 1967 and September 1973 (see Appendix) was a US $ 30 million loan to rebuild the areas affected by a major earthquake that struck Peru on May 3, 1970 (127). This loan, the only Peruvian exception to the Bank's "no compensation agreement, no loans" policy, was granted for humanitarian reasons (128); the earthquake and subsequent floods devasted large areas of the Peruvian coastal and sierra regions, especially in the Department of Ancash, and had left a tragic toll of more than 50,000 dead or missing, half a million homeless and another half a million affected in lesser ways. As already pointed out, these conditions or pressures, imposed by the Bank upon certain member-countries
to act or undertake certain measures irrelevant to the Bank's lending operations, clearly seem to undermine the Bank's self-proclaimed apolitical nature.

Before reviewing the other specific economic and social transformations effected by the Peruvian military government, the "Revolu-

tionaly Government of Peru", one should first take note of the rather ambiguous ideological and rhetorical context in which these measures were undertaken by the military government. General Francisco Morales Bermudez, then Minister of Economy and Finance, and later head of the military junta, speaking on behalf of Peru at the 1970 annual meeting of the World Bank Board of Governors, stated: (129)

The process of revolutionary development under way in our country is not modeled on orthodox capitalism or communism, since we consider that the former leads to dependency and underdevelopment, while the latter is irrelevant to Peruvian reality and unacceptable for the national and aims of our revolution.

Most of the changes in the world have been brought about by violence. Most societies have been incapable of adapting voluntarily and peacefully to basically new conditions. The Peruvian Revolution now under way thus represents one of the few exceptions in history. It is trying to achieve the political structure of a social-democratic state in which the people are the real seat of sovereignty, and in which there are "voluntary associations", "industrial communities" or "agro-industrial cooperatives" between the state and the economy, which provide security, hope and inexhaustible opportunities for social contacts and opinions, and give men an insight into the structure of their whole
community, their individual role in it and in the enterprise, and of the country as a single unit.

Within the new ideology of the "revolutionary government", the Peruvian state acquired a much more active role in the development process. Economic planning became an important factor in policy decisions; new ministries were created to supervise sectorial policies; and public administration was enlarged to unprecedented proportions both in terms of personnel and infrastructure.

Especially during its early years, the military government enjoyed popular and civil-institutional support, basically because it was undertaking social and economic measures that were long overdue. In addition to the IPC nationalization, the most important step taken by the government was the enactment of the following legislation: the Agrarian Reform Law, the General Law on Industries, the Normative Law on Mining, and the General Law on Fishing.

The agrarian reform process, applied without exceptions or privileges for the first time in Peruvian history, affected more than 1.7 million hectares throughout the country during its long period of implementation. The law established "cooperatives" and "associations of social interest" under which confiscated land, primarily the major agro-industrial sugar complexes and large
estates that had traditionally been the power centers of landowners, were organized. As an immediate result, agricultural output tended to decline and, even now, is still under its optimum production level. However, this law should primarily be assessed by its social and political consequences for Peruvian development.

The General Law on Industries was one of the most important laws enacted by the "revolutionary government". Now that the law, with many modifications, has been in effect for more than 10 years, one can see that its initial objectives have not been adequately implemented, mainly because of its inherent contradictions. First, the law reserved certain "basic industries", particularly the heavy and strategic industries (e.g., steel, cement, oil and like industries), for exclusive ownership and development by State enterprises. Second, the law created within each individual industry an "industrial community" formed by its workers, whose participation and ownership of capital would progressively increase until they held 50%, at which time the shares representing the "industrial community" capital would become the individual property of the workers holding them. In other words, workers would become shareholders of 50% of the capital without investing capital; the capital owned by original investors, consequently, would be mandatorily reduced from 100% to 50%. This issue created so much opposition from the private sector -it was, after all, a kind of expropriation
without compensation - that the government, fearing a massive disinvestment and flow of capital outside of the country, soon modified its original proposal. Instead of transferring the ownership of capital-stock to workers, the government established that the "industrial community" would have a special stock, "labor stock", that gave workers rights to dividends but no property right in capital-stock. Although this measure still benefited workers, the initial proposal had been more radical. Third, the government provided considerable tax reductions, credit incentives and technological assistance in accordance with predetermined industrial priorities. Finally, the government subsidized imports of industrial raw materials and intermediate inputs by establishing special exchange rates for them, and established unnecessarily high tariff-rate protection that gave nearly absolute protection to industries that were producing goods locally. These last measures, clearly enacted to benefit entrepreneurs, led to the consolidation and the creation of new inefficient industries that existed only because of high-tariff protection that left them in a market without competition. They were also used to over import capital goods in order to diminish dividend-sharing with workers, and to "over pay" for imports as a way to circumvent outflow-of-capital restrictions.

Some authors (130) have tried to explain these inherent contradictions in the Peruvian military government's industrial policy
as an attempt to satisfy "both sides". On the one hand, the
government promulgated certain measures, more political than
economic, to secure popular support for the government and to
prevent the infiltration of communism. On the other hand, the
government sought to rely on the private sector to provide ca-
pital, establishing strong incentives that would ultimately per-
mit a development program to be carried out. This ambiguity was
undoubtedly one of the reasons for the political crisis of the
military government that culminated in the transfer of power
and functions to the new civil government elected in 1980 (131).

The Normative Law on Mining was enacted to promote private
and state-run mining enterprises of all sizes. Oil exploration
and exploitation were to be done either solely by domestic or
foreign private enterprises or by joint ventures in which the
Peruvian state was represented by PETRO-PERU, the recently created
and wholly-owned state oil enterprise. Although a major concern
of the law was the discovery of new mineral reserves, this act-
ivity was never adequately promoted, primarily because of the
high costs of investment and the few incentives granted. Exclu-
sive state commercialization of minerals was another major dis-
incentive to private investors.

The Law on Fisheries was enacted to change the organization
and structure of the fishing industry. PESCA-PERU, a wholly-owned
state enterprise, expropriated many of the domestic and foreign fishing enterprises, and became a huge public entity. However, due to the anchovy crisis and to bureaucratic managerial difficulties, PESCA-PERU experienced an extreme over-capacity problem.

As for the financial system, the government set up a rigid exchange control mechanism that gave the government complete power to regulate currency movements, prohibited private holdings of foreign currency, and required the repatriation of funds held outside the country. This mechanism, however, did not in fact prevent the continuous outflow of foreign currency abroad.

During the late 1970's the military government, which had clearly abandoned its reformist intentions after General Morales Bermudez became head of the military junta in 1974, reversed many of the measures it had earlier tried to implement. The civil government, which assumed office in 1980, has started to make substantial modifications in specific sectors and has been giving the Peruvian state a new role, less active and more supervisory in its functions.

Although many of the measures undertaken by the military government had positive political effects, overall Peruvian economic performance suffered during these years. Most of the new measures were very costly and had to be financed by extensive bor-
rowing. Additionally, in an effort to seek and maintain popular support, the government "politicized" economic decisions (e.g., the government subsidized gasoline when prices were rapidly increasing in world markets, and indiscriminately subsidized food products that tended to favor increased consumption by middle and upper classes). In view of this political and economic situation, the World Bank remained a relatively insignificant lender to Peru. Between 1973, when Peru settled the compensation issue with the US government, and July 1980, when the new civil government assumed office, only 14 loans were granted. The World Bank institutional organization and policies that we have studied suggest the World Bank's concerns regarding Peru's "military experiment": inherently conflicting policies and ideologies, politicized economic decision-making, and the uncertain economic consequences of the political and social transformations it sought to carry out.

Now that we have described the general political and economic situation in which the World Bank made loans to Peru during the 1970's, we will examine the specific kinds of loans made during this time to see whether the World Bank's new lending policies to LDC's were implemented in Peru.

During the military government's early years, Peru was a relatively small borrower from the World Bank. At least 3 of the
4 loans granted when the military government was still carrying out its "reformist" measures (before General Morales Bermudez became junta chief in 1974) were targeted for specific projects. These loans, then, permitted the World Bank to exercise a high degree of control over the way the proceeds were to be used (see Appendix). The only loan that can be to some degree considered within the Bank's new lending policy was a US $ 25 million loan made in September 1973 to the Agrarian Bank of Peru, a state-owned agrarian development bank, to be re-lent thereafter in small amounts to farmers for the import of agricultural machinery.

After General Morales Bermudez assumed power in 1974, the World Bank demonstrated approval of the economic modifications that his government was gradually introducing by increasing the amount of loans approved for Peru. But, again, the Bank extended loans that were within the traditional capital-intensive, specific-project are. Most new loans were targeted for electrical power, highway construction and maintenance, water supply systems and mining activities.

The first program-loan ever extended to Peru was granted in May 1979. The Peruvian government, facing a critical economic situation, had prepared an "Economic Recovery Program", which the World Bank carefully evaluated before rendering its decision on the program-loan. This US $ 115 million loan was the largest
single-loan ever made to Peru. In general terms, the agreement authorized the Peruvian government to use the loan proceeds for the import of goods required to carry out the Economic Recovery Program: to import goods, mainly industrial machinery, ultimately to be used is several specific-projects. But, as already mentioned, the World Bank, in deciding to make a program-loan, is more concerned in the evaluation of the general Development Program, in this case the "Economic Recovery Program", than in the ultimate use of the purchased goods. Since no provision regarding local procurement was made, most of the loan proceeds were to be used for the import of capital goods. However, the possibility of local expenditure was contemplated through certain technical assistance studies and other smaller purchases needed for the Development Program.

During 1980, the World Bank granted two important loans to Peru that can be seen as a result of the Bank's new lending policy. First, the IBRD extended a US $ 32.5 million loan to finance a project seeking to expand Peruvian oil production, so that Peru could meet its domestic oil needs and maintain an exportable surplus in the medium run. This loan was the Bank's first project-loan to Peru for petroleum operations, a sector to which the Bank generally has been reluctant to lend, mainly because of the high risk involved. Second, the Bank granted a US $ 15 million loan for rural development, which is the Bank's first integrated rural development project. Although not significant in amount, the loan
nevertheless seeks to benefit a large number of small farmers in one of the poorest areas of the country, thereby increasing their standard-of-living.

These development, then, allow us to conclude that, because of its approval of the recent overall Peruvian economic and political situation, the World Bank is increasing lending operations to Peru and seems more willing to finance rural and small-scale sectorial projects that are important for Peruvian development.
Conclusions

The preceding discussion allows us to make the following conclusions:

1. Membership in the World Bank Group is conditional upon membership in the International Monetary Fund. Therefore, the monetary discipline imposed by the IMF seems to be a primary criterion for loan assistance by the World Bank.

2. The IBRD has a very solid financial structure. World Bank subscribed capital is formed by a 10% "paid-in" capital that provides the US dollars and other member-country currencies through which the Bank operates and by a 90% "callable" capital that constitutes the largest "guarantee fund" in any international development bank. Additionally, the World Bank has never experienced a default in any loan or guarantee it has made and, since 1949, has annually generated profits which are either maintained in the Bank's reserves or transferred through loans to the International Development Association. Consequently, the World Bank is one of the most creditworthy international organizations and, as a borrower, has been able to gain the confidence of international capital markets. Strict economic criteria guide the Executive Directors in the utilization of Bank funds.

3. Voting rights in the World Bank are based upon each country's...
total subscribed capital. The total number of votes each country has is determined by a simple formula that was intended to weigh votes in favor of smaller subscribers. This weighting of votes, however, has no practical value since the Bank's largest contributors have total control over its operations.

4. World Bank policy decisions are formulated by two collective organs in the Bank's organizational structure: the Board of Governors, which ultimately has all Bank powers but in practice acts as a supervisory entity, and the Executive Directors, who are in charge of the day-to-day activities of the Bank. Each member country is represented on the Board of Governors by one "governor" (a total of 139 in 1981). The 21 Executive Directors are either appointed, one by each of the 5 largest subscribers, or elected by the member countries not entitled to appoint an Executive Director. The mechanism for the election of the 16 Executive Directors has two disadvantages: it favors the first choice of larger subscribers and makes single regional representation difficult, though not impossible. The appointed Executive Directors cast the votes of the country they represent, and the elected Executive Directors must cast the votes of all the countries whose votes were required for his election. No dispersion of votes is possible.

5. The World Bank is a Specialized Agency of the United Nations.
The UN-IBRD specialized agency agreement is *sui generis* in that it guarantees the Bank's autonomy from the United Nations system. Both institutions currently cooperate in a series of specific fields, thereby complementing each other's activities: UN entities generally do specific sector studies, and project preparation and evaluation, while the World Bank finances the project. The Bank has always wanted to maintain its independence and to prevent UN interference because it fears the inclusion of "political" considerations in its decisions. The basic structural difference between the two international organizations is that while voting in most UN entities is based upon a "one country one vote" principle, the World Bank voting power is determined by the amount of capital subscribed by each country.

6. According to its Articles of Agreement the World Bank is forbidden from interfering in the internal political affairs of its members and from making loan decisions upon political considerations. But, although economic considerations alone should determine loan decisions, these decisions may still be politicized. Bank interference in the political affairs of a borrowing country is related to the degree to which the Bank can condition loan approval upon the carrying out of certain economic measures recommended by the Bank. Most economic measures have a direct political impact, but it is not clear to what extent the Bank's pressures have been the primary reason for
of these measures. The Bank, however, does seem to have a strong influence over the economies of member countries needing economic assistance.

When considering a loan petition the Bank evaluates the political and economic situation of a country. The "functionalist" approach defended by the Bank has recently been undermined when the Bank has considered loans to some leftist and military governments.

7. Large subscribers, especially the United States, will often instruct their Executive Directors to exert pressure on certain governments in order to make those governments undertake certain economic or political measures. In this way, large subscribers indirectly use the World Bank to carry out their foreign policy objectives, and thereby seem to undermine the apolitical nature of the Bank and clearly contravene the Charter provisions that prohibit member governments from influencing Bank officials.

8. In the Peruvian case, the US government exercised its voting power and influence in the World Bank to cut off economic aid to Peru for more than five years, until compensation for the IPC expropriation was agreed upon.

After this compensation agreement was finally reached, however, the Bank remained relatively unsympathetic toward Peruvian
requests for economic aid, until the Peruvian government undertook certain stringent economic measures and the political situation became more stable.

9. The World Bank is an important international development bank that has played a key role in LDC development efforts. It is clear that capital-exporting countries have a direct interest in aiding LDC's through international development banks so as to promote the purchase of goods they produce. But the World Bank, like the IMF, is also an institution whose underlying objective is to secure free-market, capitalist societies.
### Appendix

**World Bank loans to Peru between January 1952 and December 1980**

<table>
<thead>
<tr>
<th>Borrower</th>
<th>Project description</th>
<th>Loan Number</th>
<th>Agreement date</th>
<th>Amount of Principal a</th>
<th>Interest rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Republic of Peru</td>
<td>Port of Callao-project</td>
<td>57-0</td>
<td>23. Jan. 52</td>
<td>2.5</td>
<td>4.5%</td>
</tr>
<tr>
<td>2. Republic of Peru</td>
<td>Agricultural Machinery</td>
<td>67-0</td>
<td>8 Jul. 52</td>
<td>1.3</td>
<td>4.12%</td>
</tr>
<tr>
<td>3. Republic of Peru</td>
<td>Second agricultural machinery</td>
<td>98-0</td>
<td>12 Apr. 54</td>
<td>1.7</td>
<td>4.25%</td>
</tr>
<tr>
<td>4. Banco de Fomento Agrop. Agricultural Credit Guarantor- PERU</td>
<td>105-0</td>
<td>12 Nov. 54</td>
<td>5</td>
<td></td>
<td>4.25%</td>
</tr>
<tr>
<td>5. Republic of Peru</td>
<td>Quiroz-Piura Irrigation</td>
<td>114-0</td>
<td>5 Apr. 55</td>
<td>18</td>
<td>4.75%</td>
</tr>
<tr>
<td>6. Compania Nacional de Cemento Portland S.A. Pacasmayo Cement project Guarantor- PERU</td>
<td>116-0</td>
<td>19 Apr. 55</td>
<td>2.5</td>
<td></td>
<td>4.62%</td>
</tr>
<tr>
<td>7. Republic of Peru</td>
<td>Highway project</td>
<td>127-0</td>
<td>5 Aug. 55</td>
<td>5</td>
<td>4.25%</td>
</tr>
<tr>
<td>8. Banco de Fomento Agrop. Second Agricultural credit Guarantor- PERU</td>
<td>162-0</td>
<td>13 Mar. 57</td>
<td>5</td>
<td></td>
<td>5.5%</td>
</tr>
<tr>
<td>9. Peruvian Corporation Ldt. Railways Guarantor- PERU</td>
<td>190-0</td>
<td>3 Apr. 58</td>
<td>15</td>
<td></td>
<td>5.5%</td>
</tr>
<tr>
<td>10. Autoridad portuaria Callao Port-project expansion Guarantor- PERU</td>
<td>208-0</td>
<td>15 Sep. 58</td>
<td>6.58</td>
<td></td>
<td>5.75%</td>
</tr>
<tr>
<td></td>
<td>Description</td>
<td>Code</td>
<td>Date</td>
<td>Amount</td>
<td>Rate</td>
</tr>
<tr>
<td>---</td>
<td>------------------------------------------------------------------------------</td>
<td>------</td>
<td>-----------</td>
<td>--------</td>
<td>------</td>
</tr>
<tr>
<td>11</td>
<td>Banco de Fomento Agrop. Third Agricultural credit Guarantor- PERU</td>
<td>257-0</td>
<td>1 Jun. 60</td>
<td>5</td>
<td>6%</td>
</tr>
<tr>
<td>12</td>
<td>Empresas Electricas Asos. Huinco electric project Guarantor- PERU</td>
<td>260-0</td>
<td>29 Jun. 60</td>
<td>24</td>
<td>6%</td>
</tr>
<tr>
<td>13</td>
<td>Republic of Peru Aguaytia-Pucallpa road</td>
<td>271-0</td>
<td>19 Dec. 60</td>
<td>5.5</td>
<td>5.75%</td>
</tr>
<tr>
<td>14</td>
<td>Republic of Peru Highway maintenance</td>
<td>300-0</td>
<td>3 Nov. 61</td>
<td>10</td>
<td>5.75%</td>
</tr>
<tr>
<td>15</td>
<td>Peruvian Corporation Ltd. Railway rehabilitation Guarantor- PERU</td>
<td>334-0</td>
<td>13 Mar. 63</td>
<td>13.25</td>
<td>5.5%</td>
</tr>
<tr>
<td>16</td>
<td>Empresas Electricas Asos. II- Huinco electric project Guarantor- PERU</td>
<td>365-0</td>
<td>22 Nov. 63</td>
<td>15</td>
<td>5.5%</td>
</tr>
<tr>
<td>17</td>
<td>Republic of Peru Paita port</td>
<td>373-0</td>
<td>22 Apr. 64</td>
<td>3.10</td>
<td>5.5%</td>
</tr>
<tr>
<td>18</td>
<td>Banco de Fomento Agrop. Fourth Agricultural credit Guarantor- PERU</td>
<td>415-0</td>
<td>3 Jun. 65</td>
<td>15</td>
<td>5.5%</td>
</tr>
<tr>
<td>19</td>
<td>Republic of Peru San Lorenzo irrigation proj.</td>
<td>418-0</td>
<td>18 Jun. 65</td>
<td>11</td>
<td>5.5%</td>
</tr>
<tr>
<td>20</td>
<td>Republic of Peru La Oroya-Aguaytia road</td>
<td>425-0</td>
<td>17 Sep. 65</td>
<td>33</td>
<td>5.5%</td>
</tr>
<tr>
<td>21</td>
<td>Republic of Peru Pisco port project</td>
<td>446-0</td>
<td>13 May 66</td>
<td>9.1</td>
<td>6%</td>
</tr>
<tr>
<td>22</td>
<td>Empresas Electricas Asos. Power distribution proj. Guarantor- PERU</td>
<td>464-0</td>
<td>7 Sep. 66</td>
<td>10</td>
<td>6%</td>
</tr>
<tr>
<td></td>
<td>Description</td>
<td>Code</td>
<td>Date</td>
<td>Amount</td>
<td>Rate</td>
</tr>
<tr>
<td>---</td>
<td>--------------------------------------</td>
<td>------</td>
<td>--------</td>
<td>--------</td>
<td>-------</td>
</tr>
<tr>
<td>23.</td>
<td>Empresas Electricas Asos. Power distribution proj. Guarantor- PERU</td>
<td>511-0</td>
<td>11 Sep. 67</td>
<td>17.5</td>
<td>6%</td>
</tr>
<tr>
<td>24.</td>
<td>Republic of Peru Road reconstruction</td>
<td>706-0</td>
<td>14 Sep. 70</td>
<td>30</td>
<td>7.25%</td>
</tr>
<tr>
<td>25.</td>
<td>Banco Agrario del Peru Agricultural credit Guarantor- PERU</td>
<td>933-0</td>
<td>12 Sep. 73</td>
<td>24</td>
<td>7.25%</td>
</tr>
<tr>
<td>26.</td>
<td>Republic of Peru Education</td>
<td>949-0</td>
<td>5 Dec. 73</td>
<td>24</td>
<td>7.25%</td>
</tr>
<tr>
<td>27.</td>
<td>Republic of Peru Sixth road project-loan</td>
<td>1025-0</td>
<td>1 Jul 74</td>
<td>26</td>
<td>7.25%</td>
</tr>
<tr>
<td>28.</td>
<td>Republic of Peru Lima-Amazon transport road</td>
<td>1196-0</td>
<td>27 May 76</td>
<td>76.5</td>
<td>8.5%</td>
</tr>
<tr>
<td>29.</td>
<td>Republic of Peru Fifth power loan</td>
<td>1215-0</td>
<td>20 Sep. 76</td>
<td>36</td>
<td>8.5%</td>
</tr>
<tr>
<td>30.</td>
<td>Banco de la Vivienda Urban cities Guarantor- PERU</td>
<td>1283-0</td>
<td>12 Oct. 76</td>
<td>21.6</td>
<td>8.5%</td>
</tr>
<tr>
<td>31.</td>
<td>Emp. minera del Centro Centromin expansion Guarantor- PERU</td>
<td>1281-0</td>
<td>6 Dec. 76</td>
<td>40</td>
<td>8.5%</td>
</tr>
<tr>
<td>32.</td>
<td>Corporacion Financiera COFIDE Guarantor- PERU</td>
<td>1358-0</td>
<td>28 Jan. 77</td>
<td>35</td>
<td>8.7%</td>
</tr>
<tr>
<td>33.</td>
<td>Republic of Peru Irrigation rehabilitation</td>
<td>1403-0</td>
<td>20 May 77</td>
<td>25</td>
<td>8.5%</td>
</tr>
<tr>
<td>34.</td>
<td>Republic of Peru Water supply and power engineering</td>
<td>S011-0</td>
<td>22 Dec. 78</td>
<td>8.8</td>
<td>7.35%</td>
</tr>
<tr>
<td>No.</td>
<td>Description</td>
<td>Amount</td>
<td>Date</td>
<td>Amount</td>
<td>Interest</td>
</tr>
<tr>
<td>-----</td>
<td>-----------------------------------------------------------</td>
<td>---------</td>
<td>----------</td>
<td>--------</td>
<td>----------</td>
</tr>
<tr>
<td>35</td>
<td>Republic of Peru Program-loan</td>
<td>1693-0</td>
<td>17 May 79</td>
<td>115</td>
<td>7.9%</td>
</tr>
<tr>
<td>36</td>
<td>Republic of Peru 2nd. Irrigation Rehabilitation, Lower Piura</td>
<td>1771-0</td>
<td>4 Feb.80</td>
<td>56</td>
<td>7.95%</td>
</tr>
<tr>
<td>37</td>
<td>Petroleos del Peru/Cofide Petroleum Production Guarantor- PERU</td>
<td>1806-0</td>
<td>28 Apr.80</td>
<td>32.5</td>
<td>8.25%</td>
</tr>
<tr>
<td>38</td>
<td>Republic of Peru Puno rural development project</td>
<td>1812-0</td>
<td>28 Apr.80</td>
<td>15</td>
<td>8.25%</td>
</tr>
<tr>
<td>39</td>
<td>Republic of Peru Bayobar phosphate project</td>
<td>1888-0</td>
<td>21 Aug.80</td>
<td>7.5</td>
<td>8.25%</td>
</tr>
<tr>
<td>40</td>
<td>Empresa Siderurgica (Sider) Sider-Peru technical assistance Guarantor- PERU</td>
<td>S019-0</td>
<td>15 Dec.80</td>
<td>5</td>
<td>8.25%</td>
</tr>
</tbody>
</table>

a) in million US dollars

Source: IBRD, Statement of Loans, Latin America and Caribbean, PERU, pages 155-160
Notes

(1) Peru Economico, Que se viene en Politica Economica, Vol. 3 No. 6, Lima, June 1980, p. 7


(3) Id., at p. 52


(5) Id., at p. 14

(6) Id., at p. 18


(9) Id., at p. 63

(10) Id., at p. 64

(11) Hurni, op. cit., p. 8

(12) IBRD, Articles of Agreement, Article III, Section 4 (ii)

(13) The increase of productivity in the borrowing country is still one of the major concerns of World Bank policies.
(14) Bittermann, *art. cit.*, p. 68

(15) *Id.*, at p. 84

(16) IBRD, *op. cit.*, Article III, Section 4-viii

(17) The report of the Executive Directors to the Board of Governors on interpretation of the Articles of Agreement, was the following:

It follows, therefore, that, under Article III, Section 4 (vii) of the Articles of Agreement, the Bank, while primarily expected to make or guarantee loans for specific projects of reconstruction and development, does have authority to make or guarantee loans for programs of economic reconstruction and the reconstruction of monetary systems, including long-term stabilization loans, even if such loans are not for specific projects of reconstruction or development within the meaning of such Section.

See, First Annual Report by the Executive Directors, Washington, D.C., September 27, 1946, p. 25

(18) Bittermann, *art. cit.*, p. 70


(20) Bittermann, *art. cit.*, p. 71

(21) Article I of the International Development Association's Articles of Agreement, states:

The purposes of the Association are to promote economic development, increase productivity and thus raise standards of living in the less-developed areas of the world included within the Association's membership, in particular by providing finance to meet their important development requirements on terms which are more flexible and bear less heavily on the balance of payments
than those of conventional loans, thereby furthering the development objectives of the International Bank for Reconstruction and Development and supplementing its activities.

Reprinted in Mason, Edward and Asher, Robert, op. cit., p. 789


(23) Id., at p. 197


(25) Id., at p. 2


(27) The only two exceptions to this interpretation were the cases of India and Philippines, which became original members prior to their independance.

(28) Syz, op. cit., p. 108

(29) Bittermann, art. cit., p. 108

(30) Mason, Edward and Asher, Robert, op. cit., p. 30
(31) IBRD, op. cit., Article V, Section 3 (a)

(32) Id., Article V, Section 3 (b)

(33) Mason, Edward and Asher, Robert, op. cit., p. 106

(34) IBRD, op. cit., Article II, Sections 5 (i), (ii) and 7 (i), (ii)

(35) Mason, Edward and Asher, Robert, op. cit., p. 105

(36) IBRD, op. cit., Article II, Section 8 (a)

(37) Mason, Edward and Asher, Robert, op. cit., p. 109


(39) Hurni, op. cit., p. 7

(40) Mason, Edward and Asher, Robert, op. cit., p. 114

(41) Gross income from Bank operations less total expenses, including allocations to Special Reserve.

(42) Mason, Edward and Asher, Robert, op. cit., p. 120


(44) Mason, Edward and Asher, Robert, op. cit., p. 121


(46) Id., at p. 85

(47) Hurni, op. cit., p. 7

(48) Syz, op. cit., p. 145

(49) Mason, Edward and Asher, Robert, op. cit., p. 125

(51) Syz, _op. cit._, p. 146


(53) It is important to stress the post-negotiation character of the Participation Agreement in order to distinguish it from the joint financing which is another way of financing which we will not study.

(54) Syz, _op. cit._, p. 147

(55) Id., at. p. 148

(56) Mason, Edward and Asher, Robert, _op. cit._, p.146

(57) Syz, _op. cit._, p. 30

(58) IBRD, _op. cit._, Article V, Section 2 (b)

(59) In practice the Board of Governors meets to discuss the Annual report presented by the Executive Directors for their approval. See, IBRD By-Laws, Section 9

(60) IBRD By-Laws, Section 2 (b)

(61) Id., Section 2 (c)

(62) 1971 Annual Meetings of the Board of Governors, Washington, p. 137

(63) Syz, _op. cit._, p. 42

(64) IBRD, _op. cit._, Article V, Section 4 (b)

(65) Syz, _op. cit._, 44

(66) IBRD, _op. cit._, Article V, Section 4 (f)
(67) Id., Article V, Section 4 (g)
(68) Id., Article V, Section 5 (a)
(69) Id., Article VI, Section 5 (a)
(70) Id., Article VI, Section 5 (d)
(71) Id., Article VI, Section 5 (f)
(72) Id., Article VI, Section 5 (h)
(73) Id., Article IX, Section (a)
(74) Id., Article V, Section 2 (c)
(75) IBRD, By-Laws, Section 2 (b)
(76) Id., Section 9
(77) Specialized Agency Agreement 15, Nov. 1947, 16 UNTS 346
(78) Mason, Edward and Asher, Robert, op. cit., p. 561
(79) Id., at p. 564
(80) General Assembly Resolution 2029 (XX)
(81) Mc Namara, Robert, Address before the Economic and Social Council, November 13, 1970
See, Mason, Edward and Asher, Robert, op. cit., p. 566
(82) Id., at. p. 560
(84) Id., p. 76
(85) Most of the organizational characteristics of the World Bank are also shared by the International Monetary Fund.

(87) Most of the information has been obtained from the official document, *Assisting the Developing Countries: Foreign Aid and Trade Policies of the United States*.

(88) *Id.*, p. 2


(90) Smith, Leslie, *Financing Urbanization in Developing Countries*, in Georgia Journal of International and Comparative Law, No. 10, 1980, p 593


(92) In 1961 with the enactment of the Foreign Assistance Act (FAA), this type of aid was designated "Supporting Assistance". Then in 1971 it was renamed "Security Supporting Assistance" and in 1978 the International Security Assistance Act renamed it Economic Support Fund.

(93) *Assisting the Developing Countries*, op. cit., p. 17

(94) *Assisting the Developing Countries*, op. cit., p. 14

(95) Mason, Edward and Asher, Robert, op. cit., p. 422

(96) Syz, op. cit., p. 166

(97) The basic information was obtained from Mason, Edward and Asher, Robert, op. cit., p. 453 and complemented
with personal research, indicated in the following footnotes.

(98) IBRD, _Annual Report 1964-1965_, p. 84

(99) EC/M/66-2, Jan. 6, 1966 cited by Mason, Edward and Asher, Robert, _op. cit._, p. 453


(101) Kuczynski, _op. cit._, p. 100

(102) _Id._, at p. 175

(103) Mason, Edward and Asher, Robert, _op. cit._, p. 455


(105) Yokota, _art. cit._, p. 57

(106) Mason, Robert and Asher, Edward, _op. cit._, p. 588

(107) _Id._, at p. 588

(108) Samuel A. Bleicher, "UN v. IBRD: A Dilema of Functionalism", p. 42 cited by Mason, Edward and Asher, Robert, _op. cit._, p. 587

(109) Yokota, _art. cit._, p. 60

(110) _Id._, p. 61


(114) See footnote (11)

(115) IBRD, *op. cit.*, Article I (ii) and Article III, Section 4 (ii)


(117) Mason, Edward and Asher, Robert, *op. cit.*, p. 230

(118) *Id.*, at p. 231

(119) Hurni, *op. cit.*, p. 29

(120) One very important factor in softening the impact of world's economic situation is the control of the economy each country has and the feasibility of taking specific measures to protect itself.


(122) *Id.*, p. 20

(124) Id., p. 69

(125) Only one loan No. 706-0 was granted to Peru in September 14, 1970

(126) See President Nixon's speech, footnote (111)

(127) Annual Meeting of the Board of Governors, 1970, p. 150


(129) Annual Meeting of the Board of Governors, 1970, p. 145

(130) For an excellent, nearly profetic because of the time when it was written, analysis see Macera, Pablo, op. cit., p. 271

(131) There are many other factors, both national and international, that determine the political crisis of the military government.