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CONTENTS: Discussion of mobilization of financial resources for economic development (E/CN.1/Sub.3/25, E/CN.1/Sub.3/W.6, E/CN.1/Sub.3/W.5, E/CN.1/Sub.3/W.8, E/CN.1/Sub.3/W.9, E/CN.1/Sub.3/W.7)(discussion continued)

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DISCUSSION OF MOBILIZATION OF FINANCIAL RESOURCES FOR ECONOMIC DEVELOPMENT (E/CN.1/Sub.3/25, E/CN.1/Sub.3/W.6, E/CN.1/Sub.3/W.5, E/CN.1/Sub.3/W.8, E/CN.1/Sub.3/W.9, E/CN.1/Sub.3/W.7) (discussion continued)

The CHAIRMAN welcomed Mr. Bernstein, Director of Research of the International Monetary Fund, and thanked him for the three country studies produced by the Fund.

Mr. BERNSTEIN said the International Monetary Fund had no direct responsibility in connection with international investment, which was dealt with by the International Bank. The Fund's interest was to see that member countries made the most of their resources and to help them in framing their financial policies.

The studies that had been carried out on underdeveloped areas showed that those regions were not realizing the full productive capabilities of their resources. The failure to provide investment facilities that would open new opportunities for production and raise the efficiency of production meant that the underdeveloped countries were dissipating some of their resources in under-employment and mis-directed employment.

The studies showed that the difficulty was due, in part, to a lack of financial resources for development. The Fund technical staff had concluded that there was some deficiency in the financial organization of underdeveloped countries. When a country lacked domestic savings, some of its real resources were not used or were used in the wrong way. For instance, labour might be kept in agriculture far beyond the economic capacity of the land. Also people might hold savings in gold or silver or in foreign balances. It was important to undertake to increase the volume of savings, to mobilize savings, and to utilize them in the most effective way.

/There could be

There could be no uniform plan for overcoming any shortage of investment funds in underdeveloped countries. Any remedy must be suited to the particular requirements and possibilities of the individual country. The financial institutions required would differ according to the type of development undertaken. The country's main requirement might be additional finance to cover commercial crop production and marketing, or it might need additional finance for redistribution of land ownership and for land improvement. At the other extreme, the need might be for finance for large-scale reclamation projects and public utilities -- hydro-electric plants, transportation and communication facilities -- calling for state investment in co-operation with private enterprise. In between those extremes there might be a need for finance for industrial projects on a modest scale.

The first necessity in framing a financial programme for development was to determine what development the country needed and was capable of undertaking economically. It would then be necessary to see what institutional arrangements would facilitate the provision of capital for such undertakings. According to the direction which economic development was to take, agricultural banks, mortgage banks, development corporations, industrial banks, or other lending institutions might be required.

It was not enough to determine what financial institutions were needed; it was also necessary to see what measures should be taken to encourage savings and to mobilize them for the development projects, public and private, that could be economically undertaken.

In general, it might be assumed that if the public was assured of the value and security of its savings, the willingness to save would be greatly enhanced. For that reason, a policy of avoiding rapid inflation was essential. Beyond that, the provision of institutional facilities enabling savers to hold their savings in the form they preferred, would not only encourage a larger volume of saving, but would also channel those savings into institutions through which their availability for appropriate investment could be assured.

/It was clear

It was clear that for most people the most convenient means of holding small savings was in the form of money, or immediate claims for money. The development of popular savings banks, whose liabilities were guaranteed by the State, might be a great help in replacing hoards by institutional savings. For larger sums, the public might be accustomed to mortgages, mortgage bonds or mortgage certificates. It should be possible to parallel those forms of savings assets through the use of securities of mortgage banks, industrial banks, development institutions and industrial corporations. Obviously, if confidence could be established in State securities, it would be of enormous help in encouraging and mobilizing savings. It was quite possible, too to develop in time a public preference for participation in enterprises through ownership of share capital.

If savings were to be channeled for purposes of the greatest social value, the public must be re-educated to hold savings assets that were associated with the desired types of investment. That, however, was not enough; a re-education along such lines was a slow process. An attempt must be made to give the public savings assets somewhat similar to the type of savings assets for which they now showed a preference. For example, mortgage bonds might be issued on state enterprises; industrial banks could issue certificates secured by mortgages on industrial properties.

In some countries it might be possible to make use of the same institutions for both saving and lending, or those functions might have to be specialized. If the latter were the case, it would be necessary to find means of co-ordinating them.

It was a mistaken idea that saving and lending by themselves were enough. The financial aspects of the problem must be kept in line with economic realities. The monetary authorities must bear in mind the problem of too-rapid investment, and the possible consequences if the international sector of a country's economy were too rapidly sacrificed to the domestic sector. The economic development of a country was a problem of production, engineering and management, and the financial resources were not, by themselves, of great value if technical knowledge was lacking. The financial side of the problem should not therefore be over-estimated. The training of skilled workers and the development of scientists, engineers and business managers was equally important.

/He suggested

He suggested that the United Nations should deal with the problem on a country by country basis, and consider the financial problem in conjunction with other problems of development. It was no use trying to duplicate in an underdeveloped country the complicated financial mechanism of a more highly developed country; each country needed its own financial institutions.

Mr. Bernstein said the International Monetary Fund would always be glad to co-operate with the International Bank and with the United Nations on the financial aspects of development problems.

Mr. LIEU agreed with Mr. Bernstein that it was important for the United Nations to study financial institutions country by country in conjunction with the economic development of those countries.

In his own country one great difficulty was the lack of financial institutions -- there was no way of channeling savings to specific investments. People still tended to invest in land or urban property, but not in local industry and it was necessary to educate them. Since each country had its own habits it was difficult for the Sub-Commission to reach conclusions. He felt, however, that the underdeveloped countries had certain general characteristics in common. For example, in both Chile and China most of the business conducted by the banks was commercial.

Mr. COLLADO had been particularly impressed by Mr. Bernstein's remarks on the necessity of business management. He would be interested to know what progress was being made in the Fund's examinations of countries' financial institutions.

Mr. BERNSTEIN said the Fund had given very reasonable advice to some members, for example Ecuador, but it had not yet attempted to advise countries on the specifics of developing their financial institutions and fiscal systems so as to enable them to mobilize more capital. The Bank and the Fund must collaborate on that problem, which lay within their joint field of action; the Fund more on the monetary side and the Bank on the financial.

Mr. BRAVO JIMENEZ was in favour of considering the financial problem in terms of the structure of the economy and its development, rather than as an isolated problem. It was clear that in underdeveloped countries most of the financial resources were engaged in commercial activities, with a certain amount in light industry. In other words domestic financial resources were avilable only for activities in which a certain volume of profits was assured, and a problem was raised by those activities which did not assure a sufficient profit margin for investors, as was frequently the case in agriculture or industries requiring large fixed investment. The underdeveloped countries must study their own problems and find their own solutions.

Managerial skill should not be considered as an isolated factor -- it must be produced by the working out of the country's economic programme. A problem arose in adapting the economic and technical character of the business enterprises of more industrialized areas so as to fit in with the economy of the underdeveloped countries. In his own country, experience had shown that subsidiary branches of companies from other economically developed countries had had to operate for a time at very low capacity and on a non-economical basis while adjusting their techniques to the new environment. Each underdeveloped country must develop its own skills and technique as a co-product of economic development.

Another aspect of the problem was that the economic structure of underdeveloped countries was such that means must be devised to channel savings to the best uses. In many cases the carrying out of economic development programmes had been conducive to the concentration of a large volume of savings and it had not, therefore, been possible for large groups of the population to participate in the capital market. In particular, since the war, there had been a high concentration of capital in underdeveloped countries and little possibility of investment by the population more generally. That was an important point, for he himself felt that in many cases economic development did not raise the standard of living in a country, but merely created a monopoly of capital in its own interests. He requested Mr. Bernstein's opinion on that.

/Mr. BERNSTEIN

Mr. BERNSTEIN said that during the war the real income of Latin American countries had increased. That increase had been to some extent shared by the whole community but inevitably profits had been high and savings more concentrated than before the war. In a poor community the level of real income was likely to be so low that even small savings could not be expected. The most important thing was to raise the real income so as to provide a margin for saving. He pointed out that in a highly developed country like Belgium there were more savings accounts than people. That was due the fact that people could spare money and that it was an established tradition for everyone to have a savings account. In the Latin American countries, in the first place, the level of income of most people left nothing to spare for saving. Secondly, when the income level was raised and people were in a position to save they might choose between higher consumption and savings. At that stage, the problem of encouraging saving by the population generally arose. Then popular savings banks like those in Belgium and the Netherlands might be developed in Latin America. To develop such a system the people must be accustomed to thrift, and there must be the assurance that the investor could always get his money back. As to the disproportionate share of the rich, the distribution of savings would always be more unequal than the distribution of income. Finally, corrective measures might be introduced by fiscal policy designed to redistribute income on a more equitable basis, through taxation and by avoiding inflation.

He summed up the necessary steps as:

1) raising the real income of the whole people
2) shifting some of the taxation burden from the poor to the rich
3) encouraging the desire to accumulate savings among the poor.

Mr. PATEK said that Mr. Bernstein in his analysis of the problems of mobilizing domestic resources to finance industry in underdeveloped countries had tackled the problem only from the point of view of the capitalist economy. It might also be viewed from another angle, that of the socialist economy. He would like Mr. Bernstein's views on Government financing, which he himself thought might be better than forced saving.

/Mr. BERNSTEIN

Mr. BERNSTEIN said that among underdeveloped countries few had found it easy to develop a budgetary surplus. An almost unique case was provided by pre-war Egypt, which had built up its public revenue by a form of taxation (import and export taxes) which was easy to collect although not perhaps the best from the point of view of social justice.

The classical objective of saving in a socialist economy was to distribute to the public an amount enabling it to buy consumer goods while leaving the ownership and production of goods to the State. The national income was equal to the cost of production of both consumer and producer goods, and the value of consumer goods multiplied by their volume was the income of the people. The total volume of production less the community's income in consumer goods gave the amount of savings. That was a form of saving in which the amount was predetermined by the Government. That system might or might not give the best apportionment of the community's resources between consumption and savings. He had not emphasized it because for the majority of underdeveloped countries the problem was to induce the individual to save. He recognized, however, that State action was one way of securing more savings.

Mr. GUIMÁRAES said the problem of underdeveloped countries was chiefly a problem of the best allocation of the factors of production -- how economic resources could be diverted from one sector of the economy to another without disturbing the whole economy. He recalled the importance of foreign investments for mobilizing the factors of production or for increasing labour productivity. In underdeveloped countries the chief obstacle was lack of transport and energy, in other words public utilities, which required a large initial capital for which the country must rely on foreign investments. Domestic savings wereinadequate in an underdeveloped country because income and wages were low. That illustrated the importance of foreign capital.

The CHAIRMAN thanked Mr. Bernstein on behalf of the Sub-Commission for the very valuable and interesting statement he had made. He said that the problem of the mobilization of financial resources for economic development could be divided into three parts: to increase the total amount of savings available in any given community, to mobilize those savings and to canalize and use them in the most effective manner for the economic development of the country in question.

/The first question,

The first question, namely, how to increase the total supply of savings, constituted a very serious problem in underdeveloped countries. In India, for instance, it had given rise to much discussion. The Government's borrowing programme had failed to achieve the results expected and the latest theory to be advanced was that excessive taxation had reduced the margin of savings available.

Some underdeveloped countries, such as India, were in an extremely difficult position. The rich classes constituted the main source of money available for investments; by increasing the income and hence the savings of those classes it would be possible to secure larger amounts for purposes of investment. That might be regarded as an extreme capitalistic approach. Politically speaking, however, such a course would be impossible as the people of the country, though backward economically, were quite advanced in the political field and would naturally be against the consolidation and strengthening of the rich classes for the purpose of financing the country's economic development. Indeed, the people were not at all convinced that the capitalist system was the only possible economic system and were bent on reducing the existing inequality in the distribution of wealth and income. On the other hand, the masses were so poor that an equitable distribution of wealth and income would not leave any margin for savings.

Whatever their ideology, it was obvious that the underdeveloped countries would in the end be faced with the following alternatives: either to rely more and more on compulsory savings, that is, savings at the source, as was the practice in socialist planned economies; or else to adopt a political organization which would entail the rigid suppression of all liberal and equalitarian social and political ideas and would lead to the artificial creation of a wealthy class to finance the economic development of the country.

The second question, that of the mobilization of available savings, was of a more technical nature. The problem was to determine, first, the form in which savings should be held, in other words the form in which they would be most conducive to economic development, and, secondly, the methods by which to stimulate the preference of the savers toward such forms. In that connexion, he wondered whether differential rates of interest could play an effective part in shaping savers' preferences to conform with the requirements of economic development.

/The third

The third question was how to channel savings, once they were held in appropriate forms, so as to achieve the best results possible in the economic development of the country. He wondered whether economic development investments should be made with a view to increasing the volume of resources, and hence savings, which would be subsequently available for further economic development. The question could probably be answered only in relation to the particular country concerned, but he wondered whether something could not be said in general terms that would apply to all underdeveloped countries.

Mr. BERNSTEIN said that in the last resort economic development had to be paid for one way or another. It was not possible to escape that unpleasant fact. He could not agree with the view that a person of great wealth had done his duty to his country if he had saved some 20 or 40 per cent of his income, nor could he agree to increasing the income of the rich so as to surfeit their consumption requirements and thus increase the amount of savings available for the economic development of the country. Maldistribution of income and inequality of wealth were very great, indeed, in underdeveloped countries and their consequences much worse than in more developed areas. That was primarily a social problem, much broader in its aspects than the question of economic development. He did not approve of the tax-revision approach to this problem, and if, in any case, it appeared the only one available, would rather support increased taxes on the rich and recourse to State savings.

The small amount of savings available in poor countries was a very serious if not at times altogether insuperable obstacle to their economic development. Although the International Monetary Fund had limited itself to considering the field of domestic financial resources, it had always recognized the existence of external sources of finance. One point, however, needed particular stress: underdeveloped countries should re-shape their development plans and bring them down to an adequate level. Even in a socialist State, much could be said in favour of limiting the rate of development so as to derive more benefit from the development which was being achieved.

/The Chairman

The Chairman had asked whether differential rates of interest could not be used to induce savers to hold the kind of securities that were most effective for promoting economic development. That was precisely the method used at present, and he had proposed a modification. Its results, however, were not altogether satisfactory since it was necessary at times to pay as much as 20 per cent interest to obtain capital for a small industrial enterprise, whereas as little as one per cent might be enough return to induce the use of capital for the purchase of land, for instance. Every country had its own preferences and prejudices regarding savings. It was necessary to educate the public so that it should prefer the right kind of savings from the social point of view and, secondly, to modify the savings instruments so as to make them resemble what the public preferred. In simple terms, when a child liked chocolate but refused to drink milk, it was always possible to camouflage that milk with some chocolate. If the population of any particular country was partial to mortgages, the government could always raise money by issuing mortgage bonds in respect of a hydro-electric plant, for instance.

Regarding the third point raised by the Chairman, he thought that the best way of using savings was to invest them in enterprises which would bring in the best returns for all. Agricultural improvements might, for instance, offer the largest and best return for all the population. Furthermore, even when the interest rate was low there was need for being just as economical in the use of capital as if it were high. For a country which had many important things to do in the field of economic development, a bridge which could stand for twenty years would be just as adequate as one which would remain for fifty years at, say, twice the initial cost.

The CHAIRMAN said his question as to use of differential rates of interest had been directed to achieving differentials on a planned basis, for redirection of savings, rather than savers' preferences which now expressed themselves in differential rates. Appropriate education of the public was one way of attaining that aim.

Mr. BERNSTEIN referred members of the Sub-Commission to one of the Fund's publications -- The Concept of Latent Inflation in Private Wealth -- which touched on that problem. He emphasized that the

/taxation

taxation systems of most underdeveloped countries differentiated between various sources of income, such as income from services and income from wealth, but various income tax devices increased still further the existing disparity of income. To a certain extent the same tendency could be noticed in more developed countries. There was need to eliminate that further distortion of the disparity of income, then to correct the disparity and then perhaps even to reverse the process so that income tax should lessen rather than increase the inequality existing in the distribution of income.

Mr. MOROZOV said he could not agree with the description Mr. Bernstein had given of savings processes in a socialist economy. The representative of the International Monetary Fund had disregarded the main factor, namely that in a socialist economy means of production were owned by the people and were used in the interest of the people to raise the economy of the country. In a capitalist system, income -- often earned by lowering the real wages of the working masses -- was not used for raising the national economy of the country but was diverted to channels from which larger profits were expected.

Mr. BERNSTEIN wondered whether the difference was as great as it appeared at first. In a socialist economy, the State or the people decided on the amount of savings. The public consumed less than the total output and the surplus was left in the hands of the government, which decided on the kind of investments for which it should be used. It was a method of saving which was suited to that particular type of ecomomy. The real problem, however, was one of determining the adequate volume of savings and the right type of investments.

In a capitalist country, the process was roughly the same since once again it was for the public to decide the use to which it wished to put its income and thus to determine the volume of savings. The choice of investments was left to the business man, and though that choice was not always the best

/from a

from a social point of view, in attempting to obtain a large profit the business man had to try to achieve a greater output for the community. Consequently, such investments were not necessarily anti-social in character nor was their contribution to the social welfare of the country necessarily smaller than that of socialist investments.

Mr. MOROZOV emphasized that he had had no intention of speaking on the subject, but that he could not allow a distorted description of the socialist economic system to remain unchallenged.

The CHAIRMAN thought capitalist growth had occurred in an historical pattern in a period in which there had been no large ideological differences. Then capital accumulation had developed quickly. He wondered whether an underdeveloped country with large masses of poor people and under the influence of the most advanced social ideas could undertake capital formation from its own resources in any other way than the socialist method.

Mr. BERNSTEIN said that whatever capital formation was being achieved now in such countries was not achieved to a significant extent by socialist methods. He emphasized that some forms of investments had such wide social implications that the State should ensure that they were made.

The CHAIRMAN said that certain countries had shown a preference for holding savings in an unproductive form, such as gold in India. One of the methods by which underdeveloped countries could increase the amount of resources available for economic development would be to convert such unproductive forms into others, more conducive to economic development.

Mr. BERNSTEIN added that, especially in a country faced with balance of payments difficulties, private holdings of foreign exchange were also one of such unproductive forms. The problem was not to recapture the old savings invested in unproductive forms but to discourage any new savings being wasted that way.

/The CHAIRMAN

The CHAIRMAN emphasized that even underdeveloped economies wasted a substantial proportion of their savings in investments which were not conducive to economic development and would not increase the total supply of future savings, and mentioned armaments as being by far the most important among such investments. The atmosphere of international insecurity, for which the great Powers bore the responsibility, was a very grave obstacle indeed to the economic development of small countries.

Mr. PATEK pointed out that the result of the existence of the private holdings of foreign exchange mentioned by the representative of the International Monetary Fund was that underdeveloped countries were in fact financing the further development of highly developed countries. He said he would welcome information on the size of private foreign assets owned by underdeveloped countries.

Mr. BERNSTEIN said that the United States Treasury had published a survey of all types of foreign-owned property in the United States in 1941. United States banks were supplying regular information concerning deposits held by foreigners in the country; that information was published in the Federal Reserve Bulletin. The International Monetary Fund did not publish the information which it received on that subject from all countries. The Sub-Commission, however, could easily obtain a copy of the above-mentioned publications.

Mr. PATEK maintained that those publications would only partially answer the question since other countries, such as Switzerland, would not be included. He therefore suggested that the Secretariat might undertake a survey of all foreign assets owned by under-developed countries.

The meeting rose at 1.10 p.m.