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A.I.D. DISCUSSION PAPER NO. 9

**PROMOTING EFFECTIVE
DEVELOPMENT POLICIES:
A.I.D. EXPERIENCE IN
THE DEVELOPING COUNTRIES**

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A.I.D. EXPERIENCE IN THE DEVELOPING COUNTRIES

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These papers are designed to stimulate and serve as background for discussion. They represent the views of the authors and are not intended as statements of Agency policy.

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PROMOTING EFFECTIVE DEVELOPMENT POLICIES: A.I.D. EXPERIENCE IN THE DEVELOPING COUNTRIES

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PROMOTING EFFECTIVE DEVELOPMENT POLICIES:
A.I.D. EXPERIENCE IN THE DEVELOPING COUNTRIES

Both experience and analysis confirm that success by LDC's in achieving economic progress is heavily dependent upon their pursuit of appropriate policies and programs. Foreign assistance is very important, but its cost will be greater and its results less if the recipient country does not do its best. Since aid is limited, it should be concentrated where it will be most effective.

LDC's vary widely in their ability to mobilize and make good use of resources for development. Many are already making strenuous efforts to help themselves; five-sixths of investment taking place in the developing countries is self-financed. In every case, however, there are important measures which could improve the results achieved. This paper summarizes recent U.S. experience in attempts to encourage adoption of such measures.

U.S. efforts to link aid to improved performance are not new. From the beginning of the post-World War II aid program there were cases in which assistance was related to broad policy changes on the part of the recipient. In some instances project loans have been conditioned on specific measures of construction or operating policy having significant economic implications. Much of our technical assistance activities have been directed to increasing the ability of host countries to formulate and execute needed self-help policies and measures: for example, planning assistance, establishment or reorganization of budget bureaus, or tax reform and tax administration. However, since 1961 the U.S. has emphasized the importance of self-help efforts and has tried to relate aid to performance somewhat more systematically and consistently than before, at least in the larger assistance programs directed essentially to economic development. These efforts have been far from uniformly successful, but U.S. experience does suggest that there is considerable scope for donors to influence recipients' broad development policies.

I. Identifying needed self-help measures

Before discussing the U.S. experience in relating aid to self-help, it may be useful to indicate by a few illustrations what the U.S. means by the term, and to summarize some of the major problems of evaluating performance and self-help efforts which we have recently encountered.

Self-help measures range from steps to improve the effectiveness of specific activities to much broader efforts to undertake basic reforms in, for example, tax structure; to alter investment priorities as between sectors; to modify an entire import control system or to give substantially greater encouragement and freedom to private initiative. This paper emphasizes broader policy improvements and the ways in which donors can support and encourage such improvements. However, the success of any development effort depends not only on appropriate general policies, but also on innumerable more limited improvements in organization, management

and policies in important sectors and subsectors. These improvements can be encouraged and supported by different aid techniques, including many kinds of technical assistance as well as explicit understandings in connection with loans for capital projects.

A. Recipient Country Policies for Stabilization and Growth

Where there is severe inflation accompanied by serious pressure from a deteriorating foreign exchange position, measures to promote financial stabilization become crucial. There is wide agreement on the general principles guiding the restraints on credit and government deficits, the exchange rate adjustments, and the tax and tariff measures needed to restore a measure of balance. The IMF often takes the lead in assisting a country to work out a feasible program of stabilization, and the U.S. has frequently made part of its assistance contingent on the recipient's fulfilling its agreement with the IMF.

In an early and successful case, U.S. aid supported the Greek stabilization program formulated and carried out in the mid-fifties. The current Korean stabilization program and exchange reform is the latest in a series. Stabilization was an important element in the Bell-Dantas agreement with Brazil in 1963, and in recent understandings with Chile and Colombia. The objectives of such programs can be more directly stated than is the case for development programs, and short-term quantification of goals is often possible. Usually all parties can agree on specific measures which are cogent, and data are generally quickly available for measuring short-term performance on the main criteria selected. However, the measures are far from infallible in producing desired results. The program prescribed to control inflation in Chile appears to have underestimated the strength of accumulated inflationary pressure. In other cases, inflation has been replaced by stagnant recession.

Therefore, in many cases measures to promote both stabilization and development must be undertaken at the same time. However, as emphasis shifts from stabilization measures to policies and programs to promote development, there is much less certainty regarding the key steps to be taken.

A few general objectives can be stated fairly clearly. A country should:

- a. Increase its ability, in terms of institutions and skilled manpower, to plan and carry out development programs
- b. Increase the scale of its development programs;
- c. Increase the output of goods and services resulting from its development expenditures;

- d. Increase its own financing of development; and
- e. Increase exports and economize on imports.

The relative importance of these goals varies from country to country and from time to time. The specific measures needed to achieve them are almost infinitely varied. The appropriate measures can be identified for a particular country only on the basis of intensive study of its particular circumstances. In the countries where the U.S. has major economic aid programs, AID conducts continuing analysis, both in its field missions and in Washington, to identify the most important self-help measures and determine how the U.S. can encourage them. One of the working groups of the Development Assistance Committee of the OECD is working toward agreement among donor nations regarding the techniques which can be used to identify key self-help needs, so that donors can reach a consensus on priority measures for any specific country.

B. Evaluating Performance and Self-Help Efforts

Evaluation of self-help efforts already under way and comparison of different countries' efforts and performance is a continuing concern.

Quantitative indicators of economic performance, while useful, have some obvious shortcomings. Certain data, such as marginal savings rates, are notoriously unreliable, and the range of error may be wider than the changes in the data for the same country over a period of a few years or than the differences in the same series for two countries. Exogenous factors like the weather or world prices for key exports sharply affect short-term figures. Even if there were no statistical inadequacies, the complexity of cause-effect relationships makes it difficult to evaluate comparative performance: an index of good performance in one country may not be particularly significant for another. Moreover, quantitative indices of economic performance reflect improved country policies and programs only after a lag of months or years. If aid is to be used directly to induce and support current self-help efforts, and not solely to reward such efforts after they have been implemented and reflected in improved performance, then quantitative indicators of performance must be combined with an intimate knowledge of current host country policies and programs and their probable future effects.

If a country has already been performing well in most fields, and unless there is some special reason to expect deterioration, there is reason to assume that it will continue to do well. If a country has not been doing well, but has made a number of encouraging policy statements and is trying to pass needed legislation and broaden development efforts, donors must try to judge whether the country will be able to translate good intentions into effective action.

II. Encouraging More vigorous Self-Help Efforts

In relating aid to self-help performance, donors may assess the performance to date of various recipients and concentrate assistance on those LDC's which have demonstrated by good performance their ability to use aid effectively. This approach, pursued consistently, may not only encourage and support the efforts of countries which perform best, but may also have a helpful demonstration effect on other LDC's. This approach is ex post, in the sense that donors adjust the level and content of their aid to past performance.

Donors may go beyond the ex post approach and seek actively to influence the current and future development policies of recipients, through discussion and persuasion and possibly through offering additional aid to share the costs and risks of introducing additional important self-help measures. In practice, donors use some combination of the ex post and ex ante approaches. The following discussion examines these approaches in turn.

A. The Ex Post Response to Good Performance: Concentration and Selectivity

The 1961 report of the President's Task Force on Foreign Assistance emphasized the need to reward good performance by generous aid allocation. The report referred to persuasion as the primary technique for influencing aid recipients to undertake specific reform measures. The report stressed the idea that there would be countries whose performance we could broadly endorse, and that by concentrating aid on the countries which performed best and giving them the assurance of long-term commitments, we could exert strong influence on other countries. India was cited as a country where self-help efforts merited substantial assistance in support of long-range plans.

The U.S. has found that two major problems limit the application of this approach.

1. Conflicting Foreign Policy Interests

The United States, like most donors with large and diversified aid programs, seeks to promote a variety of foreign policy interests through these programs. In countries where the U.S. is strongly concerned for security or other interests, these may complicate application of the principle that aid should be allocated in accordance with self-help performance.

In some twenty-five countries, the U.S. conducts major economic assistance programs designed to support and stimulate development. Within this group, self-help efforts and performance become major factors in determining not only the amount but also the form and content of U.S. aid. For example, loans to finance imports of raw materials, spare parts and fertilizer are extended most readily to those countries whose

planning and performance warrants confidence that the commodities will be used to support high priority development objectives. Even within this group, however, other U.S. policy interests also influence the allocation of assistance.

In half a dozen additional countries, the United States conducts major assistance programs primarily designed to restore and maintain security and stability. In these countries the United States does press for economic self-help measures, but other considerations dominate U.S. decisions on the amount of aid.

In still other countries U.S. aid is quite limited and the U.S. is unlikely to be able to exert influence on the country's general development policies, except to the extent that it acts in concert with other donors.

2. The Need for Support Concurrent with Self-Help Measures

Some of the most important self-help measures needed in many LDC's require external support at the time the measure is undertaken as a precondition for its success. For example, U.S. willingness to make a larger part of its total aid available in the form of commodity assistance, helping to meet a possible surge in foreign exchange requirements, was of significant help to Pakistan when it decided in July 1964 to remove import controls and adjust fiscal measures on major industrial commodities and raw materials in order to permit fuller utilization of existing industrial capacity. Substantial non-inflationary increases in investment also may depend on increased external aid, at least in the short run. In such cases the ex post approach is inadequate.

B. Ex Ante Efforts to Improve Performance: Discussion and Persuasion

1. U.S. Experience

In practice, the U.S. has always made efforts to improve current policies which aid recipients are applying to development problems. The more successful instances in which the United States has played a role in improving recipients' policies were based on long and thorough discussion between U.S. and host country officials, often conducted over a period of years, concerning what measures were desirable, necessary, and feasible. These discussions were based on the best analysis which the U.S. or international agencies were able to make or obtain. The process of arriving at agreement with the host government is greatly facilitated if field staffs are maintained, with full time responsibility for economic analysis of the host country. These staffs are usually able to establish close professional contacts with financial and economic leaders of the country, public and private. In addition, U.S. non-project loan agreements in Chile, Colombia and Brazil provide for a periodic formal review of the economic situation with officials of the host country. In Chile, for example, quarterly reviews of overall Chilean performance provide a special channel for a regular flow of information and exchange of views on a broad range of policies and programs.

In Latin America, the Charter of Punta del Este sets forth agreed objectives to which each signatory country is committed. The Inter-American Committee for the Alliance for Progress (CIAP), with the assistance of the Panel of Nine (top-level experts in economic development), annually reviews each country's progress toward the goals stated in the Charter, its plans and programs, and the external requirements and internal efforts called for in the next year. The Panel of Nine also reviews intensively each country's national plan as it is prepared. Within this framework of multilaterally determined goals and international review of plans and progress, the United States can discuss programs and performance with the Latin American countries in an atmosphere of mutual endeavour.

2. Problems of Influencing through Persuasion

The goals of self-help described on page 2 above are clearly in the interests of the developing countries. They are goals shared by donors and recipients, and are not alien objectives imposed from without. Nevertheless, a number of problems may make it difficult to reach agreement on the priority which should be given to proposed self-help measures.

a. Resentment of external interference

Host country officials sometimes resent what they view as outside criticism of, and interference with, their internal affairs, and this sensitivity makes it difficult to agree on needed measures. However, in most of the countries to which the U.S. gives major economic development support, it has been possible to convince the government of the host country that the U.S. shares with it a concern for the country's long-run development. Therefore, although there may be disagreement on particular points, there is a basis for continuing analysis and discussion.

b. Differences in judgment or short-run conflicts in donor and recipient interests

There can be, and the U.S. often encounters, strong differences of opinion with the government of the developing country regarding the priority to be attached to a particular measure, or more fundamentally, the nature of the measures required to achieve agreed objectives. In particular, although no developing country wants to remain forever dependent on aid, some assign a lower priority to eliminating concessional aid and plan to wait longer for increased foreign exchange earnings than we find advisable. A continuing full exchange of views has often helped to narrow or resolve differences of this kind.

c. Divisions within the recipient government

Often there are differences of opinion within a host government regarding the best development policies, so that it is difficult to reach agreement with donor countries on the best course of action. However, in such cases discussion with U.S. and other bilateral or multilateral staff familiar with the country's situation has sometimes helped to resolve the issue and has lent support to elements within the government to carry out the necessary measures.

C. Ex Ante Efforts to Improve Performance: Incentive Programming

In the past two or three years the U.S. has attempted in a number of cases to add to its usual practice of discussion and persuasion the use of incentive programming and conditions as means of inducing and supporting needed measures. In more and more cases the U.S. considers that specific positive, explicit understandings regarding recipient performance are desirable. This trend results from concern over the slow pace of growth relative to what might be possible, stronger convictions about what is needed to make more effective use of aid in particular countries, and, perhaps, the importance of being able to make clear these concerns to the U.S. Congress and people so that there will be broader understanding of the goals and role of the aid program.

1. U.S. Experience

An early example of an effort to relate specific improvements in economic performance to significant aid commitments was the "Nineteen Points" agreed upon with the Republic of China on Taiwan in 1960 in the context of a five-year program of accelerated development. The Government of the Republic of China worked out and approved a nineteen point Economic Reform Program designed to control the level of military expenditures, develop non-inflationary fiscal and credit policies, implement tax reforms to remove tax deterrents to business, establish a uniform and realistic exchange rate, liberalize foreign exchange control and carry out a number of other measures. Some of these steps were to be completed in one year, others over a period of two, three or more years.

On the basis of these undertakings by the Chinese Government, the U.S. was willing to provide three types of aid: (i) a hard core of minimum essential grant economic aid to prevent living standards from falling due to maintenance of large military forces; (ii) supplemental grant economic aid for raw materials, spare parts and machinery, the amounts and timing to be adjusted according to performance; and (iii) Development Loan Fund loans for specific projects, in amounts depending largely on ability to prepare projects. It was also understood that one objective of the five-year program was termination of U.S. concessional economic assistance at the end of the period.

Implementation of the "Nineteen Points" in Taiwan lagged behind the timetable established in the program, but by the end of the five-year period most of the points had been largely carried out and the basic purposes of the accelerated economic development program, including termination of concessional U.S. economic aid, had been achieved.

The Bell-Dantas agreement in Brazil of March 1963 is a second example of linking substantial assistance to recipient performance. Under this agreement the Brazilian Government agreed to undertake far-reaching financial and fiscal reforms and other steps to check inflation and lay the basis for a sound development program. AID undertook, in turn, to support the program with substantial aid.

The Government of Brazil which was then in office did not fulfill its commitments in the agreement, and the U.S. consequently did not provide the assistance that had been made contingent on improved performance. The agreement may, however, have served a useful purpose in laying the groundwork for more successful efforts in Brazil a year or two later and in other countries by lending credibility to our position.

In Pakistan in the early 1960's lack of imported industrial commodities and raw materials obliged many plants to operate at a fraction of capacity. After a partial liberalization of import controls early in 1964, the U.S. indicated that if Pakistan acted to remove most controls and took steps to assure that real prices were more accurately reflected in costs to importers and users, we would be prepared to increase considerably the proportion of total U.S. aid provided in the form of commodities. This support enabled the Government of Pakistan to remove controls on imports of 51 major industrial commodities and raw materials. At the same time it imposed additional taxes increasing domestic prices so as to restrain a possible surge of demand. It is too early to judge the final economic effect of these actions, since expanded imports began to flow into Pakistan only in the last quarter of 1964. However, all indications are that utilization of industrial capacity has increased significantly.

Fuller descriptions of these cases, and of agreements reached with Chile and the current Government of Brazil will be found in the annex to this paper.

AID started its present effort to link aid more actively and explicitly to improved performance in the Latin American region. The programs there were newer; it is probably easier to introduce new practices in such cases before patterns of behaviour become fixed. The Charter of Punta del Este and the machinery of the "wiseman" to some extent precommitted Latin American governments to the principle of reform and provided a multilateral context for U.S. efforts to encourage improved performance. In many of the older Far Eastern and

Asian programs a major effort in the early AID period was to switch from Supporting Assistance to Development Loans; to do so with minimum political and economic disruption made introduction of additional strains undesirable. Also, in countries like Korea and, to a lesser extent, in Turkey, dominant security interests had to be taken into account in gauging the priority and forcefulness that should be expressed in the debate over development policy issues.

However, recently we have sought explicit commitments with increasing frequency in all geographic regions. We now have or are actively seeking more or less formal understandings related to our aid commitments covering important aspects of country policy in about ten countries including those receiving the most major U.S. development aid.

Thus far in U.S. experience loans for the import of commodities have proved to be the form of aid which lends itself most readily to incentive programming. This is partly due to the urgent need for such imports in most LDCs which are conducting vigorous development programs: loans for commodities provide a clear-cut incentive. Moreover, in many cases, aid in the form of commodities is appropriate to meet the needs which the self-help measure is likely to create. This is particularly true of liberalization measures and encouragement of the private sector. Finally, these loans can be easily increased or reduced in amount and adjusted in timing. This is important since incentive programming normally involves only a margin and not the entirety of a country program. The donor usually has political and other commitments which rule out the possibility of suspending aid if the receiving country falls short of agreed targets. Moreover, an all-or-nothing proposition is unlikely to create the atmosphere of cooperation and confidence in which incentive programming is most likely to be effective.

However, there is no reason why general conditions of economic performance could not be attached to project assistance. The Peru Mission recently proposed linking a number of broad development policy measures to U.S. undertakings to finance sound development projects up to a specified amount. When project aid includes local cost financing, the aid has the effect of program assistance and could be managed in a similar way.

Not infrequently the U.S. has required a borrower to take more specific measures in connection with project loans, and these measures may have significant economic impact. For example, in Korea certain power projects were financed on condition that power rates be substantially increased.

2. Problems of Incentive Programming

The attempt to go beyond discussion and persuasion and to use incentives and explicit self-help understandings to induce more vigorous self-help efforts poses certain problems in addition to the problems of reaching agreement.

a. Recipient capabilities and the credibility of aid incentives or conditions

One limitation we have found to the use of explicit self-help understandings is that those countries with the more chaotic economies and the greater need for reform are often also politically or administratively weak and incapable of carrying out such understandings. In these countries sincere host government determination plus supporting foreign assistance may not be sufficient to assure reform. In some countries, weak governments have avoided politically difficult self-help efforts in the belief that the U.S. would not be willing to enforce performance criteria at the risk of seeing the government collapse.

b. Conflicting U.S. foreign policy concerns

Where the U.S. has strong security or other foreign policy interests in a country in addition to interest in its economic development, or where U.S. relations with a country are strained regarding topics other than the country's development policies, the U.S. may be reluctant to risk additional strain resulting from an active effort to encourage improvements in development policy. In such circumstances the U.S. would normally continue to discuss development policies with the country's officials, but might hesitate to try to link part of the aid program to explicit self-help efforts. However, such strains can be reduced by careful preparation, including thorough discussion with the host government; by cooperating with the IBRD, IMF, CIAP, and/or other donors in encouraging needed measures; and by pointing out that there are other countries where we are also linking aid to performance. There is also growing recognition that the U.S. long-term interest in improved performance is greater than had been realized previously.

c. Political acceptability in the recipient country

It is often argued that recipient governments cannot afford politically to make policy concessions publicly linked to aid agreements. In some cases, however, a public agreement may help to clarify understanding of the issues and present the case for needed measures to elements within the government and to the general public. A public agreement which makes clear the conditions under which aid will be extended also protects the donor against recriminations if the recipient government does not fulfill the agreed conditions and the donor therefore provides less aid. This was the case in the Bell-Dantas agreement. A public agreement also minimizes the danger of misunderstanding when key officials are changed. It helps us in dealing with third countries and in explaining our actions to Congress and the Public.

However, despite these advantages it may not always be possible or desirable to record publicly an agreement regarding performance. If a formal public agreement seems politically unwise, the recipient can announce its actions and intentions unilaterally and the donor can take its own action on the basis of such announcement. As a middle ground the donor can indicate publicly that its action is being taken in order to support the measures which have been announced unilaterally by the recipient. IMF stabilization program arrangements normally take this form.

3. Conclusions Regarding Incentive Programming

A number of conclusions may be drawn from U.S. experience to date with incentive programming.

- a. Explicit understandings are not likely to be effective unless the recipient government fully understands and agrees with the stipulated measures.
- b. Explicit understandings may be effective in improving specific policies, but these improvements may not be adequate to bring about the desired economic results.
- c. It is probably more effective to concentrate influence on a few key self-help measures at a time, preferably ones which can be stated rather precisely and where action or inaction can be easily recognized, rather than to link assistance to a wide range of somewhat vague criteria.

- d. A major contribution of the recent explicit understandings regarding self-help has been the provision of a regular arrangement for review of progress and an agreed agenda for such reviews.

The Chile, Colombia and Brazil agreements provide for periodic review of progress in carrying out the various undertakings and release of our funds in stages. This should be useful in at least three ways. Such reviews facilitate flexibility, which may be desirable in relation to some of the more complex quantitative and non-quantitative undertakings which are likely to be important as stabilization and deflation problems are overcome and the need is for positive measures to accelerate development. They also permit early identification of difficulties before extensive damage is done or large amounts of money irretrievably released. They also set the stage for a continuing dialogue concerning key areas of government policy.

- e. Commodity loans have so far proved to be the form of aid which lends itself most readily to incentive programming. However, there is no reason why general conditions could not be attached to project assistance. More limited conditions having significant economic implications have been attached to U.S. project loans on a number of occasions.
- f. It is helpful to conduct negotiations for explicit self-help understandings parallel to, and where possible jointly with, negotiations between the receiving country and the IMF (where stabilization is involved), the IBRD, other multilateral lending institutions, and other bilateral donors. Therefore, some agreement among donors regarding the most important self-help measures and the scale of assistance requirements is important.
- g. For maximum influence on LDC policies, incentive programming must not only build on past and facilitate future discussion and persuasion, but must also be coupled with the ex post approach of allocating aid among countries roughly in accord with their achievements.

III. Promoting Self-Help Performance in Consortium and Consultative Group Countries

Where a developing country receives substantial aid from several donors, coordinated donor efforts to encourage and support particular self-help measures can be more effective than the efforts of any single

donor. Theoretically, consortia and consultative groups should be better than informal bilateral consultation in ensuring coordination. However, the IBRD Consortia for India and Pakistan, and the OECD Consortium for Turkey were established to reach some degree of agreement among donors on goals and requirements, in order to arrive at appropriate aid levels and to improve terms. Although the three major consortia have continued to focus primarily on levels, terms and types of aid, we have found growing agreement that recipient performance is of keen concern to all donors and that the donor groups ought to play a greater part in identifying, inducing and supporting priority self-help measures.

The World Bank staff has provided comments, criticisms, and recommendations in connection with economic reports by Bank missions and assessments of development plans in consortium and consultative group countries. While it is not possible to determine the exact extent of cause and effect, the governments of Turkey and Pakistan have acted on certain self-help measures considered important by the consortia. Turkey has taken steps to reform the State Economic Enterprises and to increase foreign exchange earnings. Pakistan has substantially liberalized imports. Recently, India's need for more rapid results from her development programs has been the subject of general concern. Although in the past there may not have been sufficiently extensive or systematic joint donor consideration of needed action by recipient countries and of donors' strategy for inducing such action, the IBRD and other institutions are gradually moving in this direction. Fuller coordination of assistance policies and programs depends on arrangements to make available to all donors thorough analysis of requirements for both internal effort and external support in each developing country where more than one donor conducts significant aid programs. Fuller coordination also calls for explicit joint donor consideration of ways to encourage the required internal effort and to provide the necessary external support.

The IMF has been effective in coordinating donor policies and promoting measures required for stabilization. IMF Standby Agreements have usually required that the developing country make efforts to obtain credit from other donors and that donors' credit be extended on condition that the recipient observe the requirements of the Standby. The IMF has usually discussed major policy issues with other prospective sources of credit, but has not called for formal group action. The IMF has taken full responsibility for technical analysis and specification of the recipient's stabilization actions on which the IMF Standby and other credits are predicated. This experience with encouraging stabilization measures may also be useful in promoting more effective development policies and programs.

Efforts to enlist the LDCs and organizations in which they themselves are represented to bring pressure on one another for improved performance have not been particularly productive to date, but are worth pursuing. If successful, such mechanisms would avoid the overtones of neo-colonialism which some LDCs tend to associate with pressure by groups of donors. The role of the OEEC during the Marshall Plan period is often cited as a successful example. The Inter-American Committee on the Alliance for Progress (CIAP) is already performing this function in Latin America and will probably grow in effectiveness as it gains experience and prestige.

A N N E X E S

CASE STUDIES OF U.S. EXPERIENCE IN ENCOURAGING IMPROVED PERFORMANCE

PAKISTAN: IMPORT LIBERALIZATION - 1964

Background:

Due to a scarcity of foreign exchange the Government of Pakistan had imposed increasingly strict controls over imports. The foreign exchange shortage distorted investment decisions and led to substantial idle capacity. It also required the retention of elaborate bureaucratic import controls which gave rise to corruption and black market operations, led to uneconomic inventories, and denied adequate supplies of raw materials to those who could use them most effectively.

Suggestions for a freer import regime had been made regularly by foreign advisors since 1957. In 1962 and 1963, with reserves rising, discussions between the AID staff in Pakistan and Pakistani officials focused attention anew on this problem and led to a mutual understanding that trade liberalization, accompanied by price adjustments, would be an important step to better utilize Pakistan's resources. AID offered to support an import liberalization program by increasing the proportion of program loan assistance within the same total aid level. Shortly thereafter, a report prepared by the IBRD in preparation for the FY 1965 Consortium meeting, similarly indicated that the most substantial contribution that could be made to Pakistan's economic growth would be to provide non-project assistance to enable Pakistan to utilize better its existing productive capacity.

Content and Form of the Agreement:

The Government of Pakistan, with AID support, took the first step toward import liberalization in January 1964 by removing licensing controls from four major iron and steel commodities. This liberalization was not accompanied by any exchange rate adjustment and it soon became clear that liberalization of only four industrial raw materials was inadequate. Consequently, further discussions with the GOP were undertaken to explore the feasibility of, and U.S. support for, a broader import liberalization program. AID agreed with the Government that if extensive liberalization were to be undertaken, \$200 million of non-project assistance for 1964/1965 would be necessary and justified. Without liberalization the non-project requirements would be considerably less. AID assured the Government of Pakistan of up to \$140 million of non-project assistance for FY 1965 (compared to \$100 million of non-project assistance for FY 1964) ^{1/} to help meet the foreign exchange

^{1/} This was a shift in composition of U.S. aid rather than an increase in the total amount.

needs anticipated if the GOP undertook, starting July 1964, to liberalize the import of all raw materials (except those which could be directly related to the production of luxury consumer goods) and spare parts, and to increase prices by at least 10% on liberalized items. The price increases were intended to restrain a possible surge of demand on removal of restrictions, in view of the cheapness of imports relative to domestic prices. Since total estimated non-project assistance requirements were at least \$200 million, the U.S. also stressed the psychological importance of obtaining support from all members of the Consortium. The program would have little prospect for success unless the other Consortium members could be persuaded to contribute \$60 million of non-project assistance.

The form the negotiation with the GOP took was a series of discussions between the U.S. representatives, the Ministry of Finance, and the GOP Planning Office. The Finance Minister was given the U.S. assurance of support at the end of April and the Karachi representative of IBRD was informed of this offer at the same time. A letter from the Mission Director to the Minister of Finance, delivered in early June, confirmed the assurance to the Government of Pakistan of up to \$140 million of non-project assistance to support an expanded liberalization program, with appropriate price adjustments. The U.S. assurance of increased assistance was made while the budget and the import program were in preparation, and before the second meeting of the FY 1965 Consortium. The second meeting (the pledging session) of the Consortium was held after both the import policy and the budget had been publicly announced.

Results:

In July 1964, the Government of Pakistan announced a new import policy which liberalized imports of 51 major industrial commodities and imposed additional taxes totalling about 10%. At the Consortium meeting approximately \$60 million of non-project assistance was pledged by other Consortium members. The effect of the import liberalization program is as yet difficult to measure because imports only began to flow into Pakistan under the program in the last quarter of 1964. However, all indications are that utilization of the factories has increased significantly. In the steel rolling mills, in the first instance, the price of steel has dropped by 15 to 20%. Shortages of raw materials have been ameliorated and it is expected that the rapid industrial growth which Pakistan has experienced the last several years will be further accelerated. It should also be noted, however, that some adverse effect on Pakistan's foreign exchange reserves has taken place since in that period non-project aid did not fully cover the additional foreign exchange demands released by the import liberalization.

In summary, although precise statistical data on physical results is not yet available, the main initial objective of restoring the allocation function to the market mechanism and removing it from the bureaucratic controls has been achieved.

PAKISTAN: FERTILIZER DISTRIBUTION IN EAST PAKISTAN

Fertilizer is sold in Pakistan at a subsidy of 25% in West Pakistan and 50% in East Pakistan. There are three government-owned chemical fertilizer plants in West Pakistan producing 65,000 nutrient tons of fertilizer annually. During the Third Plan the GOP plans to triple the productive capacity, including a privately owned ESSO plant. In East Pakistan production is 52,000 nutrient tons annually, and a 350% increase is planned for the Third Plan.

Until mid-1963 fertilizer was distributed by a government agency in each province. This system did not permit adequate and timely distribution, and resulted in excessive overstocking, particularly in East Pakistan. Since increased use of fertilizer is one of the basic ingredients of accelerated agricultural growth and since AID had financed fertilizer imports, the Mission repeatedly urged the Government to improve the fertilizer distribution system. On July 30, 1963 the Mission wrote to the Governor of East Pakistan that, unless immediate steps were taken, there would be approximately five years supply of fertilizer available in 1964 at the then prevailing rate of sales. The Mission indicated that a refund claim of \$18 million might be made unless the available fertilizer was distributed more effectively.

During August 1963 the GOEP implemented existing plans for expanded distribution of fertilizer through the private sector. Sales of urea and TSP during FY 1965 increased rapidly and are expected to increase further in FY 1965. At the end of FY 1964 carryover stocks were reduced to 42,000 tons of urea and 21,000 tons of TSP.

As of September 1964 there were over 3,000 private fertilizer distributors authorized under a cooperative plan with the Agriculture Department and Agricultural Development Corporation wholesaling fertilizer to private sector retailers. At present five districts are nearly 100% in private sector hands. The overall transfer to the private sector is scheduled over a two-year period.

FERTILIZER USE IN EAST PAKISTAN
(nutrient tons)

1960/61	23,337
1961/62	22,868
1962/63	26,537
1963/64	48,726

PAKISTAN: INCREASING TAX YIELDS

Pakistan began its Second Five-Year Plan (1960-1965) with a poor record of mobilization of resources through taxation; the tax yield

being only about 6% of GNP. The Plan contemplated increased taxation, but by mid-plan it was clear that the limited steps which had been taken would produce only about half of the modest planned increase in tax yield.

The AID Mission postulated that taxes would have to be increased at least to the level projected in the Plan early in 1964, if the Development Plan were to be implemented effectively. Prior to the fourth year of the Plan, the U.S. urged action to increase taxes and supported these urgings by refusing to release U.S.-owned rupees, which would have allowed Pakistan to finance the fourth year of the Plan with no tax increase. As a result of these efforts and because of growing Pakistani recognition of the needs for greater self-effort, Pakistan raised taxes for the year in an amount greater than 1% of GNP, the largest tax increase in Pakistan's history. Further tax measures were enacted for the current year, so that Pakistan will end its Second Plan with tax yields somewhat over 9% of GNP.

The Third Plan, which begins July 1965, contemplates that over 50% of the public development program will be financed from domestic sources as compared with only 43% during the Second Plan. This, particularly considering that the program will be almost twice the size of that for the Second Plan, is a commendable plan of progressive self-help.

BRAZIL

A. Program Loan 1963 - (Bell - Dantas Agreement)

1. Background

The beginning of 1963 marked the installation of the presidential regime which had been restored in Brazil by the October 1962 election. The Brazilian Three Year Plan, designed to achieve both stabilization and development, was released soon thereafter, and with the resumption of Brazil's contacts with the IMF, the situation appeared favorable for fruitful discussion of development and external assistance with the Brazilian Government. Santiago Dantas, Brazil's newly appointed Finance Minister, had made an initial effort at putting into effect a comprehensive stabilization program. On the strength of what appeared to be a good start, Santiago Dantas came to Washington early in March, 1963, for discussions with the IMF, IBRD and IDA, IDE and several U.S. government departments and agencies, regarding the possibilities of external assistance for Brazil's plan of economic stabilization and development.

2. Form and Content of the Agreement

Brazilian and U.S. understandings and commitments were set forth in an exchange of letters between AID Administrator Bell and Finance Minister Dantas, dated March 25, 1963. In his letter to the AID Administrator, Dantas listed a series of measures already taken by the Government of Brazil to curb inflation and undertake agricultural reform, and also cited eleven further measures to be implemented during the following months. Included were measures to improve budgetary control and give development expenditures priority; to hold the Treasury cash deficit to a stated limit during 1963; to progressively eliminate the deficits of the railroads and merchant marine; to formulate further tax reform; to maintain a coffee policy designed to yield a stated net surplus, and to secure additional non-inflationary resources as offsets to the budget deficit; to encourage foreign private investment; to adopt a flexible exchange rate policy; and to elaborate the Three-Year Plan in greater detail and in collaboration with the Panel of Nine of the OAS. The letter also stated Brazil's intention to negotiate a standby agreement with the IMF by June 1963 and to seek assistance from Europe and Japan.

Mr. Bell's letter noted this program, with particular reference to the intention to seek a standby agreement with the IMF, to initiate conversations for long-term financing with the IBRD and IDA, and to obtain financial support from the Inter-American Development Bank and from Europe and Japan.

Assuming that this program were implemented, the United States agreed to make available, subject to applicable legislation, approximately \$400 million for the period March 1963 through May 1964. Of

this, \$84 million in credits from the Export-Import Bank, AID and the Treasury were to be made available immediately, and the remainder would be disbursed as requirements developed and parallel with successful implementation of the measures described in Minister Dantas' letter. (The \$84 million represented the balance of a U.S. Government assistance package totalling \$338 million dating from May, 1961.) Two-hundred-twenty-five of the total \$400 million was to be provided by AID including \$100 million in project aid and \$125.5 million commodity assistance. The remainder would be supplied by the Export-Import Bank, the Treasury, and through shipments of PL 480 Title I commodities.

3. Results

In May, 1963, a team was sent to Rio to assist the Embassy and USAID in (a) evaluating Brazilian progress in terms of specific undertakings contained in the agreement and (b) negotiating the principal document which would serve as the basis for phasing disbursement pursuant to the March understanding. It very soon became apparent that sufficient progress had not been made to warrant the preparation of such a document.

The Brazilian officials spontaneously indicated that significant changes in the formulation and execution of the program were necessary and the Finance Minister stated that he wished to make further progress before requesting implementation of the Bell/Dantas agreement and that a postponement from June to September of the target date for implementation was in accordance with his own thinking. It was apparent that unless there was a radical change for the better, it would be imprudent to assume that improvement by September would have been sufficient to justify disbursements of United States resources for general balances of payments or budgetary purposes. Therefore, in order to alleviate existing exchange pressures, it was felt that attention should be given to other alternatives, particularly that of working towards some form of negotiated limited refunding of short-term obligations.

Eventually it became clear that the Finance Minister could not obtain sufficient support to permit implementation of his program. Finance Minister Dantas was replaced in June, 1963, by Carvalho Pinto, and Pinto was in turn replaced in December 1963 by Ney Galvao. Dantas' program was not implemented by Pinto or Galvao, nor did the president or other members of the cabinet support it. The economic situation deteriorated rapidly after September, 1963, and had reached a critical stage by the time of the revolution of March, 1964. Under these circumstances, since Brazil had not succeeded in taking the necessary self-help measures, AID limited its assistance to Food for Peace help, project assistance and programs to combat misery and privation in the Northeast.

B. Program Loan: December, 1964

1. Background

The Goulart regime was overthrown in March, 1964. The new government, headed by Castello Branco, moved quickly and vigorously to contain inflation, initiate an orderly development program, and execute a series of reforms.

The magnitude of the problem which the government had inherited was reflected by inflation, which had been running at an annual rate of 140 percent during the first quarter of 1964, an anticipated budget deficit of between 1.3 and 2 trillion cruzeiros, including huge deficits of public enterprises, and a cumbersome exchange system with an over-valued rate which was hampering exports.

Within less than two months, work was initiated on the program for economic stabilization. A Washington team was sent to Brazil in May, 1964, for consultation with senior Brazilian government officials. It was clear that the Brazilian Government had made significant strides toward the development of an effective program, but that it was too soon for such a program to have been completely elaborated and implemented. It was also clear that some sort of transitional assistance would be essential in order to give the Brazilians more time to work out their program. In June, 1964, a \$50 million contingency fund was approved by the AID Administrator in order to provide transitional supporting assistance until such time as a broad program could be worked out.

During the summer and autumn of 1964, the Brazilian Government prepared such a far-reaching program. It successfully negotiated debt rescheduling agreements with European creditor governments, Japan and the United States on July 1, 1964. In October, the Government of Brazil presented to the Inter-American Committee of the Alliance for Progress (CIAP) a statement of the actions taken and plans for implementation of the Government's economic program for the period 1964 until the end of 1966. A letter setting forth the Government's economic policies to be followed during 1965 was sent to the Chairman of CIAP on December 7. ^{1/} Brazil also entered into and successfully completed negotiations for an IMF standby agreement. A U.S. negotiating team went to Brazil in November, 1964, and conducted a series of discussions with Brazilian officials which established the basis for substantial U.S. assistance in support of the Brazilian program.

On December 14, 1964, the United States announced that it would be prepared to make available about \$450 million during calendar year 1965, including AID assistance, a Treasury stabilization agreement,

^{1/} The Government of Brazil has declined to publish the CIAP letter of December 7. Its wishes in this matter have been respected by the U.S. Government and CIAP.

Export-Import Bank credits, and commodities provided under PL 480. The announcement also stated the U.S. expectation that at least an additional \$450 million would become available from inflows of private foreign capital and from current and new programs of international financial institutions. A formal loan agreement for \$150 million in AID program loan assistance was signed on the same day by the AID Administrator and the U.S. Ambassador to Brazil and by the Brazilian Minister of Finance and the President of the Bank of Brazil.

2. Content and Form of the Agreement

The loan agreement between the United States and Brazil is based upon the December 7 letter to CIAP. In the AID Loan agreement of December 14, 1964, the United States undertakes to provide up to \$150 million in support of Brazil's program of development, stabilization and reform, as set forth in the Government of Brazil's December letter to the CIAP. The funds are to be released in four tranches as follows:

- (1) Of the first tranche of \$52.5 million, \$45 million was disbursed in January, 1965, shortly after signing the loan, under AID procedures relating to advance financing for the importation of commodities from the U.S. The remaining \$7 million included in the first tranche was scheduled for disbursement following the opening of letters of commitment in favor of U.S. suppliers.
- (2) Three further disbursements of \$32.5 million after the close of each of the first three quarters of calendar 1965 will be made to support the Brazilian program. Performance will be evaluated, in its quantitative aspects, with special attention to the federal government's current account surplus; total transfers to government entities; the net international reserve position; and the expansion of credit by the Bank of Brazil to the private sector.

3. Performance

It is too early to judge the results of Brazil's performance under the loan agreement of December 14. In spite of courageous action, pressures continue to exist, and the stabilization effort has induced a recession in business.

However, the following review of Brazilian progress as of February, 1965, gives some indication of the scope and vigor of the Government's actions:

Stabilization: The new government has (a) eliminated import subsidies; (b) undertaken far-reaching tax measures which will augment revenues by increased rates and more effective tax collection (1965 is to show an overall 10/20 percent increase in real terms over

the considerable increase achieved in 1964); (c) taken initial steps to reduce deficits in public enterprises by higher rates and more efficient administration; (d) achieved a substantial success in reducing the budget deficit during calendar 1964 from the estimated Cr\$1.3 trillion under the budget inherited from the previous government to about Cr\$700 billion; (e) provided for a further reduction of the deficit in real terms during 1965; and (f) replaced a cumbersome exchange system with a simplified system and a realistic exchange rate. Brazil entered into a standby agreement with the IMF for \$125 million in January, 1965.

Development: The government has worked out a comprehensive priority program for roads, electric power, water and sewerage facilities, agricultural credit institutions, and development banks. The government favors maximum reliance on the private sector and is developing incentives for private enterprise expansion in both agriculture and industry.

Reform: Substantial progress has been made on the reform front. In addition to the tax measures referred to above, the reforms include a new housing bill, which also provides for the establishing of a National Housing Bank; a comprehensive land reform bill approved by Congress; an improved rent control law; and a banking reform law which includes a provision for the establishment of a central bank which is now being organized. The profits remittance law has been amended and an Investment Guaranty Agreement has been signed, although it has not yet been ratified by the Brazilian Congress. In December, 1964, President Castello Branco signed a decree establishing new regulations intended to stimulate the production and export of iron ore resources by eliminating discriminatory provisions limiting private participation in this field.

Foreign Investment: The entire posture of the present government has been in the direction of stimulating private investment both domestic and foreign. The revised profits remittance legislation, the signing of the Investment Guaranty Agreement and the revised legislation concerning mineral resources are all measures intended to attract and facilitate foreign investment activities.

CHILE

The United States has extended sizeable program loans to Chile for the past three years. In 1963 and 1964, U.S. program assistance was linked to stabilization policies defined both by Chile's Standby Agreement with the IMF and by the terms of the U.S. loans. In 1965, U.S. assistance is related to more extensive performance commitments on a range of developmental measures. This growing relationship between assistance and performance is described below.

A. The Program Loan of 1963

1. Background

a. Chile's Development Plan

Chile had been the first Latin American country to produce a comprehensive national development program, published in 1960. The plan established global targets and laid out general guides to economic policy during the period 1961-70. It was extensively reviewed by the IBRD and the OAS wisemen and although significant modifications were suggested as to analytical technique and policy emphasis, it was thought to be somewhat useful as a first step toward guidelines for Chile's development effort over the decade. However, GOC practice in 1963 and 1964 indicated that the plan was not used as a guide to economic stabilization and development policies.

b. Economic Situation at the End of 1962

By the end of 1962, the Chilean economy had experienced a decade of accelerated inflation. The inflationary spiral had caused severe dislocations; the tax and tariff structures reflected measures motivated by immediate needs rather than by the requirements of a developing economy, and a high level of interest rates persisted. More important, perhaps, a pattern of business attitudes and practices had developed, including the drive to earn profits at a rate and in a manner that would compensate for the shrinking value of the currency, leading to great inefficiency in production and marketing, excessive imports, and reduced investment. Social unrest was increasing, particularly among the urban population.

Early in 1963, Chile's largest foreign lenders (IBRD, IMF, and the U.S.) agreed to continue to provide assistance only after the GOC had committed itself to major policy changes to assure some degree of financial stability. The lenders agreed to provide Chile with the following assistance: IMF, \$35 million; the DAC countries, \$18 million; and the U.S., \$60 million: of which Treasury, \$10 million; Ex-Im Bank, \$15 million; and AID, \$35 million.

2. Content and Form of the Agreement

The agreement covering the AID \$55 million program loan included the following conditions:

- a. Chile would undertake a stabilization program and enter into a one-year Standby Arrangement with the IMF, which limited Central Bank credit expansion to 12-15%, and encouraged flexible exchange policy.
- b. The GOC also would achieve a surplus of 400 million escudos in its current operations from which the bulk of public investment would be financed.

3. Performance

With the objective of raising public saving to the required amount, Chile made significant progress in initiating and implementing tax reforms. Major changes in the structure and rates of income and inheritance taxes were proposed in 1963 and finally enacted in February 1964. A full administrative reform of the internal revenue service to tighten tax collection procedures was initiated, together with a complete reassessment of all urban and rural real estate taxes. A law was passed in September 1963 to simplify the stamp tax by reducing the number of rates from 300 to under 60.

These improvements in the capacity of the Central Government to save were offset to some extent by poor performance by some state enterprises and autonomous agencies. Nevertheless, the overall level of public savings exceeded the target, as public investment outside the Central Government declined in 1963. Total bank credit expansion was well within the limits envisaged by the agreement, and government borrowing from the Central Bank was negligible. Finally, the Chilean authorities met the net foreign reserve test of the IMF, although exchange depreciation in 1963 fell short of the rise in cost of living by about one-third.

Review of GOC performance under the loan conditions was undertaken by both IMF and USAID officials, and was considered to have been an improvement over past policies, although severe inflation and other major problems persisted. The program loan was fully disbursed by September 1963.

B. The Program Loan of 1964

1. Economic Situation at the End of 1963

The Chilean situation was reviewed again early in 1964. It was recognized that the year ahead would be particularly difficult economically in view of the presidential election scheduled for the fall.

The IMF, which had had for a number of years a particularly close relation with the GOC, had entered into a new \$25 million Standby Arrangement with Chile in October 1963. For the 1964 calendar year, the U.S. Government agreed to a \$40 million AID program loan, later increased by \$15 million to \$55 million, and to a Treasury stabilization loan of \$15 million. The Ex-Im Bank provided a credit of \$15 million.

2. Content and Form of the Agreement

The content and form of the 1964 program loan was similar to the 1963 agreement. Disbursement under the loan was conditional upon GOC compliance with appropriate fiscal, monetary and exchange rate policies defined in the IMF Standby Agreement, and upon the GOC meeting quarterly current account surplus targets for the Central Government and the autonomous agencies, totalling to 640 million escudos at the end of the year. In addition, Central Bank credit expansion was to be limited to 135 million escudos. The GOC was to pursue flexible exchange rate policies; its success in so doing was to be measured by whether there was any decrease in international reserves or rise in payments arrears. The Agreement provided that the United States and Chile would review performance in these respects quarterly, prior to release of tranches of the loan.

3. Performance

During 1964 both the IMF and AID conducted quarterly reviews of Chilean performance and consulted regarding the conclusions. It was determined that Chile had largely met the specified conditions and its self-help performance was considered adequate. Savings by autonomous agencies greatly exceeded the target, although Central Government savings fell short by 15%. This change reflected marked progress toward consolidating the GOC public finances. The money supply rose less than provided for under the agreement. However, the cost of living rose steadily and substantially between 1961 and 1964, despite the fact that the increase in money supply was well within agreed limits in 1963 and 1964. Part of this acceleration was no doubt due to a rise in the velocity of circulation and a cost-push spiral. Nevertheless, the effectiveness of financial and monetary restraints in controlling inflation was again disappointing. On external account, the current balance showed considerable improvement over the 1963 level, but exchange depreciation again fell short of price increases.

C. The Program Loan of 1964

1. Economic Situation at the End of 1964

The new Frei government, installed in November, made an intensive review of the country's situation and developed a program for 1965 as a first step toward a comprehensive review of the long-term plan for the period 1965-70.

Primary elements of the GOC program are: (a) Stabilization over a three-year period, with price inflation reduced to 25% in 1965 and 10% in 1967. (b) Increasing exports and improving the balance-of-payments position, largely through mutually acceptable agreements with U.S. copper companies on expanded copper production, and through active pursuit of a flexible exchange rate policy--this time to be determined by additional measurements. (c) Expanding public investment to be financed partly by a 28% real increase in Chilean resources and with reduced reliance on Central Bank borrowing. (d) Increasing production, productivity and social justice in the agricultural sector, including higher profits to agricultural producers and formation and implementation of a limited agrarian reform program. (e) Increased emphasis on the productive sectors of the economy, including establishment of a Private Investment Fund.

In November 1964, the Government of Chile sent a letter to the Chairman of the Inter-American Committee on the Alliance for Progress (CIAP) in which it defined in considerable detail the basic elements of its program for 1965 and for the following year.

2. Content and Form of the Agreement

In February 1965, AID agreed to provide up to \$80 million in non-project loan assistance in support of the Chilean development program. The Loan Agreement refers to the performance targets set forth by Chile in the CIAP letter. The Agreement provides for disbursement in four tranches, and for thorough quarterly reviews with GOC officials of performance in selected fields, with special emphasis on monetary and fiscal policies. The first review is scheduled for April-May 1965. Chile's performance tests are much more detailed and extensive than ever before.

At the same time, backed by a favorable IMF report, Chile has negotiated a rescheduling of her heavy foreign debt. Finally, the GOC has negotiated agreements with the copper mining companies Cerro Del Pasco, Anaconda and Kennecot, which will result in some \$415 million in new investments in order to substantially increase Chilean copper production by 1970.

It is too early, of course, to evaluate the performance of the new Frei government. The first indications are that Chile is determined to embark on a program of basic reforms designed to overcome past obstacles to sound economic growth and social betterment.

TAIWAN

The Nineteen Points (January 1960)

Background

By late 1959, Taiwan's economic progress was such that, in U.S. judgment, a five-year accelerated development program coupled with substantial policy changes and supported by adequate foreign aid could bring the country to the point of self-sustaining growth. By the end of that period it would be possible to maintain a satisfactory growth rate without further concessional economic aid. At the same time, the Government of the Republic of China (GRC) was working on its third Four-Year Plan for 1961-1964. A number of policy decisions and changes were already under consideration by GRC to stabilize the economy and encourage private savings and investment.

Content of the Commitment

In October 1959, the U.S. Government proposed to GRC a five-year terminal aid program for Taiwan's accelerated economic development, including built-in incentives relating U.S. assistance to Chinese performance, and joint control and programming of grant and loan funds. The U.S. proposed to provide three types of economic aid:

- i. A "hard core" of minimum essential grant economic aid, designed to prevent living standards from falling due to the maintenance of large military forces.
- ii. Supplemental grant aid to finance imported raw materials, spare parts, and machinery and equipment needed by new and expanding enterprises, largely in the private sector. The amount and timing of this assistance would depend on GRC's performance.
- iii. Loans from the Development Loan Fund to carry out specific projects of modernization, expansion or building new productive facilities. The magnitude of this assistance would depend on the availability of projects meeting criteria, and would be strongly influenced by GRC policy changes as these affected the private sector.

The supplemental grant aid and, indirectly, project lending would increase with improved Chinese performance. The "hard core" defense support, on the other hand, could be expected to decline as economic conditions in Taiwan improved.

Both in order to achieve their own plan purposes, and in response to the U.S. proposal for an accelerated development program in January 1960, Executive Yuan of the GRC approved a "Nineteen Point Economic

Reform Program". This program was designed, inter alia, to control military expenditures, implement a non-inflationary fiscal and credit policy, reform taxes so as to remove deterrents to private business, establish a uniform and realistic exchange rate, liberalize foreign exchange controls, establish an independent public utilities commission to set rates, create a securities registration and marketing system, and sell government enterprises to private owners. Specific time targets of one, two or three years were attached to many of the nineteen points.

Results

During the first two years under the program, implementation of the nineteen points lagged behind schedule. The new income tax law was delayed, only one minor government enterprise had been transferred to private ownership, there was no permanent solution to the utility rate problem, and it was not clear whether military expenditures could be satisfactorily controlled. Nevertheless, the program did stimulate a good deal of constructive effort, and in 1963 momentum picked up. By the end of the five-year period, most of the points had been largely carried out and the basic purposes of the accelerated development program had been achieved.

In assessing GRC performance during this period, the U.S. Government considered a wide range of actions and policies rather than focusing on only a few fairly precisely measurable indicators of performance. The United States adhered in general, but not entirely consistently, to the principle of adjusting assistance additional to that required for basic defense support to GRC performance. \$69.1 million was provided in Defense Support during fiscal year 1960, of which most was released after the announcement of the Nineteen Points. In FY 1961, \$45.6 million Defense Support was made available, including a \$5 million "development component" for capital equipment, semi-finished products and industrial raw materials. With the creation of the Agency for International Development in 1961, the funding category called Defense Support was eliminated. In fiscal years 1962 and 1963, program loans of \$20 and \$15 million were provided. By this time the criteria were less related to the specific Nineteen Points, and were based instead on more general satisfaction with support for the good investment climate created by GRC policies and vigorous private industrial growth. In fiscal years 1964 and 1965, only a small amount of technical assistance was made available, and all AID assistance was terminated by FY 1965.

