PRIVATE INVESTMENT IN LATIN AMERICA

HEARINGS

BEFORE THE

SUBCOMMITTEE ON INTER-AMERICAN ECONOMIC RELATIONSHIPS

OF THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

EIGHTY-EIGHTH CONGRESS

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PRIVATE INVESTMENT IN LATIN AMERICA

TUESDAY, JANUARY 14, 1964

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON INTER-AMERICAN ECONOMIC
RELATIONSHIPS OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:35 a.m., in room 1202, New Senate Office Building, Hon. John Sparkman presiding.

Present: Senator Sparkman; Representatives Griffiths and Curtis.

Also present: William H. Moore, economist; Hamilton D. Gewehr, administrative clerk; and Donald A. Webster, minority economist.

Senator SPARKMAN. Let the subcommittee come to order, please.

I have delayed opening the hearing for a few minutes hoping that our first scheduled witness for this morning might be present. We are informed that he has arrived in town and will be here any minute. Two other members of the subcommittee are expected also, but I understand one of them has been held up and the other one is coming in from out of town. Those of us who have managed to get here are certainly ready to admit that travel and arrival times are a little uncertain and difficult in face of such heavy snow and winds.

The Alliance for Progress, which finds its expression in the Charter of Punta del Este, was signed and agreed to as a cooperative and mutual program. The charter was signed by all of the Latin American Republics including, it is appropriate to remember, Brazil, Argentina, Peru, and Panama, as well as the United States. This historic charter recognized that the cooperation of all parties would be needed if the measures and hopes for economic and social progress to fulfill the commitments of the charter were to succeed.

These hearings deal primarily with one specific aspect of that pledge for cooperation; namely, the role of private enterprise in supplying capital and producing the goods and services upon which a higher level of living can be based.

The declaration to the peoples of America set out in the charter contains among other worthy goals such as wiping out illiteracy and bringing about a steady increase in average incomes, two express objectives which I believe are worth quoting in full as background for these hearings. The mutual commitments which these sovereign countries countries agreed to included undertakings—

> To stimulate private enterprise in order to encourage the development of Latin American countries at a rate which will help them to provide jobs for their growing populations, to eliminate unemployment, and to take their place among the modern industrialized nations of the world.
>
> To maintain monetary and fiscal policies which, while avoiding the disastrous effects of inflation or deflation, will protect the purchasing power of the many, guarantee the greatest possible price stability, and form an adequate basis for economic development.

A basic proposition behind the Alliance was that substantial cooperation of private capital would be necessary to supplement Government efforts. Since private capital, to use the words of the Commerce Committee, cannot in a free society be "driven or cajoled into new fields," investment must be welcomed and, indeed, attracted by the opportunities for competitive return and the basic safety of the capital employed. In view of these hopes, one finds much that is disturbing and discouraging in the record and it is because of these reasons for concern that these hearings are being held.

The Economic Commission for Latin America of the United Nations Economic and Social Council reported last year not only a hesitancy on the part of private capital but an actual decline in the net flow of external financing to Latin America as a whole. The Commission notes that "in 1962 no progress was made with respect to net external financing." And they made this further comment:

> The year 1962 witnessed the initiation of a substantial international effort to increase the flow of such external capital * * * in the course of the next 10 years * * *. It is therefore surprising that concurrently with this international effort, the data available for 1962 indicate a level of external financing far below * * * the average for the 2 preceding years.[1]

Newspapers and magazines throughout the year have, moreover, been replete with headlines of expropriation and threats of expropriation, and of political uncertainties that cannot help but be deterrents to the businessman contemplating investment. The magazine Business Week of December 7, 1963, has an article the title of which is "United States Still a Bogeyman to Latin Americans—Main Trouble Spot Is Brazil Where Feelings Run Strong Against Heavy Inflow of North American Capital and Move Is Afoot To Form Common Policy Against United States." The magazine quotes a Brazilian as saying:

> The biggest sore spot in Brazil is private U.S. capital.

To add to the known preference of the ruling "elite" in these countries for the status quo rather than accept land and tax reforms, a Mexican banker back from a tour in South America, where he talked to businessmen in such temperate, commercial places as São Paulo and Montevideo, interpreted local business views in these words:

> These sentiments are not emotional and not ideological. Their reasoning is economic. They fear U.S. penetration in the Latin American free trade zone and they fear the United States is taking over their channels of trade.

The text of the Business Week article will be included at the conclusion of today's record. Whether these views are representative or not I cannot say.

In a sincere effort to live up to our Government's commitment under the Alliance, the Commerce Committee for the Alliance for Progress (COMAP) was created by the late President Kennedy to help accelerate the contribution of the private business sector to the Alliance for Progress. The Committee of distinguished U.S. bankers and industrial leaders, after weeks of deliberation, reported to the Secretary of Commerce on the problem and its recommendations for improving

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[1] Secretariat materials dated Mar. 29, 1963, entitled "Some Aspects of the Latin American Economic Situation in 1962," for use at the 10th session, Mar del Plata, Argentina, May 1963, p. 46.

the flow of U.S. capital. Mr. J. Peter Grace, president of W. R. Grace & Co., was the Chairman of that Committee. Mr. John D. J. Moore, vice president of the Grace Co., who was associated with Mr. Grace on that Committee's work, will be our first witness this morning to tell us something of the concerns and proposals of this group of U.S. businessmen.

With the interest and support of Senator Javits, who is a member of this subcommittee, and Senator Humphrey, Western European capital also has been stimulated to consider a cooperative program for investment in Latin America. Dr. Aurelio Peccei, executive director for Western Europe of the Atlantic Community Development Group for Latin America (ADELA), and director of the Fiat Motor Co., Inc., who was originally scheduled to appear this morning has been delayed and will appear tomorrow morning to discuss these Western European attitudes and efforts.

Our second witness this morning will, accordingly, be Mr. Philip Alexander Ray who has the very difficult task of trying to point up some of the responsibilities of the Latin American host governments and Latin American investors themselves in accepting, or at least not discouraging, private investment from outside sources.

At this point I would like to place the subcommittee announcement of these hearings in the record.

(The announcement referred to is as follows:)

CONGRESS OF THE UNITED STATES, JOINT ECONOMIC COMMITTEE

SENATOR SPARKMAN ANNOUNCES HEARINGS ON PRIVATE INVESTMENT IN LATIN AMERICA

Senator John Sparkman, Democrat of Alabama, chairman of the Subcommittee on Inter-American Economic Relationships of the Joint Economic Committee, today announced hearings on private investment and the Alliance for Progress, and released the schedule of witnesses. The hearings will be held on January 14, 15, and 16, at 10 a.m., in room 1202, New Senate Office Building.

In making the announcement, Senator Sparkman commented: "The Alliance for Progress is in trouble and one of those troubles is certainly the situation facing private investment capital—the flight of local domestic capital and the discouragements confronting foreign capital. These hearings will study and emphasize the important role which private investment plays in the concept and success of the Alliance for Progress. Unfortunately, the cooperative program aimed at an accelerated rate of social and economic progress in Latin America is too often viewed by some persons, both in the United States and abroad, as essentially a program between governments.

"Government guarantee programs as an incentive to foreign private investment will also be considered with special reference to their application and success in Latin America. Opportunities for expanded private investment depend, in part, upon trade expansion and, in this connection, the regional economic integration already underway in Latin America will be considered in the broader perspective of hemispheric integration of the Western Hemisphere as a whole."

Members of the subcommittee are:

Senator John Sparkman, Democrat, of Alabama, chairman.
Senator Claiborne Pell, Democrat, of Rhode Island.
Senator Jacob K. Javits, Republican, of New York.
Senator Len B. Jordan, Republican, of Idaho.
Representative Richard Bolling, Democrat, of Missouri.
Representative Hale Boggs, Democrat, of Louisiana.
Representative Martha W. Griffiths, Democrat, of Michigan.
Representative Thomas B. Curtis, Republican, of Missouri.

HEARINGS JANUARY 14, 15, 16, 1964: PRIVATE INVESTMENT AND THE ALLIANCE FOR PROGRESS

TUESDAY, JANUARY 14, 10 A.M., ROOM 1202, NEW SENATE OFFICE BUILDING

I. Cooperative efforts to encourage private risk capital
   "Improving the Flow of U.S. Private Investment in Latin America"—John D. J. Moore, vice president, W. R. Grace & Co.; chairman, U.S. Inter-American Council, New York, N.Y.
   "Responsibility of Latin American Host Governments and Private Local Capital"—Philip Alexander Ray, attorney, chairman, International Bond and Share, Inc.; former Under Secretary of Commerce; senior research fellow, Latin American studies, Hoover Institution on War, Revolution, and Peace, Stanford University; author, "Our Hemispheric Crisis: South Wind Red," San Francisco, Calif.

WEDNESDAY, JANUARY 15, 10 A.M., ROOM 1202, NEW SENATE OFFICE BUILDING

   "Improving the Flow of Western European Private Investment in Latin America"—Aurelio Peccei, executive director for Western Europe, Atlantic Community Development Group for Latin America (ADELA); director, Fiat Motor Co., Inc., Rome, Italy.

II. Investment Guaranties as an Incentive to Private Investment
   "An Appraisal of Programs of Government Guaranties to Foreign Investors by Capital-Exporting and/or Host Countries"—A. A. Fatouros, professor, University of Chicago Law School; author, "Government Guarantees to Foreign Investors," Chicago, Ill.
   "U.S. Government Guaranties Under the Foreign Assistance Act of 1962 With Special Reference to Latin America"—George Rublee, Assistant General Counsel for Private Enterprise, Agency for International Development, Department of State, Washington, D.C.

THURSDAY, JANUARY 16, 10 A.M., ROOM 1202, NEW SENATE OFFICE BUILDING

III. Trade Expansion Through Regional Economic Integration as an Incentive to Private Investment
   "Progress Report on Latin American Free Trade Association (LAFTA) and Central American Program of Economic Integration (CAPEI)"—Francis E. Grimes, vice president, area executive, Latin America, Chase Manhattan Bank, New York, N.Y.
   "Canadian-U.S. Free Trade Arrangement: Possible Characteristics"—Sperry Lea, associate director of research, Canadian-American Committee, National Planning Association: author, "A Canadian-United States Free Trade Arrangement," Washington, D.C.
   "A Western Hemisphere Common Market—Potentials and Implications"—William L. Clayton, board of directors, Anderson, Clayton & Co.; former Under Secretary of State for Economic Affairs, Houston, Tex.

Senator SPARKMAN. I may say that Mr. Moore's timely arrival has now made it possible to proceed in the regular order. Mr. Moore, I had just suggested that both you and Mr. Ray sit at the table and perhaps we can develop this into a kind of panel discussion.

I am glad that Congressman Tom Curtis has also come in. Congressman Curtis, do you have any preliminary statement you would like to make?

Representative CURTIS. No; other than to back up the statements that you have just made and express our deep interest in this matter and our appreciation of you gentlemen for taking the time to advise this committee. We are hopeful that through this updating and furthering of our studies that we have embarked upon, we may be of benefit to our colleagues in the House and Senate serving on the legislative committees and possibly even, who knows, of some benefit to the executive branch of the Government.

Senator SPARKMAN. Thank you.

All right, Mr. Moore. We are glad that you got here. I understand you took a train so you would be sure to be on time. It reminds me of an incident in my own experience.

One time I was going to speak in Chicago. I was to speak at noon and I was down in Alabama. Rather than take a plane, I decided to take the train. When I told the head of the organization for whom I was going to speak that I was going to take a train, he said, "I am certainly glad because that means there won't be any question about your being here on time." My train was due in at 8:30 a.m. and got in at 4:30 in the afternoon instead!

Anyhow, we are glad you got here. We appreciate your coming, and are glad to hear from you at this time.

STATEMENT OF JOHN D. J. MOORE, VICE PRESIDENT, W. R. GRACE & CO., AND CHAIRMAN, U.S. INTER-AMERICAN COUNCIL

Mr. MOORE. Thank you, Mr. Chairman. I did exactly as you did and took the night train so there would be no doubt that I would be on time. At the time we were supposed to be here the train was still in motion somewhere between Baltimore and Washington.

I will now proceed with my statement.

Mr. Chairman and members of the subcommittee, thank you for your invitation to testify here. I am really appearing, as you know, in the place and stead of Mr. J. Peter Grace, the president of W. R. Grace & Co., who was required to be out of the country on business at the time of the hearings. I am delighted to have this opportunity because I was associated with Mr. Grace in the work of the Commerce Committee for the Alliance for Progress.

We are all familiar with the work of your subcommittee and the constructive hearings it has held and the reports which it has issued on economic development and economic policies concerning Latin America.

I think you could not be holding these hearings at a more timely hour in our Latin American relations. I am not referring to the disturbances in Panama because of their mostly emotional and political nature. They are closer to the economic situation than some other facets of the problem with which we deal today, but it is a very critical moment in our Latin American relations.

President Johnson has already demonstrated his own concurrence in the late President Kennedy's description of the situation in Latin America as "the greatest challenge which the United States now faces, except for the direct matter of our dealings with the Soviet Union."

All friends of better relations between the United States and Latin America know and place great confidence in Thomas C. Mann, whom the President has appointed as Assistant Secretary of State for Inter-American Affairs and Coordinator of the U.S. participation in the Alliance for Progress. The business community has known and worked with Mr. Mann for many years and I know that they feel it is good management to have him take charge of all aspects of the Latin American activity of the U.S. Government including his new role as special adviser to the President.

The U.S. Inter-American Council, of which I have the honor to be the chairman, is composed of 154 U.S. corporations, large and small, which do business in or with Latin America. The businessmen who make up this group represent many hundreds of years of experience, living and working in Latin America and many millions of dollars of investment. One statistically minded member of our council calculated that about 80 percent of the U.S. investment in Latin America is represented in our membership and that goes to a sum in excess of $6 billion. The basic thing I am talking about is the experience of these men.

They know Thomas Mann as a thorough and conscientious professional who operates from deep knowledge and understanding of the Latin American countries and their people and who is utterly free of political or economic bias. He has been throughout his career a friend and willing helper to all who work for better relations between the United States and the Latin American countries, whether they be businessmen, labor leaders, government officials, educators, farmers, religious missionaries, or individuals dedicated to stronger people-to-people relations and cultural interchange.

Not only was President Johnson's choice of Mr. Mann for all-inclusive responsibilities in the Latin American area a most encouraging move, but Mr. Johnson's meeting at the White House with the Latin American diplomatic corps at the earliest possible moment after his assumption of the Presidency demonstrated to all the world his recognition of the importance of these countries to us. I think also that his prompt and firm message at the time of the unlawful detention of the American officials in Bolivia made an excellent impression throughout Latin America.

Now he has moved swiftly and sure footedly in the Panamanian disturbance, sending Mr. Mann and a top team to Panama, and taking a firm position as to our treaty rights concerning the canal.

The company which I represent, W. R. Grace & Co., has had, as you may know, a long and successful business life in Latin America. It was actually organized in Peru in 1854 and it is engaged in manufacturing, distributing, banking, and transportation in a number of Latin American countries with particular emphasis on the countries of the west coast. Although in the past decade it has grown into one of the largest U.S. chemical companies, neither its interest nor its investment in Latin America has diminished. Under the presidency of Mr. J. Peter Grace we have entered into a number of new and more advanced businesses in Latin America. Our Latin American investments are presently at an alltime high although in terms of the whole Grace business they constitute a smaller percentage of the entire corporation. In 1963 we invested about $12 million in Latin America and in 1964 we expect to invest a considerably larger amount.

In other words, Mr. Chairman, while we see many problems facing all of us in this hemisphere we also see many excellent opportunities for U.S. private investment.

In your chairman's letter to me of January 7 he expressed the wish that in discussing the flow of U.S. private investment to Latin America I should cover the views and conclusions of the Commerce Committee for the Alliance for Progress (COMAP), of which Mr. Peter Grace was the Chairman, and I shall be happy to do so. I was privileged to be associated with Mr. Grace and his colleagues in this great endeavor

and I welcome the opportunity to discuss COMAP before your committee. I feel its work and recommendations should have the widest possible dissemination.

In any discussion of cooperative efforts to encourage private risk capital I feel, Mr. Chairman, that the COMAP report is essential reading. It was prepared by a group of outstanding American business leaders after several months of intensive work which they undertook by appointment of Secretary of Commerce Hodges.

I will not read the list of names, but will present it for the record.

(The names of members of COMAP are as follows:)

William Blackie, president, Caterpillar Tractor Co.
Thomas D. Cabot, chairman of the board, Godfrey L. Cabot, Inc.
T. A. Campbell, vice president, Latin American affairs, the Anaconda Co.
Emilio G. Collado, vice president and director, Standard Oil Co. of New Jersey.
Dudley T. Colton, vice president and general manager, Johns-Manville International Corp.
Charles S. Dennison, vice president, oversea operations, International Minerals & Chemical Corp.
A. W. Elwood, senior vice president, international operations, FMC Corp.
Marshall Erdman, Marshall Erdman Associates, Inc.
Fred C. Foy, chairman of the board, Koppers Co., Inc.
William C. Friday, president, University of North Carolina.
John F. Gallagher, vice president for foreign administration, Sears, Roebuck & Co.
Stephen A. Girard, president, Willys Motors, Inc.
Leon E. Hickman, executive vice president, Aluminum Co. of America.
Neil Mallon, chairman, executive committee, Dresser Industries, Inc.
Walter McKee, group director, Latin American operations, Ford Motor Co.
Edgar J. Moor, assistant to vice president in charge of foreign operations, United Shoe Machinery Corp.
William J. Moreland, James C. Moreland & Sons, Inc.
Charles G. Mortimer, chairman, General Foods Corp.
Peter R. Nehemkis, Jr., Washington counsel, Whirlpool Corp.
David Rockefeller, president, Chase Manhattan Bank.
A. B. Sparboe, vice president, the Pillsbury Co.
J. Wilner Sundelson, planning assistant to the vice president, Ford international staff, Ford Motor Co.
Juan T. Trippe, president, Pan American World Airways, Inc.
Frank X. White, president, American Machine & Foundry International.
Walter B. Wriston, executive vice president, First National City Bank.

Mr. MOORE. The principal task assigned to the Committee was to analyze the flow of U.S. private investment to Latin America, identify the obstacles impeding a greater flow, and make recommendations as to how the U.S. Government might help encourage such increased investment. Their report is fully as timely today as it was when it was issued by Secretary Hodges last March, and I respectfully suggest that it be incorporated in the record of these hearings.

Senator SPARKMAN. I am well aware of the fine report. It will be received by this committee for its use.

Representative CURTIS. Mr. Moore, your suggestion was that this be put in the record of our hearings, was it not?

Mr. MOORE. Yes, it was, Mr. Curtis, but I don't know enough about the rules of your committee or your printing situation to know whether that would be feasible. I hope you can print it.

Representative CURTIS. I think it is, and I was just going to suggest to the chairman after looking at the report that we do include it because the data in these hearings should be as complete as possible. I would like to make that request and also that an exchange of letters between

Mr. Grace, as Chairman, and some of the COMAP members respecting the report be included as well.

Senator SPARKMAN. Yes. Without objection it will be made a part of the hearings and will be placed at the end of today's testimony following the article from Business Week magazine.

(See p. 55.)

Mr. MOORE. The businessmen emphasized at the outset of their report the basic proposition which governs the flow of private capital. They declare:

> In free societies private capital cannot be driven or cajoled into new fields. There is a free market for private investment and nations, areas, industries, and institutions must compete for it in a free marketplace. In other words, investment must be attracted and experience teaches us that it will be attracted to those fields where the return is most promising and where the safety of its capital is most assured.

The Committee pointed out the fundamental fact that it is misleading to consider Latin America as a monolithic entity and stressed that it must be borne in mind that each country differs as markedly from the others as do the countries of Europe.

> It would be a fatal error to attempt to equate the varying conditions of the Republics of Latin America with conditions in the United States, just as it would be a fatal error to equate the Latin American Republics with one another.
>
> These countries today present a mixed picture of advanced stages of development side by side with conditions which are centuries behind the times. It represents a picture of rapid economic growth, of great new cities as modern and industrialized as any in the world, whose peoples live within an hour's travel of fellow citizens residing in 12th-century conditions.

They stressed the essential role of private investment, not only foreign, but even more importantly, local private enterprise, to the success of the Alliance for Progress.

> An authoritative estimate indicates that 70 percent of economic activity in Latin America is in the hands of private owners while 30 percent is controlled by the Government. Of the 70 percent of privately owned enterprise some 90 percent is estimated to be owned by Latin Americans and only 10 percent by foreigners.
>
> The fact that the private sector in Latin America is so heavily made up of local private investors means that the success of the Alliance for Progress depends to a great extent not only on the participation but most of all on the enthusiastic contribution of these Latin American businessmen. Experience of all Western countries has shown that the greatest economic progress is achieved by freemen under conditions of economic liberty when the productive forces of private investment and individual enterprise are unleashed and given maximum encouragement and support.

They pointed to the remarkable achievements of Latin American businessmen whose dedicated efforts have built new industries and new cities in their countries, recommending:

> These creative businessmen are our natural allies in the Alliance for Progress and they are a main hope for Latin America's future. They should be sought out, encouraged and enlisted in the program.

We have to get to know the Latin American businessman better. I do feel myself, Mr. Chairman, that throughout the last 2 or 3 years that there has been a lot of inexact thinking with regard to the role of the local Latin American businessman. Your Committee has made trips around those countries and you have seen great new cities and industrial centers, and those were not built by foreigners. They were built by local men, most of whom came from humble origins and built

up their businesses and their investments in the pattern with which we are familiar in this country. And this criticizing them generally as oligarchs and undersirable persons, which is all too common, I think we are discouraging the very creative responsible element of Latin America that can make the wheels turn down there.

Naturally they have their undesirables. They have men who don't measure up to the mark just as we do and every other country in the world does, but as a business community, I think from your visits and I know from my long years down there, they are a progressive and patriotic, basically constructive element.

Senator SPARKMAN. Mr. Moore, Mrs. Griffiths wants to ask a question.

Representative GRIFFITHS. May I ask you how you feel we are discouraging them? What are we doing that discourages them?

Mr. MOORE. Well, for one thing, we make blanket statements, both private people and Government officials, perhaps more often in the executive than the legislative branch of our Government, to the effect that Latin American businessmen don't pay their taxes. Most Latin American businessmen do pay their taxes, by far the great majority. We make statements that they are irresponsible and don't treat their labor properly, that they keep their money in Swiss banks, and things of that sort, without any proof and without any indication as to whether there is any higher proportion of their money abroad than there was before or that there is in this country.

We are having to enact laws now ourselves to keep our people from investing in foreign securities by seeking to equalize American and foreign interest rates through taxes. I can remember 2 or 3 years ago when I was traveling around Latin America, the Treasury Department was campaigning for a bill to deduct at source interest on savings bank accounts and dividends of corporations and were stating a figure—I can't remember what it was, but it was an awfully big figure—and advertising to the whole world how much income taxes the American citizens were failing to report and pay. They had to have these deductions at source in order to make the American people pay their just taxes, and the Latins I met couldn't quite understand why we were calling them a bunch of tax dodgers while advertising to the world that we at home were having to have legislation to deduct from savings banks at source.

Also the exclusion, and it was a very pointed exclusion, of the business community and private enterprise from the Punta del Este Conference in 1961 which supposedly wrote the charter for the Alliance for Progress. There were no busines people there and it was principally through the efforts of two countries, Argentina and Peru, that the private enterprise language got into that charter at all.

That is the kind of criticism I am talking about of the Latin American business community. It is not calculated to encourage those men to work with us.

Naturally, as I say, there are irresponsible men of wealth in Latin America. I know in Paris you can see irresponsible men from every country in the world including our own. I do not believe there is any higher proportion of them in Latin America than there is in any other country.

When we indulge in the kind of criticism I am talking about, I think we are dampening their enthusiasm for our system.

Representative GRIFFITHS. May I ask further what is the discouragement resulting in, the fact that they do not cooperate with us or do not invest in their own countries, or just what?

Mr. MOORE. Yes. The fact that I think they would be less inclined to go into the joint-venture type of thing which we are trying to promote in this country, that is, one of the great items in the recommendations for investment in Latin America, that the U.S. investors should form a partnership with local investors down there.

You take a question like these various reforms we are asking them to do, social reforms, land reform, tax reform, etc. I think when they feel that the recommendation is not well founded and the criticism on which the recommendations are based is not well founded, it is much more difficult to expect them to cooperate and help put in these reforms.

Representative GRIFFITHS. Thank you.

Senator SPARKMAN. All right, sir.

Mr. MOORE. Now, we all know that at Punta del Este a goal of $2 billion a year of money to go into Latin America was established and of that $2 billion a year, $300 million was to be represented by net new U.S. direct private investment in Latin America. I don't know how this $300 million was arrived at but you could arrive at it by an average of certain earlier years, to 1961, when the charter was adopted.

In any event, it didn't materialize as we all know. In fact, instead of increasing, it dropped in 1962 down to a figure below zero; that is, there was a net flow to the United States from Latin America rather than net flow into Latin America. And on page 8 of this statement you will see the table showing 1958, $299 million, to 1963, so far this year, the fourth quarter—the figures, of course, for all of 1963 are not in yet. The fourth quarter was a little better and we will probably wind up in 1963 with a net inflow into the United States of $25 million from Latin America in the category of direct new investments.

The Committee demonstrated that far from meeting the goal announced at Punta del Este of $300 million of net new direct U.S. private investment per year in Latin America, the aggregate inflow into Latin America has been declining at an alarming rate.

In the table that I present to you, you will note that 1957 is a big year—$1,163 billion—but as you know, there was in that year $700 to $800 million in oil investment in Venezuela which inflated the figure. But looking at the normal years, 1958, and so forth, you will see what has happened to this flow of private investment.

(The table referred to follows:)

TABLE 1.—*Net new U.S. direct investment in Latin America*

	Millions		*Millions*
1957	$1,163	1962	($32)
1958	299	1963:	
1959	218	1st quarter	(11)
1960	95	2d quarter	15
1961	173	3d quarter	(42)

NOTE.—Figures in parentheses indicate a negative flow.

Mr. MOORE. The COMAP analysis of the net new direct investment revealed that the manufacturing sector has been accounting for a persistently greater share of the total, whereas mining and smelting and petroleum show declines in both absolute and relative amounts, attributable in large part to political deterrents to new extractive investments in Latin America.

Similarly, in the important category of plant and equipment expenditures, the Committee demonstrated a pattern of growth in the manufacturing sector as compared to a pattern of decline in the previously substantial expenditure of the extractive industries. The table showing these comparisons in the COMAP report through 1961 has recently been brought through 1962 with estimates for 1963 and 1964 by the Office of Business Economics of the U.S. Department of Commerce.

Now, the COMAP people analyzed these figures as you will see from tables 2 and 3 and their analysis indicated that presumably for political or for whatever reasons, the extractive industries, petroleum and mining, and the public utilities which used to be the two large categories of U.S. investment in Latin America, are not flowing southward as they used to but at the same time there is the evidence of the beginning of a trend toward manufacturing, and you will see in table 2 how the manufacturing element has grown whereas mining and smelting and petroleum have declined.

Well, this in itself is a very interesting fact because it testifies to the diversification of the Latin American economies, the growth of manufacturing plants, presumably replacing imports, and basically it is a healthy thing for their economy because it means there is evidence of more purchasing power and broader distribution of goods.

You will see that table 3 is the sales of manufacturing affiliates of U.S. companies in Latin America, and they have gone up a billion and a half dollars, 66 percent, from 1957 to 1962 which is one of the encouraging signs, I believe, in this picture.

TABLE 2.—*Plant and equipment expenditures of direct foreign investments in Latin America, major industries, 1957–64*

[Millions of dollars]

Area and industry	1957	1958	1959	1960	1961 [1]	1962 [1]	1963 [2]	1964 [2]
Latin America, total [3]	1,687	1,269	1,003	750	795	840	900	834
Mining and smelting	216	221	147	78	87	95	100	90
Petroleum	1,039	577	449	340	306	319	315	310
Manufacturing	174	202	193	207	250	281	330	288
Trade	20	31	31	35	45	46	48	58
Other industries	238	238	183	90	107	99	107	88

[1] Revised.
[2] Estimated on the basis of company projections.
[3] Includes other Western Hemisphere.

NOTE.—Detail may not add to totals because of rounding.

Source: U.S. Department of Commerce, Office of Business Economics.

The growth in the manufacturing sector is of great significance and should be looked at in conjunction with the growth of the volume of sales of the U.S. direct investment manufacturing affiliates, which is disclosed by table 3.

TABLE 3.—*Sales of U.S. direct investment manufacturing affiliates in Latin America, 1957, 1959–62*

[Millions of dollars]

	1957	1959	1960	1961	1962
Latin America,[1] total	2,435	2,830	3,180	3,770	4,190
Argentina	385	426	696	895	865
Brazil	659	764	879	940	1,125
Mexico	643	751	770	850	1,020
Venezuela	268	364	360	390	400
Other	480	525	475	695	780

[1] Includes dependencies.

Source: U.S. Department of Commerce, Office of Business Economics.

Table 3 not only demonstrates the capacity of Latin American markets to absorb the rapidly growing output of American manufacturing plants, but it also gives an idea of the vast difference in the economies of the various Latin American countries. In 1962 sales of U.S. manufacturing affiliates totaled $4,190 billion, an increase of more than 70 percent over the 1957 figure of $2,435 billion, which compares very favorably with the increase of 17 percent shown by U.S. domestic sales of manufactured goods in the same period.

It is notable that four countries, Argentina, Brazil, Mexico, and Venezuela, represented a total of $3,410 billion, or 81 percent of the continental total, while the other 15 Latin American republics represented only $780 million, or 19 percent. Cuba is omitted.

THE COMAP RECOMMENDATIONS

Based on their analysis of the flow of U.S. private investment, the COMAP members made a series of recommendations which I will list here and which are presented in depth in the Committee report. In establishing the criteria for the recommendations the Committee emphasized that proposals regarding U.S. investment should not be made without reference also to the effect on local Latin American investors. Local investment is the bulk of Latin America's private investment and the recommendations were designed therefore to stimulate local investment as well as the flow of capital from the United States. It attached primary importance to the encouragement of those enterprises most likely to contribute new jobs and upgrading in local skills, both managerial and technological. It stressed that the individual parts of the total of its recommendations should be regarded as indispensable parts of a completely interrelated package. The recommendations are summarized as follows:

(*a*) *Local currency loans*

Provide assistance to meet the problem of currency devaluation by the creation of a substantial pool of local currency funds for loans to the private sector to be available to both U.S. and locally owned enterprises.

(*b*) *Taxation*

(1) Investment incentive credit: Provide an investment incentive tax credit to encourage U.S. private investment in countries of the

Western Hemisphere similar to the recent investment incentive credit to U.S. business.

(2) Tax certificate: Provide a tax certificate permitting a minimum return on capital of 5 percent after tax to be used by U.S. companies in selected enterprises as a credit against their U.S. income tax liability when such minimum return is not achieved.

(3) Tax sparing: To encourage and stimulate new investment in Latin America, amend U.S. tax law to provide for tax sparing where the host countries offer tax incentives as part of a program to attract new basic industries.

(4) Tax allowance for foreign exchange loss: Assist in meeting the problem of currency devaluation by allowing a tax deduction against current taxable income for losses due to currency devaluation.

(5) Alliance for Progress Corporation: Provide for a special type of U.S. corporation to hold investments in, or conduct operations on its own behalf, in the less-developed countries of the Western Hemisphere, and which would be allowed deferral of taxes on income until distributed to its shareholders so long as earnings were reinvested in the less-developed countries of the Western Hemisphere.

(6) U.S. income tax allowance for foreign investment losses:

A. Where stock becomes worthless.

B. Where stock is disposed of at a loss.

(*c*) *Specific and all-risk guarantees*

(1) Extension of investment guarantees to all less-developed countries of the Western Hemisphere.

(2) Broadened application of extended risk coverage.

(3) Extension of war risk coverage, including revolutions and insurrection, to also include damages resulting from riots and civil disturbances.

(4) Revision of present contract procedures and fee schedules to provide for a multirisk contract where an investor elects to take two or more specific-risk guarantees.

(5) Standardization and simplification of contract language.

(6) Increase in the authorized statutory limits of different kinds of guarantees.

(7) Recommendation that processing fee, if adopted, be credited against initial fee payable by investors entering into final contract.

(*d*) *Other methods of private investor participation*

Recommend in very selective cases the use of management contracts, cost-plus contracts, leasing arrangements, Government equity financing and consortia arrangements for multiproject developments. This applies especially where there is political sensitivity in industries closely associated with the public interest, such as electric power, transportation, and other utilities.

The followup on the recommendations: The committee recommendations summarized above were submitted to all appropriate departments and agencies of Government. They met with varying degrees of acceptance. The particular recommendation which attracted the most serious interest on the part of the executive departments was the investment incentive tax credit, and I therefore quote the full text of the COMAP recommendation in extenso:

(1) INVESTMENT INCENTIVE TAX CREDIT

In the Revenue Act of 1962 the principle of an investment incentive credit against a U.S. taxpayer's tax liability was provided to stimulate the economy through encouragement of investment in productive facilities. An extension of this principle, modified to meet the problem of stimulating investments in the less-developed countries of the Western Hemisphere, would, in the opinion of COMAP, assist as part of a tax incentive package to encourage an additional flow of private capital under the Alliance for Progress. However, the amount of credit and the mechanism of its application will have to be tailored to assist the U.S. investor in meeting the risks under today's political and economic atmosphere in Latin America. A credit of 7 percent as applied to U.S. domestic investments in productive facilities is effectively only approximately a 3½-percent credit after factoring in the reduction in the depreciation base of the new asset.

As an incentive toward achieving the objective under the Alliance for Progress of encouraging a substantial increase in the rate of direct private investment in the private sector of the less developed countries, it is suggested that Congress extend the principle of the investment incentive credit to investments under the Alliance for Progress. Because of the special problems in Latin America it is recommended that the credit be on the order of magnitude of at least 25 percent of all new and additional investment. All credits would, of course, apply as a reduction of the tax-cost basis of the investment for the computation of future gain or loss on the investment.

Having in mind the high degree of risk and the low rate of return prospects in relation to the risks under today's investment climate in the Latin American countries, the following table will serve to demonstrate the need for an investment incentive credit on the order of magnitude of 25 percent, and possibly as much as 50 percent, if new and additional U.S. private capital is to be encouraged to assume the risks of investment in Latin America.

I would like just to concentrate on one of those recommendations because that is the one that seems to have received the best acceptance both here on the Hill and in the administrative and executive departments. That is the suggestion that an investment tax incentive, tax credit, is given for companies investing in Latin America's underdeveloped countries which are defined by law or by regulation as underdeveloped.

This is an extension of the principle that we know of in other areas for an investment credit tax payment which was done in the Revenue Act of 1962 to encourage investment in productive facilities in this country. This is an extension of that into what has been declared by our Government more than once as a desirable end, that is, the building up of private investment in Latin America. And, therefore, also in this presentation this morning we present the recommendation as was made by COMAP.

We have had a considerably favorable reaction to this and I would hope that in the course of 1964 that this recommendation may be made law.

There is going to be a question as to what is the percentage. COMAP recommended 25 to 50 percent for the tax credit and the Treasury and others seem to feel that they could live with 30 percent investment tax credit. I don't know, Mr. Chairman, whether your committee is going to make legislative recommendations, although I am sure it will make policy recommendations, and I do wish to commend to you with great earnestness the 30-percent tax credit proposal as a practical and sound economic measure which will be bound to stimulate useful private investment, and I hope your committee will see fit to advance it vigorously.

We have a chart on that which I present to the committee.

(The chart referred to follows:)

Assumed actual rate of return per dollar of investment (percent)	Effective return assuming— 25 percent investment tax credit	50 percent investment tax credit	Investment tax credit necessary to achieve a 15 percent return
	Percent	*Percent*	*Percent*
1	1.3	2.0	93.3
2	2.7	4.0	86.7
3	4.0	6.0	80.0
4	5.3	8.0	73.3
5	6.7	10.0	66.7
6	8.0	12.0	60.0
7	9.3	14.0	53.3
8	10.7	16.0	46.7
9	12.0	18.0	40.0
10	13.3	20.0	33.3
11	14.7	22.0	26.7
12	16.0	24.0	20.0
13	17.3	26.0	13.3
14	18.7	28.0	6.7
15	20.0	30.0	-------------

NOTE.—It will be seen from the above table that a 25-percent investment credit will, in effect, improve the effective rate of return to the investor by ⅓ on the net investment after the credit. A 50-percent credit, and this would be necessary to attract the capital needed to achieve the goals of the Alliance if other tax recommendations are not adopted, will have the effect of doubling the actual return. Thus, in the case of a project where the actual return is only 5 percent after taxes (which is not unusual for new ventures in today's climate in Latin America) a 25-percent investment credit would increase the effective return to 6.7 percent and a 50-percent credit would increase the return to 10 percent.

WHAT ARE THE PROSPECTS FOR PRIVATE INVESTMENT IN LATIN AMERICA?

As the COMAP report correctly discerned, the growing and shifting population and the developing social needs of Latin America are working great changes in the economies of these countries. A notable change is the switch in emphasis of foreign investment to manufacturing and away from the traditional fields of public utilities and the petroleum and mining industries. The 70-percent growth in sales in Latin America of U.S. manufacturing affiliates from 1957 to 1962 is a remarkable rise, but even more impressive are the figures which COMAP developed showing extraordinarily high rates of increase in a number of key economic indicators such as lubricants, cement, paper, sulfuric acid, and automobile and bus registrations in various Latin American countries.

The development of entire new industries such as the banana industry in Ecuador and the fishmeal industry in Peru (each contributing around $100 million in export sales per year), new chemical, plastic, automotive, pharmaceutical, electronic, and machinery manufacturing facilities in Mexico, Argentina, Brazil, and other countries are great indicators of progress and growth. Each of these in turn has created satellite industries which supply raw materials, parts, and equipment. The fishing boat and nylon net industries in Peru, and the banana box industry in Ecuador, the automobile parts industries in Argentina and Brazil are examples.

You will be hearing from other witnesses with regard to current indications of real investment interest in Latin America on the part of sophisticated European, Canadian, and Japanese financiers, and particularly with regard to ADELA, which your colleague Senator Javits, a member of this committee, has done so much to bring into being, so I will confine my comments to investor attitudes here in the United States. Recent investment surveys have indicated a much

higher interest in Latin America, citing the recent notable shift in terms of trade caused by the rising prices of coffee, lead, zinc, sugar, copper, and other major Latin American export commodities.

While of course there are many persistent problems which plague the economic scene in various Latin American countries—depreciation of currencies, balance-of-payment deficits, defects of political leadership, et cetera—there are also some very promising manifestations in addition to rising prices for Latin American products and the growth figures I have mentioned in internal business activity.

One is the development, with cooperation of U.S. businessmen, of capital formation through investment funds. The case of the Brazilian fund CRECINO is notable. Founded in 1957 with a modest investment by the IBEC group of New York, this fund now has over 44,000 shareholders and total net asset value of $23 million despite the depreciation of the cruzeiro. This and other IBEC Latin American funds have more than 65,000 shareholders. The Bavaria group in Colombia has over 60,000 shareholders in a diversified industrial corporation. Five private investment banks, called Financieras, have come into being in Colombia and more are operating in other countries. Saving and loan associations and private low-cost housing cooperatives are being formed with technical assistance from U.S. businessmen and others—including even missionaries.

Meanwhile the Latin American business leaders are working more closely among themselves and with their fellow businessmen of the other Latin countries and the United States in a manner never known before in Latin America. The leading Latin American business organization—the Inter-American Council of Commerce and Production—has just elected its first North American president in over 20 years—George S. Moore, president of the First National City Bank. Over 200 business leaders of North, Central, and South America will assemble in Santiago, Chile, in March under Mr. Moore's leadership to plan cooperative efforts to promote private investment. The important subject which will come up for discussion at Santiago, as it did in the Inter-American Economic and Social Council meeting at São Paulo in November, is the question of freer access to U.S. markets for Latin American manufactured and semimanufactured goods—"trade, not aid." There are, according to a study by the National Planning Association, as much as $1 billion worth of potential exports which the Latin countries could sell here if they were put on a special basis—comparable to that which applies to Puerto Rico.

These are the men who have the management capacity and capital to make the wheels turn in Latin America and keep them turning.

Certainly, the more we study the problems involved in the flow of private investment to Latin America, the clearer it becomes that a strong, forward-looking local business community and business leadership in these countries is absolutely essential. The problems they and we face together are, I believe, capable of solution and in confronting them together in a cooperative manner, we can find the solutions faster and on a sounder basis.

I believe that the business communities of both the United States and Latin America can be grateful to your committee for this opportunity to explore the possibilities of greater investment in this vitally important part of the world.

Thank you.

Senator SPARKMAN. Thank you, Mr. Moore. If it is agreeable with the members of the committee, we will have Mr. Ray present his paper and then we will have questions directed to either or both.

Mr. RAY. Thank you, Mr. Chairman.

Senator SPARKMAN. We are glad to have you with us, Mr. Ray, and we are pleased to have you proceed in the presentation of your paper in the way that you see fit.

STATEMENT OF PHILIP A. RAY, ATTORNEY, CHAIRMAN, INTERNATIONAL BOND & SHARE, INC.

Mr. RAY. Thank you, Mr. Chairman.

I am pleased to have been invited here to discuss the responsibilities of the host governments and private capital in Latin America. I am well aware of the fine work your committee has done in this field, and I am confident this new undertaking will be informative and influential as well.

Since for formulation of capital into efficient producing or service units, whether in industry, farming, or distribution, whether in Latin America or any place else, is the best way to create jobs for people, the basic function of the host government is to create an environment hospitable to these formulations. The job supports and houses the man and his family, and enables him to make his appropriate contribution, through local or national taxes, to community betterments such as schools and roads. The man leaves, you might say, a part of his effort on the job in the form of profits which, combined with those generated by the capital in use, enables the unit to expand with population growth and thereby to provide more jobs.

When a man and his family become consumers they create still more jobs for others. And when they become savers beyond their consuming needs or desires, then they have a chance to recoup the share of the effort they left on the job, so to speak, by participating in capital formulation themselves, either indirectly through the loan or investment of their savings by the banks or other financial institutions in which they are deposited, or directly through the establishment of new enterprises or other manifestations of individual entrepreneurship, thus perfecting the cycle of modern capitalism.

Generally speaking, the governments in Latin America are neglecting these precepts and consequently, in one degree or another, the cycle fails to work for the mass of the people. Unemployment is 25 to 50 percent in some Latin American areas. Subsistence employment is the rule. A high percentage of the people are not significantly involved in the consuming, let alone the saving, world.

In examining some of the major failures of governments in Latin America, we should not forget that we ourselves are not immune from these troubles, but are only spared in degree by the differences in our early environment as a nation and by the tenacity of some of our original ideals concerning the role of government.

Most of the Latin American governments own and operate a huge and growing array of business enterprises, confiscated, condemned, or built originally out of tax revenues or Alliance for Progress aid or Export-Import Bank funds. Mexico owns over 500, including steel,

oil, chemicals, movies, and autos, and the story can be duplicated in substantial degree almost everywhere. Many of these projects are built for prestige purposes and nearly all are losers; hence, they cannot expand soundly. The state oil monopoly in Mexico loses steadily, despite having been acquired from private interests on the confiscation platter, and it pays no taxes. In Colombia there is a special tax to finance the losses of the state-owned steel mill. An official of the Central Bank in Venezuela told me 2 years ago that the annual losses from their Government-owned plants is $125 million annually. In Argentina, the Government still owns a galaxy of industries taken over in Peron's day. Largely obsolete, either technically or in fact, they have not been able to find buyers for many of them, and now they are threatening a new round of confiscation of the petroleum facilities and concessions that have made that country self-sufficient in petroleum products in the short span of 5 years. In Peru, the private oil properties are threatened similarly, the purchase price or a substantial part of it to be derived from increasing past royalties. In Bolivia, the confiscated tin mines, still not paid for, have gone steadily downhill despite direct U.S. aid. In Brazil, the so-called Goulart plan for the takeover of all privately owned utilities is strikingly similar to the spurious decree by which Castro confiscated $1 billion of private U.S. properties in Cuba. Some governments indeed have become regular capital traps, inviting foreign investors to come in with promises and incentives and then closing the confiscation door.

Inevitably, these things retard or prevent the formulation of new job-creating facilities in the private sector, due to the threat or the reality of competition from Government enterprises not playing the same game of profits and taxpaying and to the fear of outright confiscation.

Dire as the consequences are from the standpoint of economic development, they have an even deeper relevance to the cold war conflict. Marx erroneously believed that capitalism would fall of its own internal weaknesses, but he did say often that a high percentage of state proprietorship would help pave the road to communism. Through our aid, indeed through approving utterances from high places in our Government, we are helping to create an unstable halfway house along this road.

From the standpoint, however, of the host government in a less developed country, the usual rationale for this sort of thing is that, considering the lack of adequate indigenous private capital and the political unpopularity of foreign ownership, the government has to step in. This is a real, not an imaginary dilemma for these countries, but there is a road out and we can help construct it, by helping to finance the divestment of these enterprises into local private hands and giving special incentives to enable U.S.-owned enterprises there to sell a significant share of their stock to the local people also.

Latin American governments should first take a clear stand against further entry into the enterprise field, whether by condemnation or otherwise. Then, to reverse course, they should sell the equity stock of these state-owned enterprises to the local people, including the employees concerned, in small lots and on the installment plan and at prices relevant to their true value from a profit standpoint.

In view of the limited capital available in Latin America on any widespread and large-scale basis, such as this, however, it may be

assumed that private loan capital from the United States and other developed nations, backed by adequate full-risk guarantees from our Government, would be needed to finance these transactions. The host government should in turn indemnify the U.S. Government against loss under these guarantees. In my opinion, like U.S. guarantees should be made available to any wholly owned U.S. firm operating in Latin America and willing to offer a substantial portion of its equity to employees and local people. In this day and age, any wholly foreign owned enterprise, especially in prominent fields of endeavor, such as petroleum, is the first object of nationalistic impulses and Communist propaganda.

If our future aid did nothing more than to help finance these popular divestments and bring from U.S. industry the temporary management technology to put them on their feet, while also assisting our own industries there to take in local partners, so to speak, we would have made a great contribution to Latin American development.

In the field of taxation, there has been much discussion of late, and this is a risky subject, Mr. Chairman, about which to generalize. The Alliance for Progress has laid emphasis upon a kind of tax reform generally signifying higher and better collected income taxes from corporations and upper income groups. Yet, generally speaking, less developed nations need lower taxes, in order to spark private sector growth. The good taxpaying people of Latin America are, of course, benefited by better tax collection, but they are unjustly punished by higher taxes since, to the extent evasion exists, they now already pay a disproportionately higher tax than their counterparts in our country.

Higher taxes in Latin America will assuredly divert money from investment in private development into the hands of governments far more highly centralized, socialistic and authoritarian than ours and often bent upon control of the jobs and the ownership of the producing facilities. Latin American taxes are already a powerful adverse factor in Latin American development and exports in nearly all sectors of enterprise. Nearly 50 percent of the price of Brazilian coffee ready on the dock for shipment to the United States represents Brazilian tax, yet some now propose that we prop those prices and let the U.S. household pick up the tax; 70 percent of the oil coming out of the ground in Venezuela is paid to the Government in the nature of a tax, and the Venezuelan oil in world markets has to carry the burden of oil's financing of Government losses of which I have spoken, and be priced accordingly; Government taxes take 75 percent of the net profits of private mining operations in Chile, and so on.

The problem of taxation, which is highly discriminatory and often dealt out by executive decree tailored to fit political urgencies rather than by careful legislation, needs discussion and study beyond the scope of this paper. Suffice it to say that, essentially, Latin America needs less and less discriminatory taxes at the national level, a move which would spur private development and restrict the absolutist power of the host governments, permitting the gradual evolution of a local tax system to support local improvements. As they are levied and collected now, taxes are another factor that breaks the magic cycle of development.

Aside from these retarding effects of Latin American taxation, it is also important to realize that the extent of Government intrusion

into the business life of most parts of Latin America goes far beyond anything we experience under our own Federal controls. In many Latin American countries wages are fixed by decree, without legislative action. Rents are often controlled, frequently on a sporadic and discriminatory basis. Under the latest employees' profit-sharing decree in Mexico the Government goes to each company in each industry at the end of each profit year and determines how much of the year's profits should be allocated to the employees. Even in Mexico, which we tend to regard as the best developed and most stable republic in Latin America, the single-party structure gives the President unusually great decretal powers, the legislature has little independence and even the press is controlled to a substantial degree through presidential power over the tariff on the importation of pulp. Frequently, executive decrees in Latin America determine what the hours of work should be, what days should be taken off, and what the maximum and minimum wages should be. Such government intervention fractures the growth cycle at every stage of modern capitalism and prevents the natural play of the forces of growth in the marketplace.

Any chance for the cycle to perfect itself for the mass of people is also destroyed by the rampant inflation existing in most areas of Latin America.

In the 10 years, 1952–62, in Argentina the peso depreciated 1,000 percent vis-a-vis our own dollar, in Bolivia, 2,000 percent, in Chile 300 percent, in Brazil, 2,000 percent, and in 1963 the trend has been generally worse still. In some countries, Ecuador and Mexico to name two, the currency value per U.S. dollar has remained relatively the same as compared to the foregoing fantastic inflationary spirals. But study reveals that this stability may result from stabilizing grants and credit from the U.S. Government and financial institutions. Parenthetically, this false stability has itself contributed to the flight of capital from Latin America because it has at any particular moment enabled the citizens, there being no controls, to get their money out into stronger currencies without the loss of exchange values.

The uncontrolled inflation in many places in Latin America destroys the cycle of development because it destroys savings and, even more basically, destroys any incentive to save. In Bolivia, 100 bolivianos saved in 1955 have now lost over 90 percent of their purchasing power; and Argentinian peso or a Brazilian cruzeiro saved in 1955 now has less than 15 percent of the purchasing power it had when it was saved.

In the first 9 months of 1963 in Brazil the cost of living was up 51 percent, and in Chile, in the year ended October 1963, it had gone up 53 percent.

Inflation on this scale encourages capital flight and repels new foreign capital. Further, it drives remaining local capital into nonproductive investment such as land and other undeveloped or speculative assets, as offering the best protection against the devaluation of savings, rather than into facilities that will produce jobs. To avoid losses through the depreciation of the value of profits and to accrue adequate profits for expansion, industry, and agriculture must constantly raise prices, narrowing the number of available purchasers, while salaries and wages lag behind. It is almost idle to talk of plans

for the expansion of capital investment in productive facilities, or any kind of foreign assistance, in the presence of this kind of inflation. And it can be cured by the host government.

On the question of governmental responsibility in Latin America, much attention is paid to the question of political stability. Without any doubt, the political climate prevailing in much of Latin America at various times is the largest contributor to economic underdevelopment. Nevertheless, there is little we can do within the limits of government-to-government aid or diplomacy to affect the trend in any particular country. Indeed, it appears that our foreign aid has taken upon itself a kind of neodollar diplomacy. Thus we suspend aid in Peru, then restore it; flourish our fleet to help Bosch in the Dominican Republic, then go in with aid when he is seemingly secure, then deny it when he is overthrown; hesitatingly court Jagan in British Guiana with aid because, although a Communist, he was elected to his office; deny aid in Honduras when the junta is not to our liking; withdraw our aid in South Vietnam and then as suddenly restore it; first oppose and then submit to the Brazilian request for more Latin American authority over our Government aid programs; become discouraged with aid in Haiti while extolling its accomplishments of the moment in some other place. Thus our foreign aid tends to seem to me more an instrument of diplomacy than a true expression of our deep desire to help these peoples.

If our aid were directed largely toward the idea of assisting in the expansion of the private sector in host countries willing to adopt economic policies conducive to private development, we would, in my judgment, enjoy greater success in the elimination of poverty and instability, while at the same time helping to counter the Communist offensive. If this were the direction of things, the balance of our assistance could be mainly achieved through the impartial offices of the World Bank and the International Monetary Fund.

Since in Latin America, taken overall, approximately 50 percent of the populace is in agriculture as compared with 10 percent in our own country, the most pressing problem lies in the area of agrarian reform, especially since it is on this front that the Communists place their greatest reliance. The concept of subsistence farming of small plots, especially in the production of crops in which Latin America excels—wheat in Argentina, cotton in Mexico, sugarcane in Colombia, coffee in Brazil and elsewhere, and so forth, may have some political appeal but it makes economic nonsense. Hence, "land reform" often means collectivization a la Soviet. It is said that 5 percent of the people in Latin America own 70 percent of the farms. But in the United States, 10 percent own all of it.

But this is not to say that Latin American masses can suddenly be moved from the farm to the factory; nor that means to get capital into family-size farms should be neglected. The time has come to realize that the distinction between farm and factory has been largely obliterated. Indeed, the average successful farm, growing a large consumer product, needs as much or more capital per man-hour of labor as does a modern factory.

Latin American governments have too often drained the farms of capital through tax punishment, expropriation or the threat of it,

delivery of subsistence parcels to peasants without capital or know-how, and outright collectivization. These policies have reduced the capacity of the farms to support the occupants and to produce exports at prices meeting modern-world competitive conditions.

In Mexico today the Communists are striving to deny water to individually owned plots larger than 167 acres, involving crops requiring large capital outlays for machinery, land preparation, fertilization, and irrigation. Over 75 percent of the developed land of Mexico has been confiscated in the last 30 years and divided into smaller plots, some of the richest of which have become dust bowls while large acreages of previously undeveloped land lie untilled and unbroken. Throughout Latin America, by and large, great tracts of land are available for colonization, but what incentive exists when the already developed properties are ready to hand for confiscation under the banner of land reform, and there is no capital for new land development. In Mexico, again, and in other places also, land colonization proceeds at a slow pace because the host government will not grant a full title to him who will work his land, nor the right to sell or pass the product of his labor on to his sons, but instead moves thousands of families onto state-planned, state-owned collectivist farms.

In place of confiscation, collectivization, and subsistence farming, Latin American governments should turn to colonization, tax relief, and private cooperatives for purchasing and marketing.

I should like to mention four additional measures briefly. The first is exchange controls, suited in each case to the particular needs of countries willing to pursue a new road to capital formulation. Regardless of the climate for capital, Latin Americans will continue to send much of their capital abroad through habit, unless prevented by law. To those who complain, it can be said that the people of every major European country have endured severe capital controls at various times since the end of the war.

In our attempts to generate development in the Philippines following the war, as a part of the overall independence measures, we insisted upon tight exchange controls. There is no justification in our providing aid while the Latin Americans refuse to put their capital to work in their own homeland. Yet, on the other hand, it must be recognized that new direct foreign capital will not flow to Latin America unless, as to it, there are reasonable provisions permitting the foreign owners to repatriate income and capital.

Second, present guarantee concepts have to be entirely revised. U.S. investment in a country whose government offers adequate guarantees against nationalization and like risks and adopts other measures favorable to private operations should be accorded preferential treatment under U.S. guarantee programs. As noted earlier, special guarantee and credit programs should be available, covering all risks, in cases where an existing or future enterprise will create widespread local ownership of a substantial portion of the equity.

A third essential to the creation of an improved domestic investment climate in Latin America lies in a more rapid economic integration of the Latin American Republics through the Latin American Free Trade Association and the Central American Common Market and, hopefully, even more comprehensive mechanisms. Inter-Latin

American trade is a mere 4 percent of her total world exports whereas, by comparison, 60 percent of the total world trade of the Common Market Six was conducted among themselves even prior to their integration. The rapid elimination of tariff, quota, and other barriers now existing between the Republics of Latin America would generate substantial expanded trade, enlarged markets, and new investments in Latin America.

I might add that the United States should not become a full member because this would tend to stimulate our exports to Latin America rather than new investment in Latin America, but we can take the leadership in promoting the Latin American Common Market idea and in helping Latin America to achieve better access to the markets of the developed world, a concept covered more fully by Mr. Moore, and I endorse everything he said.

The United States cannot and should not become a part of a hemispheric free trade area because this would further retard the flow of U.S. private capital into those countries. But the United States can take the leadership in promoting the Latin American Common Market idea and in helping Latin America to achieve better access to the markets of the developed world, including the United States. But, after all, if the Latin Americans will not open their markets to each other, it is difficult to expect third nations to open theirs to the Latin Americans. Such expedients as the proposed coffee agreement will only retard the growth of sound export industries in Latin America.

Finally, if Latin American nations will forego tax collections to stimulate foreign investment, we should exercise an equal forbearance. This concept has been embodied in several measures before this Congress and one measure, allowing a 30-percent tax reduction to those who will invest in Latin America, is still pending before the Congress.

In recent years there has been a huge flight of capital from Latin America. No one knows the amount. The figures are not easy to come by. A recent study concluded that there had been a net $1 billion flight of private capital from Brazil alone since the Alliance for Progress began. Estimates have been made that there are $10 to $15 billion of Latin American private capital resting in bank accounts overseas, not to mention portfolio investments. In an 8-month test period in 1962 Vision magazine found that Latin American deposits in New York banks increased 70 to 80 percent while like deposits from the rest of the world increased only 18 percent.

At the same time, the Alliance for Progress goals for the new flow of private U.S. capital to Latin America—$300 million annually—have fallen discouragingly short. In calendar year 1962, the first full year of the Alliance for Progress, we saw a negative flow of direct investment from the United States to Latin America, an actual repatriation of capital, in the amount of $32 million. The flow to Latin America went from a positive figure of $173 million in 1961 to this negative one of $32 million in 1962, or a reversal of $205 million in the first year of the Alliance for Progress.

This trend still continues, the comparable figure for the first three quarters of calendar year 1963 being a minus $38 million. In fact, some small gain in the first two quarters of 1963 was wiped out by the repatriation of $42 million of capital in the third quarter, accord-

ing to figures just released by Commerce. In some degree, the availability of new government-to-government aid offerings seems to have harshened the environment for private enterprises in these places.

Of course, it is not to be forgotten that U.S. industry is currently making over $600 million in annual new investments in plant and equipment in Latin America from local borrowings and from profits and reserves derived from their existing $8 billion of direct investment there, providing new and significant contributions to employment and growth in Latin America.

The flight of local capital from Latin America, coupled with the regression of our own private investment capital from these areas, is in major part a tragic consequence of unfavorable host government policies. In part also, of course, it is the consequence of the destruction of private property rights in Cuba and the rapid rise in the Communists' fortunes in their campaign against all private investment and private enterprise.

The trend toward Communist solutions in Latin America can only be reversed if the host governments will assist in adopting a climate agreeable to the creation of productive and employing units in all fields of private endeavor. Foremost among the measures needed are some that I have mentioned. If they were to be adopted, much of the private capital flight from Latin America would cease, much of the capital resting overseas would return, and a new flow of private capital from the United States and other industrialized capital-exporting nations of the Western World would be generated.

An ultimate ingredient in any sound plan of assistance by the United States to those republics of Latin America that will meet us half way in the creation of the environment needed for the job is the development in our own country of a purpose to export the best features of our modern widely shared capital system, founded upon a partnership between people. Through such a purpose, jointly entertained by the developed nations and those of the less developed world, we could help perfect the cycle of modern capitalism for the mass of the people in Latin America.

Thank you.

Senator SPARKMAN. Thank you very much, Mr. Ray. That is a very interesting and informative and helpful paper.

Mrs. Griffiths, do you have quetions for either or both?

Representative GRIFFITHS. I would like to clarify one point. You have mentioned as did the chairman's quotation from reports of the Economic Commission for Latin America, that there has been a downturn in the past 2 years in the amount of foreign capital going into Latin America. You gentlemen are not suggesting that the Alliance for Progress itself has caused the flight of capital out of Latin America, are you?

Mr. RAY. No. I am not suggesting that precisely. At some times and at some places I think it is evident that the availability of large amounts of government-to-government aid creates a different attitude on the part of some governments toward the private sector. And to that extent it harshens the environment of private capital development. But I do not say that one can categorically trace this regression that has occurred, that has taken place essentially at the same time as the growth in the Alliance fund, is causal in its overall sense.

Representative GRIFFITHS. And your answer, Mr. Moore?

Mr. MOORE. No. I wouldn't say that the existence of the Alliance for Progress has caused a flight of capital. I don't doubt for a minute the validity of the figures that Mr. Ray gave you. I would say that there have been certain emphasis emanating from institutions concerned with the philosophy of the Alliance for Progress which have not been particularly encouraging to private investment. Specifically, an example would be the United Nations Economic Commission for Latin America known as ECLA with its headquarters in Santiago, Chile, and which up to recently was under the management of its executive secretary, Mr. Raul Prebisch. Dr. Prebisch has since become director general of the Latin American Institute for Social and Economic Planning. He was a major architect of the Alliance and is a man of tremendous influence in the economic policies of Latin American governments. He has taken some very strong antiprivate investment positions and has stated that he believes in aspects of the very emphasis on state ownership—some call it socialization—which Mr. Ray's excellent statement has demonstrated to have been such a failure.

I would say that there are elements in the Alliance for Progress such as the role of ECLA and Dr. Prebisch which would give pause to an investor. Whether we can say it is a cause, or is simply post hoc ergo propter hoc, I don't know, but I think Mr. Ray's figures are correct—investment has declined since the Alliance.

Representative GRIFFITHS. That is, you think that an investor wouldn't invest in Brazil at least to some extent because of the Alliance for Progress making it untenable, is that right?

Mr. MOORE. No. I would say exactly the way I tried to put it, that the state ownership doctrines that are very prominent on the part of certain leading elements of the Alliance could discourage a private investor, either in his own country or a country abroad.

Representative GRIFFITHS. Would you not consider that the very thing which made us feel that it was necessary to do something, such as creating the Alliance for Progress; namely, the fall of Cuba into Communist hands, prompted others in Latin America to decide they had better make their money safe by moving it to a safe country?

Mr. MOORE. Yes. I agree with that. I think that not only Latin Americans but the decline in U.S. investment in Latin America was influenced very strongly by the Communist takeover in Cuba on January 1, 1959, and the expropriation of $1 billion of U.S. private investment plus probably 10 times as much of Cuban private investment. Cuba was a very discouraging factor to investment.

In fact, in preparing a paper for the Inter-American Development Bank we made a survey of the professional investment community in New York, Philadelphia, and Boston on that subject in 1962 and asked the professional investors what they thought the outlook for private investment in Latin America was, and I think 22 or 24 investment bankers and institutional investors were interviewed. I would say that certainly two-thirds of them started out with some such statement as, "Any investor who would put money into Latin America until we have gotten rid of Castro needs a mental examination."

The shadow of Castro and the so-called Goulart plan which Mr. Ray referred to are terrible obstacles. In fact, when you think of those things it is a wonder that there has been as much investment as there has been.

Representative GRIFFITHS. And one of these manifestations has been additional expropriation of American investment.

Mr. MOORE. Not so very many of them. Brazil is the primary one and there have been what might be called negotiated expropriations of utilities in Mexico, Argentina, and Colombia. There is a second—I don't know whether you would call it expropriation or negotiated acquisition under discussion in the oil industry in Peru. I wouldn't apply this to all of the countries.

Representative GRIFFITHS. Rapid inflation in most of these countries also has been one of the deterring factors of American investment, has it not?

Mr. MOORE. Unquestionably.

Representative GRIFFITHS. So it really isn't all due to the Alliance for Progress.

Mr. MOORE. No. I don't think either Mr. Ray or I have said that.

Representative GRIFFITHS. Well, I think it should be made quite clear because I do think other factors—the experience in Cuba, inflation in Brazil especially—have been primary causes for the reluctance of private capital. I would not want to leave the impression that you felt the Alliance for Progress was primarily responsible.

Now I would like to ask Mr. Ray, how do you propose, for instance, that Argentina get rid of that railroad and put it into the hands of private investors?

Mr. RAY. Well, I think you have to assume, first, that the railroad, which incidentally now charges something equivalent to 3 cents U.S. money for a ride of 70 kilometers, would have to—if you assume a genuine attempt to put those things into the private sector and to increase private capital markets, then first you have to assess its true earning capaciy and get some sort of a value based on that, and then you have to find people who will buy the stock. And as I said in my statement, if you were—if those governments that would do this sort of thing, and I am sure they all wouldn't all at one time, would not be able to find within their country enough capital in the hands of widespread ownership to finance the acquisition of the stock of the company. Once it was reorganized and, say, a management team went down there as part of our AID program to find out what this railroad needed and how it could be placed on a private basis—accordingly, in view of the capital lack in the hands of the mass of people and in view of our desire to create capitalists, we would have to finance the sale of that equity stock. This is a rather simple thing to do. It is done in Latin America quite frequently now, and I could give you some illustrations of where it has succeeded.

You offer the thing in small lots to people on a first-come basis on the installment plan with little or no interest, and private banks in the United States then, of course, have to finance that distribution, and that, of course, they could do by having back of it a Government guarantee.

Representative GRIFFITHS. Do you mean by that that then once our own private banks stepped in to do this, we are going to have to guarantee them that they not lose any money because, of course, they would worry for fear that their next regime in Argentina, for instance, would confiscate the whole thing again?

Mr. RAY. Well, the reason we have to step in is that if the Government parts with this asset to the people and they pay us for it over a long period of time, we are merely a financier in the meantime.

Representative GRIFFITHS. That is the first one. Now, second, you are going to have to guarantee somebody that it is not going to be reconfiscated——

Mr. RAY. That is right.

Representative GRIFFITHS (continuing). By a new government; aren't you? So you are going to have to step in twice, aren't you?

Mr. RAY. Well, part of the original guarantee package would be a guarantee by our Government against future political risks such as confiscation which we would only do, as we do under our present guarantee programs, if the host government would cosign that guarantee and, in effect, indemnify the U.S. Government. But again I say you would have to offer this way out of this dilemma and put it into effect in areas where you had reasonable assurances in the form of indemnifications from the host government that it was not going to reoccur.

Now, in my opinion if some such proposal were made, it would be avidly supported in Latin America. In other words, you wouldn't be walking into a vacuum. You would be walking into a place where popular support for it would be very great.

I have asked this question in nearly every country in Latin America and I am convinced that the people in Latin America feel that these things should be in the private sector and are hungry for a plan whereby we could assist them to do it, but they find it difficult to do themselves because they don't have the capital in the hands of the people whom they want to have the ownership.

We don't want to put it in the hands of a few wealthy people. So we have to think of a plan to diversify the ownership.

Representative GRIFFITHS. What do you think the cost of this plan would be?

Mr. RAY. Well, I think frankly the plan would not be costly at all. I think in the end it wouldn't cost us anything. I think the World War II victory loan figures are an analogy. For example, if you were making toy balloons and we went to war and they said to you: "Well, why don't you make gas masks?" you would say: "Well, how can I retool my plant to make gas masks when they may not be used in the war or war may be over next week?"

So we generated a victory loan plan which was a Government guarantee and you went to the bank and got some money backed by that guarantee up to 85 percent of the loan so the banker had a risk in it, and you retooled your plant into gas masks.

Now, we operated that program throughout World War II at a small interest charge for the guarantee and we never lost a cent.

Now, we could offer those same guarantees to put private industry back on its feet in Latin America, and in my opinion we wouldn't lose either.

Representative GRIFFITHS. What chance do you think you would have, for instance, in getting the Government of Argentina to divest itself of that railroad?

Mr. RAY. Well, it is interesting to contemplate what might happen there. I talked with a man named Mazzaferi——

Representative GRIFFITHS. What is his position?

Mr. RAY. He was president of an outfit called Dinie.

Representative GRIFFITHS. Does he have any connection with the Government of Argentina?

Mr. RAY. Yes. It was the Government corporation that owned that railroad.

Representative GRIFFITHS. I see.

Mr. RAY. And also owned a whole string of industries in every field, farms—confiscated by Peron—newspapers, buildings, everything. And I sat and talked with him for 2 hours and listened to him tell me his problems.

He said: "We are trying to get rid of these industries. We know they are a drain on the budget."

I talked with another man, Otero Monsegur, at that time head of—Deputy Head of the Central Bank. He showed me some fantastic figures of what these industries were losing. But Mazzaferi told me his problem was the industries were rundown, there wasn't enough technology around in the country to put them back on their feet. Whom do they sell them to?

I said: "What are you doing in practical terms." He said: "I will give you an illustration." He named a small shipping company and said: "What we did was sell 10 percent of that stock for a small sum to some people that know something about the shipping business and they went on the board of directors and there is one we think we are going to get rid of."

But, again, I say to do it on a mass basis you are not going to find the capital in the kind of hands we want to put it in.

Representative GRIFFITHS. So that in the end it would be a terribly difficult thing to do, wouldn't it?

Mr. RAY. Yes, indeed, it would be a terribly difficult thing.

Representative GRIFFITHS. And the people who are going to vote on this in their legislative bodies, or a dictator, even a dictator, would get quite nervous about it, wouldn't they? I mean one of the first things any government would do would be to lay off quite a few people, wouldn't they? Raise the fares and other such things? So that, politically, you are asking him to make a tremendous decision.

Now, not that I don't think it would be a great decision, but I think you meet untold difficulties, don't you? Isn't that really one of the problems?

Mr. RAY. Well, of course, it is one of the problems but I believe I am correct in saying that the great mass of Latin American people would welcome such a plan avidly and after all, the people in the governments—whether they are dictatorships or juntas of what-have-you—are, in the last analysis, sensitive to the popular reaction to things. And I am as convinced as I am sitting here that while you are quite correct, this would be difficult, if we made it a purpose of ours, we would find hands stretching out down there anxious to try to make it work with us.

Representative GRIFFITHS. Now, isn't this tremendous tax of these extractive industries really because they are foreign owned?

Mr. RAY. Yes. This is another reason why I suggest that we should have a plan to popularize the ownership of the equity of large com-

panies. Anybody who now owns 100 percent of something in Latin America needs some help to dig out. He could go around door to door and sell some of his stock on the installment plan. Kaiser has done that in Brazil. And the Union Carbide recently did it in Mexico. But if you start doing it on a mass scale, you need some sort of interim banking to finance the installment payments.

Representative GRIFFITHS. Now, isn't one of the problems of capital formulation, though, the fact that you really can't be too smart today to save money in Brazil? It is losing its value every minute, isn't it?

Mr. RAY. Sure. I tried to say as clearly as I could that unless governments will tackle this problem of inflation, there is really very little you can do through the Alliance for Progress, investment incentives, or anything of that character. You will not create capitalists. The Communists are down there busy trying to create Communists and our job ought to be to try to create mass capitalists. You don't do that with this inflation.

Representative GRIFFITHS. I enjoyed both your testimony and Mr. Moore's. Thank you.

Senator SPARKMAN. Mr. Curtis?

Representative CURTIS. I want to thank you again for your testimony. It was excellent. I just wish I knew some way of getting just a little bit of this testimony to the American people. I despair of that.

I was very interested, Mr. Moore, in your comments on the manner in which we seem to denigrate the Latin American businessman. But what disturbs me is the manner in which we denigrate our own businessmen who have been in Latin America.

I recall attending a meeting in my own community of St. Louis of exchange students at Washington University and listening to some students who were from various Latin American countries repeat denigration of businessmen in their own countries. To my surprise, professors at that university then took what they said as gospel truth without interrogating them further to find out if indeed this was so. I am very much concerned lest our business people do use improper business methods in Latin America or anywhere, including our own country, but I have found, in trying to get into this in some depth, that if the American people only knew the business practices that the overwhelming majority of our businessmen employ in Latin America, it would be a source of great pride and considerable gratification to them.

Now, not only do professors in our universities show this lack of scholarship, but it seems that when our people in Government, the news media, and the press, find anything that tends to denigrate the American system they are willing to play it up.

Now, in one sense that is healthy. We certainly don't want to be complacent. We certainly want to improve our system, and correct improprieties when they do exist. But this has gotten to such a point, that in my judgment it can only be termed a "psychopathic disease of masochism."

Have you experienced that problem in the United States with the attitude of the general public, our own public, toward American businessmen doing business abroad? I am not now talking about what you brought up, with which I couldn't agree more, because I, too, have run into what I thought were some splendid Latin American busi-

nessmen. But will you comment on my remarks, because to me this is almost the heart of this problem.

Mr. MOORE. I happen to share your feeling very, very strongly on that subject, particularly in the academic community, and a good many of the businessmen I know in this country who are concerned with this matter, including myself, and I know Mr. Ray, spend as much time as we can at the universities and we find exactly what you said, sir, that the faculty members there adopt the ideas denigrating American business abroad and the conduct of American business abroad.

I would like to say that I have spent many years in the Latin American countries, particularly in the western coast countries. I don't know Central America or Brazil as well as I know the others. And I have never known any responsible American concern to conduct itself in a manner that would fit the descriptions that you hear from our own academic and media editors, and so forth, in talking about them.

I can even recall 2 years ago a very high official of this Government writing me a letter recommending a book in which these charges were made, and I wrote to both him and to the author of the book and asked them what proofs they had of any such conduct, and got no reply except something to the effect that everybody knows this sort of thing.

I don't doubt, Congressman, that in the 19th century, in the days of freebooters, and so forth, when codes of business all over the world, the British and European and our own, were dog-eat-dog, and so forth, that conduct of that kind took place not only in Latin America but everywhere else.

Representative CURTIS. Including our own country.

Mr. MOORE. Including very much some of our country. I would say this: that our company has been, for example, in Peru for 109 years and we are in business in 27 countries of the world and 30 States of this Union. As far as we are concerned, we find the public morality—it takes two to make a corrupt bargain—the public morality of that country is high. I would put it this way: We know of none higher.

I wish I could understand this attitude—you mentioned that it was a psychological thing. I wish I thought that is all it was but I am afraid there are winds of doctrine behind it. Some 2 or 3 years ago a book was published in this country called "The Shark and the Sardines." This book was written or alleged to have been written by Juan Jose Arevalo, a former President of Guatemala. In this book Arevalo made charge after false charge against the American companies in Guatemala and other Latin American countries, and I did not—I followed this book very carefully. In fact, I wrote letters to newspapers, and so forth, about it. I couldn't find a book reviewer in any of our newspapers and magazines of general circulation who pointed out the falsehoods in this book.

My own daughter at college had the book recommended by her professor as an example of the terrible conduct of American business. It was one of these books that charged that Wall Street dominated the State Department and that American companies were all corrupt.

A good book, taking a different point of view, was written by a man named Thomas Aitken, called "A Foreign Policy for American

Business," and in that book Aitken stood up for the morality of American business abroad, but the book wasn't widely reviewed. I don't believe it had a third of the sales, certainly in campus or intellectual circles, as did this other book.

Representative CURTIS. I want to say this: that I believe that the Communist International is trying to promote this kind of thinking, and to that extent, there are some plans behind it. I think my observation that it is a psychopathic condition of the American public bordering on masochism may be stimulated by these endeavors, but it is really unrelated to that.

I think more than anything it is a shocking decline of scholarship in the United States. As a member of the board of trustees of one of our distinguished colleges, I feel a deep responsibility to try to do something about it, but it is difficult to know what should be done, other than going right back to fundamentals of scholarship. We must seek the truth in these things and get away from these generalities. If there are instances of our business people following improper techniques, we want to know about them. We want to correct them if we can. Above all, we want to know about them.

But it is equally wrong to promote false charges. In fact, I feel that this is the difficulty we are experiencing in our own country as far as the private enterprise system is concerned, because I see this similar smear attack here as well.

I want to bring this up because, in typical fashion, there are apparently few members of the press in the room. This is the kind of attendance a hearing of this nature receives from the news media. It will go largely unreported, even though the material you gentlemen have given us is material in depth. It was presented fairly and with an opportunity for those including myself, who may disagree with you to bring out their points.

On the floor of the House yesterday during a discussion—debate, if you please—of the very serious Panamanian situation, I made the remark that the tragedy was that what was said on the floor of the House, subject to rebuttal by those who disagreed, was not what we were reading in the newspapers. As far as the American people are concerned, they still aren't going to get the facts as best we can get at them or the arguments pro and con involving the situation in Panama. But what they will get is a continued denigration of the United States rather than a defense, and where there is a defense I regard it as not being put on a very high intellectual plane.

Sometimes it is said that it is just because the United States is there.

Well, that isn't the argument behind the Panamanian policy, and I suggest those who advance that argument are doing a disservice to the United States. Let's get to the fundamentals.

Mr. MOORE. Yes, sir.

Representative CURTIS. It was brought out on the floor of the House that a very fine study had been made by a subcommittee of the Foreign Affairs Committee of the House, by one of Senator Sparkman's colleagues, who was chairman of that subcommittee 2 or 3 years ago.

Mr. MOORE. I am familiar with that.

Representative CURTIS. It was an excellent——

Mr. MOORE. Congressman Selden's study, and it was excellent. I wish we had listened to some of the things he had said.

Representative CURTIS. But the point is that this study will remain essentially unreported to the people of this country today. Our State Department officials made no reference to it. They continually went on talking, disregarding the facts and arguments. They didn't even bother to criticize the report if they disagreed. The net result is that this situation is going to become worse, not better. I might say—and I am sorry Mrs. Griffiths isn't here—that I know you gentlemen didn't make the charge that things had become worse because of the Alliance for Progress, but I will make that charge myself, because I have made it before. They have moved in the Government capital, into what was supposed to have been a balanced program, and have deterred development in the private sector. Probably—in fact, I am sure—we are worse off than we were before.

Now, one request, Mr. Moore. As Chairman of the Inter-American Council, could you submit for the record a series of examples of the diversified industrial ventures by U.S. capital in Latin America? It would be useful to show how U.S. capital is being invested outside the usual channels you mentioned, such as petroleum, by groups such as IBEC, DELTEC, Creole Investment, and some others. You have done that to some degree. I wonder if you could expand upon that for the record.

Mr. MOORE. I would be delighted, and if I may ask you, if I can use the assistance of my colleagues in the Council——

Representative CURTIS. Yes.

Mr. MOORE. We would be delighted to do that. We might have a little material.

If I could mention it, Congressman, I am thoroughly delighted to hear you talk as you have about the public treatment of the subject of American business presence, if you will, in Latin America. We have some material in regard to that. Quite apart from these charges we hear over and over again against American enterprise, there is the additional factor of the picture of the United States which is given in Latin America by the human beings, the men and women, who represent American concerns down there. There are far more of them, happily, than there are Government personnel down there. And in many cases the Latin American, particularly in the back country outside the capitals, knows the United States more through the Singer sewing machine salesman or through the reliability of an American product than he does through the Embassy or the USIA, and I would like to take this occasion to just mention that.

We have a little material like that in our Council and we find that quite apart from this idea of the ugly American which is being spread with regard to the American businessman, American names like Coca-Cola and Chesterfield and Reader's Digest and Quaker Oats are symbols not only of an honest product for an honest price in those countries and full weight for your money, but of an American salesman who will go down there, learn the language, frequently go as young men and marry into the local community, and represent their country as well as their company all the time they are there. And I just want to take this occasion to speak a word for those same men who are subject to the same kind of criticism from the same uninformed, to put it

charitably, sources that we have been talking about, and if I could add some material on that line I would be delighted to do so.

Representative CURTIS. I would appreciate your adding that material.

I have just a comment. Isn't it strange how little reading the public does? To them the term "Ugly American," which is the title of this book, does not imply a hero, as he was in the book.

Mr. MOORE. Correct.

Representative CURTIS. How many people in this country realize that?

Mr. MOORE. It has been turned around.

Representative CURTIS. It has been turned completely around, which is so regrettable and so typical.

One other point I would like to develop further. I read a very interesting booklet by Ambassador Nehru of India which has just recently been published and circulated among the Congressmen. It is a very interesting and worthwhile document, I believe. In it Mr. Nehru makes a point which I have heard all too many of our prophetic and honest Americans make. He says that private enterprise cannot provide infrastructures like schools and roads in these undeveloped areas. My comment is how unobserving Ambassador Nehru and those of that school are in accepting that line of thinking. As history shows, private enterprise has to provide infrastructures, and it certainly does exactly that. It does build roads. It does build schools. For example, the Creole Petroleum Co.'s efforts in the field provide not only adult education, but primary education so that the children of their employees can gain an education.

I am familiar, too, with the operations of Aramco in Arabia where the schools have largely been built by the industry involved because it is a necessary part of good personnel practices.

Unless I am wrong—and I can be wrong in what I have said because my observations are based upon a few specifics—has your group investigated whether or not it is correct, that when an American enterprise or any enterprise moves into an area, they have to and do provide this kind of infrastructure?

Mr. MOORE. Mr. Curtis, when Mr. Ray was in Government he had something to do, as I recall it, with the Government assistance that was rendered to three American companies who formed what I call a very genuine alliance for progress in the construction of the great new Toquepala copper mine in southern Peru. In that place alone, plus the Marcona Mining Co., which is the Utah Construction Co., group, they have built miles of paved highway, grammar schools, high schools, parochial schools, Catholic—and in the case of the Utah Construction Co., a Mormon temple, if you will—a port, deepwater port, and created a whole new community with all these facilities which is infrastructural, as I understand the nature, with entirely private capital, with Eximbank loans, but those have to be paid back, but nevertheless Mr. Nehru would get quite a surprise if he could see what they put on a desert where literally before they came there was not an insect—nothing to support life. Now there are 3,000 or 4,000 people there with kids coming up to this country for training.

Representative CURTIS. It isn't only for Ambassador Nehru that I would like to see this study conducted. I would like some of our

American policymakers to do a little homework in this area since they reach conclusions which are so vital to our country and so vital to world peace. In my judgment, it is this kind of pursuit, particularly the pursuit of truth, that will lead to ultimate peace based on justice, I hope, and certainly not on this kind of denigration that seems to be going on.

I have a few specific questions here. One with Mr. Ray.

You suggest in regard to guarantees that those nations which establish adequate protection against expropriation be granted preferential treatment under the U.S. guarantee programs. I thought we had our insurance premiums based on the risk involved. I must be in error, though, because if they are based upon the risk involved, as a country improves in protecting against this risk—as the premium that the private concern would be paying for insurance against expropriation, etc.—the premium would be lessened. Would you comment? Am I in error, or do you think we need to go further? Would you just discuss it a bit for us?

Mr. Ray. Well, at the present time, Mr. Curtis, the guarantee program suffers from two difficulties in my mind. There are more, I am sure, but in the first place, it is not applicable in a number of countries. It is not applicable where a majority of the people live in Latin America, even today, in the case of nationalization. Mexico, Brazil, Chile—to name three—have not signed the necessary thing. And the presence of substantial government-to-government aid offers an easy alternative to not signing a guarantee agreement. So that there is no incentive that works now because——

Representative Curtis. Well, let me dwell on that. Maybe this is the key. Why isn't there a relationship between the amount of the premium paid for the insurance and the risk? Maybe they are just given flat premiums wherever they are. Now, if that is so, then the point is very well taken. I am shocked to find out that we didn't set this up in the beginning on a country-by-country basis and let the premium reflect the risk.

Mr. Ray. My impression has been that it does not.

Representative Curtis. Well, then, this needs looking into, and I am not surprised. My heavens, I despair of the political bureaucracy and their understanding and appreciation of the private enterprise system. Apparently they have never studied it, don't understand it, and, not understanding it, make decisions that are in conflict with the furtherance of it. This is shown by your answer right here about relating insurance premiums to risk. It would have been such a logical thing for anyone who was familiar with the system to do.

Well, I will look into it. I may be jumping to conclusions unfairly.

Mr. Ray. That was the point I was trying to get at there exactly, that to the extent that a host government will adopt these environmental factors, to that extent the risk is hereby reduced, and it should be reflected in the rates.

Representative Curtis. Of course it should, and this is the way. This is the incentive that would encourage countries to do this. Also, it would be automatic and would not require the decisions of political bureaucrats, who are not well versed in the area, to allow the marketplace to enter in.

Senator Sparkman. I may point out that tomorrow we have a witness on this very subject.

Representative CURTIS. I have one other thing for the record. I am not sure whether I am taking your name in vain, John, but I think you have a bill to permit our savings and loan companies, or domestic companies, to invest in savings and loan institutions abroad. I have, and——

Senator SPARKMAN. Yes. Same bill.

Representative CURTIS. Same bill. I don't know why we can't get this moving forward. Here is one of the most natural ways of moving the private sector down there instead of Government sector. When this subcommittee was in Buenos Aires, I was shocked to find out that our private savings and loan companies, or rather people who are interested in them—unfortunately it couldn't be our own savings and loan firms under the restrictions that we are seeking to amend in our law—couldn't invest down there. They had to set up their own separately. But even those who were willing to do it, found out that U.S. Government capital was available if they would set up a nonprofit savings and loan institution. Of course, to me, a nonprofit organization is one that has poor accounting methods because, economically, you have to pay for capital and if you are smart, you are going to put that in as a cost. But, at any rate, this was a specific example, I found, where Government money was a specific deterrent to what would have otherwise developed through the private sector.

Now, again putting in one of my own plugs——

Senator SPARKMAN. I would like to suggest Mr. Curtis, you might want to put a copy of that bill in the record.

Representative CURTIS. Yes. Along with the statement I made when I introduced it and possibly your statement, if you made one, when you introduced yours, because I think it does fit in here.

(The documents referred to are as follows:)

[H.R. 6203, 88th Cong., 1st sess.]

(Mr. Curtis introduced the following bill; which was referred to the Committee on Banking and Currency)

A BILL To authorize the establishment of an International Home Loan Bank to assist in the development of savings associations and building societies in countries where they do not now exist in order to accomplish improved living standards, to increase employment, and to better social and political conditions through facilities for savings and homeownership for the millions of people of modest but stable earning capacity

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "International Home Loan Bank Act".

DEFINITIONS

SEC. 2. As used in this Act—

(a) The term "Bank" means the International Home Loan Bank incorporated under this Act.

(b) The term "Board" means the Federal Home Loan Bank Board.

(c) The term "member", except where used with respect to a member of a Federal home loan bank, means a member of the Bank.

(d) The term "stock" means capital stock of the Bank.

(e) The term "foreign mutual thrift and home-financing institution" means an institution as to which there is outstanding a determination by the Bank that such institution (1) is a mutual institution, (2) is primarily engaged in the receipt of savings and the financing of homes, and (3) does not have in the United States, or in any place subject to the jurisdiction of the United States, any office, agency, or agent for the receipt of savings or the making of loans.

(f) The term "foreign home loan bank" means an institution as to which there is outstanding a determination by the Bank that such institution (1) is organized or incorporated under the laws of a foreign country, and (2) is pri-

marily engaged in making loans or advances to, or investing in, mutual institutions which are organized or incorporated under the laws of such country for the purpose of receiving savings and the financing of homes in such country.

INTERNATIONAL HOME LOAN BANK

SEC. 3. The Board is hereby authorized and directed to provide without regard to any other provision of law, except section 4 of the Bretton Woods Agreement Act, as amended, and provisions hereafter enacted expressly in limitation of this sentence and except as otherwise provided by the Board, for the incorporation, organization, operation, regulation, and examination of a corporation to be known as the International Home Loan Bank, which shall be under the supervision of the Board and shall be operated under the direction of a board of directors as hereinafter set forth. The Board is hereby authorized to prescribe such bylaws, rules, and regulations as it may deem necessary or appropriate to carry out the purposes or provisions of this Act, and any function of the Board under this Act may be exercised by regulations or otherwise. The Board shall be guided by the Department of State on those two aspects of its operations affecting foreign policy in order that the actions taken by the International Home Loan Bank shall be consistent with the foreign policy of this Government.

BOARD OF DIRECTORS OF THE BANK

SEC. 4. (a) The board of directors of the Bank shall consist of (1) twelve persons who, at the time of taking office, are citizens of the United States, and who (except for the initial directors who shall be appointed by the Board) shall be nominated and elected by the members, and (2) two ex officio directors, one to be nominated by the Secretary of the Treasury, and one to be nominated by the Secretary of State, who shall serve as advisers to the Bank concerning matters coming within the interests of the Department of the Treasury or the Department of State. Persons on the board of directors shall receive no compensation by reason of their service as directors. Four of the initial directors appointed to the Board shall be persons who, at the time of taking office, are presidents of Federal Home Loan Banks. The Board shall fix the initial terms of persons appointed to the board of directors, and shall fix, and may, from time to time, alter other terms of appointive members of the board of directors, except that no such term shall be fixed for a longer unexpired period than four years. The nomination and the election of directors shall be in accordance with such provisions, including without limitation such provisions with respect to classification of members and the extent of voting rights of members and the exercise of such rights, as the Board may prescribe.

(b) The Board may establish requirements concerning the eligibility and qualifications of persons elected to the office of director, and provide for (1) the selection and functions of a chairman of the board of directors, (2) the exercise, through meetings or otherwise, of functions of the board of directors or of any committee or body of said board or of the Bank, (3) the nomination of directors where members fail to make the requisite nominations, and (4) the appointment of directors in case of vacancies. Any function of the Board under this Act may be exercised by such person or persons as the Board may specify, and, to such extent as the Board may provide, but subject to such prohibitions, restrictions, and limitations as the Board may prescribe, any function of the Bank, or of the board of directors, or of the chairman thereof may be exercised by such person or persons as the board of directors may provide. Any such function or any function under this Act may be exercised without regard to whether any place at which it is exercised in whole or in part is within the United States or is subject to the jurisdiction of the United States.

CAPITAL STOCK AND MEMBERSHIP

SEC. 5. (a) The Bank shall have such capital stock as the Board shall prescribe, and such stock shall be issued and may be retired, at such times, under such circumstances, and at such price or prices as the Board may prescribe. All stock shall be without preference or priority as to dividends or assets. Stock shall be evidenced in such manner, and shall be transferable only to such extent, to such transferees, and in such manner, as the Board may prescribe.

(b) Subject to such restrictions, requirements, and exceptions as the Board may prescribe, (1) stock of the Bank may be purchased or otherwise acquired and held by any Federal home loan bank or any member of a Federal home

loan bank, or by any State chartered savings and loan association, or building and loan association authorized by the law of that State to be a member of a Federal home loan bank, or by any mutual savings bank duly chartered by any State whose savings accounts are insured by an instrumentality of the Federal Government; and (2) while holding such stock any Federal home loan bank or any such member shall automatically be a member of the Bank.

(c) Notwithstanding and without regard to any provision of any other law, but subject to such restrictions, requirements, and exceptions as the Board may prescribe, legal authority to be a member of the Bank and to purchase or otherwise acquire and to hold stock, obligations, or other securities of the Bank is hereby conferred on any Federal home loan bank, any Federal savings and loan association, any State chartered savings and loan association or building and loan association authorized by the law of that State to be a member of a Federal home loan bank, any mutual savings bank duly chartered by any State whose savings accounts are insured by an instrumentality of the Federal Government, and on any other Federal home loan bank member, but nothing contained herein shall authorize (1) any Federal home loan bank to invest any of its funds in the purchase of any such stock if, immediately after such purchase, the par value of the total amount of such stock owned by such Federal home loan bank would exceed 1 per centum of its total capital stock, reserves, and surplus, (2) any such association, mutual savings bank, or member to invest any of its funds in the purchase of any such stock if, immediately after such purchase, the par value of the total amount of such stock owned by such association, bank, or member would exceed 1 per centum of its assets, or (3) any such association or member (other than an insurance company) to invest any of its funds in the purchase of such stock if, immediately prior to such purchase, its reserves and surplus are not at least equal to 5 per centum of its savings accounts.

FUNCTIONS AND AUTHORITY OF THE BANK

SEC. 6. (a) The Bank shall have authority (1) to invest in loans or advances to, or in shares, accounts, deposits, or certificates of indebtedness of, foreign mutual thrift and home financing institutions and foreign home loan banks, or in interests in any of the same, (2) to promote and assist in the establishment and development in foreign countries of (i) mutual institutions for the receipt of savings and the financing of homes and (ii) credit and financing facilities for such institutions, and (3) to make or procure such studies and investigations and such reports as it may deem to be necessary or appropriate to assist in the carrying out of the purposes or provisions of this Act. Funds of the Bank not invested pursuant to the foregoing provisions of this subsection may be invested in such investments as the Board may approve.

(b) In the exercise of the authority conferred by subsection (a), the Bank—

(1) may issue letters of credit and letters of commitment;

(2) may collect or compromise any obligations assigned to or held by it, and any legal or equitable rights accruing to it, and, as may be determined by the board of directors of the Bank, refer any such obligation or rights to the Attorney General for suit or collection; and

(3) may acquire and dispose of, upon such terms and conditions as the board of directors of the Bank may determine, any property, including any instrument evidencing indebtedness or ownership.

(c) With a view to protecting funds of the Bank against certain risks inherent in foreign investments, the Bank shall, to the extent practicable, and if deemed advisable by the board of directors of the Bank, seek to obtain guaranties of investments made pursuant to this section under the guaranty program authorized by section 221 of the Act for International Development of 1961 (22 U.S.C. 2181), or, if available, from other appropriate public or private sources.

(d) The Bank shall be deemed an agency of the United States Government for purposes of section 612 of the Foreign Assistance Act of 1961 (22 U.S.C. 2362), and, subject to the provisions of that section, the Bank may, whenever practicable and appropriate, utilize foreign currencies purchased from the Secretary of the Treasury in carrying out its functions under this section.

BORROWINGS AND SECURITIES

SEC. 7. (a) The Bank is hereby authorized, upon such terms and conditions as the Board may prescribe, to borrow, to give security, to pay interest or other return, and to issue notes, debentures, bonds, or other obligations, or other secu-

rities. The Bank shall not make any public offering of its obligations for sale, or sell any of its obligations otherwise than by private placement, except with the approval of the Secretary of the Treasury or his designee, but the provisions of this sentence shall not be applicable to any offering or sale confined to Federal home loan banks or Federal home loan bank members or both. Any obligation or security of the Bank shall be valid and binding notwithstanding that a person or persons purporting to have executed or attested the same may have died, become under disability, or ceased to hold office or employment before the issuance thereof.

(b) Obligations of the Bank shall be lawful investments, and may be accepted as security, for all fiduciary, trust, and public, private, or other funds the investment or deposit of which shall be under the authority or control of the United States, the District of Columbia, Puerto Rico, or any possession of the United States, any public, private, or other corporation incorporated by or under any law of any of the foregoing, any county or municipality of any of the foregoing, any political subdivision of any of the same, any court or any corporate or other agency or instrumentality of any of the preceding, or any officer or officers, employee or employees, or agent or agents of any of the above. Nothing in the sentence next preceding shall authorize the investment of funds of any Federal Reserve bank in such obligations or securities, and nothing in said sentence shall authorize any national bank, in the exercise of any power vested in it pursuant to subsection (k) of section 11 of the Federal Reserve Act, as amended, to make any investment in contravention of any regulation of the Board of Governors of the Federal Reserve System issued pursuant to said subsection (k).

(c) Except as otherwise provided in this Act, no provision or requirement of or under any law relating to securities, securities exchanges, investment companies or investment advisers, or relating to indentures or agreements, or proxies or powers, with respect to securities, shall be applicable to or with respect to any stock, obligation, or other security of the Bank.

(d) All obligations of the Bank shall plainly state that such obligations are not obligations of the United States and are not guaranteed by the United States.

DEPOSITARY OF PUBLIC MONEY

SEC. 8. (a) The Federal Reserve banks and the Federal home loan banks are hereby authorized to act as depositaries and fiscal or other agents of the Bank, and the Bank is hereby authorized to use them as such and to pay them compensation therefor.

(b) When designated for that purpose by the Secretary of the Treasury, the Bank shall be a depositary of public money, under such regulations as may be prescribed by the Secretary of the Treasury, and may also be employed as fiscal or other agent of the United States, and it shall perform all such reasonable duties as such depositary or agent as may be required of it.

USE OF FACILITIES OF OTHER AGENCIES

SEC. 9. The Bank, with the consent of and in the discretion of any department, establishment, board, commission or corporate or other instrumentality of the Government, including any field service, all of which are hereinafter referred to in this subsection as agencies, may utilize and act through any of said agencies and avail itself of the use of information, services, facilities, and personnel of any of said agencies, and may pay compensation therefor, and all of said agencies are hereby authorized, at their discretion, to provide the same to the Bank as it may request. Any expenses of the Board or of the Federal Savings and Loan Insurance Corporation in connection therewith, and any expenses of the Board in connection with the exercise of any function vested in or exercisable by the Board under this Act, shall be considered as nonadministrative expenses. Nothing in this Act or any other provision of law shall be construed to prevent or affect the appointment, employment, or provision for compensation or benefits, as an officer, director, employee, attorney, or agent of the Bank, of any officer, director, employee, attorney, agent or member of any such agency.

EXEMPTION FROM TAXATION

SEC. 10. (a) All notes, bonds, debentures, or other obligations of the Bank, or other securities (including stock) of the Bank, and the interest, dividends, or other income therefrom shall be exempt from all taxation (except estate, income,

inheritance, and gift taxes) now or hereafter imposed by the United States or any possession thereof, or by any State, county, municipality, or local taxing authority. The foregoing exemption from taxation, except as to taxation imposed by the United States, shall include exemption from taxation measured by such obligations or securities or by such interest, dividends, or other income, and from inclusion of such obligations or securities, or such interest, dividends, or other income, in the measure of any such taxation.

(b) The Bank, including its franchise, activities, capital, reserves, surplus, and income, shall be exempt from all taxation now or hereafter imposed by the United States or any possession thereof, or by any State, county, municipality, or local taxing authority, except that any real property of the Bank shall be subject to State, territorial, county, municipal, or local taxation to the same extent according to its value as other real property is taxed. Nothing in this subsection shall affect the applicability of the Public Debt Act of 1941, as amended. The provisions of this subsection shall be applicable without regard to any other law, including without limitation on the generality of the foregoing section 3301 of the Internal Revenue Code of 1954, except laws hereafter enacted by Congress expressly in limitation of this subsection.

AMENDMENTS TO OTHER ACTS

SEC. 11. (a) Title I of chapter 2 of part I of the Foreign Assistance Act of 1961, as amended (22 U.S.C. 2161, et seq.), which relate to the Development Loan Fund, is amended by adding at the end thereof a new section as follows:

"SEC. 206. USE OF THE FACILITIES OF THE INTERNATIONAL HOME LOAN BANK.—Whenever the President determines that the purposes of this title or title VI of this chapter can be served by utilizing the facilities of the International Home Loan Bank, he shall provide for the referral of applications for assistance hereunder to such bank for appropriate action."

(b)(1) Section 201 of the Government Corporation Control Act, as amended (31 U.S.C. 856), is amended by—

(A) striking out "and (5)" and inserting in lieu thereof "(5)"; and

(B) striking out the period and inserting in lieu thereof the following: ", and (6) International Home Loan Bank."

(2) Notwithstanding the provisions of the first sentence of section 202 of the Government Corporation Control Act, audits by the General Accounting Office of the financial transactions of the Bank shall not be limited to periods during which Government capital has been invested therein.

PENAL PROVISIONS

SEC. 12. (a) Except as expressly authorized by statute of the United States or by regulations of the Board, no individual or organization (except the Bank) shall use the term "International Home Loan Bank", or any combination of words including the words "International" and "Home", as a name or part thereof under which any individual or organization does any business, but this sentence shall not make unlawful the use of any name under which business is being done on the date of the enactment of this Act. No individual or organization shall use or display (1) any sign, device, or insigne prescribed or approved by the Bank for use or display by the Bank or by members of the Bank, (2) any copy, reproduction, or colorable imitation of any such sign, device, or insigne, or (3) any sign, device, or insigne reasonably calculated to convey the impression that it is a sign, device, or insigne used by the Bank or prescribed or approved by the Bank, contrary to regulations of the Bank prohibiting, or limiting or restricting, such use or display by such individual or organization. Any organization violating this subsection shall for each violation be punished by a fine of not more than $10,000. Any officer or member of an organization knowingly participating or knowingly acquiescing in any violation of this subsection shall be punished by a fine of not more than $5,000 or imprisonment for not more than one year, or both. Any individual violating this subsection shall for each violation be punished as set forth in the sentence next preceding this sentence.

(b) The provisions of sections 220, 658, 1011, and 1014 of title 18 of the United States Code are hereby extended to apply to and with respect to the Bank, and for the purposes of said section 658 the term "any property mortgaged or pledged" as used therein shall, without limitation on its generality, include any property subject to mortgage, pledge, or lien acquired by the Bank by assignment or otherwise.

The terms "agency" and "agencies" shall be deemed to include the Bank wherever used with reference to an agency or agencies of the United States in sections 201, 202, 216, 283, 286, 287, 371, 506, 595, 602, 641, 654, 701, 872, 1001, 1002, 1016, 1017, 1361, 1505, and 2073 of said title 18. Any officer or employee of the Bank shall be demed to be a person mentioned in section 602 of said title 18, within the meaning of section 603 of said title, and shall be deemed to be one of the officers or employees mentioned in section 602 of said title, within the meaning of section 606 of said title.

(c) The term "bank examiner or assistant examiner" as used in section 655 of said title 18 shall include any examiner or assistant examiner who is an officer or employee of the Bank and any person who makes or participates in the making of any examination of or for the Bank, and the term "bank" as used in said section 655 shall, without regard to any provision of said section with respect to membership or insurance, include the Bank and any institution examined by or for the Bank; and the last sentence of said section 655 shall not be applicable to said section 655 as extended by this sentence. The term "bank" as used in subsection (f) of section 2113 of said title 18 shall include the Bank, and any building used in whole or in part by the Bank shall be deemed to be used in whole or in part as a bank, within the meaning of said section 2113.

(d) The terms "obligation" and "security", wherever used (with or without the words "of the United States"), whether in the singular or in the plural, in sections 471 to 476, both inclusive, and section 492 of said title 18 are hereby extended to mean and to include any obligation or security of or issued by the Bank. Any reference in sections 474, 494, 495, and 642 of said title 18 to the United States, except in a territorial sense, or the Secretary of the Treasury is hereby extended to include the Bank. Section 477 of said title 18 is hereby extended to apply with respect to section 476 of said title as extended by the first sentence of this subsection (d), and for this purpose the term "United States" as used in said section 476 shall include the Bank.

(e) References in this section to sections of title 18 of the United States Code shall be deemed to be references to said sections as now or hereafter in force.

CONSTRUCTION AND SEPARABILITY

SEC. 13. Except as otherwise provided in this Act or as otherwise provided by the Board or by laws hereafter enacted by the Congress expressly in limitation of provisions of this Act, the powers and functions of the Board, the Bank, or the board of directors of the Bank shall be exercisable and the provisions of this Act shall be applicable and effective without regard to any provision of any other law. Notwithstanding any other evidences of the intention of Congress, it is hereby declared to be the controlling intent of Congress that if any provision of this Act, or the application thereof to any person or circumstances, is held invalid, the remainder of this Act, or the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected thereby.

[Excerpt from the Congressional Record, May 9, 1963]

INTERNATIONAL HOME LOAN BANK

(Mr. Curtis (at the request of Mr. Martin of Nebraska) was given permission to extend his remarks at this point in the Record and include extraneous matter.)

Mr. CURTIS. Mr. Speaker, the greatest contribution our country can make in foreign aid is to help other countries, those who wish to emulate the success of America, understand the ideas which have guided us on our way to greatness, and adapt them for their own use. With this thought in mind, I have today introduced legislation, identical to bills which were offered in the last Congress and which have been introduced in both the House of Representatives and the Senate in this session, to establish an International Home Loan Bank.

This proposal, which has the backing of the Federal Home Loan Bank Board and the U.S. Savings and Loan League, among other groups, has as its purpose the development in other countries, especially the underdeveloped nations of the world, of a savings and loan system to promote thrift, encourage homeownership, and aid in the rise of middle class among these people. The mechanism of this bill, by which it would accomplish its goals, would be an International Home Loan Bank through which financial backing could be given to the developing savings and loan industry abroad.

Clearly, the goals which are set for the International Home Loan Bank would be important in helping homeownership in the underdeveloped countries. This form of development is meaningful apart from any Communist threat. It is a real step forward in the entire social structure of the nation establishing these lending institutions. It meets problems which exist independent of the cold war, and it envisions the involvement of the people of the recipient nation—indeed their involvement as the primary force in this matter—in the effort to overcome these problems.

Late last year, the New York Times published an article on housing needs in Latin America. This article, which appeared in the Sunday, October 21, edition of the Times, points up the importance of this problem and I ask unanimous consent that it be made a part of my remarks to help give a clearer understanding of the bill I have introduced and its goals.

"SPURS ARE SOUGHT IN LATIN HOUSING

"(By Philip Shabecoff)

"In much of Latin America, a penny saved is a rare coin—and therein lies one of the chief reasons for Latin America's acute shortage of housing.

" 'There are 18 million Latin American families now living in urban slums who can afford some kind of decent housing,' Rodman C. Rockefeller said recently.

"The problem, he explained, is that in most areas of Latin America, a lack of individual savings means that mortgages simply are not available for middle and lower class housing.

"Mr. Rockefeller, eldest son of Gov. Nelson Rockefeller, is vice president in charge of housing for the International Basic Economy Corp. (IBEC). The company, a financing development and investment concern controlled by Rockefeller interests, soon will build its 10,000th home in Puerto Rico and South America.

"Although most Latin American governments have set up housing programs, often with grants from U.S. agencies such as the Agency for International Development, millions of people continue to live in tin shacks and apartment house slums. The answer to this blight, Mr. Rockefeller believes, lies in private rather than Government housing.

"Some 50 percent of South America's urban population earns enough money to amortize mortgages, he asserted. But mortgages generally are available only for luxury housing, and on exorbitant terms.

"FEW INDIVIDUALS SAVE

"The reason for this, Mr. Rockefeller explained is that there is little individual saving in Latin America. Inflation and low income levels discourage savings in most of the countries there, and virtually no savings institutions exist in an effective form. And lack of individual savings means a dearth of capital for mortgages.

"What is needed in Latin America, Mr. Rockefeller said, is a system of insured savings and loan associations similar to that in this country. But except for recently organized projects in Chile and Peru, these institutions are rare in Latin America.

"Help may be on the way, however, as a result of a bill introduced in the Senate on October 2 by Senator George Smathers, Democrat, of Florida.

"The legislation, which was designed to help Latin Americans save their own money for private housing, was a casualty of the recent congressional scramble for adjournment and never got out of the Committee on Banking and Currency. However, Senator Smathers plans to reintroduce it when the Senate next convenes.

"The bill, an amendment to previously proposed legislation to alter the Federal Home Loan Bank Act and the Home Owners Land Act, called for the establishment of an 'International Home Loan Bank.'

"FOREIGN INVESTMENT PERMITTED

"Through this bank U.S. savings and loan companies will have the privilege of investing up to 1 percent of their assets in similar institutions in Latin America and elsewhere overseas, laying the groundwork for the establishment of savings and loan systems in those areas.

"The bill, which also was sponsored by Senator John Sparkman, Democrat, of Alabama, is reported to have a good chance of passing in the next session of Congress.

"The U.S. savings and loan organizations which might invest in counterpart institutions in South America are regarding the Chilean experiment with keen interest. A little more than a year ago, at the advice of American economic experts, 18 associations were started there under the supervision of a central bank, with American capital serving as seed money.

"The associations pay 6-percent interest on savings and charge 10 percent on mortgages, Mr. Rockefeller said. They also operate under an unusual inflation-protection mechanism which adjusts interest and principal on both savings and mortgages on the basis of an index of wages and prices.

"By the end of the first year, 23,000 people were participating in the program, and 1,780 mortgages had been approved or were in the process of approval.

"DEMAND EXCEEDS BUILDING

"Because of the associations, many new houses are being built in Chile. However, there is evidence that the mortgage system has grown faster than the construction business. Demand for houses is far exceeding actual production, Mr. Rockefeller said.

"In most cases, he explained, builders are short of sufficient working capital. It is also difficult to convince them that the new system is here to stay and that their profits for building homes will not be wiped out by inflation.

"This is where IBEC steps in. The company has built most of its houses in Puerto Rico, but it believes the establishment of savings and loan companies will provide opportunity in South America.

"IBEC already has under construction 750 houses in Santiago, Chile, and plans to build more. Most of the houses are three-bedroom dwellings that sell for $7,000 to $8,000. The company also is building in Peru, where two associations have been established, one by a Roman Catholic priest.

"One of IBEC's basic functions, Mr. Rockefeller said, is to demonstrate that U.S. industrial methods and techniques are applicable abroad.

"It is not an original idea, but we try to concentrate on businesses, such as housing, that directly affect people. We also make a profit by doing so," he said.

"One of these techniques is the IBEC method of home construction. This makes use of a house-sized steel form to mold reinforced concrete on a previously prepared floor slab. Once a site is prepared, the company can produce six houses a day on that site.

"PRECAST PANELS HELPFUL

"IBEC also uses precast concrete wall panel and roof systems in its housing projects.

"Recently, however, IBEC has recognized that its methods are not always applicable in South America. Often, the absence of materials and large-scale demand makes the mass construction method too expensive. Construction also is slowed by government inspection methods and equipment breakdowns. The company therefore is beginning to turn to local manual labor as the cheapest method of building in some areas.

"As soon as the new bill is passed, Mr. Rockefeller predicted, at least five U.S. savings and loan companies will invest in South American countries. IBEC will be prepared to construct about 2,500 housing units a year to meet the expected demand for homes.

"Mr. Rockefeller believes that the middle class housing shortage in Latin America must be alleviated for the security of this country as well as for the needs of the Latin Americans.

" 'The middle class in Latin America, which certainly has the ability to revolt, has been denied the normal material rewards that the middle class expects in the United States,' he said. 'While the Latin middle class is loyal to the Western concept of government, this denial puts a tremendous strain on its loyalty.' "

[S. 474, 88th Cong., 1st sess.]

(Mr. Smathers (for himself and Mr. Sparkman) introduced the following bill; which was read twice and referred to the Committee on Banking and Currency)

A BILL To provide for the establishment of an International Home Loan Bank, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "International Home Loan Bank Act".

DEFINITIONS

SEC. 2. As used in this Act—

(a) The term "Bank" means the International Home Loan Bank incorporated under this Act.

(b) The term "Board" means the Federal Home Loan Bank Board.

(c) The term "member", except where used with respect to a member of a Federal home loan bank, means a member of the Bank.

(d) The term "stock" means capital stock of the Bank.

INTERNATIONAL HOME LOAN BANK

SEC. 3. The Board is hereby authorized and directed to provide without regard to any other provision of law, except section 4 of the Bretton Woods Agreement Act, as amended, and provisions hereafter enacted expressly in limitation of this sentence and except as otherwise provided by the Board, for the incorporation, organization, operation, regulation, and examination of a corporation to be known as the International Home Loan Bank which shall be under the supervision of the Board and shall be operated under the direction of a board of directors as hereinafter set forth. The Board is hereby authorized to prescribe such bylaws, rules, and regulations as it may deem necessary or appropriate to carry out the purposes or provisions of this Act, and any function of the Board under this Act may be exercised by regulations or otherwise. The Board shall be guided by the Department of State on those two aspects of its operations affecting foreign policy, in order that the actions taken by the International Home Loan Bank shall be consistent with the foreign policy of this Government.

SEC. 4. (a) The board of directors of the Bank shall consist of (1) twelve persons who, at the time of taking office, are citizens of the United States, and who (except for the initial directors who shall be appointed by the Board) shall be nominated and elected by the members, and (2) two ex officio directors, one to be nominated by the Secretary of the Treasury, and one to be nominated by the Secretary of State, who shall serve as advisers to the Bank concerning matters coming within the interests of the Department of the Treasury or the Department of State. Persons serving on the board of directors shall receive no compensation by reason of their service as directors. Four of the initial directors appointed to the Board shall be persons who, at the time of taking office, are presidents of Federal Home Loan Banks. The Board shall fix the initial terms of persons appointed to the board of directors, and shall fix, and may, from time to time alter other terms of appointive members of the board of directors, except that no such term shall be fixed for a longer unexpired period than four years. The nomination and the election of directors shall be in accordance with such provisions, including without limitation such provisions with respect to classification of members and the extent of voting rights of members and the exercise of such rights, as the Board may prescribe.

(b) The Board may provide as to (1) the eligibility and qualifications of persons for the office of director, (2) the selection and functions of a chairman of the board of directors, (3) the exercise, through meetings or otherwise, of functions of the board of directors or of any committee or body of said board or of the Bank, and (4) the nomination of directors where members fail to nominate and the appointment of directors in case of vacancies. Any function of the Board under this Act may be exercised by such person or persons as the Board may provide, and, to such extent as the Board may provide, but subject to such prohibitions,

restrictions, and limitations as the Board may prescribe, any function of the Bank or of the board of directors or of the chairman thereof may be exercised by such person or persons as the Bank may provide. Any such function or any function under this Act may be exercised without regard to whether any place at which it is exercised in whole or in part is or is not within the United States or subject to the jurisdiction of the United States.

CAPITAL STOCK AND MEMBERSHIP

SEC. 5. The Bank shall have such capital stock as the Board shall prescribe, and such stock shall be issued, and may be retired, at such times, under such circumstances, and at such price or prices as the Board may prescribe. All stock shall be without preference or priority as to dividends or assets. Stock shall be evidenced in such manner, and shall be transferable only to such extent, to such transferees, and in such manner, as the Board may prescribe.

SEC. 6. (a) Subject to such restrictions, requirements, and exceptions as the Board may prescribe, (1) stock of the Bank may be purchased or otherwise acquired and held by any Federal home loan bank or any member of a Federal home loan bank, or any State chartered savings and loan association, or building and loan association authorized by the law of that State to be members of a Federal home loan bank, or any mutual savings bank duly chartered by any State; and (2) while holding such stock any Federal home loan bank or any such members shall automatically be a member of the Bank.

(b) Notwithstanding and without regard to any provision of any other law, but subject to such restrictions, requirements, and exceptions as the Board may prescribe, legal authority to be a member of the Bank and to purchase or otherwise acquire and to hold stock, obligations, or other securities of the Bank is hereby conferred on any Federal home loan bank or any Federal savings and loan association, or any State chartered savings and loan association or building and loan association authorized by the law of that State to be members of a Federal home loan bank, or any mutual savings bank duly chartered by any State, and on any other Federal home loan bank member, but nothing in this sentence shall (1) authorize any Federal home loan bank, any Federal savings and loan association or any State chartered savings and loan association, or building and loan association authorized by the law of that State to be members of a Federal home loan bank, or any mutual savings bank duly chartered by any State, or any such Federal home loan bank member to invest any of its funds in the purchase of any such stock if, immediately after such purchase, the par value of the total amount of such stock owned by such Federal home loan bank, association, or member would exceed 1 per centum of the total capital stock, reserves, and surplus of such Federal home loan bank or 1 per centum of the assets of such association or such member; or (2) authorize any Federal savings and loan association or any such Federal home loan bank member, other than an insurance company, to invest any of its funds in the purchase of any such stock if, immediately prior to such purchase, its reserves and surplus are not at least equal to 5 per centum of its savings accounts.

OPERATIONS OF THE BANK

SEC. 7. (a) As used in this section, the term "foreign mutual thrift and home-financing institution" means an institution as to which there is outstanding a determination by the Bank that such institution (1) is a mutual institution, (2) has as primary purposes the receipt of savings and the financing of homes, and (3) does not have in the United States, or at or within any place subject to the jurisdiction of the United States, any office or agency, or any agent, for the receipt of savings or the making of loans, and the term "foreign home loan bank" means an institution as to which there is outstanding a determination by the Bank that such institution (1) is organized or incorporated by or under the laws of a foreign country and (2) has as a primary purpose the making of loans or advances to, or investments in, mutual institutions organized or incorporated under the laws of such country and engaged, or authorized to engage, in such country in the receipt of savings and the financing of homes.

(b) The Bank shall have (1) authority to invest in loans or advances to, or in shares, accounts, deposits, or certificates of indebtedness of, foreign mutual thrift and home financing institutions and foreign home loan banks, or in interests in any of the same; (2) all the powers and authority customary or appropriate to conduct an international banking organization to serve such institutions and

banks; (3) authority to promote and assist in the establishment and development in foreign countries of mutual institutions having as primary purposes the receipt of savings and the financing of homes and the establishment and development in foreign countries of credit and financing facilities for such institutions; and (4) authority to make or procure such studies and investigations and such reports as it may deem to be necessary or appropriate to assist in the carrying out of the purposes or provisions of this Act. Funds of the Bank not invested pursuant to the foregoing provisions of this subsection may be invested in such investments as the Board may approve.

BORROWINGS AND SECURITIES

SEC. 8. (a) The Bank is hereby authorized, upon such terms and conditions as the Board may prescribe, to borrow, to give security, to pay interest or other return, and to issue notes, debentures, bonds, or other obligations, or other securities. The Bank shall not make any public offering of its obligations for sale, or sell any of its obligations otherwise than by private placement, except with the approval of the Secretary of the Treasury or his designee, but the provisions of this sentence shall not be applicable to any offering or sale confined to Federal home loan banks or Federal home loan bank members or both. Any obligation or security of the Bank shall be valid and binding notwithstanding that a person or persons purporting to have executed or attested the same may have died, become under disability, or ceased to hold office or employment before the issuance thereof.

(b) Obligations of the Bank shall be lawful investments, and may be accepted as security, for all fiduciary, trust, and public, private, or other funds the investment or deposit of which shall be under the authority or control of the United States, the District of Columbia, Puerto Rico, or any territory or possession of the United States, any public, private, or other corporation incorporated by or under any law of any of the foregoing, any county, or municipality of any of the foregoing, any political subdivision of any of the same, any court or any corporate or other agency or instrumentality of any of the preceding, or any officer or officers, employee or employees, or agent or agents of any of the above. Nothing in the sentence next preceding shall authorize the investment of funds of any Federal Reserve bank in such obligations or securities, and nothing in said sentence shall authorize any national bank, in the exercise of any power vested in it pursuant to subsection (k) of section 11 of the Federal Reserve Act, as amended, to make any investment in contravention of any regulation of the Board of Governors of the Federal Reserve System issued pursuant to said subsection (k).

(c) Except as otherwise provided in this Act, no provision or requirement of or under any law relating to securities, securities exchanges, investment companies, or investment advisers, or relating to indentures or agreements, or proxies or powers, with respect to securities, shall be applicable to or with respect to any stock, obligation, or other security of the Bank.

MISCELLANEOUS PROVISIONS

SEC. 9. (a)(1) The Federal Reserve banks and the Federal home loan banks are hereby authorized to act as depositaries and fiscal or other agents of the Bank, and the Bank is hereby authorized to use them as such and to pay them compensation therefor.

(2) When designated for that purpose by the Secretary of the Treasury, the Bank shall be a depositary of public money, under such regulations as may be prescribed by the Secretary of the Treasury, and may also be employed as fiscal or other agent of the United States, and it shall perform all such reasonable duties as such depositary or agent as may be required of it.

(b) The Bank, with the consent of and in the discretion of any department, establishment, board, commission or corporate or other instrumentality of the Government, including any field service, all of which are hereinafter referred to in this subsection as agencies, may utilize and act through any of said agencies and avail itself of the use of information, services, facilities, and personnel of any of said agencies, and may pay compensation therefor, and all of said agencies are hereby authorized, at their discretion, to provide the same to the Bank as it may request. Any expenses of the Board or of the Federal Savings and Loan Insurance Corporation in connection therewith, and any expenses of the Board in connection with the exercise of any function vested in or exer-

cisable by the Board under this Act, shall be considered as nonadministrative expenses. Nothing in this Act or any other provision of law shall be construed to prevent or affect the appointment, employment, or provision for compensation or benefits, as an officer, director, employee, attorney, or agent of the Bank, of any officer, director, employee, attorney, agent or member of any such agency.

(c) All notes, bonds, debentures, or other obligations of the Bank, or other securities (including stock) of the Bank, and the interest, dividends, or other income therefrom, shall be exempt from all taxation (except estate, income, inheritance, and gift taxes) now or hereafter imposed by the United States, by any territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority. The foregoing exemption from taxation, except as to taxation imposed by the United States, shall include exemption from taxation measured by such obligations or securities or by such interest, dividends, or other income, and from inclusion of such obligations or securities, or such interest, dividends, or other income, in the measure of any such taxation.

(d) The Bank, including its franchise, activities, capital, reserves, surplus, and income, shall be exempt from all taxation now or hereafter imposed by the United States, by any territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority, except that any real property of the Bank shall be subject to State, territorial, county, municipal, or local taxation to the same extent according to its value as other real property is taxed. Nothing in this subsection shall affect the applicability of the Public Debt Act of 1941, as amended. The provisions of this subsection shall be applicable without regard to any other law, including without limitation on the generality of the foregoing section 3301 of the Internal Revenue Code of 1954, except laws hereafter enacted by Congress expressly in limitation of this subsection.

PENAL PROVISIONS

SEC. 10. (a) Except as expressly authorized by statute of the United States or by regulations of the Board, no individual or organization (except the Bank) shall use the term "International Home Loan Bank", or any combination of words including the words "International" and "Home", as a name or part thereof under which any individual or organization does any business, but this sentence shall not make unlawful the use of any name under which business is being done on the date of the enactment of this Act. No individual or organization shall use or display (1) any sign, device, or insigne prescribed or approved by the Bank for use or display by the Bank or by members of the Bank, (2) any copy, reproduction, or colorable imitation of any such sign, device, or insigne, or (3) any sign, device, or insigne reasonably calculated to convey the impression that it is a sign, device, or insigne used by the Bank or prescribed or approved by the Bank, contrary to regulations of the Bank prohibiting, or limiting or restricting, such use or display by such individual or organization. An organization violating this subsection shall for each violation be punished by a fine of not more than $10,000. An officer or member of an organization knowingly participating or knowingly acquiescing in any violation of this subsection shall be punished by a fine of not more than $5,000 or imprisonment for not more than one year, or both. An individual violating this subsection shall for each violation be punished as set forth in the sentence next preceding this sentence.

(b) The provisions of sections 220, 658, 1011, and 1014 of title 18 of the United States Code are hereby extended to apply to and with respect to the Bank, and for the purposes of said section 658 the term "any property mortgaged or pledged" as used therein shall, without limitation on its generality, include any property subject to mortgage, pledge, or lien acquired by the Bank by assignment or otherwise. The terms "agency" and "agencies" shall be deemed to include the Bank wherever used with reference to an agency or agencies of the United States in sections 201, 202, 216, 283, 286, 287, 371, 506, 595, 602, 641, 654, 701, 872, 1001, 1002, 1016, 1017, 1361, 1505, and 2073 of said title 18. Any officer or employee of the Bank shall be deemed to be a person mentioned in section 602 of said title 18, within the meaning of section 603 of said title, and shall be deemed to be one of the officers or employees mentioned in section 602 of said title, within the meaning of section 606 of said title.

(c) The term "bank examiner or assistant examiner" as used in section 655 of said title 18 shall include any examiner or assistant examiner who is an officer or employee of the Bank and any person who makes or participates in the making of any examination of or for the Bank, and the term "bank" as used in said section 655 shall, without regard to any provision of said section with respect to membership or insurance, include the Bank and any institution examined by or for the Bank; and the last sentence of said section 655 shall not be applicable to said section 655 as extended by this sentence. The term "bank" as used in subsection (f) of section 2113 of said title 18 shall include the Bank, and any building used in whole or in part by the Bank shall be deemed to be used in whole or in part as a bank, within the meaning of said section 2113.

(d) The terms "obligation" and "security", wherever used (with or without the words "of the United States"), whether in the singular or in the plural, in sections 471 to 476, both inclusive, and section 492 of said title 18 are hereby extended to mean and to include any obligation or security of or issued by the Bank. Any reference in sections 474, 494, 495, and 642 of said title 18 to the United States, except in a territorial sense, or the Secretary of the Treasury is hereby extended to include the Bank. Section 477 of said title 18 is hereby extended to apply with respect to section 476 of said title as extended by the first sentence of this subsection (d), and for this purpose the term "United States" as used in said section 476 shall include the Bank.

(e) References in this section to sections of title 18 of the United States Code shall be deemed to be references to said sections as now or hereafter in force.

CONSTRUCTION AND SEPARABILITY

SEC. 11. Except as otherwise provided in this Act or as otherwise provided by the Board or by laws hereafter enacted by the Congress expressly in limitation of provisions of this Act, the powers and functions of the Board, the Bank, of the board of directors of the Bank shall be exercisable and the provisions of this Act shall be applicable and effective without regard to any provision of any other law. Notwithstanding any other evidences of the intention of Congress, it is hereby declared to be the controlling intent of Congress that if any provision of this Act, or the application thereof to any person or circumstances, is held invalid, the remainder of this Act, or the application of such provision to persons or circumstances other than those as to which it is held invalid, shall not be affected thereby.

Representative CURTIS. I have been trying to plug something you, Mr. Ray, picked up and emphasized. To me, the importance of developing a good tax system means basically local taxes. I think we need to restudy Henry George—not that I am a single tax advocate, but I don't think there is any question that the most economically beneficial tax is the tax on wealth, the property tax. It is the base of the growth of this country. It is the base from which local government derives its essential income. This is its essential source of income, the tax on wealth, property tax. Thus, it can make its own decisions on sewers, streets, schools, and so on.

When we were in Brasília, I was interested to find the mayors from all over Brazil there looking for money. I thought this was just a counterpart of what we were beginning to see in this country where the local officials were running to the Federal Government to try to get money. But it wasn't. I found out that their only source of income was whatever the Federal Government handed out. They have never developed—and this is probably true of all the Latin American countries—a local tax or a real tax based on property or wealth.

This bears directly on these other problems you mentioned of land reform and inflation. Land reform is affected because one of the

aspects of a tax on property is that it is an encouragement to utilize that property or that real estate economically, because if it is unutilized, you still are paying the tax. So it behooves you to get some income from that property, and the more you can get, the better off you are because otherwise, these taxes accumulate. This is a tax that moves with economic growth.

Although we have to use the income tax—and I think we do in this country for other reasons—we now recognize it is a real deterrent on growth. It can get so bad that people of different ideological beliefs will say we have to lower taxes as they are presently in the United States. But a property tax moves with this. So why do people in Latin America put money into land? Why not? There is no tax on it. They just sit and hold it, and the value is unaffected essentially by inflation. But if a property tax were developed, this would actually force them to try to get an economic return. They couldn't just hold it and speculate.

Well, I wanted to bring that point out again in context with what you have said, Mr. Ray. Thank you for this opportunity, Mr. Chairman.

Senator SPARKMAN. Thank you. There are a good many questions that come to mind that I should like to ask, but for my part I am going to have to leave here in a few minutes. But, Mr. Moore, you referred to this COMAP?

Mr. MOORE. These days everything has to be known by its initials. Commerce Committee for the Alliance for Progress called COMAP.

Senator SPARKMAN. Since the issuance of that report, I don't know whether there has been time for any reaction yet, but I just wondered if there have been any indications of any change in investment confidence in Latin America.

Mr. MOORE. I personally think there is considerable evidence of a change for the better, Mr. Chairman. I don't want to get into a question again of post hoc ergo propter hoc, whether or not it be because of the COMAP report. But we do know that since that time there have been some encouraging manifestations.

For example, in mid-1963 I think for the first time in, oh, it must be 20 years, I guess, a Latin American bond issue was successfully marketed and sold in Wall Street—$40 million worth of Mexican bonds were taken by U.S. private investors.

Another indication that is most encouraging is this question of commodity prices. After several discouraging years, beginning in 1958 and 1959, the declining trend which has caused terrible economic dislocations in Latin America seems to have turned for the better. Coffee, for example, at a price average of 34 cents a pound in 1962, lowest in a decade, has been rising since last spring at an accelerating rate and is now in the neighborhood of 47 cents a pound, an increase of 38 percent, and the impact of this, of course, on coffee-producing countries is tremendously favorable to them. This will benefit Brazil and Colombia and the others.

We all are familiar with the great rise in sugar prices which is of economic benefit to the Caribbean countries and Brazil, Peru, Mexico.

Copper, which was down to 24 and a fraction cents in 1958, is approaching 30 cents now, stabilized at about 29.27 cents in 1963, which was a 14-percent increase.

Tin and zinc and lead, which had a 1958 low, have risen a few cents and this is very important, of course, to Chile, Bolivia, Mexico, and Peru. I don't like to stress rising prices, but we all know the terms of trade put these countries in a terrible economic squeeze.

Another very encouraging thing, in my judgment, was the attitude adopted at São Paulo at the Inter-American Economic and Social Council meeting last month by the United States in the presence of Under Secretary Harriman who devoted a substantial part of his major address at that conference to the importance of private investment in private enterprise, the first such emphasis to be placed by any of our high officials in such countries since the beginning of the Alliance for Progress.

Senator SPARKMAN. I was just going to say that tomorrow, Mr. Peccei is going to testify and he is, as I said in my opening statement, with Senator Javits who is a member of this committee, freshly back from this conference in Paris setting up this ADELA. Are you familiar with that?

Mr. MOORE. Yes, sir. To a considerable degree. This ADELA developed, as you know, in Europe. I think it came out of the deliberations of the NATO parliamentarians of which your colleague, Mr. Javits, is a member.

Senator SPARKMAN. That is correct.

Mr. MOORE. He aroused the interest of some Germans and Italians and others and my company had the privilege of being one of the sponsors of the organization of the group. We are not yet participants in the investment, but we did participate financially in the organization of this group.

It is designed to bring European, Latin American, and United States and possibly Canadian and Japanese capital together, private capital, in joint enterprises and joint ventures and investments in Latin America. I think it is a most encouraging start and I think it will work.

The First National City Bank of New York, Standard Oil Co. of New Jersey, the Texas Co., I believe, and others are joining in this effort and will make investments in varying sizes.

One of the great things about it from the point of view of the American investor is it gives an opportunity to a company that has been in only one business, let's say oil, to spread out and diversify and get into other businesses, using the management know-how and techniques of a diversified group. I haven't heard any reports of their meeting in Paris, but I am pretty sure now that they are underway and will shortly be making their first investments.

Senator SPARKMAN. Do you feel it is an encouraging move, Mr. Ray?

Mr. RAY. Very definitely.

Senator SPARKMAN. Of course, when this Alliance for Progress program was originally set up, it was contemplated that private enterprise would play a very important part. As a matter of fact, I believe, Mr. Dillon at Punta del Este said that he estimated that there would be $20 billion spent over the next 10 years, half of which would be private enterprise. Is that not right?

Mr. RAY. Yes. The figure that sticks in my mind as mentioned by Mr. Moore was $300 million of new direct capital flow but then, of course, if you add the reinvestment of reserves and earnings already down there, you get up to a figure that you were speaking of.

To come back to the European situation, I am delighted about ADELA and I am delighted at the fact that your committee is going to hear from a distinguished European because their attitude in my experience has been a little bit closer to the one that, say, we have been expressing here this morning than has the United States attitude, and in Germany they have had a program for 3 or 4 years now where they will give their small industries full risk guarantee if they will go establish a small enterprise in Latin America, actually guarantee the profits of the enterprise for the first 5 years.

Senator SPARKMAN. Well, there are many things I should like to discuss with you, carry on, some of the specifics that were included in the Punta del Este, but as I said a few minutes ago, I must go. I am sure the time of you gentlemen is limited, too.

Let me on behalf of the subcommittee, and the full committee for that matter, express our appreciation to both of you for meeting here with us.

I would like to place in the record two tables that were compiled by the U.S. Department of Commerce. They deal with U.S. direct investments in Latin America.

(The tables are as follows:)

TABLE 1.—*U.S. direct investments in the Latin American Republics,*[1] *capital flows, earnings, values, 1950–62*

[Millions of dollars]

	Book value[2]		Average annual additions, 1950–60		1961		1962		Book value,[2] 1962
	December 1950	December 1960	Capital outflow	Reinvested earnings	Capital outflow	Reinvested earnings	Capital outflow	Reinvested earnings	
Latin American Republics, total[1]	3,803	7,431	276	170	173	255	−32	287	8,472
Manufacturing, total	726	1,499	63	72	77	95	114	100	1,893
Argentina	161	213	4	12	43	45	73	19	404
Brazil	285	[2] 515	29	31	−2	28	10	52	[2] 611
Mexico	133	391	14	16	18	7	23	13	448
Other countries	147	380	16	13	18	15	8	16	430
Petroleum, total	1,213	2,739	123	36	30	36	−115	43	3,159
Venezuela	857	1,995	100	22	−44	11	−167	10	[2] 2,202
Other countries	356	744	23	14	74	25	52	33	957
Mining and smelting	623	1,093	54	7	32	6	−3	9	1,099
Other industries	1,241	2,100	36	55	34	118	−28	135	2,321

[1] Excludes Cuba.
[2] Book values are adjusted from time to time to reflect revaluations, writeoffs, and changes in currency values.

Source: U.S. Department of Commerce, Office of Business Economics.

TABLE 2.—*U.S. direct investments in the Latin American Republics,[1] earnings and income distributed*

[Millions of dollars]

	Earnings [2]					Income distributed [3]				
	1950	1960	Average 1950–60	1961	1962	1950	1960	Average 1950–60	1961	1962
Latin American Republics, total [1]	546	829	764	964	1,028	470	641	609	730	761
By industry:										
Manufacturing	99	146	123	170	167	50	63	53	75	70
Petroleum	262	345	393	449	490	256	311	360	412	447
Mining and smelting	68	164	100	141	147	64	180	93	137	141
Other industries	117	174	148	204	224	100	87	103	106	103
By country:										
Argentina	17	46	25	100	80	6	10	11	36	45
Brazil	96	80	87	71	86	62	45	47	35	24
Chile	37	72	57	52	72	41	72	54	58	64
Mexico	43	54	54	51	63	29	65	38	46	44
Peru	21	58	32	61	52	15	48	25	57	51
Venezuela	232	428	414	467	505	236	371	369	432	477
Other countries	100	91	95	162	170	81	30	65	66	56

[1] Excludes Cuba.

[2] U.S. share in total earnings of these enterprises.

[3] Dividends, interest and branch profits, after foreign withholding taxes but before any U.S. taxes.

Source: U.S. Department of Commerce, Office of Business Economics.

Mr. MOORE. Thank you, Mr. Chairman.

Mr. RAY. Thank you.

Senator SPARKMAN. The committee will stand in recess until 10 o'clock tomorrow morning.

(Whereupon, at 12:40 p.m., the subcommittee recessed to reconvene at 10 a.m. on Wednesday, January 15, 1964.)

(The following are exhibits that were ordered printed in the record by Senator Sparkman:)

[Excerpt from Business Week, Dec. 7, 1963]

UNITED STATES STILL A BOGYMAN TO LATIN AMERICANS

MAIN TROUBLE SPOT IS BRAZIL WHERE FEELINGS RUN STRONG AGAINST HEAVY INFLOW OF NORTH AMERICAN CAPITAL AND MOVE IS AFOOT TO FORM COMMON POLICY AGAINST THE UNITED STATES

Latin America—the region that President Kennedy once called "the most critical area of the world"—will continue high on the emergency list for President Johnson.

For a brief moment, when news of Kennedy's assassination touched some unsuspected emotional spring, Latin America seemed to be drawn closer to the United States than at any time in decades. In Mexico, illiterate construction workers sobbed eloquent tributes to their friend in the White House; in Chile, the Congress met in special session to eulogize the fallen leader; and in Buenos Aires early this week, Argentinians still stood in a block-long queue outside the U.S. Embassy, patiently waiting to express their sympathy.

Awareness

Suddenly concerned that the United States might slacken its support for the Alliance for Progress, Latins expressed more appreciation and support for the aid and reform program conceived by Kennedy than they ever did in his lifetime.

The outpouring of grief revealed once against the great reservoir of friendliness to the United States that exists among the people there. But on the political level, it is doubtful that the emotional outburst will be translated into improved relations between Uncle Sam and Latin American nations.

Leftists are working to prevent such a development by presenting Kennedy, in retrospect, as an embattled champion of Latin America who went down before powerful opposing forces within the United States.

Taking count

A Business Week survey of attitudes toward the United States in Latin capitals shows that the underlying causes of tensions between the United States and Latin America are still at work, even though in Venezuela this week, pro-Castro terrorists were unsuccessful in their attempt to block election of a president who promises friendly relations with the United States.

There were signs this week that the Argentine Government may be looking for a settlement of its dispute with U.S. oil companies, and Peru appears to be moving cautiously toward coming to terms with a subsidiary of Standard Oil Co. (New Jersey).

I. RAW SPOTS

Yet the tide of resentment against U.S. capital is still rising—particularly in the bigger and industrially more advanced nations such as Brazil and Argentina. Latin Americans resent especially an amendment written into the foreign aid bill, still pending at midweek, which would try to impose U.S. concepts of territorial limits in disputes over fishing grounds.

Many are reluctant to join the United States in any moves against Fidel Castro, although few actively support the Cuban dictator. Others throw brickbats at the Alliance for Progress, with rightists claiming it only stirs up trouble with its talk of reform while leftists claim it is only another form of U.S. imperialism.

ONE MAN'S VIEW

Here it what a Brazilian businessman has to say about the current state of relations with the United States.

"The basic source of difficulty today is the upsurge of Latin nationalism, which stems from a desire to be taken seriously. Latin nationalism today is chiefly economic, though there is a strong emotional undercurrent. And the biggest sore spot in Brazil is private U.S. capital."

In this Brazilian's view, strong feeling against U.S. companies operating in Brazil is a reaction against the big buildup in U.S. investment there when former President Juscelino Kubitschek was in power. Even in a highly industrialized area such as Western Europe, where U.S. investment is overshadowed by local industry, it is a source of friction; but in Latin America, it "sticks out like a sore thumb."

Sticking together

Besides putting the squeeze on foreign companies, Brazil is the chief holdout in any U.S. attempt to line up Latin support for action against Cuba. As one Brazilian said: "Castro has few real followers here; most of us regard him as a black sheep. But he is a Latin and one of us."

In another area—the Alliance for Progress—Brazil is the main recalcitrant. At the São Paulo conference of Alliance ministers last month, Brazil proposed that control of funds be shifted from the United States to the Inter-American Development Bank.

"The Alliance for Progress is looked upon as a sort of benevolent colonialism," explained another Brazilian. "We want to be given the money to be spent as we think best. You want to dole it out to suit your own ideas. It is mutual distrust that is killing the Alliance."

II. CALMER AREAS

Such vehemence is rare elsewhere in Latin America. In Chile, for example, with its tradition of political stability, relations with Uncle Sam are pitched in a lower key.

There is some cautious optimism over the Alliance for Progress, but Chileans, like Peruvians and Ecuadorians, claim fishing rights over a continental shelf that extends as much as 200 miles to sea. They warn of potential conflict with the United States over activities of U.S. fishermen operating in waters off the west coast of South America.

Oil troubles

In Peru, most U.S. companies, and many Peruvian concerns as well, have postponed new investment and expansion plans because of the Government's threat to take over International Petroleum Co., a Jersey Standard subsidiary.

Says the head of one Lima bank: "U.S. private enterprise in Peru and the rest of Latin America seems to be going through a transition. Joint ventures with a Latin partner are the safest type of foreign investment today. Petroleum and public utilities are out."

In Peru, too, conservatives and lefists both criticize the Alliance. One wealthy manufacturer complains the North Americans are trying to tell South Americans how to run their countries." You can't make a 3-hour lunch and siesta executive into a 30-minute hamburger and glass-of-milk man overnight," he says.

A different place

About the only country south of the border where relations with the United States aren't under some strain is Mexico—a nation that has long stood aloof from the rest of Latin America, and from the United States as well. In addition, it has accepted heavy U.S. investments and profited from a flood of American tourists.

President Johnson knows Mexico better than any other occupant of the White House, and Mexicans are looking forward to a period of cordial relations. Newspapers in Mexico City are publishing old pictures of Johnson arm in arm with President Lopez Mateos.

Cause for worry

Mexicans aren't too worried about their own future; but they are concerned about what is happening in the rest of Latin America. A Mexican banker, back from a tour of South America, where he talked with nearly 400 businessmen, professed surprise at the strong anti-American feelings he encountered among executives in places like São Paulo and Montevideo.

"These sentiments are not emotional and not ideological," he observes. "These men are akin to their U.S. counterparts. Their reasoning is economic. They fear U.S. penetration in the Latin American free trade zone and they fear the United States is taking over their channels of trade."

Brazil, he adds, is trying to lead Latin America in a common policy toward the United States, beginning with local government control of foreign investments.

Mexico won't go along, this banker believes, because many Mexican businessmen already are in partnership with U.S. companies. "But Brazil," he forecasts, "may now have the support of other Latin American businessmen—which might not have been the case a few years ago."

Proposals To Improve the Flow of U.S. Private Investment to Latin America

Report of the Commerce Committee for the Alliance for Progress

FOREWORD

This report was prepared by the Commerce Committee for the Alliance for Progress, a group of 25 businessmen chaired by Mr. J. Peter Grace, president of W. R. Grace & Co., and was presented to the Department on January 4, 1963. The report presents a wide range of recommendations which, in Chairman Grace's words, "the majority of the members of the committee feel will go a long way toward stimulating the flow of U.S. private investment to Latin America, as called for in the Punta del Este program."

The success of the Alliance for Progress is one of the most important and urgent objectives of the U.S. Government. Latin America, whose republics have long enjoyed close, friendly relationships with our own country, is presently marked by slow industrial development, widespread financial strains, and acute poverty. In signing the Charter of Punta del Este, we pledged our efforts to assist the Latin American countries in curing these ills.

Among the targets that we set for ourselves was an annual $300 million of U.S. private investment in Latin America. The record of the recent past shows that the actual flow of U.S. private capital is far below this level. If the industrial advance of Latin America is to proceed at the pace required for the Alliance's success, I believe that U.S. private investment, with the invaluable technical and managerial assistance that accompany it, should be encouraged to contribute to the Latin American development effort on an increasing scale.

This report puts forward COMAP's recommendations as to how the U.S. Government, on its part, might help encourage such increased investment. The recommendations have been carefully considered in the development of the administration's policy on private investment overseas. The document constitutes the fruit of long hours of study and preparation by the COMAP Chairman and members, and I wish to express my thanks to them for this generous and valuable service to the Government and to the Alliance.

Luther H. Hodges,
Secretary of Commerce.

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I. BACKGROUND

The Commerce Committee for the Alliance for Progress (COMAP) was created to help accelerate the contribution of the private business sector to the Alliance for Progress. This assignment included stimulation of the flow of U.S. private investment to Latin America not only through identifying and implementing specific investment projects, but also through pointing out general obstacles to increased investment and suggesting means for their removal.

The latter task—removal of major obstacles and the creation of a more favorable investment climate—was identified, in a letter of the Chairman of July 27 to Secretary Hodges, as paramount. In another letter to COMAP members of August 23, it was noted that we had accepted the invitation of Secretary Hodges, Secretary Dillon, and AID Administrator Hamilton to undertake to analyze the conditions relating to U.S. private investment in Latin America and propose an action program. This task has been pursued along two lines:

First, to meet the scheduled requirements of the U.S. Government in formulating its legislative program, we have given priority to recommendations requiring particular administrative and/or legislative actions relating directly to encouraging U.S. investment in Latin America;

Second, we have gone beyond this more immediate purpose and examined a number of problems including the underlying economic difficulties confronting Latin America with an eye toward more fundamental solutions to growth impediments.

This memorandum is directed toward the first task, that of recommending immediate remedial actions that, in part, require legislation.

II. THE PROBLEM IN CURRENT PERSPECTIVE

A. The role of private capital in the Alliance for Progress

As businessmen we must emphasize at the outset the basic proposition that in free societies private capital cannot be driven or cajoled into new fields. There is a free market for private investment and nations, areas, industries, and institutions must compete for it in a free marketplace. In other words, investment must be attracted and experience teaches us that it will be attracted to those fields where the return is most promising and where the safety of its capital is most assured.

Based on this essential principle, our study has revealed certain fundamental propositions. Perhaps the most significant is the fact that in any program to raise standards of living under the Alliance for Progress the subject of private investment cannot be treated separately from the special economic, social, and political conditions which prevail in the Latin American countries today. Neither can the problems of U.S. priavte investment in Latin America be isolated from the political posture of the United States in its relations with the other nations of the Western Hemisphere. Nor can the investment considerations which concern the U.S. business community be entirely separated from those which confront its opposite number in the Latin American Republics, the local private enterprise man.

Our study has demonstrated certain alarming developments in the area of budget deficits, balance-of-payments deficits, and currency depreciation in some countries, chronic deterioration in the terms of trade in others, shortages of local currency availabilities in some, credit stringency and overcommitment in foreign debt in others. Recommendations of both a short-term and a long-term nature for dealing with this crippling economic deterioration are contained herein, but first some general observations are required.

In the first place, as pointed out above, it is clear that the objective toward the attainment of which American businessmen have joined hands with our Government through COMAP; i.e., the increase of the private investment flow, cannot be achieved if we confine our thinking solely to financial and economic measures.

Latin America is a continent in political and social ferment and this is just as truly a deterrent to private investment as are the purely economic and financial obstacles. U.S. investors are not always deterred by currency weaknesses in particular countries, or by the lack of completely assured political stability in others and the current studies of the balance-of-payments section of the Commerce Department bear this out even today.

It is clear that the current aggregate decline in the net flow of U.S. private investment has other deep causes as well. New threats are present which, in

some countries and some industries, seem literally to have destroyed investor confidence. The political menace of communism, with massive expropriations such as was the fate of private investments in Cuba when Castro took over, and the less violent but nevertheless equally crippling takeover of American investments by local expropriation as in the case of Brazil, are obvious destroyers of confidence. The same is true of the creeping erosion of investment values through the effect of plunging currency depreciation on working capital (with no related tax relief) and the tendency toward socialism by default. These pose new and discouraging problems for corporate management and the professional investor.

By the same token, the new Latin American voices of social unrest which are being heard on every side, together with the call for socialistic solutions of economic problems, both worry and intimidate the foreign investor, as indeed they do his local counterpart, the domestic Latin American private investor.

It is against such a spectrum of economic, political, and social unrest that we have made our study and formulated our recommendations. Our proposals will be insufficient to complete the task unless the philosophy of economic liberty and equal opportunity which is the basis of the free enterprise system, and which has developed the United States to its present greatness, is brought to bear in every aspect of economic, social, and political life in Latin America.

It would be a fatal error to attempt to equate the varying conditions of the Republics of Latin America with conditions in the United States, just as it would be a fatal error to equate the Latin American Republics with one another.

These countries today present a mixed picture of advanced stages of development side by side with conditions which are centuries behind the times. It represents a picture of rapid economic growth, of great new cities as modern and industrialized as any in the world, whose peoples live within an hour's travel of fellow citizens residing in 12th-century conditions. For example, in Brazil it has been estimated that in 1900 there were 54,000 persons employed in industry. Twenty years later, in 1920, there were 244,000. By 1950 there were 1,280,000 and the present figure is very close to 2 million. At the same time, the lot of the rural farmer in some parts of Brazil is untouched by progress and with deterioration of his land it may be actually worse than the lot of his grandfather.

Just as in the case of the industrial development of the United States in the 19th century, foreign private capital played a vital and important part in the industrial development of the Latin American countries. The success and the prominence of these enterprises have often been permitted to obscure the great forward surge of local investment and the emergence of an important domestic business and industrial class in Latin America. An authoritative estimate indicates that 70 percent of economic activity in Latin America is in the hands of private owners while 30 percent is controlled by the Government. Of the 70 percent of privately owned enterprise some 90 percent is estimated to be owned by Latin Americans and only 10 percent by foreigners.

B. The role of Latin American private capital in the Alliance

The fact that the private sector in Latin America is so heavily made up of local private investors means that the success of the Alliance for Progress depends to a great extent not only on the participation but most of all on the enthusiastic contribution of these Latin American businessmen. Experience of all Western countries has shown that the greatest economic progress is achieved by freemen under conditions of economic liberty when the productive forces of private investment and individual enterprise are unleashed and given maximum encouragement and support.

In furtherance of COMAP's study, one of our member companies recently conducted a survey of opinion on the Alliance for Progress among business leaders in 10 Latin American cities of 7 countries—Venezuela, Colombia, Ecuador, Peru, Chile, Argentina, and Brazil. In every city it was found that the principal concern of these men, whom the survey team found to be forward-looking, patriotic, and progressive, was the fact that the Alliance's philosophy, as they understood it, was based on government-to-government assistance rather than on the encouragement of the private enterprisers of Latin America.

These Latin American leaders pointed out that higher living standards in their countries had been achieved only by providing jobs in private enterprise and creating private payrolls. Although recognizing the vast amount that remains to be done they pointed with some pride to the achievements of private enterprise in raising living standards in their countries in wider employment, im-

provement in working conditions, advances in collective bargaining, relationships with organized labor and in the training and upgrading of local employees.

In material benefits to the population, they could show, and did show, private industry growth rates which are nothing short of remarkable in view of the extremely serious economic and financial handicaps which they face. These growth rates were achieved in a variety of significant fields which are accepted economic indicators of a rising standard of living.

They could point to a number of examples of visible progress. For instance, in the decade 1950–60. cement production increased in Colombia by 145 percent; in Ecuador by 250 percent and in Venezuela by 200 percent, compared to an increase of 45 percent in the United States. During the same period paper production other than newsprint increased by 75 percent in Argentina, 79 percent in Brazil, and 82 percent in Mexico. The U.S. increase was 53 percent in the same period.

Lubricant consumption is a revealing indicator. In the same decade this consumption increased 188 percent in Peru, 132 percent in Colombia, 100 percent in Brazil and Chile. This is in comparison with a 9-percent increase in the United States.

Automobiles in use increased over the same period 278 percent in Venezuela, 186 percent in Colombia, 185 percent in Brazil, 149 percent in Peru, as compared with 35 percent in the United States. In developing societies bus transportation is a key yardstick of social progress. In the decade bus registrations increased 290 precent in Brazil, 180 percent in Peru, 95 percent in Colombia, 87 percent in Venezuela, as compared with 17 percent in this country.

Other significant indicators such as sulfuric acid production, newsprint consumption, telephones in use, cigarette manufacturing, soft drink and beer production also showed increases greatly in excess of those achieved in the more developed countries. It is true, of course, that the Latin American increases developed from much lower bases. This demonstrates, however, the overriding importance of private enterprise which is 90 percent locally owned as the efficient source of a higher standard of living and the basis for the future growth of industrialization.

The Comap survey team found the younger business leaders of Latin America anxious to help the Alliance for Progress succeed but puzzled by what they regarded as a tendency to "export socialistic ideas to Latin America" when it seemed clear to them that private enterprise held the key to sound national development. They pointed to the phenomenal growth of new industries in Latin America—to the "banana explosion" in Ecuador which in the years since the end of World War II has seen the creation of an entirely new industry, putting that country first in the world in banana exports. This new industry's 1962 sales abroad are estimated at $84 million, putting it in first place among the country's producers of foreign exchange, and creating new farms, new jobs, new highways, satellite industries, new ports and development of new lands which previously had been only wilderness—all through private enterprise.

They pointed to the "miracle" of the huge new Peruvian fishmeat industry—conceived and created 100 percent by private investment and individual enterprise. This industry, which did not exist 10 years ago, now provides Peru with $100 million a year in foreign exchange, markets its products all over the world and has come to be one of Peru's top dollar producers, along with minerals, sugar, and cotton. This industry, too, has created new payrolls, new satellite industries, notable among which is a local boatbuilding industry which has constructed in Peru some 5,000 steel fishing boats. They told of the many new industrial companies which have come into existence as suppliers to the growing infant automobile manufacturing industry of Brazil and Argentina.

These men pointed to the remarkable growth of such relatively new industrial cities as Medellin and Cali in Colombia, Chimbote, Toquepala, and the Lima-Callao area of Peru, the miles of new factories between São Paulo, and Santos in Brazil, the rapid industrial growth of Mexico City and Monterrey, as evidence that private enterprise, not government, was the creator of economic growth and rising standards of living in Latin America for those in urban areas who have obtained employment through this industrial expansion.

In every country which our survey team visited, they found individuals and organized groups of businessmen who are devoting a great deal of their time, effort, and money to the development and carrying out of social programs in such fields as education, public housing, and job training; to the dissemination of information about the private enterprise system; to combating communistic influences in the universities and secondary schools; to community better-

ment activities; and most importantly, to the management of growing business enterprises to provide better opportunities for more people.

These creative businessmen are our natural allies in the Alliance for Progress and they are a main hope for Latin America's future. They should be sought out, encouraged and enlisted in the program. They want to help but, in too many cases, they have reason to believe that they are mistrusted and shunned.

One of the best means for correcting these misunderstandings and enlisting the cooperation of Latin American businessmen would be to set up, in each country, binational coordinating committees of progressive business leaders to render assistance to the local AID Director, not only in publicizing the objectives of the Alliance, but in selecting, screening, and advising on desirable projects and programs. This suggestion was made, again and again, as our survey team talked with businessmen in the various countries.

One particularly valuable specific advantage which the AID Directors could gain from the establishment of such local advisory committees would lie in the area of uncertainty which exists with regard to the significance of the Alliance for Progress policies with regard to land reform and tax reform. In each country in Latin America and even between regions within the same country agricultural and land conditions and economics differ. Since land reform has been made such an important concept in the Alliance philosophy, these local committees could assist the Alliance most significantly in furnishing local expertise and understanding with regard to land reform problems.

Similarly, it seems clear that in many instances the call for tax reform in Latin America is more truly a call for more efficient and modern tax administration and collection. Already some specialized technical assistance is being furnished through AID to Latin American governments.

The local committee of businessmen could be invaluable to the AID Directors in appraising directions in which this assistance could be furnished.

Thus these local committees, by bringing the rather broad concepts down to specifics in their areas, could do much to dispel uncertainties and doubts which may well be discouraging to foreign investors and to local private enterprisers.

C. Role of U.S. private capital in the Alliance

The urgent need for private capital—both domestic and foreign—in achieving the purposes of the Alliance for Progress was recognized at the Punta del Este meeting where the member nations pledged themselves, among other things, to the following objective:

"To stimulate private enterprise in order to encourage the development of Latin American countries at a rate which will help them to provide jobs for their growing populations, to eliminate unemployment, and to take their place among the modern industrialized nations of the world."

It was prescribed, moreover, that national development programs of the Latin American countries should incorporate "* * * the promotion through appropriate measures * * * of conditions that will encourage the flow of foreign investments and help to increase the capital resources of participating countries in need of capital."

Despite the attention that the Alliance for Progress has commanded since Punta del Este, there are widespraed erroneous impressions on the way in which the program is intended to accomplish its objectives. In particular, many people both in Latin America and in the United States have been under the impression that the Alliance for Progress is largely a program of U.S. Government financial aid conducted on a government-to-government basis. This impression has been unfortunate and all possible steps should be taken to correct it. Government grants and loans have an important and necessary place but private capital with its greater effectiveness and far larger potential is of the essence and is the basic long-term sustaining factor that can maintain a high rate of growth.

The objectives of the Alliance for Progress call for a very sustantial increase of investment in Latin America. In aggregate terms, investment must be raised about in line with the increase in the growth rate targeted. The minimum GNP growth target under the Alliance of 5 percent per year—2.5 percent per capita with a 2.5 percent population growth—is 32 percent higher than the annual growth of 3.8 percent[1] which actually occurred in the period 1957 to 1961, and this means that the amount of annual investment capital should be rising also by at least 32 percent.

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[1] Source: "OAS, Economic Survey of Latin America in 1961," ch. VI.

While a great deal needs to be done in the areas of public overhead capital and social and human development, it is clear that the major part of the investment must come from the private sector, which provided about 70 percent of all fixed investment in the decade of the 1950's in Latin America. In addition it is the private sector which must provide the management and technology needed to raise the living standards of the Latin American people.

Yet in the face of these targets, and the necessity of a rapid increase in private investment, there is evidence that private investment in Latin America has fallen significantly. In particular, the aggregate flow of private direct investment from the United States has been in a declining trend. Total net inflow of private U.S. investment, including portfolio capital and loans, has followed the same general pattern as follows:

U.S. private capital inflow into Latin America

[In millions]

	Net new direct investment	Net portfolio and loan capital	Total U.S. private capital inflow
1957	$1,163	$164	$1,327
1958	299	51	350
1959	218	144	362
1960	95	254	349
1961	141	119	260
1962, 1st half	(29)	111	82

Source: U.S. Department of Commerce.

While the year 1957 was unusual, primarily due to extraordinary payments made to Venezuela by petroleum companies, the figures exhibit a clearly declining tendency throughout the period, turning to disinvestment in the first half of 1962 in the net new direct investment category. What is of particular significance is that some of the most productive kinds of investment are being lost to Latin America at a time when special effort is called for to obtain more, not less, investment from all sources.

The productivity of U.S. manufacturing investments in Latin America is of a high order. Exact productivity comparisons of U.S. capital with other capital in similar industries are not available. However, from U.S. Department of Commerce data, it can be estimated that productivity of U.S. manufacturing capital in Latin America in 1959–60 was about 40 percent[2] on assets employed, while the average productivity of investment[3] in Latin America was about 25 percent.

Another striking indication of the contribution which U.S. manufacturing enterprises have made to Latin American economic growth is given by the rates at which production of U.S.-owned firms rose as compared with the manufacturing sector as a whole in the period 1955 to 1960.

Average annual percent change, 1955–60

	Index of total manufacturing production	U.S. manufacturing enterprises, sales value in dollars
Venezuela	9.0	31.0
Mexico	7.5	19.4
Brazil	14.0	19.0
Argentina	0	9.7

Source: UNECLA, U.S. Department of Commerce.

[2] Value added to GNP as percent of total assets employed.
[3] Consists of all capital including public capital.

It is clear from these data on most of the larger countries of Latin America that the advance in manufacturing production—the sector in which Latin America has done particularly well in the last 5 years—was paced and stimulated by U.S. investment. In each of the major four countries, U.S. manufacturers increased sales at very much higher rates than did the manufacturing industry as a whole. Correspondingly, a drying up of new U.S. capital inflow cannot fail to have an adverse effect on the economies of Latin America at this critical time.

A decline in net U.S. investment also affects local private capital directly. Local capital combines with U.S. equity capital in the assets of U.S. manufacturing companies in Latin America; in addition, locally owned enterprises depend on U.S. firms as users or suppliers for their products. Thus, U.S. capital either invested or withdrawn is likely to have a direct influence on investment or withdrawal of capital by local investors. Moreover, when U.S. private investment tends to withdraw, it is more than likely that local private investment is also declining and is seeking more secure investment opportunities in other areas of the world. That local capital outflow from Latin America has, in fact, accelerated in 1961 and 1962 is clearly evident from an analysis of the balance of payments of the seven largest countries[4] which show greatly increased residual outflows of funds, after taking account of the major known long-term capital items. These residual capital movements, which are indicative of capital flight, were as follows in the years 1951–62:

7 major Latin American countries, short-term capital inflows or (outflows)

[In millions]

	Yearly	Cumulative from beginning of outflow in 1953		Yearly	Cumulative from beginning of outflow in 1953
1951	$259		1957	($50)	($1,554)
1952	760		1958	(647)	(2,201)
1953	(666)	($666)	1959	(191)	(2,392)
1954	(263)	(929)	1960	(89)	(2,481)
1955	(119)	(1,048)	1961	(653)	(3,134)
1956	(456)	(1,504)	1962, estimated	(780)	(3,914)

NOTE.—Annual averages: 1951–57, (76); 1958–60, (309), 1961–62, (717).

Source: Calculated from IMF data.

After the large outflow of residual capital in the recession year 1958, there was an improvement in 1959 and 1960 but a drastically greater outflow in 1961 and 1962.

It is clear then, that the economic progress of Latin America is directly endangered by the drying up or flight of uch of its most productive potential investment. And it is equally clear that a determined and extraordinary effort is needed to halt or reverse this trend.

The flight of local national capital from Latin America should be considered in relation to the fact that the Alliance program anticipates raising $4 in Latin America for each $1 of external capital.

For our present purposes, it would be relatively easy to recommend actions which, if acceptable to the U.S. Government, could conceivably result in a flow of U.S. capital to Latin America approximating the total envisioned in the Alliance program. We might even, through extraordinary measures, offset a continuing flight of local national capital. This, however, if it departed from the need to encourage local Latin American initiative in creating a more favorable climate, would change the entire concept of the Alliance as a plan to promote sound conditions for economic development for the long run. Fundamentally we

[4] Major countries analyzed include Argentina, Brazil, Chile, Colombia, Mexico, Peru, and Venezuela.

must be able to look to the time when the countries of Latin America can secure much needed capital by the very fact of a hospitable climate for private investment. This requires free markets, the rule of law, and respect for capital. Private foreign capital cannot be driven, it must be attracted, and investors understandably will shun countries where they encounter currency disorders, exchange controls, confiscatory taxation, expropriation, and the like.

Thus, as a first basic requirement for the attainment of our objective of accelerating the contribution of U.S. investors to the Alliance for Progress, we must take a strong stand in support of the position adopted by the Council of Finance Ministers at the recent Mexico Conference of the Inter-American Economic and Social Council:

"* * * the private sector should have available incentives to strengthen the role which it is destined to play in the economic and social growth of Latin America under the Alliance."

The Council also reminded governments that:

"The flow of foreign private capital to Latin America has diminished and there is strong evidence of substantial capital flight from Latin America. Taking into account the limitations to the availability of public funds, it is clear that the objectives of the Alliance cannot be achieved without the full participation of the private sector and adequate measures must be taken to assure maximum contribution to growth by the private sector."

The actions taken by some Latin American governments themselves have been a prime source of discouragement to U.S. as well as local private investment and we strongly urge that the stand taken by the Council of Ministers at Mexico be supported. However, it is concluded that it would be extremely shortsighted if this Committee went no further than to suggest that the U.S. Government take a strong stand with the Latin American governments against restrictive actions on the private sector. This course by itself would not compensate for the fundamental economic conditions in most of the countries in Latin America which have in considerable degree been responsible for the kinds of policies that have been unfavorable to foreign private capital.

As a part of the task of developing recommendations, we are analyzing major influences on economic progress in Latin America. We have concluded that there is little hope for creating the kind of climate that U.S. investors want in Latin America without increasing substantially the amount of assistance which is being extended, and even then it is unlikely that normal conditions attractive to foreign capital can be created for a number of years. Certainly the continuance of the Castro influence will be a major deterrent.

In the meantime, therefore, and while the risks are so great and the rates of return so disproportionately small, actions must be taken by the U.S. Government to offset a part of these risks and raise the returns in order for the targeted amounts of U.S. private capital to be invested in Latin America. It is with these actions, necessary on the part of the U.S. Government, that we are mainly concerned here.

The approach that has been taken in our recommendations is one which we believe will provide a degree of assurance that the targets will be attained. Anything short of this, we firmly believe would be a disservice. Rather than fall far short once again, it would be far preferable to provide adequate authority from the beginning in view of the emergency nature of the problem. The most desirable course of action appears to be a maximum, early impact program that will overcome the doubts as to the ultimate success of the Alliance. It is in the light of these requirements and in the spirit of scoring an early success that specific recommendations have been formulated.

D. U.S. private investment by major sectors

In formulating action to encourage private investment it is important to examine the composition of investment by sector. Information is available in considerable detail for the three major investment sectors: manufacturing, petroleum, and mining and smelting. These three industries had a total net new U.S. direct investment, Latin America including Western Hemisphere dependencies, of $149 million in 1961. In addition to net new direct investment, the trend of investment activity overall and in the three major sectors can be appraised particularly in terms of the increase in book value (net new direct investment plus retained earnings) and in terms of outlays for fixed assets (property, plant, and equipment).

Net new direct investment.—For perspective, the following table shows the breakdown by year over the period 1957–61 for net new direct investment for the three major industries:

Net new U. S. direct investment

[Dollars in millions]

Year	Latin America including Western Hemisphere dependencies: Manufacturing	Petroleum	Mining and smelting	Total	Manufacturing as percentage of total manufacturing, petroleum and mining and smelting	Petroleum as percentage of total manufacturing, petroleum and mining and smelting	Mining and smelting as percentage of total manufacturing, petroleum and mining and smelting
1957	$99	$867	$137	$1,103	9.0	78.6	12.4
1958	70	163	81	314	22.3	51.9	25.8
1959	56	50	90	196	28.6	25.5	45.9
1960	125	24	(60)	89	140.4	27.0	(67.4)
1961	73	41	35	149	49.0	27.5	23.5
Total	$423	$1,145	$283	$1,851	22.9	61.8	15.3

Source: U.S. Department of Commerce

It is of interest to the problem of encouraging an increased flow of investment that, excluding the unusual year of 1960 when there was a net outflow in the mining and smelting industry, investment in manufacturing has accounted for a persistently greater share of the total, increasing from only 9 percent in 1957 to 49 percent in 1961. In 1960, manufacturing accounted for 140 percent of the total net new direct investment and for the last 2 years, 1960 and 1961 combined, manufacturing accounted for 83.2 percent of the total. Correspondingly, investment in petroleum has declined from the peak of $867 million in 1957, when it accounted for 78.6 percent of the total, to only $41 million in 1961, when it accounted for 27.5 percent of the total. At the same time, investment in mining and smelting has declined from $137 million in 1957 to $81 million in 1958, when it accounted for 25.8 percent of the total and to $35 million or 23.5 percent in 1961.

The sharp decline in absolute amounts and in percents of the total in petroleum and mining and smelting relate, in large part, to political deterrents to new extractive investments in Latin America and to a lesser degree, to the development of resources elsewhere.

Net new direct investment and retained earnings.—In addition to net new direct investment, the book value of U.S. investments in Latin America is affected also by retention of a part of earnings. The total of net new U.S. direct investment and retained earnings of U.S. enterprises in Latin America, including Western Hemisphere dependencies, can be seen in the next table for the three major industries.

Net new U.S. direct investment and retained earnings

[Dollars in millions]

Year	Latin America including Western Hemisphere dependencies: Manufacturing	Petroleum	Mining and smelting	Total	Manufacturing as percentage of total manufacturing, petroleum and mining and smelting	Petroleum as percentage of total manufacturing, petroleum and mining and smelting	Mining and smelting as percentage of total manufacturing, petroleum and mining and smelting
1957	$166	$965	$150	$1,281	13.0	75.3	11.7
1958	129	187	104	420	30.7	44.5	24.8
1959	127	78	104	309	41.1	25.2	33.7
1960	211	63	(68)	206	102.4	30.6	(33.0)
1961	157	84	44	285	55.1	29.5	15.4
Total	790	1,377	334	2,501	31.5	55.1	13.4

Source: U.S. Department of Commerce.

It can be noted that the trend in the total of net new direct investment and retained earnings has followed much the same pattern as net new direct investment by itself; i.e., the percentage of the total represented by manufacturing has increased over the period and in 1961 accounted for 55.1 percent of the total for the three sectors. Petroleum and mining and smelting on the other hand both have decreased in absolute amounts and in percent of the total over this period.

Plant and equipment expenditures.—In addition to the inflow of net new direct investment and the retention of earnings by U.S. enterprises in Latin America, the level of investment activity can be measured meaningfully by expenditures of U.S. enterprises on property, plant, and equipment. These have shown the following trend, 1957–61:

Property, plant, and equipment expenditures [1]

[In millions]

Year	Amount	Year	Amount
1957	$1,429	1960	$625
1958	967	1961	653
1959	789		

[1] Including Western Hemisphere dependencies. Including only the following industries—manufacturing, petroleum, and mining and smelting.

Source: U.S. Department of Commerce.

As can be seen, there has been a sharp decline in property, plant, and equipment expenditures from the peak of 1957 and likewise from the levels of 1958 and 1959. In order to test current investor attitudes on plans for expenditures, a telephone survey was conducted, by the Department of Commerce on November 14 and 15, of 21 large manufacturing companies, and the results indicate a moderate cutback from previous plans for 1962 and 1963, with further cutbacks in 1964. Furthermore, since a substantial part of the investment programs was conceived in 1960 and 1961, it is the conclusion of those making the survey that there could be a very sharp decline in the actual outlays as time goes by.

It is significant to note also that the trend of property, plant and equipment expenditures is very different as between the petroleum and mining and smelting industries where these expenditures have been declining steadily since 1958, and manufacturing where some increases have been maintained. The following table shows the expenditures in relation to their main source of financing, depreciation, and depletion allowances.

U.S. INVESTMENTS IN LATIN AMERICAN MANUFACTURING, PETROLEUM, AND MINING AND SMELTING

Depreciation and depletion compared to plant and equipment expenditures

[Dollars in millions]

	Manufacturing			Petroleum			Mining and smelting		
	Depreciation allowances	Plant and equipment expenditures	Plant and equipment expenditures as percent of depreciation allowances	Depletion and depreciation allowances	Plant and equipment expenditures	Plant and equipment expenditures as percent of depletion and depreciation allowances	Depletion and depreciation allowances	Plant and equipment expenditures	Plant and equipment expenditures as percent of depletion and depreciation allowances
1957	$45	$174	386.7	$224	$1,039	463.8	$79	$216	273.4
1958	60	201	335.0	300	548	182.7	75	218	290.7
1959	70	193	275.7	327	449	137.3	74	147	198.6
1960	80	207	258.8	350	340	97.1	92	78	84.8
1961	105	249	237.1	404	309	76.5	102	95	93.1
1957–61 totals	360	1,024	284.4	1,605	2,685	167.3	422	754	178.7

Source: U.S. Department of Commerce.

As can be seen, while property, plant and equipment expenditures in manufacturing have increased somewhat over the period, there has been a sharp decline in these expenditures in petroleum and mining and smelting as compared with the 1957–58 levels. Much of this decline, of course, is the result of the obstacles placed on investment in the sectors, such as the termination of new concessions for petroleum development and the high tax rates applying. In addition, the generally adverse political climate for investments in the extractive industries has been a massive deterrent.

U.S. enterprises in manufacturing have increased their outlays for property, plant and equipment to levels considerably in excess of depreciation allowances; e.g., these expenditures were 259 and 237 percent of depreciation in 1960 and 1961, respectively. The reverse is the situation in mining and smelting where the expenditures were only 85 and 93 percent of depreciation and depletion in 1960 and 1961. Similarly, in petroleum these outlays were only 97 and 77 percent of depreciation and depletion. The extent to which depreciation and depletion allowances have been used for fixed asset outlays has declined sharply in petroleum and mining and smelting since 1958.

In no one of the major industrial sectors examined can it be said that there is investment growth of the magnitude required under the goals of the Alliance.

E. The role of European capital in Latin America

In any discussion of the problem of economic development and raising of the standards of living of the countries of Latin America, it is essential that consideration be given to the role of European private investment as well as that of U.S. private investment. There are encouraging signs of a healthy interest on the part of European investors and, in fact, considerable investment flow from Europe has been evident in recent years. The Economic Committee of the NATO Parliamentarians, under the chairmanship of Senator Jacob K. Javits, has been working with the officials of the Organization for Economic Cooperation and Development (OECD) as well as with officials of the Common Market and the inter-American organizations and with private European industrialists, toward creating a coordinated European-United States-Latin American effort in this direction.

At the recent meeting (November 16, 1962) of the NATO Parliamentarians a recommendation was approved which can have major significance. Taking note of the need for accelerated economic development of Latin America under the Alliance for Progress, the NATO Parliamentarians recommended the calling of a conference on private enterprise and public cooperation for Latin American development to be held during 1963. The organization of the conference would be in the hands of the Secretary General of the OECD and the President of the Inter-American Development Bank in coordination with the Secretary General of the OAS.

Such a conference could well bring to fruition the constructive work done by the Economic Committee and other European groups and we urge full support of the conference. Contemporaneously, the private enterprise community of Europe held a major conference on Latin America in Brussels in November under the auspices of the International Association of Christian Employers (UNIAPAC). At this meeting a group of the top industrial and financial leaders of Europe declared their readiness to join in all forms of constructive effort to work with both United States and Latin American private enterprisers in the development of the Latin economies.

It is particularly important that the proposed conference recommended by the NATO Committee also undertake questions of trade at a time when firm and long-range policies must be formulated governing the access to the European Common Market of tropical agricultural products from both Africa and Latin America.

F. Criteria for recommendations

It is the primary purpose of the recommendations made here to stimulate action toward the attainment of the targets set for U.S. private investment at Punta del Este. In the process, a contribution should be made to more fundamental goals—the improvement of the basic strengths of these economies with the collateral advantage in the long-range health of U.S. private investment in Latin America. With these objectives in mind, a number of principles have been applied as guides in developing our recommendations.

(1) Recommendations with respect to U.S. investment should not be made without reference also to the effect on local Latin American investors. If we succeeded only in getting U.S. investors to take up the opportunities which are available and that might otherwise be taken up by the local investors, we would not have added much to the net situation in Latin America. Furthermore, any one-sided program in favor of U.S. investors could not help but create unfavorable local attitudes. The recommendations, therefore, have been made on the grounds that they will not only stimulate U.S. investment but local national investment as well, both immediate and long range, without which these economies cannot hope for sustained growth. They are designed to increase the total of all private investment.

(2) The recommendations have as a first purpose the stimulation of new investment. Obviously, however, there is the need in many countries of Latin America to raise the profitability of existing U.S. enterprises where the returns are disproportionately small solely due to the unusual conditions specific to these countries. Profitability on existing investments cannot fail to affect decisions on new investments. The profitability of existing investments affects new investment directly since a large part of capital expenditures of U.S. firms in Latin America comes from plowed-back earnings. Department of Commerce data show that in 1961, 34 percent of capital expenditures in manufacturing came from earnings retained in Latin America.

(3) It is of primary importance to encourage those enterprises which will contribute most to providing new jobs and to the upgrading of skills, both managerial and technological. This means that there must be a rapid buildup, particularly in the manufacturing and servicing sectors of the economies. As a result of this need and the realities of investment opportunities in the extractive industries, our recommendations relate heavily to manufacturing and servicing but do not exclude the extractive industries.

(4) A guiding principle in developing our recommendations has been recognition of the mutuality of interest among the United States and Latin American governments and private investors in the Alliance for Progress. This is a basic principle of the Alliance itself and should be observed in taking action with reference to private investment. It provides the basis for cooperation on the part of the U.S. Government in actions initiated by Latin American governments. For example, tax sparing is an area of initiative on the part of Latin American governments to attract new investment. In the spirit of the Alliance, it seems to us compelling that the U.S. Government not cancel out the benefit of this initiative on the part of Latin American governments by the inability of U.S. investors to take advantage of these incentives under U.S. tax laws. Therefore, where Latin American governments have provided special tax incentives for new investment, we consider it one of the very highest priorities for action on the part of the U.S. Government to introduce tax sparing on an across-the-board basis with respect to all U.S. investments in countries that are participants in the Alliance program.

(5) Finally, the individual parts of the total of recommendations should be regarded as indispensable pieces of a completely interrelated package. We sincerely believe that this package of recommendations is critical to the degree of assurance that the Alliance for Progress should have for its ultimate success. Any whittling away at individual pieces or their elimination from this package, we feel, would be highly damaging to the agreed objective.

With the above principles as guidelines, we have included recommendations in the following areas:

(*a*) *Local currency loans.*—Provide assistance to meet the problem of currency devaluation by the creation of a substantial pool of local currency funds for loans to the private sector to be available to both United States and locally owned enterprises.

(*b*) *Taxation.*—

(1) Investment incentive credit: Provide an investment incentive tax credit to encourage U.S. private investment in countries of the Western Hemisphere similar to the recent investment incentive credit to U.S. business.

(2) Tax certificate: Provide a tax certificate permitting a minimum return on capital of 5 percent after tax to be used by U.S. companies in selected enterprises as a credit against their U.S. income tax liability when such minimum return is not achieved.

(3) Tax sparing: To encourage and stimulate new investment in Latin America amend U.S. tax law to provide for tax sparing where the host countries offer tax incentives as part of a program to attract new basic industries.

(4) Tax allowance for foreign exchange loss: Assist in meeting the problem of currency devaluation by allowing a tax deduction against current taxable income for losses due to currency devaluation.

(5) Alliance for Progress corporation: Provide for a special type of U.S. corporation to hold investments in, or conduct operations on its own behalf, in the less developed countries of the Western Hemisphere, and which would be allowed deferral of taxes on income until distributed to its shareholders so long as earnings were reinvested in the less developed countries of the Western Hemisphere.

(6) U.S. income tax allowance for foreign investment losses:

A. Where stock becomes worthless.

B. Where stock is disposed of at a loss.

(*c*) *Specific and all-risk guarantees.*—

(1) Extension of investment guarantees to all less developed countries of the Western Hemisphere.

(2) Broadened application of extended risk coverage.

(3) Extension of war risk coverage, including revolutions and insurrection, to also include damages resulting from riots and civil disturbances.

(4) Revision of present contract procedures and fee schedules to provide for a multirisk contract where an investor elects to take two or more specific-risk guarantees.

(5) Standardization and simplification of contract language.

(6) Increase in the authorized statutory limits of different kinds of guarantees.

(7) Recommendation that processing fee, if adopted, be credited against initial fee payable by investors entering into final contract.

(*d*) *Other methods of private investor participation.*—Recommend in very selective cases the use of management contracts, cost-plus contracts, leasing arrangements, government equity financing and consortia arrangements for multiproject developments. This applies especially where there is political sensitivity in industries closely associated with the public interest, such as electric power, transportation, and other utilities.

We are, of course, conscious of the fact that some of the recommendations that follow will cost money either in the form of lost revenue to the Treasury or in the assumption of risks. We are not in a position to estimate these costs. A large sum does not appear to be involved particularly in relation to the whole AID program for this area. It is our view that the benefits of the private sector participation will be much larger than the results of some of the present AID expenditures and hence more than justify the cost.

III. LOCAL CURRENCY FINANCING

Provide assistance to meet the problem of currency devaluation by the creation of a substantial pool of local currency funds for loans to the private sector to be available to both U.S. and locally owned enterprises.

The economic and political risks which confront investments in Latin America include the very substantial risk of exposure to currency devaluation. The balance-of-payments problem, inflation, and consequent currency depreciation have, for many years, been a way of life in most Latin American nations, with a resulting adverse effect on earnings in terms of U.S. dollars, as well as an erosion of U.S. dollar investments in Latin American enterprises, particularly manufacturing.

The effects of exchange devaluation on U.S. private investment in Latin America is the subject of a separate memorandum dated November 10, 1962 (see app. A). This memorandum points up the serious effects of exchange devaluation on the dollar profitability of U.S. investments in Latin America. The losses incurred are actual and immediate for U.S.-based corporations. Generally accepted accounting practices and the Securities and Exchange Commission require that such losses be reflected currently against the profit and loss of the U.S. parent company.

In any consideration of the problem of stimulating an increased flow of private investment, the impact of foreign exchange devaluation as a deterrent to investment in Latin America is a factor which must be recognized, particularly in the light of the violent exchange depreciation which has taken place this year in the currencies of major Latin American countries such as Argentina, Brazil, Chile, and Colombia.

Basically, there are two ways to meet the problem of currency devaluation which offer a substantial means of mitigating its impact. These are:

(1) Creation of a substantial pool of local currency capital funds for loans to the private sector to assist in the financing of working capital and local curency fixed asset expenditures.

(2) Allowance of a tax credit against the U.S. income tax liability of the U.S. investor for foreign exchanges losses on Latin American investments resulting from currency devaluation. (Discussed under the tax recommendations of this memorandum.)

Institutional funds in Latin America are extremely limited and commercial banking facilities are inadequate to meet the needs of industry (both local and foreign owned), let alone an expansion of the private business sector. Additional amounts of local currency capital should be made available to supplement the capital of investors, both United States and local.

Public Law 480 has done relatively little to provide the much-needed local currency capital in Latin America. According to Public Law 480 statistics, only 6.6 percent or $45.5 million, out of a total of $694.6 million of title I, Public Law 480 foreign currency funds provided in Latin America through June 30, 1962, were allocated to private enterprise. The allocation of the funds as reported was as follows:

Planned use of foreign currencies	Public Law 480	Dollar equivalent (millions)	Percent
Common defense	Sec. 104(c)	2.3	0.3
Grants for economic development	Sec. 104(e)	28.5	4.1
Loans to private enterprise	do	45.5	6.6
Loans to foreign governments	Sec. 104(g)	473.2	68.1
U.S. uses		145.1	20.9
Total		694.6	100.0

Source: 16th Semiannual Report of Activities Carried on Under Public Law 480, 83d Cong., dated Aug. 20, 1962.

Under the Cooley amendment to Public Law 480, approved August 13, 1957, up to 25 percent of foreign currency proceeds from sales of agricultural commodities can be used for loans to private enterprise. As the above figures show, this has not produced a substantial pool of funds for private enterprise loans.

A reorientation of the lending procedures under Public Law 480 could make an increased contribution in those countries where the sale of surplus U.S. agricultural commodities is possible. In the past, these have included Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Peru, and Uruguay. Public Law 480 proceeds as a source of future local currency loans to private enterprise will, of course, depend on agreements with the Latin American countries for the sale of surplus agricultural commodities.

One example of reorientation occurred in August 1962 when a loan agreement was finally concluded with Brazil whereby $7 million of section 104(g) funds under the May 1961 commodity sales agreement with Brazil are to be made available for local currency loans to private enterprise through Banco Nacional do Desenvolvimento Economico (BNDE).

In similar fashion, the full 25 percent permitted by the Cooley amendment to Public Law 480 should be obtained. Such has not been the case in certain countries. A particular case is Brazil where, prior to the August 1962 agreement, none of the Public Law 480 funds had been allocated to the private sector. It is our further understanding that no loans under the August 1962 agreement have as yet been made to the private sector.

If the executive branch of Government wishes to use Public Law 480 as a means of assisting the private sector in economic development, an amendment to the law increasing the Cooley percentage from 25 to, say, 50 percent could be sought. We would recommend a further amendment specifying that up to one-half of all the Cooley loans be made available for new investment by local companies, and the balance for investment by U.S.-owned companies similar to the recent Brazilian agreement. At the same time, loans to foreign governments (sec. 104(g)) which through June 30, 1962, accounted for 68.1 percent of total availabilities, should be reduced. These latter loans are primarily made for expenditures by governments in the public sector.

However, Cooley funds can be generated in only those countries in need of, and interested in, purchasing U.S. surplus agricultural commodities. Even with the amendments suggested, only relatively moderate sums would be made available. What is needed are new sources of local currency funds under U.S. Government control to be loaned to the private sector. While we share the U.S. Government's reluctance to make pure balance-of-payments loans, we recognize that such loans will at times continue to be necessary. Where such situations arise we suggest the following as one method of improving the position of the private sector. This is to require the establishment of a local currency account in the equivalent value of dollar loans such as balance-of-payments dollar loans, to be used for loans to both U.S. and local private enterprise. Thus, when the AID or other U.S. agency makes a loan of this type, the recipient government should be required to establish an equivalent amount of local currencies in what might be called a counterpart account. In such a case, the recipient government will acquire the counterpart local currencies through the sale of the dollars.

Because of U.S. balance-of-payments problems, it should be stipulated that the dollars may be used only to finance imports from the United States or to cover payment of other dollar obligations in the United States.

The local currencies deposited in the counterpart account should be used to make loans to both U.S. and local private firms, through appropriate commercial lending institutions. By this technique, sizable funds may be shifted to the much more effective private sector.

Admittedly the U.S. Government would have to use firmness and persuasion to implement such a plan in certain Latin American countries, and in some it may not be feasible at all, at the present time. In terms of the ideal, it would, of course, be preferable if the governments of the host countries were not involved at all and the funds were made available directly through the commercial banking system. In all events, the availability of the foreign currencies should be on condition that they are used for business purposes in the host country and that the local U.S. AID administration retains the right of guidance and audit.

IV. TAX RECOMMENDATIONS

While taxes are not the only criteria which managements must take into consideration in weighing each new investment, they are nonetheless an important factor in the potential profitability of a new investment. At best, many new Latin American businesses are marginal, especially in the early development years. Business managements, recognizing their responsibilities to stockholder, must weigh each new investment against the business and political risks involved, and unless they can foresee a profit commensurate with those risks, they will not invest. It is quite natural that the tax factor be considered and it will include the benefits of tax incentives, if any, available to the investor.

Thus, management will be more likely to invest if the profit outlook is improved by tax incentives in the early development years. This being the case, tax incentives become a vital factor in any decision to commit new or additional capital funds for investment in the less developed countries of the Western Hemisphere.

To achieve the objectives of the Alliance for Progress, the following changes in U.S. tax policy are considered essential:

(*1*) *Investment incentive tax credit*

> Provide an investment incentive tax credit to encourage U.S. private investment in countries of the Western Hemisphere similar to the recent incentive credit to U.S. business.

In the Revenue Act of 1962 the principle of an investment incentive credit against a U.S. taxpayer's tax liability was provided to stimulate the economy through encouragement of investment in productive facilities. An extension of this principle, modified to meet the problem of stimulating investments in the less developed countries of the Western Hemisphere, would, in the opinion of Comap, assist as part of a tax incentive package to encourage an additional flow of private capital under the Alliance for Progress. However, the amount of the credit and the mechanism of its application will have to be tailored to assist the U.S. investor in meeting the risks under today's political and economic atmosphere in Latin America. A credit of 7 percent as applied to U.S. domestic investments in productive facilities is effectively only approximately a 3½ percent credit after factoring in the reduction in the depreciation base of the new asset.

As an incentive toward achieving the objective under the Alliance for Progress of encouraging a substantial increase in the rate of direct private investment in the private sector of the less developed countries, it is suggested that Congress extend the principle of the investment incentive credit to investments under the Alliance for Progress. Because of the special problems in Latin America it is recommended that the credit be on the order of magnitude of at least 25 percent of all new and additional investment. All credits would, of course, apply as a reduction of the tax cost basis of the investment for the computation of future gain or loss on the investment.

Having in mind the high degree of risk and the low rate of return prospects in relation to the risks under today's investment climate in the Latin American countries, the following table will serve to demonstrate the need for an investment incentive credit on the order of magnitude of 25 percent, and possibly as much as 50 percent, if new and additional U.S. private capital is to be encouraged to assume the risks of investment in Latin America.

Assumed actual rate of return per dollar of investment (percent)	Effective return assuming		Investment tax credit necessary to achieve a 15 percent return
	25 percent investment tax credit	50 percent investment tax credit	
	Percent	*Percent*	*Percent*
1	1.3	2.0	93.3
2	2.7	4.0	86.7
3	4.0	6.0	80.0
4	5.3	8.0	73.3
5	6.7	10.0	66.7
6	8.0	12.0	60.0
7	9.3	14.0	53.3
8	10.7	16.0	46.7
9	12.0	18.0	40.0
10	13.3	20.0	33.3
11	14.7	22.0	26.7
12	16.0	24.0	20.0
13	17.3	26.0	13.3
14	18.7	28.0	6.7
15	20.0	30.0	

It will be seen from the above table that a 25-percent investment credit will, in effect, improve the effective rate of return to the investor by one-third on the net investment after the credit. A 50-percent credit, and this would be necessary to attract the capital needed to achieve the goals of the Alliance if other tax recommendations are not adopted, will have the effect of doubling the actual return. Thus, in the case of a project where the actual return is only 5 percent after taxes (which is not unusual for new ventures in today's climate in Latin America) a 25-percent investment credit would increase the effective return to 6.7 percent, and a 50-percent credit would increase the return to 10 percent.

(2) *Tax certificate*

Provide a tax certificate permitting a minimum return on capital of 5 percent after tax to be used by U.S. companies in selected enterprises as a credit against their U.S. income tax liability when such minimum return is not achieved.

In addition, and to direct investments into specific projects considered of importance to the Alliance, a special incentive credit to investors who would undertake certain qualified projects under the Alliance should be provided in the form of a certificate credit against U.S. taxes of the investor to be spread over a period of years. To qualify, each investment would have to be approved by the U.S. Government and certified as essential to the development of the host country and as requiring protection, in the form of an incentive credit, against excessive risks of low or no earnings in the development years.

The prospective investor would be required to submit to the appropriate agency of the U.S. Government full information as to the location, purpose of the project, plans for financing, and other pertinent data and, when required, evidence of approval of the project by the host country.

If the project is approved by the appropriate U.S. Government agency as essential to the objectives of the Alliance for Progress, a fixed percentage certificate,

say 5 percent after taxes, would be issued to the investor, certifying the investment and entitling the investor to the credit against his U.S. income tax liability.

To illustrate, a potential investor considers the projected return after U.S. tax on a new venure too low to warrant taking the risk involved. To secure the development of the project, the U.S. Government would grant a tax certificate for, say a period of 10 years, equal to a 5 percent after-tax return on the investment which certificates would be accepted in any year by the U.S. Government as a credit against the investor's U.S. income tax liability. To the extent the certificate exceeded the investor's U.S. tax liability, it could be carried forward and applied against future taxes.

The effect would be to guarantee the investor a minimum return on the investment. By applying the certificate as a credit against the U.S. investor's overall tax liability, the investor would receive the benefit of the incentive credit regardless of whether the new foreign investment operated at a nominal profit or at a loss, or whether such earnings as there might be were retained in the business and reinvested instead of being paid out to the investor. This would assist in reducing the risk to the investor and provide the U.S. parent company with dollars to meet fixed charges and dividend requirements to public shareholders in the United States.

The certificate credit procedure would encourage the retention of earnings in the business abroad for expansion of the business, if needed. To encourage the reinvestment of earnings during the development years, it is further suggested that any reinvested earnings during the term of the certificate would provide a base for increasing the tax certificate credit by the appropriate percentage of any such reinvested earnings.

To the extent earnings are distributed to the investor, they would be reported for tax purposes. It would be further provided that the certificate credit for any given year shall be reduced by the amount of any earnings distributed to the investor in excess of 5 percent after taxes in such year. The objective would be for the U.S. Government to share in any loss, or in any shortfall below the fixed percentage rate during the period of the investment incentive credit. To insure against any undue accumulation of retained earnings during the period of the credit, the period of recapture might be extended for a fixed period of years beyond the term of the tax certificate incentive credit with appropriate safeguards to the U.S. Government.

(3) Tax sparing

To encourage and stimulate new investment in Latin America amend U.S. tax law to provide for tax sparing where the host countries offer tax incentives as part of a program to attract new basic industries.

To develop their economies and put people to work, a number of Latin American countries have introduced tax incentives of one sort or another to attract new industries. However, they have discovered that their proferred incentives do not prove as attractive to the U.S. investor as anticipated, because the U.S. tax laws largely negate the benefits of the incentives. This is quite contrary to the case in some other industrialized nations, such as France, the Netherlands, Belgium, and Canada, which by their laws either do not tax foreign earnings at all, or give them favorable tax treatment, with the result that their investors obtain some or all of the benefits of local tax sparing on oversea investment.

The position of the Treasury staff which opposes tax sparing is set forth in a staff paper dated October 18, 1962. The Treasury memorandum is responded to in a memorandum, a copy of which is attached as appendix B. This memorandum (app. B) also sets forth our views on the merit and effectiveness of tax incentives combined with tax sparing as a means of stimulating the flow of private capital into the less developed countries.

The need is for rapid U.S. investment in the Latin American countries, and one important incentive to this end, which is the least costly of all incentives to both the host country and the United States would be prompt enactment of a statute recognizing a credit against U.S. taxes for taxes spared by the host countries as an inducement to new investment. Although the treaty procedure as a basis for implementing tax sparing is, ideally, to be preferred because of the opportunity to obtain a quid pro quo, it has proven so unsatisfactory in practice since 1954 that we recommend its abandonment and the substitution of an amendment to the U.S. tax law granting a credit against U.S. income tax for income taxes spared by less developed countries of the Western Hemisphere. If the need is felt for some control over the application of the tax sparing amendment,

such control might be exercised through a provision that it would only apply to taxes spared by countries designated by the President.

The Treasury staff, in its memorandum of October 18, 1962, expresses the view that tax sparing will encourage the repatriation of earnings and capital contrary to the objectives of the Alliance for Progress. We do not agree with this conclusion. It fails to recognize the realities that if an increase in the flow of capital investments in the underdeveloped countries of Latin America is to be achieved, reasonable returns of the investments must be anticipated. Institutional lenders and shareholders in U.S. corporations who represent the major potential source of private capital for investment in Latin America expect their loans to be serviced and reasonable dividends on their shareholdings to be paid at regular intervals.

The Treasury's apprehension, although not shared by us, could be met by providing for a carryforward of the benefits of tax sparing where tax incentives are granted by the host country, and thus eliminate any incentive for rapid repatriation such as the Treasury fears. This could be accomplished by a simple amendment to the U.S. tax law, which would presume that any dividends, when distributed by a company which has benefited from a tax incentive, are distributed first from earnings accumulated during the period of the tax incentive until such earnings have been fully distributed, after which the current presumption under the law would again apply; i.e., that dividends were presumed to be paid first from the latest accumulated earnings. This would eliminate any possible motive to repatriate profits at an accelerated rate.

Tax incentives have proved effective in attracting capital to Puerto Rico under its Operation Bootstrap program, and they can do the same for many of the Latin American countries if our Government will reciprocate by making the tax incentives meaningful to the U.S. investor through tax sparing. In the absence of tax sparing, U.S. investors in Puerto Rico have been able to realize the full benefit of the tax incentives by operating through a subsidiary U.S. corporation which could be liquidated after the tax holiday, with the operation continuing as a branch of the parent thereafter. However, use of a U.S. corporation in other less-developed areas does not permit taking advantage of tax incentives in this way. Likewise, State and local tax incentives have done much in the United States to promote industry in the less-developed sections of the country.

It is our position that tax incentives by the host countries, combined with tax sparing by the United States, will be most effective in stimulating the flow of additional investments in Latin American countries and it is therefore our conclusion that enactment of tax sparing legislation is essential to the success of the private sector's contribution to the Alliance for Progress.

It should be noted that recognition of "tax sparing" was recommended in the report dated April 1959 submitted by Mr. Ralph I. Straus, at the request of the Department of State on the subject of "Expanding Private Investment for Free World Economic Growth" prepared pursuant to section 413(c) of the Mutual Security Act of 1954, as amended.

(4) *Tax credit for foreign exchange loss*

> Assist in meeting the problem of currency devaluation by allowing a tax deduction against current taxable income for losses due to currency devaluation.

The effects of exchange devaluation on U.S. private investment in Latin America, particularly manufacturing and service industries, have been discussed in considerable depth in a separate memorandum dated November 10, 1962. The effect of currency devaluation, which is a way of life in Latin America, is one of the most adverse factors affecting the profitability of investments in Latin America. Although exchange losses are a cost of doing business in these countries, impairment of investments in subsidiary enterprises incorporated in Latin American countries, through loss in the value of working capital and the inadequacy, in dollars, of local currency provisions for depreciation, is not currently recognized as an allowable deduction for tax purposes, either in the United States or in the foreign country. Foreign exchange losses due to currency devaluation often are the difference between a profit and a loss on an investment in Latin America, particularly in a year of drastic currency devaluations such as have occurred in Argentina, Brazil, Chile, and Colombia in 1962.

It is the recommendation of COMAP that impairment of investments in subsidiary companies incorporated in less-developed nations that are members of the Alliance for Progress, through loss in the dollar value of local currency

working capital and through inadequacy, in dollar value, of local currency provisions for depreciation, be recognized as ordinary income deduction allowable to the parent company for U.S. income tax purposes. It is again of interest to note that the Straus report recommended that a deduction against ordinary income be allowed for tax purposes for foreign exchange loss required by the Securities and Exchange Commission to be shown in published financial statements.

(5) *Alliance for Progress corporation*

Provide for a special type of U.S. corporation to hold investments in, or conduct operations on its own behalf, in the less-developed countries of the Western Hemisphere, and which would be allowed deferral of taxes on income until distributed to its shareholders so long as earnings were reinvested in the less-developed countries of the Western Hemisphere.

It is recommended that there be created a special regime for taxation of Alliance for Progress corporations, in order to encourage and facilitate investments in the less-developed countries of the Western Hemisphere. Such a corporation would be a corporation domestic to the United States, similar to that contemplated in H.R. 5, 86th Congress (the Boggs bill). This would be a special type of U.S. corporation which would hold investments in companies operating in the less-developed member countries or conduct on its own behalf business operations in this area, or both. The income of such corporations would be free of U.S. tax so long as it was devoted to expanding investments in the less-developed countries of the hemisphere, and would be subject to U.S. tax only when distributed to its shareholders. This would provide a facility for use, free of U.S. tax, of the cash flow generated by investments in one or more of the less-developed member countries to develop and expand other investments in other less-developed countries. Here again, the Straus report recommended a similar type of domestic corporation to stimulate foreign investments.

(6) *U.S. income tax allowance of foreign investment losses*

(*a*) *Where stock becomes worthless.*—Under present law a U.S. parent company which owns at least 95 percent of the stock of a foreign operating subsidiary may deduct from ordinary income its loss on worthlessness of the subsidiary's stock and securities. However, where the stockownership is less than 95 percent, the loss is treated as a capital loss deductible only from the parent's capital gains, if there happen to be any, and if there are no capital gains, it is not deductible at all.

Today it is frequently desirable, and sometimes required by law, that local nationals hold substantial, and sometimes controlling, interests in new businesses established by U.S. investors engaged in operations abroad. We therefore recommend that losses arising from worthless stock or securities of companies operating in less-developed countries in the Western Hemisphere be allowed as deductions from ordinary income regardless of the amount of stock held by the U.S. investor and regardless of whether the investor is a corporation or an individual.

(*b*) *Where stock is disposed of at a loss.*—Under present law, if the U.S. parent company owns at least 80 percent of the stock of the foreign operating subsidiary it may not deduct any loss on complete liquidation of the subsidiary if the distribution in liquidation is less than the parent's cost of its subsidiary's stock. Whatever may be said about the propriety of this rule in cases of domestic subsidiaries which have deducted their own losses for U.S. tax puropses, it is clearly inappropriate when the subsidiary is one incorporated in and operating in a foreign country.

If the parent owns less than 80 percent of the subsidiary's stock, a loss on liquidation of the subsidiary is treated as a capital loss deductible only from the parent's capital gains, if there happen to be any, and if there are no capital gains it is not deductible at all. Losses on sales of the subsidiary's stock are also treated as capital losses. This rule was designed to limit the drain on the revenue caused by unlimited deduction from ordinary income of the extraordinary losses on securities realized during the great depression of the thirties. It is clearly inappropriate at a time when encouragement of U.S. investment in less-developed areas has become a part of the official policy of our Government.

We recommend therefore that all losses on liquidation of stock or securities of companies operating in less-developed countries in the Western Hemisphere be allowed as deductions from ordinary income even where the stock or securities are not entirely worthless, and that losses on sale of such stocks or securities also be allowed as deductions from ordinary income.

V. INVESTMENT GUARANTEE PROGRAM

A. Outline of the present program

(*a*) *Specific-risk guarantee.*—For countries where guarantees are available, AID offers investors protection against losses arising out of inconvertibility, expropriation or confiscation, and war, including revolution or insurrection.

Of the 32 Latin American Republics (excluding Cuba) and Western Hemisphere dependencies, a total of 28 are currently participating in the program. However, expropriation insurance is not available in 9 of the 28 countries, including countries such as Argentina, Chile, and Peru. Only five countries—Colombia, Dominican Republic, Nicaragua, Panama, and Venezuela—participate in all three specific-risk coverages. Two of the Western Hemisphere dependencies—Jamaica and Trinidad/Tobago which recently received their independence—have indicated their desire to negotiate agreements on their own behalf to cover all three risks. The nonparticipating countries include Brazil and Mexico.

Scope of Protection:

(1) Convertibility: Provides insurance against inability to convert foreign currency investment proceeds (capital and earnings) into U.S. dollars. Unavailability of foreign exchange resulting from blockage of conversion and transfer of currencies into U.S. dollars or undue delays by law or administrative action or introduction of discriminatory exchange rates would qualify as a basis for a claim under the guarantee. However, the convertibility guarantee is not intended to offer protection against depreciation or devaluation of local currencies.

(2) Expropriation: Protects equity and loan investor against expropriation or confiscation assuring compensation according to the terms of the contract. Government action, including revenue raising or regulatory measures whose substantive intent is to divest, which prevents the enterprise from operating or the investor from disposing of or recovering the assets is protected. Breaches by the host government of a contract with the investor where this materially affects the continued operation of the enterprise may be considered expropriatory.

(3) War risk: Protects against losses which are deemed the direct result of international war, revolution or insurrection, but does not protect investors from damages resulting from riots or civil disturbances.

The cost of each type of insurance is one-half of 1 percent of the face amount in the contract. For any portion of the face amount authorized but not elected for coverage in any given year, one-fourth of 1 percent "standby" fee is charged. The maximum term under any of the three types is 20 years.

(*b*) *Extended-risk insurance.*—The 1961 act provides for extended-risk guarantees to cover up to 75 percent of both loan and equity investments against loss from such risks (both political and economic) as the President may determine. Losses from fraud or misconduct for which the investor is responsible are excluded. Since no guarantees have been issued under the present program (although approximately $55 million is outstanding under prior Development Loan Fund "all-risk" authorization), there has not been developed a detailed program or a rate basis which, in any case, would be subject to negotiation between AID and the investor. It is understood that a fee of 2 percent is presently contemplated.

The 1961 act specifies that emphasis in granting extended-risk guarantees be placed on projects furthering social progress and development of small independent business enterprises. The act also makes special provisions for investments, by U.S. citizens or U.S.-chartered corporations, in pilot or demonstration private housing projects, particularly in Latin America, but including other underdeveloped nations.

B. Recommended changes in the investment guarantee program

1. Extension of investment guarantees to all less-developed countries of the Western Hemisphere.
2. Broadened application of extended risk coverage.
3. Extension of war risk coverage, including revolutions and insurrection, to also include damages resulting from riots and civil disturbances.
4. Revision of present contract procedures and fee schedules to provide for a multirisk contract where an investor elects to take two or more specific-risk guarantees.
5. Standardization and simplification of contract language.
6. Increase in the authorized statutory limits of different kinds of guarantees.
7. Recommendation that processing fee, if adopted, be credited against initial fee payable by investors entering into final contract.

The increasing attention given to the investment guarantee program, reflected in a very rapid rise in application and contracts negotiated, suggests the importance of this effort in stimulating U.S. private foreign investments. As of September 30, 1962, $1 billion of specific-risk guarantees had been issued, with $771 million currently outstanding. During fiscal year 1962, 91 specific-risk contracts totaling $307 million were completed, representing 42 percent of total guarantees outstanding. Applications for approximately $2.6 billion, of which approximately 42 percent relate to Latin America, were pending as of September 30, 1962. As more use is made of investment guarantees there arises a correlative interest in improving and refining the program.

The following proposed revisions are recommended for consideration. Each is of sufficient importance that, if adopted and successfully implemented, the program would be advanced significantly.

(1) Geographic coverage: Sorely needed is the extension of investment guarantees to all Alliance for Progress countries. Lacking comprehensive geographic coverage, the program has often failed to provide vital stimulus where most needed, particularly in Latin America, an area where stimulation of U.S. private foreign investment is an explicit goal of the administration's Alliance for Progress program. Many countries have not joined the program because of a reluctance to enter into bilateral agreements with the U.S. Government providing for U.S. subrogation rights and succession to the investor's property rights or foreign currency assets, most-favored-nation treatment for losses due to war, and arbitration, following payment of a claim under an investment guarantee. The 1961 (and 1962) legislation, however, has been interpreted as having liberalized the requirement of bilateral agreements under the former ICA program, and to have given AID authority to make "suitable" arrangements with the host country. As a result, AID has devised a "liberalized" bilateral, which is expected to eliminate the most serious objections to acceptance by foreign governments.

Host government agreement to the succession of the U.S. Government to local currency assets upon payment of a convertibility claim, recognition of U.S. subrogation rights following expropriation for which a claim under an expropriation guarantee has been paid, and agreement to negotiate or submit to arbitration matters relating to such claims, are all important insuror protection devices incorporated in both existing and the new "liberalized" bilateral treaties.

Granting the significant advantages underlying bilateral treaties, protecting private investors and the insuror alike, the need for extending investment guarantees to nations not currently under the program is vital to the continued and increased success of the program and, in particular, crucial to prospects of effectively promoting U.S. private investments in the more important nations of Latin America.

It is appropriate to note that as a result of a recent concerted effort of AID to secure agreements to AID's newly "liberalized" bilateral, Colombia and Venezuela have agreed to full coverage and Argentina seems prepared to follow suit. It is recommended that these efforts be continued so as to ultimately provide coverage throughout the underdeveloped countries of the Western Hemisphere.

The AID administrative requirement that private investors negotiate with host governments the acceptance of their investment proposals under the bilateral investment guarantee agreement precludes the need for AID to scrutinize all proposed investments and determine their "priority" or "acceptability" for the intended countries other than on very general grounds. This is the present practice.

(2) Extended risk: Since its authorization under the 1961 act, no guarantees have been issued under this category, apart from Latin American "housing" guarantees. However, three guarantees issued pursuant to the former Development Loan Fund all-risk guarantee program, are still outstanding, under one of which a substantial claim was required to be paid. Lacking experience with both the extended political and commercial risk coverage and the program to promote Latin American housing, AID is still in the process of establishing guidelines. So far the specific coverage, political, and economic, which the investor would be entitled to under the program has not been detailed. We understand that under current policy emphasis under this part of the program is on special situations or areas where investments may have high political importance and to industries having "social" impact (e.g., housing, land and agricultural reform programs, savings and loan institutions). It is recommended that a broader application of extended risk coverage be adopted, with the

emphasis not only on projects of political or social importance, but that it also be made available to cover other essential and high risk projects.

There is a substantial pool of institutional funds (insurance company, pension funds, etc.) which could be tapped as an additional important source of capital. The institutional lender is generally not interested in investing in Latin America. This is due not only to the investment climate, but also because of the limitations of State laws and the basic policies governing their operations. This is a source of funds where extended-risk guarantees covering both the political and economic exposure might well result in insurance companies and pension trusts being willing to make loans to Latin American companies, particularly those owned and managed by companies with technical know-how and knowledgeable in operating in the Latin American climate.

(3) War-risk coverage: In the 1961 Foreign Assistance Act, war-risk coverage was extended from international war losses to include losses arising from revolution or insurrection. Further clarification of the scope of coverage of these categories is needed, and it is recommended that the coverage be further extended, if necessary by legislative enactment, to clearly include risk of losses through riot or civil disturbance. These types of risk can hardly be distinguished from the general category of rebellion or revolution, yet it is important that coverage for such possible events be provided if the program is to effectively insure against major political risks not otherwise insurable.

(4) Specific-risk guarantee and fee consolidation: While it is necessary that convertibility, expropriation, and war-risk protection continue to be offered, each independently of the other, certain problems arise where an investor elects more than one coverage. An investor who seeks coverage under any two or all three of the specific-risk guarantees finds that the aggregate face amount of the contracts substantially exceeds what may be required to cover his real exposure and that the fees may well be excessive in relation to the potential profitability of the project.

It is therefore recommended that AID offer the investor who elects more than one coverage on the same investment the option of consolidating face amounts of protection so as to reflect the true extent of the U.S. Government's liability. This has the further advantage in that the legislative authorization for the isuance of guarantee contracts could be more effectively applied to cover a greater number of projects. It is further recommended that the fee schedule be revised to establish a set of fees for consolidated coverages as well as a fee for each separate specific-risk guarantee if taken out separately. The fee schedule recommended follows:

A fee of one-half of 1 percent for contracts covering a single specific risk;

A fee of three-fourths of 1 percent for any two specific risks covered under a consolidated multirisk contract;

A fee of 1 percent for consolidated multirisk contracts covering all three specific risks.

It is also recommended that the one-fourth of 1 percent "standby" fee be continued where an investor elects to carry any part of the coverage on a "standby" basis with the right to elect prior to each anniversary date the face amount of the guarantee (up to the maximum stated in the contract) to be effective for the ensuing year.

(5) Standardization and simplification of contract language: While great care is taken to avoid ambiguities wherever possible, difficult questions have arisen regarding accepted definitions. It is understood that AID has arranged for professional assistance to review present contract procedures and language with the objective of removing ambiguities wherever possible, to standardize the several individual specific-risk contracts, and to draft a consolidated or multirisk contract combining the various types of coverage. It is recommended that this is an area where collaboration with private industry would be most constructive in developing a standardized form of contract which would simplify concepts and remove ambiguities.

(6) Guarantee extensions and reserve requirement: A 25-percent "probable net ultimate cost" reserve for each of the three specific-risk guarantees was formerly required and functioned to limit total guarantees which could be issued. At present, administrative interpretation of the revised statutory language, under the 1962 amendments to the Foreign Assistance Act, is that although a reserve will be maintained, its function should be the provision of funds adequate for prompt payment of claims arising out of a grave crisis, rather than for payment of all ultimate claims. Correlatively, it is now understood that the full faith and credit of the U.S. Government attaches to all guarantees. Thus, the effec-

tive ceiling on total guarantees which may be issued is $1.3 billion currently authorized to be outstanding in the 1962 act for specific-risk guarantees, $180 million for extended risks, and $60 million for housing. Changes in the existing statutory language are still deemed desirable to confirm the above interpretations. With a total of $771 mililon in specific-risk guarantees outstanding and applications of approximately $2.6 billion, it is evident that the present authorized ceiling of $1.3 billion should be substantially increased.

It is recommended that the authorized limits be raised as follows:

Specific-risk guarantees to $2 billion.
Extended-risk guarantees to $500 million.
Housing guarantees to $250 million.

(7) Processing fee: AID is presently weighing the desirability of charging a modest processing fee (as in the German program) to discourage frivolous applications. If such a policy were adopted, it is recommended the fee be credited against the initial fee payable by investors entering a final contract.

VI. OTHER METHODS OF PRIVATE INVESTOR PARTICIPATION

Recommend in selective cases the use of management contracts, cost-plus contracts, leasing arrangements, equity financing and consortia arrangements for multiproject developments.

The foregoing proposals have the purpose of either reducing the risk or increasing the rate of return on investments in Latin America. However, these proposals will not be sufficient to induce the private sector—United States or national—to provide capital for the expansion of the public utility sector. This group, particularly the electric power, transportation, and other utility companies are vital to industrial expansion and unless they develop output and services ahead of demand the expansion of the manufacturing, distribution, and extractive industries is retarded. The history of the postwar period has been that the public utility sector has lagged behind in almost all Latin American countries and increasingly the burden of providing these services has shifted from the private to the public sector and the latter has not been able to bridge the gap because of the heavy financial burden entailed and lack of technical and operating know-how. Under governmental rate controls, often dictated by political considerations, and inflation economies, private capital cannot be induced to do this job. As a result, the trend of more and more utility operations passing to government hands will continue and drastic and unique solutions must be adopted if these roadblocks to industrial expansion in Latin America are to be removed. No feasible unilateral action on the part of the U.S. Government can either reduce the risk sufficiently or raise the rate of return to bring in the necessary private capital. Since overall growth is dependent on investment in these sectors as well as in the sectors where private capital can be attracted, the overall success of our program is dependent on the use of devices other than those previously proposed.

The important guiding principle in all investment activity is the most efficient utilization of available resources, particularly of managerial and technological know-how in Latin America, and this means the maximum involvement of private enterprise in all possible forms. By the nature of the investment climate in which these utility groups operate, there is little hope that the private sector will permit itself to become more deeply involved without, in many instances, elimination of risk. This can be accomplished in a number of ways which are familiar in U.S. experience, especially in wartime. In times of maximum national necessity, the U.S. Government has employed means which have eliminated financial risk at the same time that private enterprise has been brought in to create and operate the activity. This has been especially successful in the transportation and communication groups.

Management contracts

The management contract represents one technique that couples government ownership with private business know-how.

The justification for this technique is in the higher degree of efficiency that results from private operation. It is well recognized that government corporations are less efficient and their enterprises have constituted heavy burdens on national finances. It is proposed, therefore, that the AID direct its efforts and funds toward providing management from the U.S. private sector. These enterprises might include not only electric power and transit facilities but communication, water supply, and other resource developments. Management contracts

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should have a termination date with a provision that local management would be trained within that time. Authority for management contracts now exists and it is recommended that greater use be made of this arrangement.

Cost-plus contracts

Cost-plus contracts represent a second method of combining government assumption of risk with the operational know-how of private industry. Cost-plus contracts are widely used in government and private industry procurement and in industrial management. Authority to enter into such contracts now exists and should be used.

Leasing

Another technique is to lease facilities to U.S. private enterprise that have been financed by AID or the host government. The U.S. company would put up the working capital but could cut its losses by terminating the lease. Also, through making available local currency loans, the private investor could be protected from much of the losses that might otherwise be occasioned by currency devaluation. If it was anticipated that the project could move completely into the private sector at a future time, a provision could be included permitting the U.S. company to buy the project at a given multiple of earnings.

Government equity financing

The private entrepreneur could be involved even more fully in a project despite extraordinary risk by the U.S. Government contributing equity financing and low-cost loans directly to the U.S. investor. This device could be used imaginatively together with the tax certificate and extended-risk guarantee mechanisms discussed earlier to reduce risk and raise the return. It appears realistic to us that through flexible administration of such a program, capital needs, and the needs for the management and technical skills of the private sector, could be brought to bear in a large number and wide range of enterprises which otherwise are not likely to be served.

Consortia arrangements

One further method by which the U.S. Government might take the initiative in bringing the private sector into the picture is the use of consortia for multiproject developments. Thus, the development of an agricultural region might require construction, transport, food processing, marketing, etc. Each might be essential in a large development project and might only be assured of participation through joint financing—United States and Latin American, and possible European. Consortia-type arrangements should also be considered where joint industrial efforts are indicated on single projects.

The above techniques of bringing the private sector in on essential projects, where otherwise the choice might be a purely governmental effort with its attendant inefficiencies, are illustrative of the possibilities under a bold and imaginative program for maximum participation by the private sector.

VII. HOUSING

The members of COMAP are intensely interested in the critical needs in the field of low-cost housing throughout Latin America. However, the committee recognizes that many competent studies have been made on this subject and there is already a great wealth of information available both to the Congress and to the executive departments of the U.S. Government on this problem. Rather than burden this report with material already submitted by highly competent authorities both in Government and private industry we will advert only to our belief that the bottleneck in the problem is the lack of knowledge of the technique of large-scale housing construction, and the absence of adequate credit machinery for the financing of low-cost housing.

In the recent Congress there was introduced by Senator Smathers a bill for the creation of an International Home Loan Bank. Under the terms of this bill (S. 582) there would be created within the U.S. Government an International Home Loan Bank whose shares would be taken up by Federal and State loan associations in the United States. Other proposals suggest that these organiza-

tions be permitted to invest a small percentage of their capital (up to 1 percent) in savings and loan operations in Latin America. The great advantage of this proposal is that it would bring to the Latin Americans the home financing techniques which have developed low-cost housing into such an enormously successful private industry in the United States.

Appendix A. Effects of Exchange Devaluation on U.S. Private Investment in Latin America

Added to the economic and political risks which confront investments in Latin America is the risk of exposure to the impact of currency devaluation. Balance-of-payments problems, inflation, and consequent currency depreciation have for many years been a way of life in most Latin American nations, with a resulting adverse effect on earnings in terms of U.S. dollars, as well as an erosion of U.S. dollar investments in Latin American enterprises, particularly manufacturing.

Data maintained by the U.S. Department of Commerce shows total U.S. direct private investment in Latin America and Western Hemisphere dependencies at $9.1 billion in 1961. Of this figure, $1.4 billion is in Panama and in the Western Hemisphere dependencies, which up to now have been relatively free of exchange devaluation problems. Of the remaining $7.7 billion, petroleum and mining and smelting account for $4.4 billion. Of the balance of $3.3 billion, manufacturing investments in Latin America account for $1.7 billion—roughly 20 percent of the total U.S. direct private investment in Latin America and the Western Hemisphere dependencies.

Manufacturing in Latin America is almost always for the home market. Therefore sales are in local currency, and such businesses are carried on basically in terms of the currencies of the respective countries. The impact of foreign exchange devaluation is paramount to these manufacturing enterprises. Devaluation is a phenomenon, not generally recognized or understood, with which manufacturing managements must reckon day by day. It affects every decision taken and is often a key life and death factor for the business.

This is quite the contrary for exporting industries, including petroleum and mining and smelting, since in large part they export their products for hard currencies. These businesses are conducted fundamentally in dollars, and therefore exchange devaluation does not have the same impact on them that it does on manufacturing enterprises.

Because such a large segment of U.S. investment in Latin America is not exposed to the effects of devaluation to the same degree as is manufacturing, the problems of exchange devaluation are not widely understood throughout U.S. business and Government circles.

Since manufacturing investments are vitally affected by the problem, devaluation has a special significance for the Alliance for Progress. Certainly it is unnecessary to dwell on the fact that industrialization through manufacturing is precisely the kind of economic development most needed to carry out the concept of the Alliance for Progress, to create jobs, capital and consumer goods, and to stimulate capital formation and mass markets, as part of the program for improving the standards of living of the peoples of the Latin American countries. U.S. private investment in manufacturing, with its know-how is generally welcomed in Latin America.

Thus, it is doubly important that the problem of exchange devaluation and its adverse effect be understood by all those interested in the success of the Alliance for Progress.

History of devaluation in Latin America

The table entitled "Exchange Rates, 1926–62" shows the rate of exchange to the dollar, year by year, from 1926 through 1962 (estimated), for the currencies of nine major Latin American countries together with related percentages of increase or decrease.

That statement shows three distinct patterns: a period of devaluation from 1926 through 1940; a period of stability during the war; and a more intensive period of devaluation after the war from 1946 to the present.

Exchange rates, 1926–62

[Yearend free or nearest equivalent rate in foreign currency units to the U.S. dollar]

Yearend	Argentine pesos		Bolivian bolivianos		Brazilian cruzeiros		Chilean pesos *		Colombian pesos		Ecuadorean sucres		Mexican pesos		Peruvian soles		Venezuelan bolivares	
	Rate [2]	Percent change [1]	Rate [3]	Percent change [1]	Rate [4]	Percent change [1]	Rate [5]	Percent change [1]	Rate [6]	Percent change [1]	Rate [7]	Percent change [1]	Official rate	Percent change [1]	Rate [8]	Percent change [1]	Rate	Percent change [1]
1926	1.09	0	3.13	(0.9)	6.93	(15.5)	8.26	(4.2)	1.02	n.a.	4.98	9.9	2.07	2.5	2.67	6.8	5.25	n.a.
1927	1.04	(4.6)	3.11	(.6)	8.45	21.9	8.26	0	1.02	0	5.18	4.0	2.12	2.4	2.68	.4	5.22	(0.6)
1928	1.04	0	2.79	(10.3)	8.35	(1.2)	8.20	(.7)	1.02	0	5.18	0	2.08	(1.9)	2.52	(6.0)	5.20	(.4)
1929	1.05	1.0	2.79	0	8.47	1.4	8.26	.7	1.04	2.0	5.00	(3.5)	2.08	0	2.50	(.8)	5.19	(.2)
1930	1.20	14.3	2.82	1.1	9.34	10.3	8.26	0	1.04	0	5.00	0	2.11	1.4	2.74	9.6	5.41	4.2
1931	1.50	25.0	3.08	9.2	14.22	52.2	8.26	0	1.04	0	5.00	0	2.10	(.5)	3.59	31.0	6.55	21.1
1932	1.71	14.0	4.72	53.2	14.04	(1.3)	12.66	53.3	1.05	1.0	5.64	12.8	3.14	49.5	4.52	25.9	6.15	(6.1)
1933	1.89	10.5	5.85	23.9	12.56	(10.5)	12.99	2.6	1.22	16.2	7.46	32.2	3.56	13.4	5.31	17.5	3.92	(36.3)
1934	2.98	57.7	6.62	13.2	11.86	(5.6)	25.00	92.5	1.62	32.8	n.a.	n.a.	3.60	1.1	4.34	(18.3)	3.73	(4.8)
1935	3.06	2.7	6.85	3.5	12.06	1.7	25.00	0	1.79	10.5	n.a.	n.a.	3.60	0	4.19	(3.5)	3.88	4.0)
1936	3.02	(1.3)	12.7	85.4	17.23	42.9	27.8	11.2	1.77	(1.1)	10.53	n.a.	3.60	0	4.02	(4.1)	3.19	(17.8
1937	3.41	12.9	29.4	131.5	16.03	(7.0)	26.3	(5.4)	1.84	4.0	11.66	10.7	3.60	0	3.96	(1.5)	3.19	0
1938	3.87	13.5	45.5	54.8	20.15	25.7	27.0	2.7	1.77	(3.8)	14.12	21.1	4.92	36.7	4.47	12.9	3.19	0
1939	4.40	13.7	45.5	0	20.85	3.5	32.2	19.3	1.77	0	14.84	5.1	5.52	12.2	5.33	19.2	3.19	0
1940	4.23	(3.9)	55.6	22.2	21.00	.7	33.3	3.4	1.82	2.8	16.03	8.0	4.85	(12.1)	6.17	15.8	3.19	0
1941	4.24	.2	55.6	0	19.76	(5.9)	31.3	(6.0)	1.82	0	15.02	(6.3)	4.86	.2	6.50	5.3	3.26	2.2
1942	4.23	(.2)	50.0	(10.1)	19.64	(.6)	31.3	0	1.82	0	14.39	(4.2)	4.85	(.2)	6.50	0	3.35	2.8
1943	4.06	(4.0)	45.5	(9.0)	19.63	(.1)	32.2	2.9	1.82	0	14.08	(2.2)	4.85	0	6.50	0	3.35	0
1944	4.02	(1.0)	52.6	15.6	19.58	(.3)	31.0	(3.7)	1.81	(.5)	14.05	(.2)	4.85	0	6.50	0	3.35	0
1945	4.07	1.2	58.8	11.8	19.50	(.4)	32.1	3.5	1.82	.6	13.76	(2.1)	4.86	.2	6.50	0	3.35	0
1946	4.10	.7	62.5	6.3	19.42	(.4)	39.4	22.7	1.82	0	14.64	6.4	4.86	0	7.90	21.5	3.35	0
1947	4.81	17.3	62.5	0	23.25	19.7	50.8	28.9	1.83	.5	18.25	24.7	4.86	0	10.00	26.6	3.35	0
1948	9.26	92.5	90.0	45.4	26.55	14.2	65.4	28.7	2.68	46.4	18.01	(1.3)	6.88	41.6	16.60	66.0	3.35	0
1949	15.80	70.6	116	27.6	30.75	15.8	99.0	51.4	2.86	6.7	18.42	2.3	8.65	25.7	16.08	(3.1)	3.35	0
1950	19.49	23.4	103	(11.2)	32.00	4.1	72.5	(26.8)	3.08	7.7	18.25	(.9)	8.64	(.1)	15.01	(6.7)	3.35	0
1951	27.62	41.7	189	83.5	30.00	(6.2)	92.5	27.6	3.30	7.1	17.22	(5.6)	8.65	.1	15.36	2.3	3.35	0
1952	23.20	(16.0)	189	0	36.50	21.7	128	38.4	3.70	12.1	17.39	1.0	8.60	(.6)	15.72	2.3	3.35	0
1953	20.83	(10.2)	720	281.0	55.00	50.7	220	71.9	3.17	(14.3)	17.40	.1	8.60	0	19.96	27.0	3.35	0
1954	26.25	26.0	1,890	162.5	76.00	38.2	315	43.2	3.45	8.8	17.40	0	12.49	45.2	19.06	(4.5)	3.35	0

1955	36.10	37.5	4,260	125.4	66.75	(12.2)	630	100.0	4.16	20.6	17.38	(.1)	12.49	0	19.55	2.6	3.35	0
1956	37.45	3.7	7,745	81.8	65.65	(1.6)	600	(4.8)	6.86	64.9	18.76	7.9	12.49	0	19.05	(2.6)	3.35	0
1957	37.00	(1.2)	8,565	10.6	90.50	37.9	773	28.8	6.22	(9.3)	16.58	(11.6)	12.49	0	19.17	.6	3.35	0
1958	67.30	81.9	11,950	39.5	140.50	55.2	1,105	42.9	8.21	32.0	16.70	.7	12.49	0	24.63	28.5	3.35	0
1959	83.25	23.7	11,910	(.3)	200.00	42.3	1,053	(4.7)	7.02	(14.5)	17.00	1.8	12.49	0	27.71	12.5	3.35	0
1960	82.60	(.8)	11,910	0	206.00	3.0	1,053	0	7.24	3.1	17.50	2.9	12.49	0	26.83	(3.2)	4.25	26.9
1961	82.70	.1	11,910	0	318.00	54.4	1,053	0	8.78	21.3	21.80	24.6	12.49	0	26.85	0	4.58	7.8
1962 (estimated)	130.00	57.2	11,910	0	500.00	57.2	1,850	75.7	9.50	8.2	23.50	7.8	12.49	0	26.85	0	4.55	(.7)

[1] From previous yearend.
[2] 1926–36 official; 1937–46 controlled free; 1947–54 curb; from 1955 free.
[3] 1926–37 controlled; 1938–52 curb; from 1953 free.
[4] 1926–35 official; 1936–52 curb; 1953–60 free; from 1961 bank rate.
[5] 1926–38 official; 1934–61 free; broker's free rate established on Jan. 15, 1962.
[6] 1926–48 official; from 1949 free.
[7] 1926–46 official; from 1947 free.
[8] 1926–45 official selling; 1946–59 draft; from 1960 free.
*1 Escudo=1,000 pesos.

NOTE.—Average annual percent increase/(decrease):

	Argentina	Bolivia	Brazil	Chile	Colombia	Ecuador	Mexico	Peru	Venezuela
1926–40	10.2	22.8	8.2	10.5	4.2	8.7	6.3	6.2	(3.5)
1940–45	(.8)	1.1	(1.5)	(.7)	0	(3.0)	0	1.0	1.0
1926–61	13.2	26.5	11.5	14.9	6.4	4.3	5.3	6.8	(.4)
1936–61	14.2	31.5	12.4	15.6	6.6	3.0	5.1	7.9	1.5
1946–61	22.2	42.0	20.4	24.4	11.1	2.7	6.5	8.5	2.1
1956–61	17.2	9.0	37.0	11.9	5.1	3.1	0	7.1	6.5
1961–62 (estimate)	57.2	0	57.2	75.7	8.2	7.8	0	0	(.7)

Source: International Monetary Fund, International Financial Statistics.

The increase in the rates of exchange of these nine currencies, together with the equivalent devaluation in terms of the dollar, for 1926 through 1940 follows:

1926–40	Average annual increase in rate of exchange—that is in local currency units per dollar (percent)	Average annual rate of devaluation—that is, in dollar value of local currency units (percent)
Bolivia	22.8	18.6
Chile	10.5	9.5
Argentina	10.2	9.3
Ecuador	8.7	8.0
Brazil	8.2	7.6
Mexico	6.3	5.9
Peru	6.2	5.8
Colombia	4.2	4.0
Venezuela	(3.5)	(3.4)

During World War II there was very little devaluation in the Latin American currencies, and, in fact, certain of the currencies (Ecuador, Brazil, Argentina and Chile) actually strengthened slightly.

Since the end of World War II the currencies in Latin America have devalued at a considerably faster rate than they did prior to World War II as shown by the following table.

1946–61	Average annual increase in rate of exchange—that is in local currency units per dollar	Ratio of average annual increase in rate of exchange 1946–61 versus 1926–40	Average annual rate of devaluation—that is in dollar value of local currency units
	Percent	*Times*	*Percent*
Bolivia	42.0	1.8	29.6
Chile	24.4	2.3	19.6
Argentina	22.2	2.2	18.2
Brazil	20.4	2.5	16.9
Colombia	11.1	2.6	10.0
Peru	8.5	1.4	7.8
Mexico	6.5	1.0	6.1
Ecuador	2.7	0.3	2.6
Venezuela	2.1	(1)	2.1

1 Not significant.

The following table shows the violent devaluation of the currencies of Argentina, Brazil, and Chile in 1962.

[Percent]

1962 estimated	Estimated 1962 increase in rate of exchange, that is, in local currency units per dollar	Estimated 1962 rate of devaluation, that is, in dollar value of local currency units
Chile	75.7	43.1
Argentina	57.2	36.4
Brazil	57.2	36.4

From the foregoing figures it is evident that currency devaluation is not only a way of life in Latin America, but that the problem is becoming more acute.

How devaluation affects a manufacturing business

Devaluation of the local currency affects a manufacturing business in four different specific ways:

1. It reduces the dollar value of the local currency earnings. Thus for example, if a company earns 100,000 pesos and the exchange rate is 1 to 1, it earns $100,000; if the exchange rate goes to 2 to 1, it earns only $50,000.

2. It reduces the dollar value of the investment in net working capital. For example, if a company has 100,000 pesos in net working capital and the exchange rate is 1 to 1, it has net working capital equivalent to $100,000; if the exchange rate increases to 2 to 1 there is a loss in value of the net working capital of $50,000. Accepted accounting practices require that such losses be taken currently against profit and loss if certification of financial statements presented to stockholders and government agencies, such as the SEC, is to be obtained. Notwithstanding this requirement, no tax deduction either locally or in the United States is allowed for such losses.

3. It reduces and makes inadequate the dollar value of the local currency provision for depreciation. For example, if a company has $100,000 or 100,000 pesos, at the exchange rate of 1 to 1, invested in fixed assets, with a useful life of 10 years, the annual provision for depreciation should be $10,000 to maintain the integrity of the investment. Since the local currency depreciation allowable for tax purposes is based on the original local currency value of the fixed assets of 100,000 pesos, the annual provision for depreciation is 10,000 pesos. At a rate of exchange of 1 to 1, this is equivalent to the required $10,000.

If the rate of exchange increases to 2 to 1, this 10,000 pesos is only equivalent to $5,000, and it becomes necessary to reserve another $5,000, to provide full dollar depreciation on fixed assets. Here again this is required to be provided currently against profit and loss under accepted accounting practices and as in the case of the exchange loss on working capital no deduction for tax purposes, either locally or in the United States, is allowed.

4. If the company manages to raise prices (almost always inadequately as will be shown later) to compensate for the effects of devaluation, in an effort to maintain the basic dollar rate of return and the integrity of the investment, the company's local tax bill increases. This is so because no recognition for tax purposes is granted by the local government for the erosion of the investment in working capital resulting from exchange devaluation, or for the deficiency in the provision for depreciation.

Examples of the effects of exchange devaluation

There follows in the statement examples showing the adverse effects of exchange devaluation on U.S. owned manufacturing enterprises in Latin America, assuming:

1. Capital invested 50 percent in fixed assets and 50 percent in working capital—roughly the average in the United States for U.S. business. This is also the ratio indicated by U.S. Department of Commerce data for U.S. private investments in manufacturing in Latin America, in the 4 years 1958–61, i.e., 50 percent in fixed assets, and 50 percent in working capital (inventories, receivables, and other assets, such as cash and securities).

2. Fixed assets are depreciated at the rate of 10 percent a year.

3. Local tax rate of 35 percent.

4. Return on investment—15 percent after local taxes but before U.S. taxes, and 12.5 percent after U.S. and local taxes.

5. In the first year of operation the exchange rate for the local currency is 1 to 1 to the dollar. In the second year the exchange rate increases to:

   (i) 1.15 to 1, an increase in the rate of exchange of 15 percent, or a devaluation of 13 percent; and

   (ii) 1.30 to 1, an increase in the rate of exchange of 30 percent, or a devaluation of 23.1 percent.

   (It will be noted that the maximum rate of devaluation assumed in the examples of 23.1 percent is far below the rate of devaluation this year in Argentina, Brazil, and Chile.)

6. Since the effects of exchange devaluation vary depending on the turnover ratio of sales to capital invested, the hypothetical examples are developed on two alternative bases:

   (i) A sales to capital invested turnover ratio of 2 to 1; and

   (ii) A sales to capital invested turnover ratio of 1 to 1.

CASE I.—*Illustration based on a 2-to-1 turnover ratio ($2,000 sales to $1,000 investment)* [1]

Line No.		1st year		2d year—15-percent rise in local currency exchange rate to 1.15 to the dollar, equivalent to a 13-percent devaluation				2d year—30-percent rise in local currency exchange rate to 1.30 to the dollar, equivalent to a 23.1 percent devaluation			
		A Exchange rate 1 to 1		B No increase in sales price or expenses		C 21-percent price increase, required to maintain original U.S. dollar return and an assumed 15-percent increase in expenses		D No increase in sales price or expenses		E 42-percent price increase, required to maintain original U.S. dollar return and an assumed 30 percent increase in expenses	
		Local currency	U.S. dollar equivalent	Local currency	U.S. dollar equivalent	Local currency	U.S. dollar equivalent	Local currency	U.S. dollar equivalent	Local currency	U.S. dollar equivalent
1	Sales	2,000	$2,000	2,000	$1,739	2,419	$2,103	2,000	$1,538	2,839	$2,183
2	Manufacturing cost and other expenses	1,719	1,719	1,719	1,495	1,977	1,719	1,719	1,323	2,235	1,719
3	Depreciation (10 percent per year)	50	50	50	43	50	43	50	38	50	38
4	Total expenses	1,769	1,769	1,769	1,538	2,027	1,762	1,769	1,361	2,285	1,757
5	Operating profit	231	231	231	201	392	341	231	177	554	426
6	Local taxes at 35 percent	81	81	81	71	137	119	81	62	194	149
7	Net profit after local taxes	150	150	150	130	255	222	150	115	360	277
	Exchange devaluation provisions necessary to:										
8	Maintain dollar depreciation at $50	----	----	----	(7)	----	(7)	----	(12)	----	(12)
9	Recover loss in dollar value of working capital	----	----	----	(65)	----	(65)	----	(115)	----	(115)
10	Balance—Net profit before U.S. taxes, after providing for exchange losses—Available for return on investment	150	150	150	58	255	150	150	(12)	360	150
11	U.S. taxes, net of foreign tax credit applicable to net profit before U.S. taxes	----	25	----	10	----	25	----	0	----	25
12	Net to investor after all taxes	----	125	----	48	----	125	----	(12)	----	125

13	Percentage return, after all taxes, on investment of $1,000	12.5		4.8		12.5		(1.2)		12.5
14	Increase in local currency needed to buy 1 U.S. dollar (percent)			15.0		15.0		30.0		30.0
15	Rate of local currency devaluation (percent)			13.0		13.0		23.1		23.1
16	Increase in local currency operating expenses over 1st year (percent)			(2)		15.0		(2)		30.0
17	Increase in sales price over 1st year, necessary to maintain original dollar return (percent)			(2)		21.0		(2)		42.0
18	Ratio of price increase, needed to maintain original dollar return, to increase in rate of exchange			(2)		[3] 1.4		(2)		[3] 1.4
19	Ratio of price increase, needed to offset devaluation and maintain original dollar return, to rate of local currency devaluation			(2)		[3] 1.6		(2)		[3] 1.8

[1] Investment, $1,000, of which: fixed assets, $500; working capital, $500.
[2] No increase assumed in this example.
[3] Times.

CASE II.—*Illustration based on a 1-to-1 turnover ratio ($1,000 sales to $1,000 investment)* [1]

Line No.		1st year		2d year—15-percent rise in local currency exchange rate to 1.15 to the dollar, equivalent to a 13-percent devaluation				2d year—30-percent rise in local currency exchange rate to 1.30 to the dollar, equivalent to a 23.1-percent devaluation			
		A Exchange rate 1 to 1		B No increase in sales price or expenses		C 26.9-percent price increase, required to maintain original U.S. dollar return and an assumed 15-percent increase in expenses		D No increase in sales price or expenses		E 53.9-percent price increase, required to maintain original U.S. dollar return and an assumed 30-percent increase in expenses	
		Local currency	U.S. dollar equivalent	Local currency	U.S. dollar equivalent	Local currency	U.S. dollar equivalent	Local currency	U.S. dollar equivalent	Local currency	U.S. dollar equivalent
1	Sales	1,000	$1,000	1,000	$869	1,269	$1,103	1,000	$769	1,539	$1,183
2	Manufacturing cost and other expenses	719	719	719	625	827	719	719	554	935	719
3	Depreciation (10-percent per year)	50	50	50	43	50	43	50	38	50	38
4	Total expenses	769	769	769	668	877	762	769	592	985	757

5	Operating profit	231	231	231	201	392	341	231	177	554	426
6	Local taxes at 35 percent	81	81	81	71	137	119	81	62	194	149
7	Net profit after local taxes	150	150	150	130	255	222	150	115	360	277
	Exchange devaluation provisions necessary to:										
8	Maintain dollar depreciation at $50	---	---	---	(7)	---	(7)	---	(12)	---	(12)
9	Recover loss in dollar value of working capital	---	---	---	(65)	---	(65)	---	(115)	---	(115)
10	Balance—Net profit before U.S. taxes, after providing for exchange losses—available for return on investment	150	150	150	58	255	150	150	(12)	360	150
11	U.S. taxes, net of foreign tax credit applicable to net profit before U.S. taxes	---	25	---	10	---	25	---	0	---	25
12	Net to investor after all taxes	---	125	---	48	---	125	---	(12)	---	125
13	Percentage return, after all taxes, on investment of $1,000	---	12.5	---	4.8	---	12.5	---	(1.2)	---	12.5
14	Increase in local currency needed to buy 1 U.S. dollar (percent)	---	---	---	15.0	---	15.0	---	30.0	---	30.0
15	Rate of local currency devaluation	---	---	---	13.0	---	13.0	---	23.1	---	23.1
16	Increase in local currency operating expenses over 1st year (percent)	---	---	---	[2]	---	15.0	---	[2]	---	30.0
17	Increase in sales prices over 1st year, necessary to maintain original dollar return (percent)	---	---	---	[2]	---	26.9	---	[2]	---	53.9
18	Ratio of price increase, needed to maintain original dollar return, to increase in rate of exchange	---	---	---	[2]	---	[3] 1.8	---	[2]	---	[3] 1.8
19	Ratio of price increase, needed to offset devaluation and maintain original dollar return, to rate of local currency devaluation	---	---	---	[2]	---	[3] 2.1	---	[2]	---	[3] 2.3

[1] Investment $1,000, of which: fixed assets, $500; working capital, $500.
[2] No increase assumed in this example.
[3] Times.

The examples show how a U.S. investment in a manufacturing business in Latin America is affected by currency devaluation. For the sake of simplicity, local currency units are referred to as "pesos" in this discussion.

In case I, column A shows the results in local currency and U.S. dollar equivalent during the first year of operation, assuming a sales/investment turnover ratio of 2 to 1 and based on an exchange rate of 1 to 1. The result is a $150 profit after local taxes but before U.S. taxes, and $125 after U.S. taxes, on 2,000 pesos of sales.

Column B shows that with a 15-percent increase in the exchange rate, to 1.15 to 1 (a 13-percent devaluation), the $150 pre-U.S. tax profit drops to $58, a reduction of $92 or 61.3 percent. This loss of $92 in profitability is made up as follows:

Reduced dollar value of local currency aftertax profit (line 7, tables preceding)	$20
Depreciation deficiency (line 8)	7
Loss in dollar value of working capital (line 9)	65
Total	92

Column C shows that to compensate for the exchange devaluation and a 15-percent increase in operating costs (a reasonable assumption based on the increase in the exchange rate) the business would require a sales price increase of 21 percent. This is necessary to recover the $92 shown above, as well as the resulting increase in local taxes of $38 (from $81 to $119).

If the exchange rate moves up by 30 percent to 1.30 to 1, or a devaluation of 23.1 percent (col. D), the $150 pre-U.S. tax profit drops to a loss of $12, a drop of $162 or 108 percent. This reduction of $162 is made up as follows:

Reduced dollar value of local currency earnings (line 7)	$35
Depreciation deficiency (line 8)	12
Loss in dollar value of working capital (line 9)	115
Total	162

Column E shows that to compensate for a 30-percent increase in the exchange rate (a 23.1-percent devaluation) and again, assuming that operating expenses go up in the same ratio as the increase in the local currency exchange rate, the business would require a sales price increase of 42 percent to recover the $162 loss detailed above, as well as the increased local taxes of $68 (from $81 to $149).

Case II presents a similar set of hypothetical examples except that a sales/investment turnover ratio of 1 to 1 has been assumed. In the case of these examples, an increase in sales price of 26.9 percent would be required to compensate for an assumed increase of 15 percent in the exchange rate to 1.15 to 1 (a 13-percent devaluation). To compensate for an increase of 30 percent in the exchange rate to 1.30 to 1 (a 23.1-percent devaluation) would require a sales price increase of 53.9 percent.

To summarize, the following are the key points provided by the analysis:

	15 [1]		30 [1]	
Turnover ratio of sales to capital invested	2 to 1	1 to 1	2 to 1	1 to 1.
Initial rate of return (percent)	12.5	12.5	12.5	12.5.
Rate of return—no increase in sales price or expenses (percent).	4.8	4.8	(1.2)	(1.2).
Percent of initial net profit lost	61.6	61.6	109.6	109.6.
Percent sales price increase, necessary to maintain original rate of return, assuming increase in expenses equal to increase in exchange rate.	21.0	26.9	42.0	53.9.
Ratio of sales price increase, necessary to maintain original dollar return, to increase in exchange rate.	1.4 times	1.8 times	1.4 times	1.8 times.

[1] Percent increase in local currency exchange rate.

It is possible to calculate an infinite number of variations of examples of the effect of exchange devaluation. However, the foregoing examples show that in the absence of other mitigating factors, for a U.S.-owned manufacturing company in Latin America with a normal capital mix and a normal turnover of sales to investment, a relatively modest devaluation can have a disastrous effect on profits.

Based on the historical devaluations which Latin American currencies have undergone, the increases in rates of exchange of 15 and 30 percent used in the foregoing examples are not unrealistic.

Price increases in Latin America

It may be argued that since inflation is a way of life in Latin America, as well as exchange devaluation, sales price increases should compensate for the adverse effects of devaluation. In practice, it has been difficult, however, to increase prices sufficiently to maintain predevaluation dollar earnings—not to mention the normal growth in profits that should accrue over the years.

In the examples shown, it is demonstrated that to offset the effects of exchange devaluation, sales price increases are required that range from 1.4 to 1.8 times the increase in the exchange rate (or put in another way, from 1.6 to 2.3 times the rate of devlauation).

There follows a statement showing the actual price increase for a number of basic products, largely manufactured in the respective countries, for the years 1946 to 1961, in Argentina, Brazil, Colombia, Chile, Peru, and Mexico. These actual price increases are compared with—

1. The actual increases in the rates of exchange of these countries over the same period; and
2. The calculated price increases needed to offset devaluation and maintain predevaluation dollar earnings, using the minimum and maximum price increase factors of 1.4 and 1.8 times the increase in the rate of exchange, as developed in the hypothetical examples, in order to obtain
3. The actual price increases as a percent of the minimum to maximum price increases needed to offset devaluation.

1946–61 actual local price increases of basic products (largely manufactured in the respective countries) compared with increases needed to offset increase in rate of exchange

[In percent]

	Brazil	Peru	Mexico	Colombia [1]	Argentina	Chile
Actual price increase 1946–61:						
Cement	1632	661	36	55	3460	3540
Steel	684	1226	252	62	2095	4371
Textiles	700	276	121	32	2915	3142
Shoes	987	(2)	(2)	(2)	(2)	5605
Biscuits	1167	256	78	149	(2)	(2)
Cornstarch	1300	320	(2)	111	(2)	2426
Beer	671	440	106	100	(2)	2700
Gasoline	(2)	411	236	(2)	(2)	3009
Caustic soda	478	(2)	32	196	(2)	(2)
Paint	(2)	380	205	129	(2)	8177
Increase in rate of exchange	1537	240	157	166	1917	2573
Equivalent to devaluation of	94	71	61	62	95	96
Price increase needed to offset increase in rate of exchange applying—						
Minimum: 1.4 times the increase in rate of exchange based on case I—2-to-1 turnover business	2152	336	220	232	2684	3602
Maximum: 1.8 times the increase in rate of exchange based on case II—1-to-1 turnover business	2767	432	283	299	3451	4631

	Minimum (percent of 2152 percent)	Maximum (percent of 2767 percent)	Minimum (percent of 336 percent)	Maximum (percent of 432 percent)	Minimum (percent of 220 percent)	Maximum (percent of 283 percent)	Minimum (percent of 232 percent)	Maximum (percent of 299 percent)	Minimum (percent of 2684 percent)	Maximum (percent of 3451 percent)	Minimum (percent of 3602 percent)	Maximum (percent of 4631 percent)
Actual price increase as percent of minimum and maximum price increase needed to offset increase in rate of exchange:												
Cement	76	59	197	153	16	13	24	18	129	100	98	76
Steel	32	25	365	284	115	89	27	21	78	61	121	94
Textiles	33	25	82	64	55	43	14	11	109	84	87	68
Shoes	46	36	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	156	121
Biscuits	54	42	76	59	35	28	64	50	(2)	(2)	(2)	(2)
Cornstarch	60	47	95	74	(2)	(2)	48	37	(2)	(2)	67	52
Beer	31	24	131	102	48	37	43	33	(2)	(2)	75	58
Gasoline	(2)	(2)	122	95	107	83	(2)	(2)	(2)	(2)	84	65
Caustic soda	22	17	(2)	(2)	15	11	84	66	(2)	(2)	(2)	(2)
Paint	(2)	(2)	113	88	93	72	56	43	(2)	(2)	227	177

[1] Colombia data are for 1951–61 in absence of adequate 1946–61 data.

[2] Not readily available at time of study.

It will be noted that we have analyzed the price history for 10 basic products largely manufactured in the 6 countries (roughly 60 items), citing, except for 17 items for which the figures are not readily at hand, examples of actual price experience in Latin America during the 15 years from 1946 to 1961. Of the price history comparisons of 43 items in these 6 countries (which comprise 81.3 percent of the GNP of Latin America), only 12 show price increases equal to 100 percent or more of the amount computed to be the minimum required to maintain dollar earnings necessary to offset the effects of devaluation (not to mention the normal expected growth in profits generally anticipated by business). Of these 12, only 6 have met the maximum standards (1-to-1 turnover basis). An exceptional case is steel in Peru which, since 1957, has been produced by the Government-owned steel mill. Prior to 1957 steel was imported into Peru.

It is clear from this analysis of the actual exchange devaluations in these 6 countries in Latin America and the price history of 10 basic products, that there is a wide disparity on the downside between the price increases actually obtained for most of the items and the amount needed to offset the effects of currency devaluation on U.S. dollar earnings.

U.S. executives who are responsible for the management of U.S.-owned local manufacturing enterprises find themselves in constant debate with their local managements as to the real earnings reportable in any given year. Even when local managements are alert to the problem it is often difficult, if not impossible, to obtain adequate price increases due to price controls imposed by the local governments to combat inflation.

Furthermore, it so happens that many foreign-owned manufacturing enterprises in Latin America compete in one way or another with locally owned activities. The owners of these locally owned companies do not have to convert their annual profit-and-loss statements and balance sheets into U.S. dollars, and they often fail to realize what is actually happening to them; i.e., the erosion of their investment in terms of hard currency values as a result of the currency devaluation phenomenon.

The moment of truth, of course, ultimately comes home to them when massive plant replacement becomes necessary, and in part as their working capital needs increase in direct relation to the rate of inflation in the country. The local owners find themselves devoid of the resources needed to finance their replacements and their progressively increasing working capital requirements—the result of overstating earnings for years and decapitalizing their companies slowly but surely through the payment of dividends.

The following comparison of the dollar value of reported local currency common stock net income per share for 1955 versus 1960 of 23 leading Chilean,

Argentine, and Brazilian companies, for which published information is available, will serve to emphasize the impact of exchange devaluation on the reported earnings of companies (not one of which shows an increase) in these 3 countries whose currencies have suffered violent exchange devaluation.

	Dollar value of common net income per share		Percent decrease
	1955	1960	
Chile:			
Farmo-Quimica Del Pacifico S.A	$0.0157	$(0.0008)	105.1
Textil Vina S.A	.0820	(.0036)	104.4
S.A.C. Saavedra Benard	.2571	.0316	87.7
Fabrica de Panos Bellavista-Tome	.8161	.1604	80.5
Tejidos Caupolican S.A	.0608	.0136	77.6
Compania Industrial	.0493	.0141	71.4
Hucke Hermanos S.A.C	.1535	.0576	62.5
Manufacturas Sumar, S.A	.1341	.0557	58.5
S.A. Yarur Manufacturas Chilenas de Algodon	.184	.094	48.9
Cia. Distribuidora Nacional	.525	.285	45.7
McKay & Cia. S.A	.1424	.0792	44.4
Cia. Chilena de Navegacion Interoceanica	.018	.011	38.9
Cia. Manufacturera de Papeles y Cartones S.A	.1230	.0844	31.4
Cia. De Industrias y Azucar S.A	.0816	.0562	31.1
Argentina:			
Celulosa Argentina S.A	.57	.22	61.4
Cia. Quimica S.A	[1] .63	.36	42.9
Fabrica Argentina de Alpargatas S.A.I.C	.76	.46	39.5
M. S. Bagley y Cia. Ltda	7.03	4.66	33.7
Brazil:			
Cia. Industrial e Comercial-Brasmotor	3.79	.31	91.8
Cia. Nitro-Quimica Brasileira	5.42	2.81	48.2
Industrias Reunidas F. Matarazzo	19.18	10.71	44.2
Quimbrasil-Quimica-Industrial Brasileira S.A	.35	.20	42.9
Orquima-Industrias Quimicas Reunidas S.A	1.47	1.00	32.0

[1] 1956.

An actual example

In order that the discussion of the problem will not be presented solely on the basis of hypothetical figures, however realistic, there is presented an actual example of a U.S.-controlled manufacturing enterprise in Latin America. The statement presents the results of a $7 million investment in a textile manufacturing company in Chile for the period 1957 through 1962 (estimated).

Chilean Textile Co., comparative statement of income

[Chilean Escudos and U.S. Dollar amounts in thousands]

	1957		1958		1959		1960		1961		1962 (estimated)		6-year average	
	Local currency	U.S. dollar equivalent at Esc. .74 [1]	Local currency	U.S. dollar equivalent at Esc. 1.01 [1]	Local currency	U.S. dollar equivalent at Esc. 1.05 [1]	Local currency	U.S. dollar equivalent at Esc. 1.05 [1]	Local currency	U.S. dollar equivalent at Esc. 1.05 [1]	Local currency	U.S. dollar equivalent at Esc. 1.70 [1]	Local currency	U.S. dollar equivalent
Net sales	4,778	6,439	5,691	5,635	8,191	7,801	7,193	6,851	8,887	8,456	9,721	5,728	7,410	6,818
Costs and expenses	(4,151)	(5,594)	(5,298)	(5,246)	(6,906)	(6,578)	(6,468)	(6,161)	(7,779)	(7,401)	(8,332)	(4,907)	(6,488)	(5,981)
Depreciation, per local books	(169)	(228)	(146)	(144)	(359)	(342)	(225)	(214)	(208)	(198)	(260)	(153)	(228)	(213)
Local income taxes	(83)	(112)	(43)	(43)	(136)	(129)	(104)	(99)	(214)	(203)	(269)	(158)	(142)	(124)
Net income per Chilean books	375	505	204	202	790	752	396	377	686	654	860	510	552	500
Exchange devaluation provisions necessary to:														
Maintain dollar depreciation at required level		(425)		(388)		(87)		(85)		(169)		(175)		(221)
Recover loss in dollar value of working capital		(340)		(607)		165		42		92		(2,155)		(468)
Total		(765)		(995)		78		(43)		(77)		(2,330)		(689)
Net profit (loss) in dollars before Chilean dividend and U.S. taxes		(260)		(793)		830		334		577		(1,820)		(189)

[1] Composite rate at which income and expenses were converted during the year.

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Compution of return on capital invested

[U.S. dollars in thousands]

	1957	1958	1959	1960	1961	1962 (estimated)	6-year average
Capital invested including intercompany loans	$7,109	$7,970	$7,117	$6,976	$7,039	$6,308	$7,087
Percent return on capital invested:							
Net profit (loss) in dollars, after provision for foreign currency devaluation, but before U.S. taxes, as above	(260)	(793)	830	334	577	(1,820)	(189)
Add interest (after local taxes) paid on intercompany loans	224	290	291	88	88		164
Adjusted net profit (loss) in dollars before Chilean dividend and U.S. taxes	(36)	(503)	1,121	422	665	(1,820)	(25)
Percent return on capital invested before Chilean dividend and U.S. taxes	(0.5)	(6.3)	15.8	6.0	9.4	(28.9)	(0.4)

Taking the year 1958, the statement shows that the company had sales of 5,691,000 Chilean escudos, equivalent to $5,635,000 at the prevailing exchange rate of 1.01 escudos to the dollar. The net income on the Chilean books in 1958 was 204,000 escudos, equivalent to $202,000. Ostensibly, then, the business earned some profit, but even this inadequate profit on the $8 million investment in that year was before recognizing the deficiency in the provision for depreciation, and the erosion of the investment in working capital, resulting from exchange devaluation.

To maintain the integrity of the investment, the U.S. parent company had to provide in its consolidated financial statements for the inadequate dollar depreciation and the decline in the dollar value of the investment in working capital.

As indicated early in the memorandum, the local currency depreciation is based on the local currency values at which the fixed assets are booked at date of acquisition. Thus, as the local currency depreciates in value in terms of the U.S. dollar, the local currency provision for depreciation becomes inadequate to cover the amortization of the investment in fixed assets. In the case of the Chilean textile company under review, the required U.S. dollar depreciation was $532,000 for the year 1958. However, the U.S. dollar equivalent of the local currency provision of 146,000 escudos is only equivalent to $144,000 at the exchange rate prevailing in 1958, leaving a deficiency of $388,000 to be provided as a supplemental dollar provision to maintain the integrity of the investment. The additional $388,000 of supplemental dollar provision for depreciation is the result of the cumulative effects of devaluation over the intervening years between the date of investment in fixed assets and the end of 1958.

Furthermore, the deterioration in the rate of exchange from escudos 0.74 to the dollar to escudos 1.01 to the dollar in 1958 resulted in a loss of $607,000 in the investment in net working capital.

These two exchange losses, $388,000 for the supplemental depreciation provision and $607,000 for the loss in working capital, total $995,000. Since the company only earned $202,000 before these exchange losses, the result was a net loss of $793,000.

The capital invested in the business, including intercompany loans, was $7,970,000 in 1958. Taking the net loss of $793,000, and adding back to that the aftertax cost of interest on intercompany loans (since this is income to the parent company), the net U.S. dollar result before Chilean dividend and U.S. taxes was a loss of $503,000, equivalent to a loss of 6.3 percent on the capital investment.

Admittedly a substantial recovery was made in 1959, when the company earned a 15.8 percent return on the investment (pre-Chilean dividend and U.S. taxes) as a result of substantial price increases and relative exchange stability. However, in 1960 and 1961 when the exchange rate continued stable at 1.05 escudos to the dollar, the return dropped to 6 and 9.4 percent respectively before Chilean dividend and U.S. taxes—a modest return in relation to the exposures, and despite the continued exchange stability.

These lower returns were caused by the fact that the maintenance of the exchange stability was only accomplished by drastic austerity measures brought

about by the Government in an attempt to curb the almost fantastic average annual inflation which had been experienced before President Alessandri came into office.

This period of austerity in which the exchange was artifically held stable was followed by violent exchange devaluations in 1962 when the escudo devalued by an estimated 43 percent, with the result that this company will lose an estimated $1,820,000 or 28.9 percent of its investment in 1962.

Looking at this textile business from the point of view of the 6-year average from 1957–62 (estimated), the dollar profit per the Chilean books averaged $500,000 per year. However, this profit was illusory because the average additional depreciation provision required to maintain the dollar investment in fixed assets was $221,000, and the average loss in the dollar value of net working capital was $468,000, resulting in an average net loss before Chilean dividend and U.S. taxes of $189,000 per year. Adding back to the net loss of $189,000, the aftertax interest paid on intercompany loans of $164,000, the business lost an average per year of $25,000 before Chilean dividend and U.S. taxes. On the average capital invested over the 6-year period of $7,087,000, the average annual net loss of $25,000 is equivalent to an annual average loss of 0.4 percent on the investment.

In short, the investment of $7 million was totally unremunerative over this period, when all economic factors are taken into account, as they must under sound accounting and financial concepts, despite the fact that the return on the Chilean books showed for the 6-year period an average return of approximately 7 percent per annum, which is, of course, what Chilean competitors would believe they were earning.

This poor profit performance was basically due to the Chilean textile company's inability to raise prices to compensate fully for the adverse affects of exchange devaluation.

CHILEAN TEXTILE CO.

Percent of exchange devaluation 1957 through 1962 (estimated) compared with price increases during the period

[Base year, 1956]

	1957	1958	1959	1960	1961	1962 estimate	Increase (decrease), 1962 versus 1956
Cumulative increase in rate of exchange	30.0	77.0	84.0	84.0	84.0	198.0	198.0
Cumulative percent devaluation	23.0	44.0	46.0	46.0	46.0	66.0	(66.0)
Cumulative price increase over 1956 needed to offset increase in the exchange rate, based on the factor of 1.8 developed for a business with 1-to-1 turnover in the examples	54.0	139.0	151.0	151.0	151.0	356.0	356.0
Cumulative actual sales price increase since 1956	21.0	65.0	149.0	180.0	191.0	238.0	238.0
Cumulative actual sales price increase above (below) price increase needed to offset increase in exchange rate since 1956, based on the 1.8 factor developed for a business with a 1-to-1 sales turnover in the examples in the statement on page 10	(61.0)	(53.0)	(1.0)	19.0	26.0	(33.0)	(33.0)
Percent return on capital invested before U.S. taxes per statement on page 18	(.5)	(6.3)	15.8	6.0	9.4	(28.9)	(.4)

The foregoing statement shows the textile sales prices rising 238 percent over the period 1957 through 1962, compared with an increase in the exchange rate of 198 percent. The price increase required to offset the 198-percent increase in the exchange rate, using the 1.8 ratio would have been 356 percent in this business with a 1 to 1 sales turnover ratio. Thus the actual price increase of 238 percent fell short of the required increase by 33 percent.

Yet even the required price increase would not have been sufficient for the business to have made a reasonable profit during the 1957–62 period. Had prices increased each year at the rate of 1.8 times the increase in the exchange rate, the 6-year average for the "adjusted net profit in dollars before Chilean dividend and U.S. taxes" would have been approximately $550,000 (rather than the loss

of $25,000 per the statement. The "percent return on capital invested" would then have averaged about 8 percent before Chilean dividend and U.S. taxes, or approximately 5.5 percent after all taxes, hardly an adequate return on an investment in Latin America. This low return is primarily due to the low profit margin of the business at the start of the period resulting from the inability in prior years to raise prices sufficiently to fully compensate for currency devaluation, as was also the case during the period 1957–62.

As indicated earlier, no tax deduction is allowed for exchange devaluation losses on investments in foreign subsidiaries operating in Latin America under U.S. tax law, nor generally under Latin American tax laws. Yet it should be noted that all certified consolidated financial statements of a U.S. parent company and its foreign subsidiaries prepared for official corporate purposes in the United States, including statements filed with the Securities and Exchange Commission, must be prepared within the framework of the generally accepted accounting practices followed in the case of the Chilean textile company and in the examples previously shown.

As stated at the outset, the key life and death factor in the profit and loss performance of a U.S. manufacturing subsidiary in Latin America is often the annual exchange losses with which the business must cope. To stimulate U.S. investment in manufacturing in Latin America, which is so desirable to achieve the goals of the Alliance for Progress, it is essential that the nature of these exchange losses be understood and recognized as a cost of doing business in Latin America. If the flow of private capital to Latin America is to be stimulated, such cost should be allowed as an ordinary and necessary expense for tax purposes.

The following excerpt taken from the 1961 annual report of Sears, Roebuck & Co., will serve to highlight the impact of exchange devaluation losses on U.S. investments in Latin American enterprises:

"Latin American subsidiaries, Mexico and South America * * *

"The company's equity in the net income of these subsidiaries (before translation losses) was $6,891,369 * * * Because of the decline in value of the Brazilian, Colombian, and Venezuelan currencies in 1961, the company's equity in its Latin American subsidiaries has been reduced by a translation loss of $4,004,956 at yearend. Under conservative accounting practice, such a translation loss is treated by Sears as a reduction of the net income of the subsidiary for the year in which it occurs * * *."

"Translation losses" are explained in the Sears report as losses which occur "to the extent that the dollar value of the net current assets of a foreign company has declined because of a year-to-year change in the rate of exchange." The translation losses of $4,004,956 are the equivalent of 58.1 percent of the reported equity of $6,891,369 of Sears in the net income of their Latin American subsidiaries.

This memorandum has been prepared for the purpose of pointing up the problem of exchange devaluation and its effect on U.S. investments in Latin America. The hypothetical examples have been presented on a simplified basis to demonstrate the basic factors which give rise to foreign exchange losses and the accounting treatment required to give economic recognition to the financial impact of such losses. For this reason, certain refinements have been omitted, such as projected increases in working capital requirements to finance increased investments in inventories, accounts receivable, etc., as a result of devaluation. Obviously, as the investment in working capital increases, so does the exposure to greater loss from currency devaluation.

It should also be mentioned that the effect of devaluation on working capital can be, and is, hedged to the extent possible by borrowing locally to finance working capital requirements, or through so-called swap transactions, etc. While these measures help to mitigate the impact of exchange devaluation, it also involves an economic cost in the form of interest expense which must be absorbed by the business. Commercial credit facilities are grossly inadequate in Latin America, and particularly so in countries subject to runaway inflation, with resulting violent currency devaluation. Under these conditions, the opportunity to finance working capital requirements locally, and thus hedge the exposure to devaluation, is limited.

Appendix B. Tax Sparing and U.S. Investment in Latin America

There is a strong belief among companies doing business in Latin America that a credit for tax sparing should be a part of the recommended program to stimulate additional private investment in Latin America. The degree of unanimity on this subject would, under normal circumstances, make it unnecessary to support it with an extensive presentation of the underlying reasons for which this view is held. However, in this case the Treasury Department staff has taken a contrary view, setting forth its reasoning in a memorandum dated October 18, 1962.

It is proposed to discuss individually here the specific arguments advanced in the Treasury staff paper. Before doing so, however, it is appropriate to mention that the staff paper recognizes that "Tax policy can undoubtedly assist us in our efforts to attain our objectives in this area and continuing study is being given to alternatives to a credit for tax sparing which do not suffer from its disadvantages and which, in addition, have important merits of their own that are not shared by the tax-sparing device." Recognizing the great importance also of political and economic climates favorable to new investment, a position with which everyone would agree, the memorandum also states that "Tax policy rather, must be integrated with other important policy measures—American and foreign—which are designed to provide an atmosphere and economic climate in which the prospects for profitable investment may become promising." It may be that there are preferable alternates to tax sparing, but we feel that until they have been determined (and we are aware of none to date, whether advanced by the Treasury Department or others), it is entirely appropriate to consider the incentives which are available, of which a credit for tax sparing is certainly an important one.

Turning to the Treasury staff paper, it advances several philosophies in opposing tax sparing. One of these is that a credit for tax sparing would involve, to use the exact words, U.S. participation in foreign tax discriminatory practices. Another is that a credit for tax sparing would be contrary to the American Government's policy of equal treatment of income from all sources. Here it seems important to consider what is our immediate objective. Certainly it is above all to stimulate private investment in Latin America. If incentives are required to achieve this objective, as they most certainly are, then how can an incentive be provided that does not (by definition) involve some measure of discrimination? There is certainly equality, however, in the sense that tax sparing would offer the same opportunity for anyone willing to take the very special risks inherent in making investments in those countries offering tax incentives. To say that there is discrimination between new and established investments also hardly seems germane to the problem. Again, the objective is to stimulate new investment. This is what the incentive is needed for and is certainly quite normal in tax legislation to distinguish between the past and the future. To claim also that there would be discrimination between companies investing in different countries in the world does not seem pertinent. There are already all kinds of Government-sponsored differences, many of a tax nature, which the investor has to assess in determining whether or not to make investments in particular countries abroad.

In all this, the Treasury memorandum seems to be making the assumption that differences in tax treatment brought about by foreign tax incentives and tax sparing were unfair and would be considered so by many or most taxpayers. However, in the minds of knowledgeable men the many special political and economic risks which exist in the less developed countries of the world easily justify the incentives. The use by Puerto Rico of tax incentives to stimulate new investment has generally been looked upon as a logical method of achieving a desired and desirable result.

The Treasury staff memorandum seems to fail to distinguish the priority objective and to recognize the urgency with which a solution must be found. The memorandum states that "the United States *presumably* (italic supplied) seeks to encourage foreign investment of a kind that involves a more or less long-term commitment, in which the foreign enterprise may be expected to grow over a period of years, presumably in large part at least out of retained profits." It would certainly be desirable that each foreign investment in a less developed

country imply a long-term commitment, with the major part of earnings to be reinvested. The facts are, however, that with risks being what they are, it is a major accomplishment to achieve any increase in investment in the areas with which we are concerned. Benefits will accrue from any new investments even if it were felt, as we do not, that tax sparing would discourage some reinvestment. Certainly it would appear shortsighted to withhold approval of tax sparing on the grounds that other still unspecified legislation might encourage a greater amount of long-term-commitment type of investment.

There can be little question that such investment would decrease measurably if the investors felt means were not available to repatriate earnings at any time, should they desire to do so. Can anyone believe, for example, that recent Brazilian legislation placing limits on the remission of dividends from Brazil (and also excluding from the "registered investment" base the earnings retained in the business to finance expansion) is not going to make it extremely difficult to encourage any non-Brazilian to make new investments in that country? In fact, in Brazil it is now necessary to first remit earnings as dividends, to the extent permitted under the law, and then send them back to Brazil as a new investment in order for reinvested earnings to be recognized as registered investments eligible for future earnings remittances.

It is not unreasonable to suggest that one of the characteristics of human nature is to want to have the ability to take action if it becomes desirable even though in the great majority of cases such action might never be felt necessary. In other words, the ability to remit earnings if desired can be a major factor in a company's decision as to whether or not to increase its stake in a foreign country, whether through reinvestment of new investment, from the United States.

The Treasury staff memorandum also makes the argument that a credit for tax sparing would, under normal circumstances, be of little or no benefit to the American investor. This is very difficult to understand. Does it mean, for example, that the American investor abroad is to expect no dividends from the foreign venture in the 5- or 10-year period for which his tax incentive applies? How is it expected that the American parent company is to generate the funds which it requires to serve debt obligations in the United States and to pay dividends to stockholders?

Private enterprise has to contemplate a return on its investment. Otherwise, funds are not going to be committed in support of the objectives of the Alliance for Progress.

The memorandum makes a further point that it would be unlikely that, after the expiration of the tax holiday, the foreign subsidiary would be distributing dividends out of profits of those years to which the tax-sparing credit would apply. Here again this view fails to reflect the practicalities of doing business abroad. In order to protect a company against the inevitable devaluation of currencies, and in a sense to prevent the erosion of funds available for reinvestment, it is entirely possible, and often happens, that the subsidiary will declare out a dividend well in excess of the current year's earnings, if it has developed cash from depreciation or similar sources, and does not have immediate plans for the reinvestment of these funds.

In short, the Treasury staff's position that a credit for tax sparing is considerably less significant than it is generally believed to be can only be described as being at odds with the experience of those who have faced the problems and who know how, in fact, foreign subsidiaries must operate under the difficult conditions in which they find themselves.

Another point which the memorandum makes is that the credit for tax sparing would weaken and erode local tax systems. Here it seems to imply that the U.S. Government should have a right to determine what the tax policies and procedures of the foreign countries should be. It also seems to be saying that while the United States is not unwilling to see tax incentives used by foreign countries, it considers that to the extent that such incentives must depend upon U.S. cooperation to be made truly meaningful, they somehow become undesirable.

Tax incentives can be in the form of a tax holiday given to a new industry to assist it through the development years, or, as in the case of the Peruvian industrial promotion law, can be in the form of a waiver of tax on earnings invested in a new basic industry or reinvested in the expansion of an existing basic industry. Such laws permit the host country to be selective in its efforts to foster those industries which are of first importance to it. The Treasury memorandum here implies that the U.S. Government should make these decisions and that tax sparing somehow makes our program dependent on the foreign government. But, as a practical matter, can we visualize a tax incentive system for Latin America

administered by the U.S. Government on a selective basis? Is it not fair to conclude that the foreign government is going to be reasonably selective and intelligent in its choice of industries to be encouraged?

The absence of tax sparing in our tax policy seriously reduces the assistance extended by the host country in the form of tax incentives. This is even more true in the case of the benefits extended under programs such as that provided in the Peruvian industrial promotion law. Under present U.S. tax law, dividends are presumed to have been paid from the most recent earnings, and this is so whether or not such earnings are available for distribution to the shareholders. This rule, in the absence of tax sparing, penalizes the U.S. investor in a Peruvian company cooperating under the Peruvian industrial promotion law.

The purpose of this law is not only to stimulate new private investment generally, but what is more important under the goals of the Alliance for Progress, is to provide a particular incentive to locate new industry in outlying areas of Peru where industry is badly needed. To accomplish these objectives, the law grants income tax exemption on certain specified percentages of profits if set aside for reinvestment within a 2-year period in new productive facilities approved by the Peruvian Government. The percentage of profits exempt from taxation varies between different parts of the country. In the Lima area it is up to 40 percent; in the remaining coastal areas of Peru it is up to 60 percent; and in other outlying areas it can actually be 100 percent.

Thus, if a Peruvian subsidiary invests up to 60 percent of its earnings in new productive facilities in any part of the coastal area (other than the Lima area) and distributes the remaining 40 percent to its U.S. shareholder, the effect under existing tax law on each dollar of dividend received would be as follows:

	Tax on each dollar of dividend received		
	Assuming no investments under industrial promotion law	Assuming 60 percent of earnings reinvested under industrial promotion law	
		Ex-tax sparing	With tax sparing
Dividend paid	$1.00	$1.00	$1.00
Gross U.S. tax at 52 percent	.520	.520	.520
Foreign tax credit:			
Peruvian dividend tax	(.200)	(.200)	(.200)
Deemed tax credit	(.370)	(.148)	(.370)
Net U.S. tax	.000	.172	.000
Total taxes actually paid on dividend distributed:			
Peruvian dividend tax	.200	.200	.200
Peruvian corporate or deemed tax	.370	.370	.370
U.S. taxes	.000	.172	.000
Total	.570	.742	.570

As shown above, if the U.S. investor does nothing to cooperate to further expand industrial development in Peru in accordance with Alliance objectives, there would be no U.S. tax since the available foreign tax credit exceeds the U.S. tax and the overall tax on the dividends received would be the 57 cents of Peruvian taxes on each dollar of dividend received. On the other hand, if 60 percent of earnings are reinvested in expansion or in a new investment, the total taxes paid, ex-tax-sparing, on each dollar of dividend would be increased by an additional U.S. tax of 17.2 cents since, in reality, the present U.S. tax code nullifies 22.2 cents of the Peruvian incentive. This is so because the deemed foreign tax credit is reduced from the 37 cents actually paid on the earnings from which the dividend is paid to 14.8 cents. This inequitable result stems from the rule that dividends are presumed to be paid out of the most recent earnings. If 60 percent of earnings are set aside in a reserve for reinvestment (as they are required to be under the law), they are not earnings available to the shareholder. Yet under the foreign tax credit formula, they are so treated. Thus, it is fact—not theory—that the earnings available to the shareholder and from which the dividend is paid were subject to 37 cents of Peruvian income

tax—not the watered-down deemed credit of 14.8 cents allowable under the existing rule.

Latin American countries are now experiencing widespread unemployment, low productivity, and inadequate industrialization. As a result, there is dissatisfaction on the part of citizens of Latin American countries and susceptibility to welcoming radical economic innovations and even foreign political ideologies. There are two primary approaches available to such countries to encourage the initial establishment of new industries:

(1) Subsidies to industry or government participation in capital investments in industry based on grants or loans of capital by more prosperous countries, primarily the United States; or

(2) Establishment of tax incentives to provide additional encouragement to private capital to take the risk inherent in establishing a new industry in Latin America.

Tax incentives are an inexpensive tool for improving substandard economies in that they do not require any investment by a government either foreign or United States.

The less developed country which has not as yet established an economically strong economy, does not have funds to assist private enterprise in making investments or to provide subsidies or other nontax incentives for such investments. If such nontax incentives are to be made available, the governments normally must seek increased grants or loans from other governments or from the international lending agencies. As to the United States, this in turn means using Alliance for Progress funds or increasing the demands on its taxpayers.

For the less developed countries, this is a bootstrap operation. The major resource of any country is gainfully employed people. Basically, income is created only when people work. If, in absence of tax incentives, citizens of a less developed country would be idle and nonproductive, their support imposes additional economic burden on the remainder of the country. On the other hand, if through tax incentives, businesses are established which provide employment and which make available goods which the country can utilize in its own economy or export, income has been generated where none existed before.

Thus, the less developed country risks neither capital nor tax revenue by granting the tax incentive, but hopes to gain a harvest in the form of prosperous enterprises providing gainful employment and, ultimately, additional tax revenues.

Likewise, the advantage of tax sparing to the United States is apparent. The United States may achieve its objective of assisting less developed countries, and, in particular, the countries of Latin America, to develop their economies and put people to work without requiring the diversion of available funds. Here again the United States gives up only the right to tax income which would not otherwise exist in absence of the tax incentive granted by the less developed country.

To repeat, a primary advantage of the tax incentive tax-sparing approach is that it is a low-cost method of stimulating the economies of less developed countries.

Finally, the primary question is what can be done to maximize new U.S. investment in Latin America. The facts here are that business managements cognizant of their responsibility to stockholders, must weigh each new investment with the special economic and political risks involved; they must also contemplate a profit which they consider to be commensurate with the risks. To the extent that the profit outlook is improved by the combined effect of a tax incentive in the foreign country and a credit for tax sparing in the United States, management will be more likely to make investments in Latin America than otherwise would be the case.

Memorandum by Three Members of COMAP, January 28, 1963

A REAPPRAISAL OF THE ALLIANCE FOR PROGRESS

Last spring, the Commerce Committee for the Alliance for Progress (COMAP) was launched with a view to seeking ways in which American business could further the Alliance. A few days ago, the Chairman of the Committee, J. Peter Grace, submitted a report to the Commerce Department and to other agencies, recommending certain legislative proposals relating to the Alliance. The following memorandum sets out the observations and conclusions of three members of COMAP who, while agreeing with many of the points made in the Grace report

feel that there are certain aspects of the problem which need a somewhat different emphasis. For this reason we feel justified in submitting a separate commentary.

We have become increasingly concerned lest the Alliance for Progress fail to achieve its objectives for lack of a proper focus for its activities.

As one illustration, the initial concept of Comap's role appears to have been directed at finding ways to meet the Punta del Este program of $300 million a year of net new U.S. private investment in Latin America by devising short-range measures on the part of the United States to encourage such investment. If such measures would really get the Alliance off the ground, they might be justified. But we are disturbed by the feeling that even if such measures were taken, and were successful in inducing an expanded flow of U.S. investments into Latin America, the basic problem of making the area attractive to local savers and investors would remain. Indeed, such a program could do positive harm by making local governments feel even less urgency than they do now for achieving a proper investment climate.

What is needed is a comprehensive reappraisal, not of the broad objectives of the Alliance for Progress, but of the policies and actions which will best achieve these objectives. The first year's operation of the Alliance saw heavy emphasis placed on government planning, government-to-government loans and grants, income redistribution through tax and land reform, public housing, and other social welfare measures. Many of these steps were commendable. Yet they were not in most cases accompanied by efforts to push through economic reforms which would encourage private initiative and enterprise. The continued outflow of private funds from Latin America is sufficient proof of the critical character of the current situation.

Many countries in Latin America need social reforms as well as measures to provide greater equality of opportunity. However, these broad objectives cannot be achieved without a more rapid rate of economic advance than now is in prospect. And rapid economic growth cannot be achieved without greater emphasis on the private sector. The fact is that some 80 percent of Latin America's national income is today generated by private activities. Consequently, the Alliance for Progress can succeed if—and only if—it builds upon this base and places far greater emphasis on the encouragement of private initiative and investment, both local and foreign.

To reorient the Alliance for Progress in a direction which offers promise of achieving its objectives involves difficult and sweeping economic reforms. Currencies need to be stabilized through measures to bring government budgets under control and to avoid inflationary increases in the supply of money and credit. Efforts along these lines could lead to the removal of the many exchange controls which still remain and which inhibit economic growth in many nations. At the same time, governments should act to remove the network of other controls which restrict enterprise and sustain local, high-cost monopolies. Economic growth, and the real benefits to all participants in the community which can accrue from growth, are maximized in an atmosphere of political and economic stability under which competitive private enterprise can thrive.

In a very real sense, the Alliance for Progress is concerned with the age-old problem of trying to bake a bigger pie and divide the slices more evenly at the same time. The emphasis to date has been mostly on the side of slicing the pie. While such efforts may be desirable in the long run, the immediate effect has been to shrink the potential size of the pie. Experience around the world shows clearly that the national welfare is better served by far through policies which enlarge the entire pie.

To accelerate economic advance in Latin America, efforts on many fronts will be required. Governments have important roles to play in such areas as schools, health, farm extension services, and roads. However, the overriding need is for an increased flow of private capital from both local and foreign sources and for a significant and continuing improvement in the efficiency with which all resources, including most importantly human resources, are used.

For these reasons, we urge that U.S. policies be reoriented to place far greater emphasis on the encouragement of private enterprise and investment. What has been done to date along these lines is simply not enough. The encouragement of private enterprise, local and foreign, must become the main thrust of the Alliance. This would involve two major changes in U.S. policy.

The first requirement is that the governments—and, as far as possible, the people—of Latin America know that the United States has changed its policy so as to put primary stress on improvement in the general business climate as a

prerequisite for social development and reform. It must be made clear that U.S. policy in this hemisphere is based on the need for rapid economic growth and on the belief, confirmed by all available evidence, that this can be achieved within a reasonably free political framework only if private capital is given the opportunity to work in a favorable environment. This means that our policies should be consistent throughout the area and should discourage tendencies toward nationalization of industries and encourage setting up explicit rules which provide for truly reasonable indemnification where nationalization has taken place.

In addition we should discourage policies which tend to distort normal economic relationships, policies leading to overvalued, and multivalued exchange systems, complex import controls with high and highly variable tariffs, quotas and other forms of trade restriction, price controls, and highly unpredictable budgetary practice. In short, emphasis should be placed on creating an atmosphere in which private business planning can go on without undue concern about possible changes in the rules of the game. Countries following these policies should be given tangible and active support.

To make this position clear and unambiguous, it would be necessary for the President to proclaim it in a major address in which he not only spells out the rationale behind the new policy, but also indicates the tools available to the United States to help make it effective. The most important of these tools would be the U.S. foreign aid program.

A second requirement concerns a change in the criteria for granting aid. U.S. foreign aid policy is a branch of U.S. foreign policy, which should be directed toward achieving specific foreign policy goals. By and large it has not been effectively used for this purpose in Latin America. In its simplest terms, our goal in Latin America should be to help nations of the area grow economically while they retain internal political freedom, and thus remain part of the Western community of nations. Without economic growth the other goals will be much more difficult, if not impossible, to achieve. In order to get growth, which comes first both in time and in relation to goals involving redistribution of income, capital is needed. Most of this must come from internal sources. Thus, foreign aid should be used as an inducement to nations to adopt policies which will improve the business climate and thereby increase domestic savings and investments. The United States should concentrate its economic aid program in countries that show the greatest inclination to adopt measures to improve the investment climate, and withhold aid from others until satisfactory performance has been demonstrated.

The extent to which this policy would differ from the present one in Latin America can be seen by indicating what it would not involve:

Unless there are overpowering political considerations, the United States would not lend money or make grants in countries which persist in policies which discourage private investment.

The United States would not grant balance-of-payments loans of the "bail-out" variety though it should cooperate with the IMF on constructive balance-of-payments loans and stabilization programs.

The United States would not provide foreign aid in such a way as to finance the expropriation of privately owned companies in any field of endeavor.

On the positive side, the United States would seek opportunities to get individual countries started toward rapid growth. Assistance on a relatively large scale would be focused in a few countries that appeared most likely to carry out measures needed to encourage investments and establish the widest area of economic freedom.

Nowhere in the whole broad range of current economic problems is there one more compellingly significant for the United States than that of supporting the economic and social advance of our neighbors to the South.

We are persuaded that the most important way in which the United States can help is by exporting the ideas implicit in a free economy. Certainly, money or goods alone will not do the job. Free enterprise is the basis of our own growth, and it provided the framework on which our social and political institutions, imperfect as they still are, have evolved. We feel certain that free enterprise can be the basis of growth in Latin American—indeed, that there is no known alternative that still permits a substantial measure of individual freedom.

We also believe, however, that to encourage such an evolution in Latin America the United States must change its role from one that emphasizes short-run economic palliatives combined with recommendations for sweeping social and economic reforms to one that places the greatest emphasis on the longer run goals of creating an environment in which freedom of the marketplace is recognized for what it is, a major pillar of free and prosperous societies.

EMILIO G. COLLADO,
Vice President and Director, Standard Oil Co. of New Jersey.
DAVID ROCKEFELLER,
President, The Chase Manhattan Bank.
WALTER B. WRISTON,
Executive Vice President, First National City Bank.

W. R. GRACE & CO.,
New York, N.Y., January 31, 1963.

Mr. DAVID ROCKEFELLER,
President, the Chase Manhattan Bank, New York, N.Y.

DEAR DAVID: I received your letter of January 28 this morning and hasten to thank you as well as Pete and Walt, to whom I am writing separately, for what I feel is an excellent contribution to the COMAP effort.

With the literally hundreds of pages of material that had to be reviewed by the busy executives comprising the COMAP membership, during the Christmas and New Year's period, before formal submission to Secretary Hodges, I have been reluctant to send the COMAP membership the 140-page letter that I wrote on January 16 to General Clay in his role as Chairman of the President's Committee To Strengthen the Security of the Free World, with copies to the other members of this Committee. I felt that there should be some breathing space, so to speak, for the COMAP members so that they would not be inundated with so much material coming over their desks in such a short period of time.

I attach hereto a copy of my letter to General Clay. I feel that when you have had the time to read this letter you will see that, rather than your view being different from mine, we are as of one mind.

For instance, on the first page of your letter you state that you cannot be sure that the U.S. Government:

"* * * under the best circumstances, could improve the business climate in Latin America sufficiently to stimulate capital formation and economic growth, on an adequate scale, and in good time. But it is in this realm that we must focus our efforts or we will surely fail."

Further, on page 2 of your letter:

"Therefore, the full weight of U.S. foreign economic policy must be shifted and brought directly to bear on this problem. This implies a more active use of our foreign aid program than before—and it probably should, if properly administered, imply an even larger program in terms of dollars spent."

On pages 1 and 2 of my letter to General Clay, I wrote:

"I can think of no aspect of our Government's operations today where a review is more urgently needed than in the foreign aid field. This is particularly true of the program for Latin America, the Alliance for Progress, which I am convinced is in an extremely precarious condition. My reason for writing to you is that I have never been so deeply disturbed about a major aspect of U.S. foreign policy and, having recently completed a study of the problems involved, would like to convey certain conclusions and recommendations to your Committee.

"While the Alliance takes cognizance of the economic and social problems of Latin America, the amount of aid which it proposes to provide is grossly inadequate and the manner in which the aid is to be made available—i.e., mainly on a government-to-government basis—raises extreme doubt as to the effectiveness of any amount of aid in attaining our objective. In brief, General, as I believe is shown conclusively in this letter, the program, in its present size and form, cannot succeed and we are in great danger of suffering a major defeat to our strategic interests in this hemisphere."

"* * * As a result, I am now convinced that, unless the Government proceeds now with an all-out program for Latin America under the Alliance for Progress,

any opportunity to maintain free and friendly allies in this hemisphere will be lost."

You will note that on page 14 of my letter to General Clay I wrote:

"From our conversations with many people in the United States and in Latin America, it seems clear that the Alliance for Progress is making very slow progress and is in grave danger of failing.

"It seems to me beyond question that, in the present highly marginal and explosive economic and political atmosphere in Latin America, with there being no basis for fundamental improvement in sight, the chances of success for the Alliance for Progress on its present scale are dim. What we are doing and have promised under the Alliance compares most unfavorably with what is needed for success and what we did in similar circumstances for other parts of the world."

On page 1 of your memorandum you state that you "feel that there are certain aspects of the problem which need a somewhat different emphasis."

I think that your memorandum gave an excellent definition of what this different emphasis should be:

"What is needed is a comprehensive reappraisal, not of the broad objectives of the Alliance for Progress, but of the policies and actions which will best achieve these objectives. The first year's operation of the Alliance saw heavy emphasis placed on government planning, government-to-government loans and grants, income redistribution through tax and land reform, public housing and other social welfare measures. Many of these steps were commendable. Yet they were not in most cases accompanied by efforts to push through economic reforms which would encourage private initiative and enterprise."

"* * * And rapid economic growth cannot be achieved without greater emphasis on the private sector. The fact is that some 80 percent of Latin America's national income is today generated by private activities. Consequently, the Alliance for Progress can succeed if, and only if, it builds upon this base and places far greater emphasis on the encouragement of private initiative and investment, both local and foreign."

This ties in exactly with what I said to General Clay and his committee on pages 72 and 73 of my letter:

"The signatories to the Punta del Este agreement agreed from the start that, without the private sector, both local and foreign, success could not be achieved, as best put by Mr. Moscoso in the same speech as follows:

" 'The signing countries further concurred that success could be achieved only with the fullest participation of the private sector in this vast endeavor. As the charter puts it, and I quote: "* * * the countries signing this declaration have agreed to stimulate private enterprise in order to encourage the development of Latin American countries at a rate which will help them to provide jobs for their growing populations, to eliminate unemployment, and to take their place among the modern industrialized nations of the world." '

"In this context, the flight of Latin American private capital and the net outflow of U.S. private capital, beginning with the middle of 1961 through September 30, 1962, the first year that this has happened since the end of World War II, appear to doom the Alliance for Progress to failure if the Charter of Punta del Este meant what it said. President Kennedy best put it to the COMAP Committee reception at the White House on May 9:

" 'If local and American capital dry up, then all our hope of a decade of development in Latin America will be gone.'

"The economic pressures to which these Latin American economies have been subject, together with government policies adverse to business, compounded by Communist inspired pressures to create social unrest, have resulted in a most unsatisfactory climate for both local and foreign private capital investment."

And on pages 75 and 76 of my letter to General Clay:

"With the adverse trend continuing and deepening, it is difficult to envision U.S. private capital flowing to Latin America, or a reversal of the outflow of Latin American capital.

"Yet, as Mr. Moscoso put it in the same Chicago speech:

" '* * * as Latin American policymakers delve more deeply into the concrete problems they face, as they see the indispensable need for capital investment, they cannot help but recognize that a substantial part of this capital has to come from private sources * * * domestic and foreign. The overall investment need for the 10-year program of the Alliance has been estimated at $100 billion. Of this total, $80 billion will have to be generated by Latin America itself—most of it by the private sector.'

"And further from Mr. Moscoso in a speech of December 8:

" 'This U.S. share can be estimated at $13 billion, with $3 billion coming from new private investments. The private sector, I feel, will meet the estimate for it, if the investment climate in Latin America is adequate.'

"The fact of the matter is that the investment climate is not adequate now; it wasn't adequate in 1961, as shown by the outflow of U.S. capital in the last half; and it was barely adequate in the late 1950's, when the flow of U.S. private capital was slowing down before reaching a halt, commencing with the second half of 1961. Furthermore, the inadequacy of the investment climate becomes greater each day, as anyone can conclude who follows Latin American developments in the daily newspapers."

In urging that U.S. policies be "reoriented" to place far greater emphasis on the encouragement of private enterprise and investment, you suggest that the governments and, as far as possible, the people of Latin America learn "that the United States has changed its policy so as to put primary stress on improvement in the general business climate as a prerequisite for social development and reform." You also suggest changing "the criteria for granting aid" to the point where the United States—

"* * * should concentrate its economic aid program in countries that show the greatest inclination to adopt measures to improve the investment climate, and withhold aid from others until satisfactory performance has been demonstrated."

This is exactly in line with the thought that I expressed to General Clay on pages 94 through 100, as follows:

"* * * I feel strongly that we must not only increase the size of our aid program, to the point where a real impact will be achieved, but also insist that the Latin American governments embark on feasible self-help measures—an absolute requirement, if the Alliance for Progress growth goals are to be achieved. Included in such self-help measures, should be, not only reasonable fiscal and monetary reforms, but also the many steps which can be taken to bring all the skills and resources of the private sector, local and foreign, into the battle. These need to be energetically supported by the Latin American governments, with no compromise or concessions to Communist attempts to discredit the free enterprise system.

"If $600 million a year—30 percent of the $2 billion foreign capital portion of the Alliance for Progress program—is expected to come from new foreign private investment, which it is, and, if the majority of the remaining $80 billion over the 10-year period is expected to come from local private investment, which it also is, how can the Alliance succeed, even with generous quantities of U.S. taxpayers' money, if the private sector, both local and foreign, is impeded from making its full potential contribution?

"Exerting the necessary influence over the content and application of the aid programs will not be easy. No government, however needy, wants to be placed in the posture of being told how to behave by another government, and particularly, by a strong power such as the United States. This is especially true in Latin America, whose peoples are proud and sensitive. Considerations of 'amor propio' are matters of honor to them, and must play an important part in determining how influence is brought to bear.

"Our task is the more difficult, because the history of our aid program appears to the Latin Americans to indicate that a completely independent 'aid with no strings attached' position can be adopted with no harmful effects, indeed with little risk. In fact, they believe they see some positive correlation between the degree of uncertainty that can be created, as to their willingness to cooperate with the United States, and the amount of aid the United States is willing to give. In certain cases, they have seen, for some time, much greater amounts of aid given than they themselves have received, without any apparent preconditions, to countries which, on no count, can be said to be free nations, such as Yugoslavia, and which are, in fact, members of the Communist camp. The reaction of the Latin American countries to all this is very natural. They see the opportunity to obtain aid, and to determine, without restrictions, the uses to which it is put, which, unfortunately, may be to shore up inefficient government activities, or for other uses, with motivations primarily political in nature, now trending alarmingly in certain countries toward the support and encouragement of Marxist aims.

"Thus, the United States has, by its past practices, greatly weakened its ability to influence the effective use of aid. In my judgment, we have virtually no chance of overcoming this obstacle with an aid program of the current size.

"However, if we will support an aid program of proper size, and with astute handling, we have a pretty good chance, throughout Latin America, to achieve a good measure of cooperation with our objectives, without the appearance of dictation. I feel certain, also, that our insistence on reasonable standards of political, monetary, fiscal, and business responsibility will, if consistently held, increase the respect of these countries for the United States, and thus, further facilitate the conduct of the Alliance.

"As mentioned elsewhere, there has been a heavy government-to-government emphasis in the aid program to date. This policy involves us in the gravest of dangers and, in my view, should be drastically modified in an expanded Alliance program.

"In recommending that we do insist, as a condition to our expanded aid program, on effective measures being taken to provide a healthy climate for both local and foreign private capital, I am not proposing that we force anything down unwilling throats. The point is that the development plans of the Latin American countries already strongly stress the private sector, and yet, in too many cases, these countries are not taking the measures that will permit the private sector, and hence, their own development plans to work.

"As a concrete example of how the development plans, under the Alliance, are seriously endangered, it is worth noting that, in Chile's 10-year development plan published a few months ago, investment in the private sector accounts for 50 percent of the total projected investment over the 10-year period, and of this 50 percent, nearly one-third is expected to come from direct private investment from abroad. Yet, the plan fails to provide for effective means of encouraging, or of channeling, savings into the private sector, and recent government policies, with respect to the important copper industry about which we are aware of no change, have tended to discourage the inflow of private investment from abroad.

"In essence therefore we would only be proposing measures which are a sine qua non for the success of their own development plans, which they have formulated as part of the Alliance. Anyone opposing such prerequisites to expanded aid would be effectively opposing the fruition of their own development plan and would either be misguided, or unfortunately, as may be the case, in certain instances, acting in outright bad faith.

"The fact that any opposition would have to be exposed to the strong light of truth and reality is what makes me confident that, if the matter is handled adroitly, we can successfully link reasonable requests for self-help and responsibility to an expanded aid program.

"In considering the question of self-help, a first priority is maximum productive use of resources already on hand in Latin America. This is, of course, only good commonsense, but an extremely important concept to apply in our aid program. There is abundant evidence that it is not being applied now and this fact is one of the principal reasons cited by the opponents of foreign aid in opposing appropriations for this purpose. Their position, in this respect, cannot be assailed unless, in conjunction with an expanded aid program, compliance with sound economic and business principles is obtained.

"I feel most strongly on this point, General, and believe that it is the only realistic approach to the solution of the very complex problems of Latin America. I fully realize that much of the resistance to compliance with sound economic principles in Latin America is the result of unyielding opposition of a political nature. We are told that it is politically unfeasible, by responsible officials of Latin American governments, to do those things which they themselves know should be done. I feel that it would be a great mistake to continue to go along with this philosophy.

"We have to succeed in raising the discussions of the problem of what should be done in response to our assistance above the level of politics. We must drive home a basic point of our assistance program—the mobilization and productive employment of domestic resources. The primary contribution of foreign assistance is to break the bottlenecks to more effective use of domestic resources."

And particularly in connection with your excellent suggestion that the President proclaim our new policy in a major address, on page 112:

"We need to pursue solutions to these problems at all levels, including an intensification of the efforts being made to encourage an understanding of the role of private investment as the key element in the attainment of the economic development objectives of the Alliance for Progress.

"I would like to suggest that a step in the right direction would be the calling of a hemispheric conference of the heads of states, at which the concept of the partnership of government and private capital in the attainment of the objectives of the Alliance would be put forward, as a major new driving force for the Alliance. This question of full acceptance of the desirable role of private capital, both local and foreign, in the development of Latin America is fundamental, vital, and still remains unclarified or unaccepted, partly through confusion caused by Communist propaganda, and partly through plain bad faith. Unless it is completely resolved, we will have very little assurance that the additional aid, which these countries sorely need, and really have to have, if the Alliance is going to succeed, will be part of an integrated package of public- and private-sector efforts that will spell the success of the democratic free society in Latin America."

I repeat the very important point from page 2 of your letter:

"* * * therefore, the full weight of U.S. foreign economic policy must be shifted and brought directly to bear on this problem. This implies a more active use of our foreign aid program than before—and it probably should, if properly administered, imply an even larger program in terms of dollars spent."

Here again I couldn't agree with you more and I have delineated specifically how much additional aid the United States should furnish Latin America on pages 78 through 86, and summarized (pp. 135 through 137) in the general conclusions at the end of the letter to General Clay as follows:

"Increase our official financial assistance to Latin America to a level two to three times the current level, i.e., at minimum to $2.5 billion per annum. Our official aid, under the Punta del Este agreement, is $1.1 billion which, after repayments and interest on outstanding debts to the United States, amounts to about $800 million.

"This amount of assistance would still not be sufficient to offset the financial deterioration that has occurred in these countries since 1950–56, as the result of the adverse trend in terms of trade, and unfavorable trends in capital movements, which, as noted on page 60, amounted to $2.7 billion for the seven largest countries alone. The minimum amount of aid recommended, of $2.5 billion, may prove even more deficient with the continuance of the outflow of U.S. private capital, estimated at $37 million for the first 9 months of 1962, versus an inflow of $141 million in 1961, an unfavorable swing already of about $180 million, and a deficit from the Punta del Este goal, for U.S. direct investment alone, of about one-third for $1 billion. In addition, the deficiency will become even larger still, if the inflow of private capital, other than U.S. direct investment, declines from the 1961 level of $947 million, and it appears likely that this has already happened, as the result of the developments of recent months in Brazil, Chile, Peru, and elsewhere.

"Furthermore, the $2.5 billion of aid recommended is only slightly more than $12 per capita, and this is less than the per capita levels of aid given to 18 of the 38 major recipient countries, during the 3 consecutive highest years of U.S. aid to them. Increasing our aid to the recommended level would be much more consistent with our traditional strategic relationship with Latin America, than continuing at the level of recent years. The need in Latin America is for an impact program that is convincing of our concern, and has a reasonable chance of breaking the vicious circle of decay, both material and spiritual, confronting these countries."

In retrospect, perhaps I should have immediately sent out copies of my letter to General Clay on January 16 so that all of the Comap members would have known that I had gone into the greatest of detail on not only the reorientation of our aid program, but increasing its size as you have indicated, and applying the criteria, for granting aid, of encouragement to private enterprise and improvement in the investment climate.

On second thought, it probably is just as well that I did not, because we now have the benefit of the excellent memorandum and letter from you and Pete and Walt prepared independently, which I am sure will be of great assistance in the coming months as the administration considers the recommendations of the Comap Committee.

With renewed thanks for your letter and kindest regards, I am,

Sincerely,

J. PETER GRACE.

(At the hearing held on January 15, 1963, Representative Curtis asked that the following excerpt from the Congressional Record be placed in the hearing record as of this day:)

RECENT DEVELOPMENTS IN ARGENTINA

(Speech of Hon. Bourke B. Hickenlooper, of Iowa, in the Senate of the United States, Wednesday, November 13, 1963)

Mr. HICKENLOOPER. Mr. President, I should like to offer a few comments on recent developments in Argentina, and I select this country for two reasons. First, I think it is generally agreed that Argentina has probably the best potential for development into a stable and self-sufficient free country in its parts of the world.

Mr. MORSE. Mr. President, the Senator is delivering a very important speech. I would like to have the Senate hear it.

The PRESIDING OFFICER. The Senate will be in order.

Mr. HICKENLOOPER. I may say parenthetically that the general principles which I shall attempt to develop in my remarks appy to any other countries in Latin America which are engaging in or planning to engage in expropriation of American property, and to any countries in any other part of the world which are engaging in or planning to engage in the expropriation of American property.

Argentina has many advantages not generally shared by most other South American countries, among which are a highly literate population which is predominantly European in stock, the absence of vast land reform problems, plus the possession of natural resources which are considerable.

My second reason for selecting Argentina is that what is happening there has a direct relationship to some of the difficulties our foreign aid efforts are facing in other areas.

On the basis of such measurements as per capita gross national product, number of telephones and radios, miles of railroads and highways and the like, Argentina is already one of the most highly civilized and advanced countries in South America. Its major challenge is to achieve stability of government and to put into practice sound economic policies which can eliminate the effects of years of mismanagement, inflation, a wasting of assets, decline of agriculture, and deficits both in its budget and its balance of payments.

The plight of the Government-run railroad provides a good example of the kind of economic chaos which has been allowed to develop. The volume of freight carried has fallen from 60 million tons in 1942 to less than 30 million tons; yet in the same period, the number of railroad workers has climbed from 90,000 to over 225,000. The result is an annual deficit of some $300 million which the Government is forced to cover.

Such examples can be found in nearly every sector of the economy. In fact, over recent years there has been only one bright spot of any consequence in the whole picture, and this is in the petroleum industry. For years, imports of oil had been steadily rising, in spite of the fact that there is oil within the country. By 1958, Argentina's total annual oil production amounted to only 36 million barrels, and the nation was forced to import some 65 million barrels to meet its needs. Oil was in fact the largest import item, and cost roughly the Argentines $220 million a year in foreign exchange.

Looking back over the painful history preceding them, the Government at that time decided that a different approach might be worthy a try. For almost half a century, the control of oil operations had been in Government hands. Foreign capital and experience had been largely excluded. But faced with such a phenomenal deficit in the balance of payments from a single source, the Argentine Government decided to try a new approach.

It invited outside capital and assistance to supplement the state's own efforts, and the results have been dramatic. In the long decades preceding this event, petroleum production had been built up gradually to 36 million barrels a year, against imports which had climbed to 65 million barrels, as I have noted.

In the 4 years following the time the Argentine Government opened the doors to assistance from private enterprise, the production of oil nearly tripled, while the amount the country has to import has been reduced by roughly 70 percent. In 1962, production had reached nearly 100 million barrels, while imports had shrunk to less than 20 million.

I believe when we get the accurate figure at the end of 1963, it will be even more startling. In terms of foreign exchange, Argentina's expenditures for

buying petroleum or oil products were cut from $220 million a year to $75 million, and the goal of self-sufficiency was in sight. There was even talk of an exportable surplus.

Behind this tremendous accomplishment lie some interesting facts. In general terms, what it took to make the job possible was a combination of capital, technology, and efficiency—in all of which the Argentine Government had been lacking. These key elements were supplied by American oil companies, in competition against each other, who came in, negotiated contracts running up to 40 years, and proceeded to supply the money, personnel, equipment, and techniques which turned the tide.

To date, these companies have invested an estimated $300 million in Argentina since 1958. Their experiences have varied. Several companies have spent close to $50 million in largely unsuccessful exploration efforts. Another company, which has developed production, brought in some $60 million in capital and reinvested another $40 million from the sale of the oil in further exploration and development activities. In general terms, these companies have continued to invest money in Argentina, without any significant return thus far.

This kind of confidence in the country's future has also bred confidence. In addition to the direct investment in exploration and development, there has been the predictable economic fallout in other areas, bringing additional outside investment in transport, refining facilities, and petrochemicals—which together have been estimated at close to another $100 million, added to the economy.

If we add to this the further stimulation to the economy in terms of royalties to the provinces for oil and gas produced within their territories, plus the very basic fact that the oil industry has provided a growing number of jobs for nationals over a period in which nearly every other segment of the Argentine economy has been stagnant, we recognize that here is a very substantial contribution to the development of the country.

This has been done with private enterprise, private investment, and private venture.

I should note that it has also been a real contribution to the pocketbook of the American taxpayer, since here is something approaching a half-million dollar shot in the arm to a country we want to help, but which did not have to come out of U.S. foreign aid, the International Monetary Fund, the World Bank, or any other of the many organizations to which we so largely contribute.

One could be pardoned for assuming that the Argentine Government would also recognize the magnitude of this contribution to the welfare of its people. Unfortunately, this does not appear to be the case. There is now a new Government in office in Argentina, and one of its major articles of political faith seems to be a determination to abrogate the contracts or to nullify them to use their own language, negotiated by the previous government with the U.S. oil companies.

While it is perhaps not too difficult to appreciate the political charm of sloganeering about "throwing out Yankee imperialists" during a Latin American election campaign, it is very hard indeed to discern any semblance of rationality in such an action in this instance. In practical terms, this would amount to a frontal attack on the only really sound and hopeful economic development that has occurred in that country in the last decade.

The reasons expressed by the new Government for this extraordinary proposal have been rather nebulous thus far, consisting mainly of charges that the contracts are illegal and uneconomic. The only argument which the Government has advanced regarding their legality, to my knowledge, is that the contracts were not submitted to the Argentine Congress for ratification.

While I am not expert on Argentine constitutional procedure, I cannot help but be impressed by the logic of some of the comments which the oil companies have made in this regard. As they point out, the agreements merely put them in the position of hired contractors. They have engaged to spend a good deal of money, time, and effort in trying to find oil—but any oil found becomes automatically the property of the Government. The companies do not have title to it. They cannot export it. All they can do with it is deliver it to the Government at a previously agreed upon price. Both legally, and in effect, they are simply contractors hired by the state oil agency to help do a job which that agency had neither the capital nor the ability to do itself.

If the state oil agency has to get the approval of congress to hire a contractor, then presumably the state-run railroad would have to get congressional approval to sign a contract to repair freight cars. The oil companies assert that there is no such precedent in Argentine law, or anywhere else for that matter,

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so far as anyone knows, and I find this quite believable. Any country which operated along these lines would have to keep its congress in session 24 hours a day.

Aside from this is the interesting fact that everyone accepted the contracts as legal and binding, and both parties attempted to live up to their terms for about 5 years, until a new government come in. I say "attempted to live up to their terms." The U.S. companies actually overfulfilled their contractual obligations. They drilled more wells and found more oil than even the Government had hoped at the time the agreements were made. While the country is still not self-sufficient in oil, it has gotten a good deal closer than anticipated in such a short period.

The Argentine Government's performance is note quite so good, not so much because it did not try but because of the general fiscal chaos which has existed within the Government. The state oil agency, to which the U.S. producing companies are obliged to deliver the oil, has not been able to pay for the oil. It is currently behind in its payments to the tune of tens of millions of dollars.

One American oil company alone is owed more than $28 million for oil it has produced with its own capital and know-how, and has delivered it to the Argentine Government agency. It is holding the sack for that amount of oil, to say nothing of any recoupment on its investment. Other oil companies are owed comparable amounts, in keeping with the extent of their operations and contracts.

As for the Government's other charge—that the contracts are uneconomic—it is unlikely that the oil companies would disagree with this assertion. They have clearly been uneconomic for the companies thus far, since the companies have continued to invest, and reinvest, and are left at the moment with not much to show for their effort except overdue bills.

Just why the contracts are uneconomic to the Argentine Government is difficult to see. As I have noted, they have saved the Government millions of dollars in desperately needed foreign exchange. As to the price the Government pays the companies for the oil—and this is quite apart from any considerations of sanctity of contract—it appears to be considerably less than the cost of oil of comparable quality imported from Venezuela, the Middle East, or anywhere else in the free world. The former Secretary of Energy and Fuels recently testified that the oil supplied by the contracting companies costs between 20 and 50 percent less than similar types of imported crude.

That is the testimony of Argentine officials themselves. The witness pointed out that this represents oil which the Government was in no financial or technical position to find oil and develop it itself.

Not only have the U.S. companies been supplying oil at lower rates than it could be imported; under their contracts they are also charging less for a barrel than the Government oil agency can produce it through its own efforts, on the basis of cost estimates submitted to the Congress by that agency. And on the basis of the Government's own per barrel valuation, the value of the oil already delivered by one company exceeded the price charged by some $20 million. To put it another way, the Argentine Government has received oil for a price $20 million less than it would have cost to produce it itself, according to its own figures. Yet the Argentine Federal company has not even paid for all the oil.

When we add to these considerations the fact that, at the end of the contracts, the Government will receive free of charge all permanent facilities installed by the companies—including pipelines and other expensive installations—it is perplexing, to say the least, to find that Government calling the contracts uneconomic.

It is also appropriate to wonder what lies ahead. In order to find and produce the quantity of petroleum required to meet Argentina's growing needs over the next 9 years, it is estimated that an investment of some $1.7 billion will be required. This is an average of nearly $200 million a year, and it would be interesting to know where a deficit-ridden government and a bankrupt state oil agency would propose to get capital funds on this order, particularly if they pursue their presently announced course.

Abrogation of the oil contracts would, to a very considerable extent, succeed in drying up outside capital funds from all quarters and for all purposes. If a contract made with one government is likely to last no longer than the inauguration of the next government—particularly in South America—then the whole concept of long-term investment can no longer apply either, a conclusion which will be speedily drawn by potential investors everywhere.

From reports coming out of Argentina, it appears that some of the politicians there profess to see a solution by simply having the state oil agency take over all

oil operations. That such a course would be naive in the extreme is rather obvious. The record indicates that the U.S. companies have done more to increase oil production in 4 years than the state had accomplished in half a century, and it took a large amount of capital in addition to know-how.

Moreover, Argentina simply does not have the financial capabilities to pay the costs of taking over the U.S. operations. Beyond this, it does not have the funds to commit to needed further oil development.

About the only foreseeable consequences of this cavalier course would be to render any contract with the Argentine Government next to worthless in international circles, while hastening the Argentine oil industry down the road its railroads have already gone.

One other alternative has been hinted at—that Argentina might make up its oil deficiency by importing Russian oil. It is no secret that the Communists would be delighted to see this happen. With the tragic example of Cuba before them, I doubt that a majority of Argentine citizens would care to follow that course, since they value freedom highly.

As I said at the start of these remarks, what is happening in this particular situation typifies some of the dilemmas facing our foreign aid program in a number of areas. It is my understanding that our viewpoint is that we wish to do whatever we can to assist freely elected governments throughout the world, where we can assist, with the necessarily rather imprecise goal in mind of advancing the caûse of human freedom, in which we believe.

I have no quarrel with this objective; I support it. But at times it is hard to see how to go about it. Take the case in point. Here is a country which is emerging from the shadow of years of dictatorial rule which left a legacy of bankruptcy and economic decline. The Argentine people apparently want stability and economic growth, under an elected government. Since these are goals which we support, we have been trying to assist in this undertaking, with funds exacted from the American taxpayer and through freely made private investment.

But developments such as those in regard to the oil contracts are enough to give anyone pause. So far as foreign aid is concerned, we must recognize that we are dealing with a sovereign government, and that it is neither proper nor desirable on our part to presume to tell that government how to conduct its affairs.

When such a government proposes to follow a course, however, which is clearly designed to compound its financial difficulties—and damaging bona fide private American interests in the bargain—we had better ask ourselves how long we can continue to underwrite such experiments. We have no mandate from the American taxpayers to continue to pour their income down bottomless pits, and they appear to exist all over.

It is one thing to love thy neighbor as thyself, as the Bible enjoins us; but this is becoming a pretty large neighborhood. American aid just about blankets the globe. If every sovereign government on earth wishes to dig its own economic grave, it has a sovereign right to do so, I presume; but the American Government also has a sovereign right to refuse to pay the cost of excavation. Indeed, we could not do so even if we wanted to; there is simply not that much money in America, or anywhere else in the world, for that matter.

I think it might be helpful if this fact could be slightly better appreciated by some of the many countries which look to us for support. It might as well be understood that while the United States is willing to continue to contribute to the cause of freedom throughout the world, it does not plan to bankrupt itself in the processs, and thus sacrifice its own freedom, leaving the field to the enemies of freedom.

To make this understood, I think we had better start today. One way to do this is to make it plainly understood that the U.S. Government is not prepared to give money, goods, or services to countries which will not even honor their obligations to U.S. citizens and corporations. Unilateral abrogation of such obligations by other countries should be understood to be synonomous with unilateral cessation of aid from this country.

Mr. MORSE. Mr. President, will the Senator from Iowa yield?

The PRESIDING OFFICER (Mr. McIntyre in the chair). Does the Senator from Iowa yield to the Senator from Oregon?

Mr. HICKENLOOPER. I have a number of newspaper articles, communications, and so forth, which I wish to discuss and to have printed in the Record, but I can do that a little later. They are in further reference to the amendments we adopted last year and to those we adopted this year in regard to these items.

I am happy to yield to the Senator from Oregon.

Mr. MORSE. Mr. President, I wish to ask about these amendments. The Senator from Iowa and I have held conversations, not only in regard to what is happening in Argentina, but also in regard to what is happening in other Latin American countries. The Senator from Iowa knows that I am very much concerned about the application of the Hickenlooper amendment to these situations. In fact, some of us considered trying to broaden the Hickenlooper amendment; but after my discussion with the Senator from Iowa, I am inclined to agree with his view that probably no other amendment is needed, if there is clear agreement as to what the Hickenlooper amendment already encompasses.

So far as the situation in Argentina is concerned, our proper course is very clearly indicated by the facts in that case. If the Argentine Government nullifies those oil contracts and refuses to follow the procedures of international law which the Hickenlooper amendment encompasses, and if the Argentine Government expects to share in any way in the economic assistance provided by the United States, our State Department must notify the President of the Argentine that the Hickenlooper amendment will be applied, and that there will be no "maybe" about it.

So my first question is—in dealing somewhat with a hypothetical case, but also relating to the situation in the Argentine—If the President of Argentina proceeds to nullify these oil contracts, is it the opinion of the Senator from Iowa that the Hickenlooper amendment will apply and the U.S. Government will be obligated to carry out its provisions, which, if a satisfactory adjustment of these claims is not made by the Argentine Government, will result in the cessation of our economic aid to Argentina?

Mr. HICKENLOOPER. In my opinion, the answer to that question is "Yes." I believe the amendment of last year—the provision now in the law—could be extended, by proper interpretation, to cover such a situation of nullification of contracts, as compared with expropriation or seizure of physical property. But certainly under the amendments we have adopted and under the additional amendment which now is before us, which specifically refers to nullification and to action which has the effect of destroying the property rights of individuals, I think there is no question that it applies and that it would have to be applied not only to nullification of these oil contracts, which have been in effect since 1958, but also to the fruits of them, of which Argentina has taken advantage. The latter point raises a further question, for this is not a question of nullification of contracts after they were entered into, but before performance was had under them—although under some legal concepts, damages might be due in that situation. On the contrary, in this case performance has been had, and the oil has been delivered under the provisions of the contracts, and up to this time the contracts have been consummated in full good faith. Therefore, at this time nullification would amount to a direct seizure of property rights, and the amendment will apply.

Mr. MORSE. The Senator from Iowa and I have talked with other members of the committee and other members of the subcommittee—because both of us are members of the Subcommittee on Latin American Affairs; these members are very much concerned about whether the nullification amendment applies to this year's bill. I said to them that I think it does. However, this is a good time to clarify that situation and to leave no doubt about that matter.

Will the Senator from Iowa take time to refer to the Hickenlooper amendment of last year and also to the proposed changes in it, as contained in this year's bill. In my opinion this supports his contention, in which I join, that the Hickenlooper amendment, as it will be in existence after the enactment of this bill, will cover the Argentine oil contract nullification case.

Mr. HICKENLOOPER. I shall be very happy to do so; and I think it should be made part of this record.

I call the attention of the Senator from Oregon and the attention of other Senators to the report of the Foreign Relations Committee on House bill 7885, dated October 22, 1963, at page 67, and to the item on that page beginning with "(e)". I ask unanimous consent that this portion of the report be printed in the Record.

There being no objection, the excerpt from the report (No. 588) was ordered to be printed in the Record, as follows:

"(e) The President shall suspend assistance to the government of any country to which assistance is provided under this *or any other* Act when the government of such country or any [governmental] *government* agency or subdivision within such country on or after January 1, 1962—

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

"*(2) has taken steps to repudiate or nullify existing contracts or agreements with any United States citizen or any corporation, partnership, or association not less than 50 per centum beneficially owned by United States citizens, or*

"[(2)] *(3)* has imposed or enforced discriminatory taxes or other exactions, or restrictive maintenance or operational conditions, *or has taken other actions,* which have the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property so owned,

and such country, government agency or government subdivision fails within a reasonable time (not more than six months after such [action or after the date of enactment of this subsection, whichever is later] *action or, in the event of a referral to the Foreign Claims Settlement Commission of the United States within such period as provided herein, not more than twenty days after the report of the Commission is received*) to take appropriate steps, which may include arbitration, to discharge its obligations under international law toward such citizen or entity, including [equitable and] speedy compensation for such property in convertible foreign exchange, *equivalent to the full value thereof,* as required by international law, or fails to take steps designed to provide relief from such taxes, exactions, or conditions, as the case may be [,]; and such suspension shall continue until [he] the President is satisfied that appropriate steps are being taken, and no other provision of this Act shall be construed to authorize the President to waive the provisions of this subsection.

"*Upon request of the President (within seventy days after such action referred to in paragraphs (1), (2), or (3) of this subsection) the Foreign Claims Settlement Commission of the United States (established pursuant to Reorganization Plan No. 1 of 1954, 68 Stat. 1279) is hereby authorized to evaluate expropriated property, determining the full value of any property nationalized, expropriated, or seized, or subjected to discriminatory or other actions as aforesaid, for purposes of this subsection and to render an advisory report to the President within ninety days after such request. Unless authorized by the President, the Commission shall not publish its advisory report except to the citizen or entity owning such property. There is hereby authorized to be appropriated such amount, to remain available until expended, as may be necessary from time to time to enable the Commission to carry out expeditiously its functions under this subsection.*"

Mr. HICKENLOOPER. Mr. President, the amendment of last year provides as follows:

"(e) The President shall suspend assistance to the government of any country to which assistance is provided under this Act when the government of such country or any agency or subdivision within such country on or after January 1, 1962—

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

"(2) has imposed or enforced discriminatory taxes or other exactions, or restrictive maintenance or operational conditions, which have the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property so owned,".

Then it provides the methods of determination, arbitration, and so forth.

I have read the language down to that point, as contained in the present law. Now I read the additions which were made in the committee this year, in strengthening that language.

The present law reads as follows:

"(e) The President shall suspend assistance to the government of any country to which assistance is provided under this"—and this year we added—"or any other."

The words "or any other" were added this year. So the language would then read:

"(e) The President shall suspend assistance to the government of any country to which assistance is provided under this or any other act when the government of such country or any"—and we substituted for the word "governmental" the word "government"—"government agency or subdivision within such country on or after January 1, 1962"—

Paragraph (1), which I read a while ago, would remain the same.

Then we added (2), a paragraph which reads as follows:

"(2) has taken steps to repudiate or nullify existing contracts or agreements with any United States citizen or any corporation, partnership, or association not less than 50 per centum beneficially owned by United States citizens, or"—

Then we pass to the new (3), which was the old (2), which would read—

"(3) has imposed or enforced discriminatory taxes or other exactions or restrictive maintenance or operational conditions"—

And then we would insert the words—"or has taken other actions."—

Continuing to read the section—"which have the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property so owned."

One of the reasons for inserting the words "or has taken other actions" is that the language would give a direction to the President to use broad discretion in determining the rights and interests of American property abroad. We name it as specifically as it is reasonably possible to do so. The language "or has taken any other action" would have that effect. The President would have the responsibility and the discretion to determine when American property is being seized.

The present law provides, in effect, that those provisions would go in effect if "such country, government agency, or government subdivision fails within a reasonable time—not more than 6 months after—such action or after the date of enactment of this subsection, whichever is later."

The law passed last year provided "to take appropriate steps," and so on. This year we have inserted the language that where the country, government agency, or government subdivision has failed to take, "within a reasonable time—not more than 6 months after such action or"—I am now reading the insertion—"action or, in the event of a referral to the Foreign Claims Settlement Commission of the United States within such period as provided herein, not more than 20 days after the report of the Commission is received."

We added that language because there is a new addition calling for a referral to the Foreign Claims Settlement Commission, for the reason that that Commission has machinery and legal history to set up for evaluation foreign held properties as a result of their experience in settling foreign claims, at least especially following World War II.

All of what I am talking about will be in the record.

Another provision provides for the President to request the Foreign Settlement Claims Commission to evaluate such property. He would then make a determination as to whether or not the valuation set on the property abroad would be a reasonable valuation or not. If it is considered to be unreasonable or unfair, he must withhold aid. If it were a fair evaluation, it would be up to the owners either to take it or leave it. If they should prefer not to take it, and the determination should be that the valuation was a fair valuation, then, of course, they would be left to their own devices within the countries to fight it out in any way they might desire.

Mr. Morse. Mr. President, I thank the Senator from Iowa for joining me in making the legislative history. The language from the old act, with the previous Hickenlooper amendment, plus the new language in the bill that has come to the floor of the Senate from the committee, leaves no room for doubt that it covers nullification of contracts in which property values, as well as outright expropriation of property, are involved. The American business concerns that have expressed such great concern to the Senator from Iowa and to the Senator from Oregon ought to appreciate the fact that the Senator from Iowa sought to draft language that would protect them in connection with almost any possible contingency that could develop if a foreign government should seek, by one means or another, to expropriate the value of the porperty or nullify contractual relations that would have a bearing upon the value of the property.

As the Senator knows, the Kennecott Copper Co. has extensive copper mining holdings in Chile. So does Anaconda Copper Co. I have met with officers of the Kennecott Co., as has the Senator from Iowa. I have told them that I know nothing about the merits of their case, just as I know nothing about the merits of the case of the American oil companies in the Argentine. It is not for me to pass judgment on the merits of the case, however. It is a Senator's duty, as I see it, to make certain that procedures are established under which these companies would have an opportunity to establish the merits of their case and under which they would be protected from unfair discriminatory practices against them on the part of any foreign government because they are American concerns.

As the Senator knows, it is alleged by the Kennecott Copper Co.—and they have made more than a prima facie case in support of their allegation—that the Chilean Government is following a discriminatory tax policy that is aimed at the Kennecott Co. It may discriminate against other companies. But there is no doubt about the fact that it discriminates against the Kennecott Co. if he allegations are accurate, and they appear to be.

The result is that the Kennecott Co. cannot operate its mining properties, and not being able to operate its mining properties, it is suffering great loss even in trying to maintain the companies. It looks upon this move on the part of the Chilean Government as an effort to finally force Kennecott either to dispose of its property in Chile for an unfairly low price or to abandon it and give up even trying to maintain it, which would thereby make it possible for the Chilean Government to enter into what would amount to a form of expropriation of the property.

Mr. HICKENLOOPER. It is situations of that kind which the words "or any other means" in this year's bill are intended to cover, by way of giving the President discretion to determine that those so-called any other means are in effect a denial of property rights, or the destruction of the rights of American owners in foreign countries, and would therefore call for the operation of this amendment. There is a responsibility on the administrator to use his discretion.

Mr. MORSE. Plus the language, now, in the new subsection (3), which was the old subsection:

"(2), has imposed or enforced discriminatory taxes or other exactions, or restrictive maintenance or operational conditions, or has taken other actions, which have the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property so owned."

Mr. HICKENLOOPER. That is correct. There was a provision against discriminatory taxes in the amendment which we put in the bill last year, but we wish to add the words, "or has taken other actions." It is a fine distinction, when one comes to argue with some of the "legalistic" people in foreign countries.

Suppose the Government owns a part of the mining industry, and private operators own some other portion of the mining industry. The Government could very well conduct its own mining without regard to taxes, but could levy taxes upon the one or two other privately owned businesses in an amount great enough to drive them out of business.

The Senator referred to the company in Chile. The company has had imposed upon it, according to my information, a tax of 87 percent of net profits, leaving only 13 percent. I do not have the details, but the government refused to allow what are recognized in this country as the ordinary expenses of doing business. They toss items into "net profits" which are not net profits at all, but are current operating expenses. The company is going backward all the time. The government is proposing new requirements for expansion—new buildings; new this, that, and the other thing—which are beyond the capacity of the company, if it is to keep its nose above water. It cannot operate in that kind of situation.

Those are discriminatory taxes. Those are excessive requirements, which are, in effect, a confiscation of the property of Americans.

Mr. MORSE. They seek to impose requirements for expansion on the company and force it to operate at a loss, apparently in the hope that forcing it to operate at a loss will also force it to sell its properties for a song, and get out of Chile. There are other copper companies that could very well find themselves in the same position, if they do not watch out.

Mr. HICKENLOOPER. The Senator is correct. The threatened oil property expropriation in Peru, is in many ways patterned after the Argentine proposal.

Mr. MORSE. That is correct.

Mr. HICKENLOOPER. In northwestern Peru along the desert area and the ocean, many millions of dollars were spent by American and other oil companies in an attempt to develop oil fields. The program did not develop too successfully. There is a geologic promise of oil in the Iquitos area, the area back of the mountains. It has cost millions of dollars to fly in equipment and American engineers and technicians to cover the jungle. People have been living in the jungle for years. Private companies have put up their money, exploring on behalf of the Government of Peru under contracts and agreements.

I now understand that there is good promise of oilfields being discovered after years of effort and the expenditure of millions of dollars. But now that oilfields have probably been discovered the proposal is made that Peru expropriate them,

to take advantage of all the expenditures made. Such a seizure would be a repudiation of contracts and obligations.

Mr. MORSE. We must beware of such situations all over Latin America, if we let these precedents be set.

I have one final question. Will the Senator turn to section (e) on page 67 of the committee report, which reads:

"The President shall suspend assistance to the government of any country to which assistance is provided under this or any other act when the government of such country or any government agency or subdivision within such country on or after January 1, 1962"—

Does the things listed thereafter. Does the Senator agree with me that the language "under this or any other act" would prohibit the President of the United States from using his contingency fund to be of assistance to one of these countries, if it were determined the country had violated the terms and conditions of the so-called Hickenlooper amendment?

Mr. HICKENLOOPER. I believe it would. I believe it is broad enough to do that. It is the intent to cut off aid, bounty, gifts and assistance to countries which not only are using such for their own ulterior purposes but also are defrauding, in effect, American investors whom they have invited to come to those countries. There is one exception. We agreed to an amendment yesterday exempting the Peace Corps.

Mr. MORSE. And the cultural exchanges, also.

Mr. HICKENLOOPER. Yes; the cultural exchanges, as well. I voted for that exemption for various reasons. I believe that humanitarian operations probably have a little different complexion. It is my understanding and my intention—and I believe that of other Senators who voted for the amendment—that if the abuses are great enough, it is within the discretion of the President even to halt those operations.

Mr. MORSE. We made it very clear yesterday, in the legislative history, that the amendment did not put the Peace Corps in the position where it could not be taken out.

Mr. HICKENLOOPER. That is correct.

Mr. MORSE. Or that the cultural exchanges could not be stopped. That will fall within the discretion of the President.

Mr. HICKENLOOPER. We made that very clear.

Mr. MORSE. I should like to make another point clear, I completely agree with the statement of the Senator from Iowa about the situation in Chile or in Argentina. If it should be found after analysis of the merits of the positions of the companies involved, that those governments are following a course of action—Chile in regard to the Kennecott Copper Co., and Argentina in regard to the nullifying of contracts of these oil companies—in flagrant violation of the Hickenlooper amendment, the President would be prevented also from using the contingency fund to get around the Hickenlooper amendment.

Mr. HICKENLOOPER. I believe the Senator has correctly stated the case. I should like to invite attention to another contingency. There are problems of patent rights which were acquired and exist under law in those countries. Patent rights are not physical, tangible rights.

They are intangible rights, but rights, nevertheless. Many countries are threatening to seize American patent rights, to abrogate them and to destroy them, even though they were granted legally under the laws of the country, or under treaties or agreements, and have a limited time to run, as is the case in our own country.

Those rights are undoubtedly rights, just as tangible property rights are.

Mr. MORSE. Lastly, I spoke recently on the Chilean situation. Tomorrow I shall put in the Record, in support of legislative history being made tonight, further data dealing with the Chilean tax discriminatory policy in connection with American companies in Chile.

I say most respectfully to my President, "You had better prod your State Department to action, because Chile is proceeding with a course of action that cannot be reconciled with granting her any aid, until she changes her discriminatory policy against American business."

The paradox is that Chile, along with the Argentine and many other Latin American countries, has been pleading and begging to get foreign investors to come in. Foreign investors have been offered inducements to come into those countries. That fact places those countries under an obligation to follow a nondiscriminatory policy in respect to those investors—the same policy that is followed with respect to domestic investors.

There is an election campaign in progress in Chile, and candidates are vying with one another to see who can make the strongest anti-American statements; but we cannot let Chilean politics do irreparable damage to American investors, who, in my judgment, must be recognized as having some international law rights.

The State Department ought to be told to "get on the ball" so far as the Chilean and Argentinean situations are concerned, and make perfectly clear to those governments that if the merits of the cases substantiate the allegation that they are in violation of the Hickenlooper amendment, aid will be stopped.

It is our money. If they are going to take it, they ought to take it subject to reasonable terms and conditions that we are seeking to lay down in the foreign aid bill.

I thank the Senator for joining me in making the legislative history. The legislative history being made tonight will not be the last time we shall hear about the subject. We are making legislative history tonight that will arise again and again, and will cause some questions to be asked of the State Department—for example, "What have you done with respect to the Argentine and Chile, or any other country that follows a policy or takes steps that discriminate against American investments in those countries, when they are not protected? What have you done to put the Hickenlooper amendment into full force and effect?"

Mr. HICKENLOOPER. I thank the Senator for his contribution. To button this matter up, I shall put in the Record evidence of expropriation and seizure policies. I want to appear in the Record in connection with this discussion one thing about which the Senator well knows, because we have discussed it. The Foreign Assistance Act already contains a provision as to the announced and adopted policy of the United States, in section 601, part III, chapter 1, under the head of "General Provisions." For ready reference, this language is contained in the report of the Committee on Foreign Relations on the pending bill, which I referred to earlier in my remarks. I read from page 60 of the report:

"Accordingly, it is declared to be the policy of the United States to encourage the efforts of other countries to increase the flow of international trade, to foster private initiative and competition, to encourage the development and use of cooperatives, credit unions."—

After referring to several other activities, the paragraph continues—"and to encourage the contribution of U.S. enterprise toward economic strength of less-developed friendly countries, through private trade and investment abroad, private participation in programs carried out under this act."

And so forth. We have announced that it is our policy to encourage these very people to go into those countries with American private capital, private enterprise, private ingenuity and money, whether it be in agriculture, mining, or electrical development, or other development. We have encouraged that with one hand, and with the other hand we have failed to stand up and protect the claims of those investors, and the equity of their rightful claims.

Mr. MORSE. The Senator from Iowa is correct.

Mr. HICKENLOOPER. That is all we are trying to reach. I think the sentiment of Congress is pretty well developed in that respect.

I call the attention of the Senator to an announcement which is very interesting. It is stated in a bulletin dated November 12, published by the Alliance for Progress: "U.S. Firm Studies Argentine Investment." It calls attention to the fact that Alcan Pacific Co. of Sacramento, Calif., an Alaskan corporation—and the Senator from Alaska should take note of this—with diversified experience in construction contracting is going to conduct a survey in the Argentine, and proposes to make an initial investment of about $1 million on some kind of development project. As the bulletin states, the company expects to obtain about one-half of this amount, equal to $900,000, in pesos and dollars from public and private lending sources. The Alliance for Progress is putting out further encouragement and announcements.

The constituents of the Senator from Alaska had better be very careful before they put any of their own money into that area by way of private investment, unless we make clear to those countries that American property will be equitably protected, one way or another, once it goes into that country with the authority and approval of the government that invited it.

Mr. MILLER. Mr. President, will the Senator yield?

Mr. HICKENLOOPER. I yield.

Mr. MILLER. First, I commend my able colleague for his very thorough and timely speech. I should like to ask a couple of questions with a view to adding

something to the legislative history which was just discussed by the Senator from Iowa and the Senator from Oregon.

On page 67 of the report of the Committee on Foreign Relations, to which the Senator from Iowa just referred, I invite attention to the fact that subsection (e) reads:

"The President shall suspend assistance to the government of any country to which assistance is provided under this or any other act when the government of such country or any government agency or subdivision within such country on or after January 1, 1962—"

Does certain things. Subsection (2) under subsection (e) has been added by the committee this year.

Is it the intention that any actions taken, as described in subsection (2), from January 1, 1962, on, shall have the results that have been described with respect to the other items that were listed in the act last year?

Mr. HICKENLOOPER. That is the exact intention of the amendments. They refer back to January 1, 1962. It is the intention to have the amendments which we are adding to the present law become retroactive to January 1, 1962. I think that is pretty well understood by the State Department.

Mr. MILLER. So if an oil company had a contract repudiated after January 1, 1962, but prior to the date of the enactment of this act this year, it could seek relief under this act?

Mr. HICKENLOOPER. That is correct.

Mr. MILLER. I have another question——

Mr. HICKENLOOPER. Before the Senator goes to his next question, I point out that in the discussions in the committee and with Members of the Senate in connection with these amendments—I am sure I speak without fear of contradiction by committee members in connection with the intent of this legislation—it was believed that, if there should be any technical legal failure of any kind in connection with these amendments, there is still enough discretionary power in the Chief Executive to accomplish the objectives; and we expect the administration to do so, even though there may be some legal question under which someone may attempt to crawl in an attempt to avoid the conditions of this provision.

There is broad discretion in the act. We are merely trying to button it up doubly and triply.

Mr. MILLER. The Senator would like to have the administration take action about the way in which he would expect them to take action with respect to their own personal property or money in a similar situation. Is that correct?

Mr. HICKENLOOPER. I hope they do not handle their personal property in the way in which they handle Government property. Therefore, I do not know whether the comparison is quite apt. However, the Senator's observations are well taken.

Mr. MILLER. I should like to ask one or two more questions.

Mr. HICKENLOOPER. I yield.

Mr. MILLER. On page 67 of the report it is stated that if the foreign government, the recipient of our foreign aid, does any of these acts, and if "such country, government agency, or government subdivision fails within a reasonable time to take appropriate steps to discharge its obligations under international law toward such citizen or entity," and so forth.

I suppose that refers to the confiscation of property, and means that an appropriate payment should be made; and we provide further that it be made in convertible foreign exchange.

My question is with respect to the situation described in subsection 2 regarding the nullification of existing contracts.

We do not have the taking of property as such, but we do have damages. Is it the intention behind this provision that under international law damages which may arise from actions taken to repudiate or nullify existing contracts shall also be paid in convertible foreign exchange?

Mr. HICKENLOOPER. Yes.

Mr. MILLER. Equivalent to the full value of the damages?

Mr. HICKENLOOPER. Yes; there is a body of international precedent and law and agreement that has been built up. I am not quite sure what international law is. I know what it is said to be. I am not quite sure what it is, however, It is a hodgepodge of itinerant agreements, treaties, international agreements, and this, that, and the other thing. We could probably go back to the days of Genghis Khan, and pick up old parchments to seek out what international law is. However, there is a generally recognized procedure and form and system of evalu-

ation, to the effect that we must give value for property seized. That principle is pretty well recognized.

Mr. MILLER. In other words, we want that procedure to apply with respect to damages which arise under a nullification of a contract.

Mr. HICKENLOOPER. Yes.

Mr. MILLER. I invite my colleague's attention to the wording of the act, about 10 lines from the bottom on page 67 of the report, where it is provided:

"To take appropriate steps, which may include arbitration, to discharge its obligation under international law toward such citizen or entity, including speedy compensation for such property in convertible foreign exchange."

We do not include speedy compensation for such property or damages.

Mr. HICKENLOOPER. No; I believe it was the intent of the committee that under our concept and the concept of most jurisdictions which have a system approaching ours, and even under international law, damages apply when a contract is subject to cancellation or nullification. I believe damages are included.

Mr. MILLER. When the Senator refers to speedy compensation for such damages, he means for such property in a broad sense, including not only personal property, but also property rights under contracts. Is that correct?

Mr. HICKENLOOPER. Yes. Damages under any view include property rights. That may have to be determined by hearing.

Mr. MILLER. The reason why I am asking these questions is that I am afraid that our experience has been that some interpreters of what we do in Congress like to play games with words; and we wish to make it clear that we are covering all reasonable contingencies, so that there will not be any confusion or any excuse that they did not understand what we intended, after they read the report.

My last question relates to the next item, in which reference is made to a failure to take steps designed to provide relief from such taxes. There are two ways to interpret that language. One would be that relief from such taxes would mean not imposing them in the future. That is a form of relief. At least we would not get hit a second time. I suggest—and I would like confirmation from my colleague—that the intention is not quite that easy, but that we intend, as I interpret it, that if discriminatory taxes have been imposed, the relief would relate to the imposed taxes, as well as any future taxes of like kind.

Mr. HICKENLOOPER. It most certainly is the intent, if discriminatory or confiscatory taxes have been imposed, that they be reexamined and readjusted on the basis of equity and fairness, and that, of course, under the law would be the responsibility of the Administrator to determine, or in such other forum as may be properly set up to determine that question.

Mr. MILLER. I thank my colleague.

Mr. MONRONEY. Mr. President will the Senator yield?

Mr. HICKENLOOPER. I yield.

Mr. MONRONEY. I compliment the distinguished Senator from Iowa for his very illuminating and thorough study and presentation of this issue. It strikes me if our aid is to mean anything it will have to be used to make a country self-sufficient. The Senator gave us a graphic illustration when he said that a foreign exchange drain that cost Argentina $220 million a few years ago has been cut to $75 million by the great assistance that has come from American oil companies.

It is my impression that these contracts were arranged at the convenience of the Argentine Government, knowing their fetish for preserving for themselves their mineral rights, and that in order to accommodate the Government of Argentina, the oil companies said, "We will contract with you. We will find the oil, if we can find it, and then we will deliver it to you at a price that will be far below the market price." That price was far below the price of the state-owned oil company.

Mr. HICKENLOOPER. Yes; the Senator is absolutely correct. However, it really goes beyond that. The state-owned oil company had been attempting for years to develop oilfields. They had developed a little oil here and there, but they did not have the money, and they did not have the techniques or the know-how or the competence to do it. They invited the American oil companies to come in and look over the field. They then entered into a contract which was in all probability one of the most advantageous oil contracts ever entered into. I happened to be down there after the contract had been in effect for 2 years. I talked with Argentine officials and with private individuals. Everyone was delighted with it. They were getting oil cheaper than they could produce it themselves.

Mr. MONRONEY. And they were saving foreign exchange.

Mr. HICKENLOOPER. Yes; they were saving foreign exchange. I have tried not to be extravagant in my statement in connection with what I have said. I have tried to underplay rather than overplay it, but there is much competent authority which declares confidently that if the Argentine Government had met its commitments and had paid for the oil as it was received, probably at the end of this year it would have been self-sufficient in oil.

Mr. MONRONEY. Reinvestment of the payment for the American-produced oil to find new sources——

Mr. HICKENLOOPER. And new development.

Mr. MONRONEY. That is correct.

Mr. HICKENLOOPER. The Argentine oilfields—the Senator from Oklahoma represents, in part, an oil-producing State, so I will not attempt to tell him how an oilfield is operated—are in a peculiar situation, so I am told. The oilfields and wells require constant attention and highly skilled know-how. It is not like putting a hole down in the ground and from then on not paying much attention. Oil wells require constant attention. Oilmen could probably describe the situation in more detail; I cannot. But that was one of the troubles. The Argentine Government did not know how to handle the wells. The wells are now producing oil, but the Government is not paying for it. They allowed American capital and know-how to be invested to the extent of $200 or $300 million, and are now proposing to confiscate and talk about settlement later.

Mr. MONRONEY. Is that not worse than expropriation? Labor, know-how, techniques, and machinery have been moved into Argentina. at the invitation and request of that country, is now taken without any alternatives being offered in the way of compensation. Argentina land, previously worthless, might now be worth millions of dollars, yet these oil companies would receive no compensation?

Mr. HICKENLOOPER. The land itself probably is not owned by the oil companies. I think the operations are on an employment or contractual basis, as I tried to point out; and under the agreements, at the end of the leasehold or contractual period, the property would eventually revert to the Argentine Government.

Mr. MONRONEY. The producing well would be left intact for the benefit of the country that had invited the oil company to come in. The oil company would be paid for its labor. The arrangement would be a labor contract.

Mr. HICKENLOOPER. That is correct.

Mr. MONRONEY. It would extend for several years, to compensate the company not only for its risk investment, but also for its labor and machinery.

Mr. HICKENLOOPER. It is a production contract.

Mr. MONRONEY. The companies took the greatest risk, it seems to me. The Senator is absolutely correct. The amendment seems sufficient to cover this situation, but does it apply to the Alliance for Progress loans as well as to other aid which is purely and exclusively American?

Mr. HICKENLOOPER. It does. It applies to any act under which we operate.

Mr. MONRONEY. Even though the act authórizes the placement of investments within a consortium such as the Alliance for Progress?

Mr. HICKENLOOPER. That is the intent.

Mr. MONRONEY. I think this is important. Even if a court should perhaps say that it is not, the Senator knows, and it is cited in the earlier reports concerning the act that it is our desire to assist countries by making them self-sufficient, but the act imposes upon the Chief Executive of the United States the obligation to take action of his own accord when there is a violation of the spirit of foreign aid, which we have so hopefully extended to so many nations of the world.

Mr. HICKENLOOPER. The Senator is correct. The President has power to do that in his discretion.

Mr. MONRONEY. There is no question about it.

Mr. HICKENLOOPER. Two interesting things have begun to develop.

When people begin to scheme how they can take the property of someone else, they develop some interesting theories.

The Argentine Government is now attempting to say—this was a political maneuver in their political campaign—that the contracts which were entered into in 1956 and 1957 were illegal; that therefore, the companies have no rights in them, and that the Government can nullify the contracts. The word "nullification" is used.

However, at the same time, the Government exercised the sole right of taxation on their property and said that it would retroactively tax the property under contract. That was illegal. Of course, if the contract was illegal, the taxes are illegal. There is no provision for taxes. But it depends on whose "ox is being gored," as they cast their eyes upon the interpretation of the contract.

Mr. MONRONEY. Can the Senator from Iowa assure the Senator from Oklahoma and other Members of the Senate that even if the language in the amendment does not specifically include the Alliance for Progress, it is the intention of the Senate, in referring to any other law, that those laws authorizing our investment in the Alliance for Progress would be affected, and that the amendment would not only empower, but would in fact be a direction to the Chief Executive that under this set of circumstances the refusal to honor a just debt would bring into force the full effect of the Senator's amendment, even though it involved direct American aid?

Mr. HICKENLOOPER. The Senator is correct. The amendment refers to the AID programs; and the Alliance for Progress is a part of the aid program complex of the United States. It refers to the Alliance for Progress just as much as it does to any other aid program which is in operation anywhere in the world.

Mr. MONRONEY. I thank the Senator from Iowa and compliment him on his fine presentation.

Mr. HICKENLOOPER. I thank the Senator from Oklahoma for helping to develop the basis and effect of the amendment.

Mr. CARLSON. Mr. President, will the Senator from Iowa yield?

Mr. HICKENLOOPER. The Senator from Kansas is a member of the Committee on Foreign Relations. He can testify in his own right as to the intent, because he, too, labored on the amendment.

Mr. CARLSON. The Senator from Oklahoma raises an interesting point as to whether the Alliance for Progress might not be a part of our foreign aid program and therefore not be covered by the amendment on which the distinguished Senator from Iowa has worked not only at this session but in previous sessions.

The truth is that title VI of the act is the Alliance for Progress. There was never any question in committee that the Alliance for Progress was covered in the Senator's amendment.

Mr. HICKENLOOPER. There can be no question that the Alliance for Progress is an integral part of the entire international aid or assistance program.

Mr. CARLSON. If there had been any question, it would have been well taken care of because, as the Senator from Iowa has stated—and I want the Record to be clear—there was no division of opinion in the committee, among any of its members, as to what we thought was the meaning of the language; and what we wrote into the language is what is known as the Hickenlooper amendment. We wanted it to be all-inclusive. We wanted it to be administered on that basis.

I pay my compliments to the distinguished Senator from Iowa for his continuing efforts in behalf of protecting American investors who, we hope, will go into other foreign countries and help to develop them on a private industry basis. The Alliance for Progress is one of our finest programs, and this is the type of amendment we need to protect private industry, and we hope it will.

Mr. HICKENLOOPER. I thank the Senator from Kansas. It is not my intention to protect any one individual from any other individual. What concerns me, and I am sure what concerns the Committee on Foreign Relations and the entire Senate, is that American investors who are invited to go into other countries and are encouraged to develop land by contributing their own capital, know-how, and risk, and will do other things which will add to the basic expansion of those countries that are less developed, will receive fair, equitable, honorable treatment, by any kind of moral and legal standards which we all recognize as just. We want equitable treatment for them.

The amendment is not an attempt to guarantee profits to any company. It is not an attempt to obtain for any American company any undue concessions. It is merely an attempt to guarantee that their investments, their property, their efforts, their techniques and know-how, will not be permitted to be used in a country under the guise of a fair contract or a fair proposition, and once they have developed something that is worthwhile, have the government of that country, under the claim of a taking for government purposes, take the creation of those people without adequate and full compensation.

Mr. LAUSCHE. Mr. President, will the Senator from Iowa yield?

Mr. HICKENLOOPER. I yield.

Mr. LAUSCHE. As the Senator from Iowa knows, I also am a member of the Foreign Relations Committee; and it is my conviction that in the drafting of

this section, with the amendments which have been offered to it at this session, it was the intention of the Foreign Relations Committee to provide protection to American investment: first, against expropriation; second, against unlawful violation of contracts; and third, against indirect expropriation through the imposition of taxes or other exactions and excises by foreign governments. I think a reading of subsection (e) will disclose that to be the fact.

I know that the Senator from Iowa, in attempting to make this provision all-embracive, insisted upon including, as new language in the bill, the following, which has pertinence to what the Senator from Oklahoma has said: "or any other act."

That addition and the others will make this part of the act read as follows:

"(e) The President shall suspend assistance to the government of any country to which assistance is provided under this or any other act when the government of such country or any government agency or subdivision within such country on or after January 1, 1962—

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

"(2) has taken steps to repudiate or nullify existing contracts or agreements with any United States citizen or any corporation, partnership, or association not less than 50 per centum beneficially owned by United States citizens, or

"(3) has imposed or enforced discriminatory taxes or other exactions, or restrictive maintenance or operational conditions, or has taken other actions, which have the effect of nationalizing, expropriating, or otherwise seizing ownership or control of property so owned."

I concur in the statement of the Senator from Iowa that if by chance this language is not found adequate to reach the Alliance for Progress, the committee intended that it should be reached and that the President should not extend aid either directly to countries or indirectly to countries through the Alliance for Progress.

Mr. HICKENLOOPER. Yes.

There has been some rumor—although I do not allege this to be a fact, because I do not know—that certain Government officials in handling the program have been thinking about a device under which our aid funds would be put into an international pot, and when that international pot distributes the money, it will not be affected by expropriation within certain country, and in that way an attempt might be made to avoid the impact of this amendment.

I say I do not know that is the case, and I do not allege that it is; but I have heard rumors that that is one device which has been discussed as a means of getting around this so-called Hickenlooper amendment and still getting the money to some of these countries, through an international intermediary or pot or account.

I merely wish to say to all and sundry in the Senate and in the State Department and elsewhere that of course that would be a most inexcusable subterfuge and avoidance of the clear intent, not only of this legislation, but also of the will of the Senate itself, in my judgment. I do not say that anyone in the State Department is attempting to do that; but those rumors have been going around.

Mr. LAUSCHE. I hope that is not true.

Mr. HICKENLOOPER. So do I.

Mr. LAUSCHE. I believe the provisions we have written into the bill contemplate aiding the countries to which we are sending help and contemplate insuring the doing of justice to the American investors whom we are encouraging to make investments abroad.

I should like to have a discussion with the Senator from Iowa about another point. He has pointed out the bankrupt condition of the Argentine economy because of the governmental ownership of the railroad and the oil mineral mines since 1958.

Mr. HICKENLOOPER. And also the telephones.

Mr. LAUSCHE. Yes, also the telephones and other public services. In the statement the Senator from Iowa made a few minutes ago to the Senate, he said:

"The plight of the Government-run railroads provides a good example of the kind of economic chaos which has been allowed to develop. The volume of freight carried has fallen from 60 million tons in 1942 to less than 30 million tons; yet in the same period, the number of railroad workers has climbed from 90,000 to over 225,000. The result is an annual deficit of some $300 million which the Government is forced to cover."

Mr. HICKENLOOPER. That is the inevitable result that has so frequently come from government takeovers and government operation of what should be private enterprise and private business.

Mr. LAUSCHE. Am I correct in understanding that in 1942, 90,000 workers handled 60 million tons of freight, but after the Government there took over the railroads, the number of railroad workers increased to 225,000, but they handled only 30 million tons of freight?

Mr. HICKENLOOPER. That is correct, according to information which I have received and which I believe correct. That is a fantastic situation, but it is stated to be the case.

Mr. LAUSCHE. It is said by certain labor leaders that unless certain things are done in the United States, our Government should take over the U.S. railroads. I wonder what would happen if that were to be done in the United States. In my judgment we would follow the same course—led by the Devil—that has been followed in countries that have tried to socialize the public utility services.

Mr. HICKENLOOPER. In almost every instance—and I know this occurred not only in Argentina, but also in a great many other countries—when the governments took over those businesses, political pressures on the legislative bodies and the other political bodies in those countries forced an increase in the number of jobs in those industries. It was said, "Put this man to work" or "Put this political henchman to work"; and thus the employment rolls became filled with political henchmen, until the result was as in the case of the Argentine railroads, on which the volume of freight has decreased from 60 million tons in 1942 to less than 30 million tons, although in the same period the number of railroad workers there increased from 90,000 to more than 225,000 who now handle only a little more than one-third of the amount of freight formerly handled by the much smaller number of employees. A similar development has occurred in very many places in the world; and it seems that, inevitably, when the government takes over, the political pressure to create a job for "good old Joe who worked for us down in the third precinct" has its effect, and employment is thus increased greatly, but inefficiency also develops.

Six or seven years ago, when I was visiting in one of the countries of Latin America, I talked with the president of that country, which 4 or 5 years theretofore had taken over the railroads and the telephone system. He said he was trying then not only to have some kind of compensation paid to those companies, but also to get the railroad companies and the telephone company to take back their utilities and operate them again, because his government could not operate them satisfactorily, and was swamped by the burden of making the attempt to operate them, because of the inability of the government to operate them efficiently. So that is the situation which develops again and again.

Mr. LAUSCHE. Mr. President, in that connection I should like to point out that the International Monetary Fund and World Bank has, as a prerequisite to the granting of financial aid to Argentina, insisted that the overstaffed labor force of the railroads there be reduced by at least 60,000. I refer to that as corroboration of the position taken by the Senator from Iowa in regard to what has happened in Argentina, through its panacea of governmentally operated railroads.

Mr. HICKENLOOPER. Yes, indeed.

Mr. LAUSCHE. Mr. President, will the Senator from Iowa yield further to me?

The PRESIDING OFFICER (Mr. Brewster in the chair). Does the Senator from Iowa yield further to the Senator from Ohio?

Mr. HICKENLOOPER. I yield.

Mr. LAUSCHE. Mr. President, will the Senator yield? I should like to get to the subject of mining of oil by the Argentine Government.

Mr. HICKENLOOPER. I yield.

Mr. LAUSCHE. I understood the Senator from Iowa to say that by 1958, although Argentina was supplied with an abundance of oil in the ground, the nation was importing oil and was not able to supply its own needs.

Mr. HICKENLOOPER. I must take some exception to the Senator's statement that Argentina found itself supplied with an abundance of oil. The trouble was that Argentina thought there was oil there, but they had been unable to develop it in sufficient quantities anywhere nearly to meet their needs. They could not bring out the oil. They thought the oil was there. That is why they brought in American companies and asked them to enter into contracts to try to develop the oil that they hoped was there. Some was being developed, but not very much.

Mr. LAUSCHE. The oil mining companies were governmentally operated?

Mr. HICKENLOOPER. They had been for many years.

Mr. LAUSCHE. According to the statement of the Senator from Iowa, by 1958 Argentina's total annual oil production amounted to only 36 million barrels of oil, and the nation was forced to import approximately 65 million barrels to meet its needs?

Mr. HICKENLOOPER. The Senator is correct.

Mr. LAUSCHE. Oil was, in fact, the largest import item and cost roughly $22 million a year in foreign exchange?

Mr. HICKENLOOPER. The Senator is correct.

Mr. LAUSCHE. After the government called in the American companies and gave up its own proclivity toward governmental operations, what was the experience in producing oil in Argentina?

Mr. HICKENLOOPER. The experience was that the American companies went into Argentina under contracts with the Argentine Government and began to develop the oilfields and explore for new deposits. The Senator will note that there was only about a 4- or 5-year period in which not alone American know-how, techniques, and machinery were used, but also American capital went in there. It was private money and not Government money. By 1962 production had risen to about 100 million barrels.

From approximately 36 million barrels the production had risen to 100 million barrels. Imports went down from 65 million barrels to 20 million barrels. Meanwhile the population of Argentina had gone up. The number of automobiles in Argentina had risen. The use of oil had gone up. So they needed a great deal more oil in 1962 than they did in 1958.

One or two automobile factories were started in Argentina. The need for oil was expanded. The production of the American companies with American capital and know-how had reduced the import necessity and increased the production.

This year they owe one company about $28 million for oil that had been produced and handed over to them. They have not paid for it all, and they owe some other companies millions of dollars. It is freely predicted that had Argentina gone ahead in an unrestricted operation under the contracts, by the end of 1963 Argentina would have been practically self-supporting in oil. In another 2 or 3 years Argentina could have been a net exporting nation of a substantial amount of oil.

Mr. LAUSCHE. Mr. President, it is my understanding that the record shows that in Argentina the state-owned petroleum industry was opened to private enterprise in 1958. American and European companies are now operating throughout the country. Although approximately $280 million of foreign exchange is saved yearly, and Argentina is virtually self-sufficient in oil, the national oil monopoly has dissipated its earnings and requires budget support from the central government. Is that in substance the understanding of the Senator from Iowa?

Mr. HICKENLOOPER. It is my understanding that that is the evidence which we have.

Mr. LAUSCHE. I should like to get down to what the Senator from Iowa is urging. Argentina asked foreign capital to come in and operate the industry privately.

Mr. HICKENLOOPER. Contracts were made with the companies involved.

Mr. LAUSCHE. They went in in 1958. Now Argentina is threatening to breach the contracts——

Mr. HICKENLOOPER. To nullify them.

Mr. LAUSCHE. The amendment which the Senator from Iowa has offered contemplates an avoidance of that purpose and effort?

Mr. HICKENLOOPER. Not exactly. We recognize the sovereignty of a sovereign nation to do almost anything it desires to do within its own boundaries. We reserve the right of sovereignty here.

What we would say is that if the Government seizes American property which is lawfully there under an agreement without full compensation for the damages and the loss caused and for the property they have seized, we reserve the right to determine what we will do with our aid money. We would withdraw our aid money. We would not attempt to superimpose our ideas of sovereignty upon Argentina or upon any other country, but we would reserve the right to say what we will do with the money of the taxpayers of our country. We would withdraw aid from them and give them no more aid, if they proposed to play that kind of game.

Mr. LAUSCHE. Mr. President, will the Senator yield further?

Mr. HICKENLOOPER. I yield.

Mr. LAUSCHE. I should like to conclude my participation in the present discussion. Several months ago I read in an article that one could travel 60 kilometers in Argentina for the amount of pesos which would be equal to 2¾ cents of American money. I could not believe the statement. I had an investigation made. The report was that in Argentina, for the equivalent of 2¾ cents, one could travel 60 kilometers on the governmentally operated transportation system.

Mr. HICKENLOOPER. Thirty-six miles.

Mr. LAUSCHE. That is the charge. The amount was not adequate to liquidate the costs. For that reason, the Argentine Government is in the distressing position in which it now finds itself. That is why practically all the socialistically operated countries are likewise attempting to meet such conditions as I have described.

Mr. HICKENLOOPER. The example stated by the Senator from Ohio could be applied to quite a number of countries. I have in mind one particular small Latin American country in which the Government owns the telephone system. Theoretically, one could talk from one side of the country clear across to the other side for the equivalent of about 22 cents. Why? Because the Government owns the system and the Government is afraid of political reprisals at the polls if the rates are raised to the point at which the system would be at least halfway self-supporting. They pour more money into the operation and thus subsidize it heavily. The net result is that unless the average person pays a handsome sum for a telephone, he cannot get a telephone without a 6- or 7-year wait. He might not get through on the long-distance telephone lines anyway, but if he could, the cost would be about 22 cents. That is the rate for a call clear across the country. Political pressure will not permit them to charge a realistic and practical rate to pay the necessary costs and provide a decent or proper telephone service.

Mr. LAUSCHE. I commend the Senator for his contribution.

Mr. HICKENLOOPER. Mr. President, I had not intended to take this long this evening, but I believe a great many points have been cleared up.

I should now like to read a letter which came into my office last Saturday. I have given it my attention last night and this morning. It is a letter from a man who is quite conversant with Latin America. I do not know him personally, but I have talked with him on the telephone. His name is Eric N. Baklanoff, director of the Graduate Center for South American Studies, at Vanderbilt University in Nashville, Tenn.

I believe this letter is quite pertinent and makes some very telling points. Mr. Baklanoff has specialized in Latin America, its development and its economics. I have permission to use his letter.

The letter is dated November 6, 1963:

"DEAR SENATOR HICKENLOOPER: I should like to commend you on the provisions which you have attached to the foreign aid bill to safeguard the legitimate interests of U.S. citizens and corporations abroad.

"In respect to the current investment climate in Latin America, U.S. investors have been disengaging themselves from the area for good reasons. Brazil has expropriated $145 million of U.S.-owned utilities without compensation and nationalist politicians there are casting hungry eyes upon the largely Canadian owned $600 million Brazilian Traction Co. The recently enacted profits remittance law penalizes the reinvestment of profits by foreign companies in that country and in the current year the flow of private foreign capital to Brazil is a tiny fraction of the high levels sustained in the period 1956–61. Creeping expropriation of foreign-owned utility companies has been commonplace throughout Latin America as utility rates were frozen by official decree during the course of inflationary rises in money costs and prices. The consequence, of course, has been a squeeze on profits, failure of new investment in this key sector, and poor service. Government-induced shortages and inadequate service then becomes the 'grounds' for nationalizing the foreign firms to put an end, once and for all, to their allegedly 'exploitative' and 'abusive' practices.

"In Venezuela and Peru Castro-Communists have with impunity sabotaged U.S. property valued in the millions. In Chile, the U.S. copper companies have been paying taxes to the Chilean National Government equal to 85 percent of net profits"—

As I said a while ago, I believe the latest figure is 87 percent of the net profits. That is my best information—

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"and expropriation of their holdings is a credible possibility after the next presidential election in that country. Meanwhile, the new Argentine administration is moving to unilaterally break its contracts with the foreign oil companies to the disadvantage of the latter although it is recognized that these companies, by making Argentina self-sufficient in petroleum, have saved that country roughly $300 million annually in foreign exchange resources.

"The suggestion, increasingly advanced in our country, that the U.S. Government should insure private firms against expropriation by Latin American governments is not a satisfactory answer. The reason for this is elementary: public funds committed by us to the Alliance for Progress would increasingly be used to bail out private American companies rather than for the social and economic development of Latin American countries.

"In the absence of totalitarian police state rule in Latin America, which would extract capital from workers and peasants as well as provide the requisite industrial discipline, it becomes necessary, if economic development is desired, to rely heavily on a structure of incentives among which the monetary factor is necessarily important. If our premise is correct, then it would appear that the proper procedure for our Government would be to do everything in its power to remove as many of the political uncertainties which currently face private investors south of the Rio Grande.

"One answer, I believe, is power politics—less at home and more abroad: penalize unacceptable behavior, reward that which is acceptable to us; differentiate between trusted allies and uncommitted opportunist states to the benefit of the former. For example, if country B in Latin America threatens to 'go Communist' because of a short-fall in U.S. public assistance, let's put that threat to the test.

"In short, we are a great power (some like to call us the Colossus of the North) among nations. For a change, let's act like one.

"Sincerely,

"ERIC N. BAKLANOFF, *Director*."

In closing, let me point out that we have discussed Argentina today at great length, but the same principle applies to Chile, Peru, or any other country in Latin America. It applied to Honduras, when that country threatened to expropriate American property several months ago. It would apply to any Latin American country which attempted to expropriate and seize the property of Americans, legitimately invested in those countries with the prior approval and agreement of those countries. So, I do not wish it to be understood this evening that we are talking about only Argentina. We are also talking about a possible wave of expropriation and seizure which might sweep across the Latin American continent because it may be "easy money" to seize the property of the "Yankees to the north."

It also would apply to any other country in the world.

It already has applied to Ceylon, and it will apply to any other country in the world that wishes to get something for nothing from "Uncle Bountiful," who has been quite generous during the past 15 to 20 years in his largess. The countries which really need our aid should take advantage of the opportunity to stabilize themselves, to advance themselves, to live with the family of nations, a status to which they aspire and which we hope they will attain.

Mr. FULBRIGHT. Mr. President, will the Senator yield?

Mr. HICKENLOOPER. I yield.

Mr. FULBRIGHT. The Senator from Iowa has taken the lead in the committee in the introduction and perfection of what is commonly called the Hickenlooper amendment, which I believe, and I am sure the committee believes, would apply to situations such as he has described in Argentina and in other countries.

I think that in fostering this amendment he has rendered a great service and that it is a great improvement in the bill.

I do not believe there is any doubt that the amendment applies to the situation in Argentina. If the officials of that country have any respect for or hope in the Alliance for Progress, they will find a way to comply with the provisions of the amendment. In other words, if they insist on expropriation, they will find themselves in a process of decompensation, as provided for by the amendment.

Mr. HICKENLOOPER. I thank the Senator from Arkansas, the very able chairman of the Foreign Relations Committee, who has been helpful in obtaining an objective study of this matter in the committee, and who has contributed valuable suggestions as to how to best approach a difficult situation.

It is not my feeling, and I think it is not that of members of the committee, to impose conditions or situations which are so oppressive that they will not work.

We want, in fairness, equity, and decency, to assist other countries to establish themselves on a basis of stability and progress. That is what we are searching for. But I am sure most of us are of the opinion that for them to continue along the lines which they have been following will lead to nothing but economic chaos and destruction—from which we hope we can lift them, if our aid counts for anything. If it does not, and they are not able to take advantage of the bounty which American taxpayers are supplying them, we had better pull out and see what will happen.

I hope we can work out with those countries a basis of equity, fairness, decency, and appropriate concepts of property and moral rights, such as their own citizens have, and that we can make progress. I rely upon the State Department to be cooperative in using its vigor, authority, and great influence in accomplishing this objective.

That concludes my remarks, Mr. President. I appreciate the patience of Senators in listening to my remarks, but I believe this is a record which we have made for a firm understanding by countries of the world that there is an end to our gullibility or our unrequited bounty, and that while we are, I am sure, willing to go far in our assistance to other countries, there is a limit beyond which we will not go. Other countries had better understand this quickly, not only for their own general progress, but for the good of the common goal of the advancement of human liberty and economic development.

PRIVATE INVESTMENT IN LATIN AMERICA

WEDNESDAY, JANUARY 15, 1964

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON INTER-AMERICAN ECONOMIC
RELATIONSHIPS OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The subcommittee met, pursuant to recess, at 10 a.m., in room 1202, New Senate Office Building, Hon. John Sparkman presiding.

Present: Senators Sparkman, Javits, and Jordan, and Representatives Griffiths and Curtis.

Also present: William H. Moore, economist; Hamilton D. Gewehr, administrative clerk; and Donald A. Webster, minority economist.

Senator SPARKMAN. Let the committee come to order, please.

May I say that the hearings today are really a continuation of the hearings on yesterday. The first part, particularly, is a continuation of our discussions of yesterday. After that, we have two other witnesses who will deal specifically with programs for Government guarantee programs of private investments.

I want to call upon the Senator from New York, Senator Javits, to present our first witness today since I know that he has something to say about him and the program which he represents.

Senator JAVITS. Mr. Chairman, thank you very much.

Mr. Chairman, this is a particularly felicitous moment for me, as I have the honor to introduce to the committee the witness for today, Dr. Aurelio Peccei, the executive director of Italconsult, which is a very important firm, with heavy emphasis on Latin America, operating in an economic and consulting capacity in Rome and having very important affiliations with the Fiat Co. in that country.

Mr. Chairman, I would respectfully request that Mr. Warren Wilhelm, foreign manager, economic department, Texaco, may be brought forward to set with Dr. Peccei and identify himself for the record.

Senator SPARKMAN. Mr. Wilhelm, will you come forward and be part of the panel?

Senator JAVITS. Thank you, Mr. Chairman.

Mr. Chairman, the Atlantic Community Development Group for Latin America—ADELA—project had been initiated by me within the Economic Committee of the NATO Parliamentarians' Conference in November 1962 to see what could be done about bringing private enterprise in Western Europe and in other developed Western nations into closer collaboration with United States and Latin American private enterprise in the economic development of Latin America. Through a working party of the NATO Parliamentarians' Conference, of which I am Chairman, and through private efforts, ADELA was established in April 1963 with three executive directors

loaned by their respective companies, without cost to ADELA, to develop a private enterprise investment company for the foregoing purpose. Dr. Aurelio Peccei—Fiat, Italconsult—is executive director for Europe, Dr. Julio Gonzalez del Solar—Inter-American Development Bank—is executive director for Latin America, and Mr. Warren Wilhelm—Texaco—is executive director for the United States, and Mr. Herbert J. Blitz is executive secretary.

Throughout this whole organizing phase, I had the most able cooperation of Senator Hubert Humphrey, of Minnesota, who gave ADELA invaluable support; and the leadership in the private sector of Emilio Collado, vice president and director of Standard Oil Co. of New Jersey and George Moore, president of the First National City Bank of New York.

On January 10 and 11, ADELA moved into its second phase as a result of the Paris Conference, which I attended along with about 100 leaders of both the public and private sectors from the United States, Europe, and Latin America; including Prof. Thorkil Kristensen, Secretary General of the OECD, Willard Thorpe, Chairman of the DAC; Jose Mora, Secretary General of the OAS; and Felipe Herrera, President of the Inter-American Development Bank.

As a result of 2 days of deliberations a new instrument has been devised, which is expected to be called the ADELA Investment Co. The go-ahead decision was taken by a group of leading corporations and banks from the United States, Japan, Italy, Switzerland, and Belguim which have pledged equity capital participation, the time of their personnel, and their technical know-how. About $6 million of the $40 million in equity capital to be sought from non-Latin American sources has now been firmly pledged by major corporations from these countries and an interim organizing committee of eight, composed of four corporations from the United States, three from Europe and one from Japan, charged with establishing the ADELA Investment Co., has been formed of which the United States and European cochairmen are Emilo Collado, vice president and director of Standard Oil Co. of New Jersey and Gianni Agnelli, vice chairman of the board of Fiat, Italy.

This interim organizing committee will now proceed to draw up the ADELA Investment Co.'s corporate charter and seek to broaden its capital base, especially through added support from West Germany, Great Britain, and Sweden. A total impact of $200 million is envisaged on Latin American development from ADELA, based on its own equity capital, equity capital from Latin America, and loans, principally from the Inter-American Development Bank—IADB. While the IADB is prohibited by its charter to enter into equity investments, an arrangement is visualized wherein the operations of the two organizations will, in suitable projects, be closely coordinated.

To assure the continued interest of governments and international agencies in the ADELA Investment Co., there would also be established shortly a consultative committee composed of personalities concerned with the operations of germane international organizations.

Now, Mr. Chairman, this is an extremely auspicious opportunity for the private enterprise system to demonstrate what it can do, both for itself in terms of Latin America, and in a private enterprise way.

The companies to be enlisted in ADELA have hundreds of millions of dollars in Latin American investments and are capable of hundreds

of millions more. It will be noted, Mr. Chairman, that one of the big problems of the Alliance for Progress is the fact that private investment on a net basis is practically dried up. If it were restored, it could represent, in my judgment, the difference between success and failure for the Alliance.

Now Mr. Chairman, I emphasize those points because, knowing the chairman's views on the private enterprise system and how helpful it can be, and they are also the views of my colleague, Senator Jordan and friends in the House of Representatives, I believe they will find this development of the subject most interesting. To my mind, if it can work out, and I believe it has an excellent chance, it is a historic breakthrough by the private enterprise system in assuming the responsibility it should carry for the development of newly developing countries, in this case with a concentration on Latin America.

Thank you, Mr. Chairman.

Senator SPARKMAN. Thank you, Senator Javits. Let me say that I was intrigued by the idea and very much interested in it. I hope it may prove to be highly successful.

Now, Dr. Peccei—do you have a paper?

Mr. PECCEI. Yes, sir.

Senator SPARKMAN. You may present it as you see fit. Read it, summarize it, or discuss it. In any event, it will be printed in full in the record. We are glad to have you with us.

STATEMENT OF AURELIO PECCEI, EXECUTIVE DIRECTOR FOR WESTERN EUROPE, ADELA, AND WARREN WILHELM, EXECUTIVE DIRECTOR FOR UNITED STATES, ADELA

Mr. PECCEI. Thank you, Mr. Chairman.

Mr. Chairman, gentlemen, (1) it is a compliment to the wisdom of this committee that it is attaching major importance to the question of investment in Latin America, a question of critical significance for Latin America, for Europe and for the United States—and I am honored to be asked to deal with how the flow of investments originating in Europe can be improved.

No mission is offered to our generation which is as important as to bring Latin America into the rhythm of economic and social progress which is now being enjoyed by the United States and Western Europe. We all know that, if productive activities in Latin America are not reinvigorated and reinforced, the tendency in that continent will be unfavorable not only in what concerns private activity, but equally in the area's overall growth and political equilibrium.

In the course of my remarks today I want to describe to you the effort which we of the ADELA group have launched to deal with this problem, and I will also make other general comments.

As many among you know, the Atlantic Community Development Group for Latin America (called ADELA for short) was formed in April 1963, with the leadership of Senator Jacob Javits, as the result of resolutions adopted in November 1962, at the Conference of NATO Parliamentarians. The ADELA group, with which Senator Hubert Humphrey soon became associated and to which he has given invaluable support, has concerned itself primarily with the formation of a new initiative to accelerate the injection of European, as well as United

States and Japanese private capital into Latin America in partnership with local capital.

On Friday and Saturday of last week the undertaking was moved into a new and more concrete phase as a result of the ADELA meeting in Paris, which was attended by approximately 100 leaders of both the public and private sectors from North America, Japan, Europe, and Latin America.

(2) Before considering the ADELA undertaking in more detail, we should look at the Latin American problem in broad terms.

Today, much more than in previous centuries inequality is resented, and breeds unrest among nations no less than within nations. In this regard, a very high priority both in timing and in effort has to be given to Latin America as here the trend is the reverse of what it should be.

The growth rate has dropped since the late fifties. Increase of per capita income is losing momentum, and in 1962 came to a standstill.

This economic slowdown, right in a period when Latin America is in the political forefront as perhaps the main world area of major immediate concern, is the product of many complex factors. One of these is the decline of direct investment from the outside.

The latest data from the Economic Commission for Latin America (ECLA) reports indicate that, at the end of the last decade, direct investment from the outside, for the whole of Latin America, averaged $540 million per year; including reinvestments, and that in 1961 this figure had dropped to $350 million. In the same period the flow of long-term loans—mainly governmental—went up from $320 million per year to $950 million, which shows a great deterioration of the investment to indebtedness ratio, and a growing reliance upon the public sector.

As to the matter under review, namely investments, the European portion of the total for the whole of Latin America in recent years is estimated at 22 percent; i.e., less than $80 million per year.

(3) It is a critical matter that Europe has, to so large an extent, turned away from Latin America.

There are Europeans who understand clearly the urgent need for Europe to play an active and forward role in Latin America. Unfortunately, they are in the minority. One finds very broadly in Europe a feeling not only that the trend is very adverse in Latin America, but also that Europe can afford to stand aside from the entire problem.

We have in this respect to consider that European countries, in most cases, have historical ties with other parts of the world, that is, former dependent or associated territories.

No wonder, therefore, that the majority of European governments have not yet taken clear and effective decisions to play an important role in the rescue of Latin America from its present difficulties; and that the key people and staff of the leading industries and banks in Europe are much less informed about Latin America than their counterparts in the United States. And, as the texture of mistrust is generally interwoven with misinformation, a widespread lack of confidence in Latin America is the consequence.

My colleagues and I, in discussing the ADELA undertaking in Europe, have encountered many fine leaders who understand fully that the problem of the underdeveloped areas may well determine the whole

future of the free world, and it is the response of these leaders that has made the ADELA undertaking possible.

Yet one must also be clear that in Europe one still finds many inward-looking members of the business community who believe that the world stands still, and that it is foreign to their functions to step out of the well-guarded walls of their own companies, and take part in facing the problems which are daily surging from the third world which surrounds us.

(4) All in all it is high time for a full range of activities and measures to be started in Europe with the aim of obtaining greater participation by its capital and entrepreneurship in Latin American development. I should like to express here in all modesty some thoughts on certain points which seem to me relevant in the search for new ways to achieve this end.

At the very outset, we must realize that to be efficient any new approach should be consistent with Latin American receptivity, and therefore has to stem out of understanding and sympathy with what the Latin Americans themselves are doing or can do.

Today more "active" societies living in a far wider range of development levels exist than at any other time in history. In the years to come the tremendous technological progress, demographic explosion, and the revolution of rising expectations will widen the gaps and accentuate the differences among these societies: One of our greatest tasks is to avoid this world of ours being split into incompatible fragments.

To achieve this as to Latin America, we must make a gigantic effort over a very short period of time, perhaps within this so-called development decade, and the effort must start with understanding.

Accordingly, in the first place Europe must be supplied not only with factual information on Latin American economics, but also with good interpretation of the undercurrents and present evolutionary trends of the Latin American society.

The task of organizing this steady flow of objective Latin American information is both urgent and difficult, but by no means impossible, provided it would be taken up with an adequate budget by the inter-American agencies, and under the expert management available in this country.

European businessmen will then be in a much better position to judge not only the drawbacks, but also the prospects and advantages of their enterprise in a continent which—if we do not act foolishly—is bound to overcome the present difficulties and expand within the Western World.

Secondly, European governments must be called upon to accord to Latin America the priority which that continent will actually have in the history of events of the free world in the next decade or two. How this change of policy can be obtained is a question having some delicate aspects, which I could not surely be expected to touch upon.

It seems clear, however, that the United States, which is now going through a period of drastic soul searching on the best ways to lay down the lines of future assistance programs to Latin America, should include in its Latin American policies the European aspects and should very actively seek the cooperation of European countries.

The necessity for European governments, on their part, to define a more stable policy toward certain Latin American countries is obvi-

ous if we only think of the haphazard and ineffective functioning of the Paris Club—the main European coordinating instrument—which has been so far used mainly for last minute interventions to prevent the financial collapse of these countries.

Unlike this erratic procedure, thought should now be given in Europe to the necessity of a thorough review by Europe and the United States of the financial situation of the major debtors of the Continent and of their capacity to repay and service their foreign indebtment, with a view to rescheduling their debts over long enough periods, and with some grace spells, so that the new refund schedule would not impair their own capacity to invest in development.

Thirdly, an aspect of the political decision requested from the European governments, concerning the drawing up and implementation of an economic and financial policy toward that Continent, specifically concerns the Inter-American Development Bank, which Europe should get to know more about and consider as the multilateral regional institution for Latin America.

The IADB is offering several operating possibilities by means of which European private and public funds could be channeled to Latin America, and as a multilateral official institution it offers also an element of guarantee and protection to the funds it seeks.

The techniques offered to assure this flow of European finance are very flexible, but the results have been somewhat slow to come in. The IADB has offered (*a*) bond sales, of which only one issue has so far been placed, in Italy, for about $25 million at 20 years; (*b*) placement with IADB of funds in trust; (*c*) placement with European banks of participations in its loans to Latin America; (*d*) parallel direct loans by IADB and European financial institutions; (*e*) reception by IADB of funds in administration, which has been the case so far respecting operations with German and Dutch banks.

This rather small performance by Europe in support of IADB operations is why I think that access by the IADB to European sources of financial capital should be facilitated by all possible means. Among other measures, European countries should accord to IADB bonds priority, tax exemption and eligibility privileges similar to those accorded to the World Bank bonds. Efforts should also be continued toward the promotion of a European fund similar to the social progress trust fund and likewise placed under the administration of IADB, perhaps in cooperation with the European Investment Bank.

(5) To sum up, I want to emphasize very strongly that here there is more than a question of Europe sharing the U.S. burden.

The traditional relations between industrialized countries and underdeveloped countries have changed. These relations now must be internationalized, and Europe must set up for herself a full range of policies to take part in the process.

That brings me to tell you more in detail about the nature and scope of the ADELA undertaking and its present status.

With the wise guidance of Senators Javits and Humphrey, we believe that a rather important breakthrough has been accomplished in less than 1 year. A new instrument has been devised—to be called the ADELA Investment Co.—which will contribute significantly and in the near term toward some of the fundamental objectives which I have outlined. It has been an exciting task, during which

I have greatly benefited by the stimulating collaboration with my colleagues, and especially the forward-looking economist and citizen, my good friend, Warren Wilhelm, our U.S. Executive Director.

(6) The ADELA Investment Co.'s objectives are to mobilize a multinational private effort to assist the Latin American private sector through investment over and above that which is already moving to Latin America.

The company will be financed by equity capital commitments from leading private corporations of the United States and Europe, in about equal amounts, and Canada and Japan. The total capitalization objective is about $40 million. When there are added to this sum the Latin American capital that will be activated through partnership arrangements, and borrowings that will be justified by the equity capital, a total impact of $200 million is envisaged.

These funds will be pumped as risk capital into moderate-sized industrial and possibly agricultural projects involving new or expanded productive activities.

The implementation of the ADELA program will represent a unique experiment and can be a turning point in the economic development of Latin America.

Its immediate result will be a powerful boost to the private sector of the countries where this new type of capital will be injected. In the course of a few years it may also transform these countries into growth points for neighboring areas.

The broader results can be of even greater importance.

As the national and integration planning movements mature, availability of ADELA capital will prevent vacuums from being created if indigenous capital does not take up the development projects or sectors identified for private activity, and will avoid these vacuums being filled by the public sector. ADELA will be instrumental in influencing favorably the investment climate as, thanks to its unique multinational backing and links with inter-American agencies, it will be able to speak with considerable effect in persuading Latin American Governments of the conditions essential for a vigorous and expanding private sector. ADELA will be able to help develop new entrepreneurial ventures which would otherwise not be born, and it will catalyze technical and consulting activities of a similar multinational origin.

And, finally, ADELA will bring Europe close to Latin America. The plan is to have the company established and headquartered in Europe, and the management possibly headed by a European. The number and quality of European leaders already committed, and those who will follow, will constitute the most powerful pressure and action group so far engaged to stimulate European interest toward Latin America.

ADELA will of course work in close cooperation with other groups and agencies dedicated to Latin America.

The extent of the service it can render to improve the flow of Western European investment to Latin America, and to promote new coordinated policies, both in and outside Europe, is invaluable at this crucial moment for Latin America, and occurs at the precise instant when a major reorganization and reassessment of policies within the Alliance for Progress are taking place.

At the Paris meeting, the "go ahead" decision was taken by a number of leading corporations from both sides of the Atlantic and from

Japan, which have pledged equity capital participation, time of their personnel and know-how assistance. Because of the support forthcoming from these great companies, the undertaking has now moved to a more advanced stage, with the formation of a committee charged with organizing the operating company. This committee, with European, American, and Japanese members, is cochaired by Mr. Gianni Agnelli, vice chairman of Fiat, and Mr. Emilio Collado, vice president and director of the Standard Oil Company of New Jersey.

The ADELA undertaking deserves, now, the full support of the Northern Hemisphere private sector, and the strong endorsement of official agencies and administrations, in order to proceed with maximum strength.

I am confident you will give your support. It would surely be the finest reward for Senator Javits and others who originated the plan, and for those of the private business sector who have accepted the responsibility for its implementation.

Thank you very much.

Senator SPARKMAN. Thank you very much.

Mr. Wilhelm, do you have anything to add?

Mr. WILHELM. No, Mr. Chairman, I think the statement was excellently presented and stated the case very well.

Senator SPARKMAN. Let me clarify my own understanding of one point. This organization is to be capitalized at $40 million. Combining this with the money that may be expected from Latin American countries, through formation of partnerships and associations and so forth, you envisage a program of $200 million. Is that initial program expected to be replenished over the years?

Mr. PECCEI. If I may answer the question, that is the initial stage of the undertaking. The $200 million pumped into medium-sized ventures is already a rather important amount but it will not be the limit of the capital injection that ADELA seeks to introduce into Latin America; first, because some of these ventures, once well started, may permit a return of the capital as the ADELA equity share may later be sold to local capitalists replenishing the ADELA capital for starting additional ventures.

Secondly, there are many international funds available for private sector development which are not now being used and they may be channeled through ADELA for their actual implementation of private enterprises in Latin America.

Thirdly, there is a rather big mass of flight capital from Latin America which now sits in Swiss banks or in this country which will be prompted to come back through ADELA. So I think that the $200 million financial capital to go into ventures in Latin America will be the first stage which will be reached, anyhow, in 3 or 4 years, but there will be much more capital which will move into Latin America as the result of ADELA.

Senator SPARKMAN. Has the organization been set up already—that is to say, is ADELA actually already in existence?

Mr. WILHELM. The company has not been incorporated, but we feel that whereas, until the Paris meeting, the entire matter was in the hands of a very small group of people actively working on it, it has now passed to another and more concrete phase with the formation of the organizing committee, cochaired by two very important industrial

leaders and with the membership of that committee comprising very important companies in the world who will now give leadership and time to carrying forward to completion the idea of the ADELA company.

Senator SPARKMAN. Mrs. Griffiths?

Representative GRIFFITHS. I would like to ask you, exactly what kind of projects are you going to invest in?

Mr. PECCEI. We have in mind on this one moderate sized industrial projects. A quantity of new ventures need to be launched in Latin America to cope with local demands and demands projected by the integration movement in Latin America. Manufacturing industries, processing of agricultural products produced in the countries, supplies of existing big industries, plus fabrication of steel produced by big plants. A wide area of industrial, and we think some agricultural, products deserve attention.

Representative GRIFFITHS. Are you going to supply some of the management out of Europe or out of the United States for operating these plants, or are you going to train the people there?

Mr. PECCEI. I think that management is a crucial ingredient of success of each project. So management has to be provided in one way or the other.

The talents, the large talent potential available in Latin America which has not been developed, just because there is not the occasion—there is a quantity of trained Latin Americans coming out of Latin America and working in this country, the United States, who will go back into Latin America and may be the trainers, the new leaders, the new managers for these ventures. But in any case, we must face the problem that management in the initial stage should in many cases be provided from the United States, Europe, or Japan.

Representative GRIFFITHS. I observed, when this committee was last there, that for instance, in the matter of women's purses, for which there would be a wide market, a purse, an alligator purse sold for $50. A comparable purse in the United States would be $300. But the purse was so poorly made, it had no style, it was not really a usable purse. They needed artists, they needed craftsmen.

I observed also in Uruguay, they had a fur. I think it was mouton. It was the best there is in the world, but they couldn't cut it. So that again, they needed people who knew how to take care of this. Now, where are these people going to come from?

Mr. PECCEI. Both from outside and from Latin America—there is a wealth of human resources there which are not developed. If I may comment on your remark, in many Latin American countries, the finishing, the presentation, the achievement of products has changed very much in the last 10 years in the São Paulo area, in Buenos Aires, in Chile, in Mexico. There has been a large change, notwithstanding the slow development rate. So in purses, other objects you mentioned, they are made much better in their own localities now.

Representative GRIFFITHS. I think the big problem an industrial plant, an automaker, for instance, has in Latin America, is that you have not a wide enough spread market. There are not enough people with enough money to buy the product and there are not enough people who are trained to run a plant. So that I think capital is going to be one of the rather smaller problems in a way.

Mr. WILHELM. The answer to one of your questions is summed up by a remark Dr. Peccei made once; in order to have a rocket you need an astronaut and in order to have an astronaut, you need a rocket. We are very much caught in that circle in the matter of development of modern industry in Latin America. Certainly, there are many potential skills that are not being utilized because of the very slow rate of growth and development. In turn, in other places, of course, the lack of skill is holding back development.

But by establishing here a channel, a framework which relates the enormous resources of the Northern Hemisphere private sector to Latin America in this field of moderate-sized industry, we think that a mechanism is provided which will enable many of these problems to be approached in an intelligent way.

Representative GRIFFITHS. I would say the Latin American trade group is extremely helpful to us, I think, in reducing their tariffs.

What are you going to do about confiscation? How are you going to protect yourselves against confiscation?

Mr. PECCEI. First of all, we think that our philosophy, our way of acting, will land us in areas which are not subject to confiscation and not in some other areas which have attracted European or U.S. capital in the past. We are heading toward medium-sized industries, manufacturing industries for local consumption; not public utilities, not very large projects. We think that the best use for our capital and the best service to Latin America will be to try to manufacture, to produce what is considered within their development plans the foremost necessity, the best priority, either for foreign exchange saving or foreign exchange earning possibilities of the project, or for local consumption.

So we think that there is in-built in the industries that we have in mind a much greater safeguard than what generally is considered from the United States and in Europe an investment in Latin America.

Representative GRIFFITHS. Thank you. I think it is a great idea and I hope you are successful.

Senator SPARKMAN. Mr. Curtis?

Representative CURTIS. I will yield to Senator Javits.

Senator SPARKMAN. Senator Javits.

Senator JAVITS. Mr. Chairman, first let me emphasize that the testimony of these witnesses is as highly rated experts in this field.

I find it very difficult, because of my relationship to this project, not to answer some of Mrs. Griffiths' questions. So I would like to, if I may, state for the record several points:

The very largest and most important companies on both sides of the Atlantic—aside from bringing Europe into Latin American development, which is, to my mind, the paramount question—represent tremendous technical resources.

They command great sources of capital, which can be brought in if they have an interest, such as they may very well get through ADELA. Each of these companies is capable of investing 10 or 20 times or more the amount of capital in every one of these Latin American countries than their actual investment in ADELA. They also have literally thousands of technical and managerial people.

ADELA would give them a channel through which to go into partnership with Latin American entrepreneurs. That is the point about attracting back flight capital. Indeed, the very basis of the company's

operations would be joint ventures with Latin America. The training of Latin American personnel would come directly from the availability of trained personnel by the major companies on both sides of the Atlantic and from Japan which have an interest in the ADELA Investment Co.

So it has tremendous opportunities.

Now, as to confiscation. Mrs. Griffiths wasn't here, perhaps, when I spoke. I have just come back from the ADELA Conference in Europe and the main question asked by European banks and industrialists was: "What about confiscation or currency difficulties in Latin America?" Now, I am going to ask the witness in a minute a question about that. The answer is one given by the witnesses, which is that the type of enterprise that this company would tackle, the type of enterprise that needs to be tackled, has traditionally not been the subject of confiscation unless a country went Communist. Then, of course, everything is confiscated, but that is the very thing we are trying to fight against here.

But short of that, most often, there is no expropriation in these particular lines.

Secondly, I deeply believe that there is room for government guarantees on both sides—that is, by the host country and by the country of which the corporate investor in ADELA is a national.

Third, it is not expected that this company will operate in every Latin American country, but only those that are most congenial to this type of operation. Hence, the risks of expropriation become lessened.

Now, there is always a risk of expropriation, but there is for any investment, even in the United States. Government sovereignty is, of course, complete in terms of expropriation, provided it is with fair compensation, as it would always be in this country. Those are the answers, incidentally, that I made to the Europeans in this respect. Now, I would like to ask the witnesses, if I may, Mrs. Griffiths, this question:

What relationship do you gentlemen believe that the governments should have—that is, the governments both of the host countries for these investments and the governments national to those who are the investors in ADELA? What relation to ADELA Investment Co. do you believe that both sets of governments should have?

Mr. WILHELM. I will try to answer that, Senator.

I think that the device of pooling a great deal of capital—I should say a substantial sum of capital from a great many countries—into a pool which will then be commingled and used in the different Latin American countries, probably does not fit very well with the established devices for capital-exporting countries guaranteeing the programs. That has not been fully explored.

I think that the most important way of achieving the result, which is that these investments will be in a secure position and that the undertaking as a whole will have a beneficial effect on the investment climate in Latin America, will be inherent in the nature of the undertaking; that is, it will have behind it the whole of the capital-exporting sector of the free-world industrialized countries. By selecting for investment countries where an attractive climate is offered as primary areas of operation, and by being also in a position to say that if this piece of legislation which is in the hopper in a Latin

American legislature is passed this will very seriously impair the possibilities of investment in that country, we believe a very strong position can be developed. Not only can there be persuasion on the local level, but also follow through by action in backing up what one says.

Also, there will be contacts with inter-American agencies, which are an extremely important channel of communication to Latin American countries. It is crucial in this sector, where the problems are in the mind as well as in the legal books. We think a very important contribution can be made toward developing a more stable climate.

Senator JAVITS. It is also contemplated, is it not, that this company could make agreements with Latin American countries, both with relation to specific investments and in respect to the general manner of its operation, with respect to nondiscrimination and other considerations regarding its investment in that country; is that correct?

Mr. PECCEI. This is so. I think that some kind of arrangement with the host country could be made. I would favor arrangements which could cover a sector of an industry which is of paramount importance for that country and into which ADELA, as well as other investors, both foreign and domestic, may operate.

Senator JAVITS. Do you believe it is more likely that we can get Europe tied into Latin American development through private enterprise than we could through the European governments doing what the United States is doing in public aid? In other words, is a private enterprise movement from Europe with respect to Latin America more likely of achievement in your researches, and you have been all over Europe, both of you, than there is the likelihood of the governments moving in with their own Alliance for Progress?

Mr. PECCEI. Indeed, it is much more advisable and likely that private capital will go this way than the European governments could make up their mind and come in in a political way, in the fashion of the Alliance for Progress.

Senator JAVITS. Have you found in a general way that the European governments like this idea?

Mr. PECCEI. We have found in European governments very warm support for this kind of project. I should say that many officials in governments are in this even more advanced than private sectors themselves, in seeing the need for private action because they see the impossibility of their governments to act quickly in the way that is necessary and feel they have to trust in the private sectors to come forward and do the job while it can be done in the best way.

Senator JAVITS. Dr. Peccei, you have been widely through Latin America recently on this very project; haven't you?

Mr. PECCEI. Yes, sir.

Senator JAVITS. Can you give us some estimate of how much of the economy of Latin America is still in the hands of private enterprise, in percentages?

Mr. PECCEI. I think that GNP-wise, we have more than two-thirds and probably even more than three-fourths of the total production produced by the private enterprise.

Senator JAVITS. In Latin America?

Mr. PECCEI. In Latin America.

Senator JAVITS. This is a marked difference, is it not, from Africa, the Middle East, and Asia?

Mr. PECCEI. Of course; there is no comparison between Latin America and the Middle East, and Asia, and Africa in many aspects. This is one of them. I think that in Latin America, with a certain amount of initiative, with a certain push now, we may go over the hump rather easily and have the private enterprise perform very well.

Senator JAVITS. Will you agree with me, Dr. Peccei and Mr. Wilhelm, that the decisive breakthrough in saving Latin America from going the Communist way is perhaps more dependent on what the private enterprise system will be able to accomplish in the next 10 years than anything else?

Mr. PECCEI. Indeed, sir. That is crucial. We have this, say, 10 years and in this 10 years, we may determine the outlook by going in or by withdrawing from private activity in Latin America.

Senator JAVITS. Finally, is it the intention of the ADELA company to be, for all practical purposes, the private enterprise presence in Latin America?

Mr. WILHELM. I think, Senator, that potentially; yes. I believe we would be saying too much to say within the first year or two, it would be that. But I believe if the ADELA movement very strongly succeeds, then there will be a movement for finding new funds for it and if it succeeds, that will be very easy. It can, without using words too strongly, become a very important presence in Latin America.

Senator JAVITS. The Inter-American Development Bank has no investment affiliate like the World Bank, has it?

Mr. PECCEI. No.

Senator JAVITS. Will you describe for us what is expected to be the relationship between the Inter-American Development Bank and the ADELA Investment Co.?

Mr. PECCEI. The Inter-American Development Bank by charter cannot enter into equity investment. It can do practically any other kind of financial operation, but not equity: that is, it can extend loans, underwrite, guarantee, and there is a clear necessity for a regional development financial institution such as the Inter-American Development Bank to have a kind of affiliate, an instrument, in order to deal with the need for equity capital. So we think that cooperation between the Inter-American Development Bank and ADELA will be ample and at various levels, would be an arrangement by which the policies of the Inter-American Development Bank and ADELA would be coordinated, because they are aimed at the same effect.

On the second level, the information and the wealth of knowledge about Latin America which resides in the Inter-American Development Bank should be put at the disposal of ADELA.

Third, we think at the operative level, there might be ample scope for housekeeping, interchange of personnel, and finally, a managerial cooperation for the enterprises in which both the Inter-American Bank and ADELA have interests.

I think ingenious people and people of good will will find many fields for cooperation between the two institutions.

Senator JAVITS. What is the difference between ADELA Investment Co. and a number of other investment companies which have started for Latin America such as the CREOLE Investment Corp., which is an offshoot of Standard Oil of New Jersey, International

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Basic Economy Corp., which is organized by the Rockefeller Bros., DELTEC Panamerica, which is another private enterprise company operating in Latin America? Will you give us the difference that you see between those companies and this one?

Mr. WILHELM. I will try to do that, Senator. It is a hard question, because each of those is different.

Senator JAVITS. Let's get a generic basis.

Mr. WILHELM. As compared with the CREOLE operation, there are fundamental similarities, the two fundamental differences being that the responsibility of ADELA is multinational and multilateral in nature, whereas CREOLE is one company and one country. ADELA can work in Latin America and use its power of maneuver in order to help bring about a favorable climate.

As compared with another range of institutions, the development banks, to a substantial extent they are banks rather than entrepreneurs and they deal mainly in loan capital rather than equity capital. We believe that ADELA will be able to play a greater role in creating activity, in putting together undertakings, although certainly very close cooperation with those institutions will be desirable.

Then when one considers an operation such as DELTEC, for example, one finds that its primary role has been an attempt to develop capital markets in Latin America, rather than having substantial capital of its own.

Senator JAVITS. Thank you.

Mr. Chairman, I ask unanimous consent to include as part of the testimony of the witnesses a memorandum describing the activities of the Atlantic Community Group for Development in Latin America, dated September 16, 1963; a second memorandum dated December 27, 1963, on the availability of investment opportunities; the record of attendance at the meetings just held in Paris at the headquarters of the OECD on January 10 and 11, and a brief statement as to the actions which took place at those meetings, all to fill out the testimony of those witnesses.

Representative GRIFFITHS. Mr. Chairman, may I ask a question? How much money has been raised?

Senator JAVITS. $6 million has been committed for, but the understanding, Mrs. Griffiths, is this: These are very high-level people and the organizing committee is not actually going to press the button to push this thing into motion unless it is satisfied that it has enough to go forward with. In this case, the nature of the appearance is more important even than money. A great point was made in Paris about the fact that it would be necessary to have an important participation from one or more companies from Germany, France, and Great Britain before this matter could really go forward.

Again I repeat, Mr. Chairman, it has been entirely work, by me, in the private sector. It is hard for people to understand why a Senator will work very hard in the private sector in order to accomplish something in the public sector. Part of my trip was to Germany, precisely for the purpose of enlisting the support that is needed.

So part of the answer is that this committee of eight very high level and important international business people will not actually push the button to start this thing unless they are satisfied that in terms of its auspices, it can really perform the mission which has been outlined before the committee today.

Senator SPARKMAN. Without objection, the several insertions will be made.

(The documents referred to follow:)

SEPTEMBER 16, 1963.

ATLANTIC COMMUNITY DEVELOPMENT GROUP FOR LATIN AMERICA (ADELA)

12 Rue de Castiglione, Paris I, France
110 East 45th Street, New York, N.Y.
1726 Massachusetts Avenue NW., Washington 36, D.C., U.S.A.

THE ADELA INVESTMENT COMPANY

The Atlantic Community Development Group for Latin America (ADELA) is the outgrowth of proposals approved by the NATO Parliamentarians last fall and sponsored by the chairman of their economic committee, U.S. Senator Jacob K. Javits. These proposals called for greater participation of Europe, and renewed over-all efforts, in regard to the economic development of Latin America.

The NATO Parliamentarians' resolution embodying these proposals recommended that the Secretary General of the Organization for Economic Cooperation and Development (OECD), the Secretary General of the Organization of American States (OAS), and the President of the Inter-American Development Bank (IADB) jointly lend support to the initative. These three organizations agreed that the undertaking should be carried out by a private group.

Through private efforts, the group was formed in April of 1963, consisting of three executive directors lent by their own organizations: Dr. Aurelio Peccei (Fiat, Italconsult) for Europe, Dr. Julio Gonzales del Solar (Inter-American Development Bank) for Latin America, and Mr. Warren Wilhelm (Texaco) for the United States. Mr. Herbert J. Blitz is executive secretary, working out of Washington, D.C., and Mr. Maurice Guernier heads the Paris office. The Ford Foundation and interested private business firms are financing the expenses of the present preparatory work. Senator Hubert H. Humphrey of Minnesota has joined in the effort with Senator Javits. ADELA has as advisers President Felipe Herrera of the IADB, Dr. Milton Katz of Harvard, and a number of outstanding private business leaders. Contact is maintained with the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC), as well as with the Business and Industry Advisory Committee of OECD (BIAC).

To assure liaison with the Economic Committee of NATO, a working party of parliamentarians, chaired by Senator Javits, was established. The approach adopted by the ADELA group, which this paper summarizes, received the approval of the parliamentarians in a meeting in Paris in July.

I. Objectives

Formation of ADELA reflects awareness that the present rate of economic growth of Latin America is inadequate, creating a situation dangerous to the free world. It is a matter of urgency to find means for pumping additional energy and economic dynamism into Latin America. If the present political-economic system of Latin America—substantially democratic and based primarily upon private activity— fails to deliver in Latin America, this type of system will be considered to have a poor prognosis in the other developing areas, most of which are far behind Latin America in development of infrastructure and a competent local entrepreneurial class.

The private sector constitutes perhaps two-thirds of the area's economy. Satisfactory overall growth is demonstrably impossible unless this sector moves ahead. But its performance at the present time is agreed by all to be inadequate in most of the countries, especially as regards new investment activity of local and foreign capital.

Among the fundamental factors hampering private activity in Latin America are the balance-of-payments weakness and heavy short-term debt obligations of most Latin American countries, inflationary pressures, shortage of internal working capital, and political instability which often results in governmental policies harmful to the confidence and expansionary tendencies of the private sector. The position of the private sector is also impaired by the fact that most of the instruments of foreign assistance support the public rather than the private sector. Regardless of intentions, governmental and intergovernmental

foreign assistance programs have found it difficult to give adequately effective assistance to the Latin American private sector.

After extensive consultations in Latin America, Europe, and the United States concerning these problems, ADELA has concluded:

First, that its main objectives will be to mobilize a multinational private effort to assist the Latin American private sector;

Second, that the most effective resource to be mobilized is equity capital, over and above that which is already moving to Latin America; and

Third, that the channeling of this additional capital shall be in a form best calculated not only to protect the investment, but also to have important beneficial side effects which, along with other efforts, will help to bring about improvement in conditions now hampering the vitality of the Latin American private sector.

The ADELA directors have therefore undertaken the groundwork for establishment of a multinational equity capital investment company, financed by subscriptions of risk capital from the largest industrial and financial companies in Europe and North America, for investment in moderate-sized Latin American projects, normally in conjunction with Latin American private capital. Projects will be those involving new or expanded productive activities.

The ADELA Investment Co., as a private undertaking, and operating on a long-term basis, will follow the principles of protecting its investment and seeking an adequate return. At the same time it will provide a means by which leading Northern Hemisphere companies can help—over and above their own direct activities—to encourage and strengthen the Latin American private sector.

Shares of $500,000 will be offered to banks and other financial institutions and shares of $250,000 or $500,000 to industrial and commercial corporations. The ADELA Investment Co. will be incorporated when an adequate initial multinational subscription has been achieved. The objective is to reach a capitalization of, say, $40 million in equity, about equally subscribed by Europe and the United States, and also with Canadian and Japanese subscriptions.

II. Present status

The stage of work is as follows:

1. In extensive discussions in Latin America in May to June, the directors found an overwhelming opinion that the ADELA Co. could bring an additional source of strength to the Latin American private sector.

2. The IADB is actively exploring with ADELA methods by which the Bank could assist ADELA projects through loan finance and other means. The Bank is prevented by its charter from engaging in equity investment, and has indicated its belief that the ADELA Co. could become a significant source of equity capital for development projects for which the Bank would provide loan capital.

3. Key officials of the U.S. executive branch have expressed the judgment that the ADELA programs would represent an important advance toward assisting the Latin American private sector. Likewise, a favorable reaction has been received from a number of important officials of European governments and OECD.

4. Close relations are being maintained with the International Christian Union of Business Executives (UNIAPAC) and the European Committee for Cooperation with Latin America (CECAL). It is hoped that the UNIAPAC local chapters in Latin America can work closely with the ADELA Co. in developing investment projects. Consultation has also been maintained with the Atlantic Institute in Paris regarding European public policies toward Latin America.

5. The proposed ADELA action plan was discussed with perhaps two dozen of the leading business personalities of Europe, in July, in order to seek their advice and support. The plan in its present form has the benefit of their suggestions. Although the plan was then at an early stage of development, the European response was exceedingly favorable in all but a few cases. A substantial number of these leaders indicated their readiness to participate financially in the ADELA Investment Co. when it is formed.

6. The directors are now presenting the undertaking to U.S. financial and industrial leaders to obtain their advice, support, and financial participation.

III. ADELA Investment Co.

The fundamental financial, organizational, and operating features of the ADELA Investment Co. are envisaged as follows:

1. Financial participation by European and North American corporations will be entirely in the form of equity capital, part to be paid in initially, and the balance according to a schedule to be determined.

2. Organizational structure will include a widely representative board of directors meeting perhaps once or twice a year to review general policies. Investment policy and major operating decisions will be delegated to an executive committee, elected by the board.

3. Operating responsibility will rest with the general manager, who will participate in meetings of the executive committee. The directors believe that he should be (*a*) European, (*b*) with a record of outstanding competence in business management, (*c*) familiar with Latin America, and (*d*) personally committed to the objectives of the ADELA undertaking. If the financial commitment sought from Europe and North America is attained, it is believed that it will be possible to persuade the European business community to come forth with an individual of high qualifications, who will bring to ADELA the assurance of prudent and efficient management.

4. The ADELA Investment Co. will be incorporated in Luxembourg or Switzerland, and one, two, or three offices (or branches) will be established in selected Latin American countries, as the operation is developed. While the charter will permit flexibility to operate anywhere in Latin America, initial operations will be concentrated, and will begin where the investment climate is suitable and the conditions provided are most favorable.

5. Projects will be selected mainly in moderate-sized ventures in manufacturing, and possibly agriculture.

6. Projects will be sought which do not require excessive protection in the form of tariffs or monopoly supply positions. As Latin American integration proceeds, and industrialization develops, uneconomic and high-cost ventures built on the basis of special protection will be vulnerable. It will be apparent to the executive committee and general manager that the best long-term prospects are in undertakings which will be to the highest extent competitive within Latin America as a whole, and eventually in world markets.

7. It is expected that the interests and objectives of the company will in many cases be served best by making investments in combination with local capital. In certain cases, "buy back" provisions would enable the local partner to regain a majority position, or full ownership, under circumstances and terms preestablished in the partnership contract. However, it is recognized that the issue of partnership with local funds requires to be approached in a flexible manner, on a case-by-case basis.

8. Any single shareholder would have but a small percentage position in ADELA, a maximum of about 1 percent when the full financial plan is realized. Each ADELA participant would continue to operate in its own way in Latin America. Any conflict of interest, as between a company's holding in ADELA and its investment in its own direct operations, would be minimal. Similarly, individual influences upon ADELA would be minimal. As to ADELA's management philosophy, broad ownership by many leading firms, and their control through the board and executive committee, assure that ADELA will follow policies reflecting the consensus of the United States-European business community leadership.

9. Arrangements will be sought, as between the investment company and the subscribers, whereby for suitable compensation the subscribers would provide technical and managerial assistance for projects in their areas of activity. In cases where these arrangements are impractical, or insufficient, outside technical assistance will be sought.

10. In most instances investments will be made from the investment company's own capital. However, the charter would be flexible, so that in particular situations the company could act in other forms; e.g. mainly as promoter bringing together the local investment opportunities and one or more of the subscribers, or an outside investor. This route would be especially appropriate where the project requires very extensive technical and managerial assistance from Northern Hemisphere parties.

11. It is anticipated that assistance of IADB and AID will be obtained in regard to feasibility studies of projects. The ADELA program is greatly strengthened by the moral support of IADB, as well as by the expectation of IADB loan capital for many ADELA undertakings. Channels for continuing consultation with IADB will be established, as well as with IBRD–IFC.

12. Once ADELA has invested its capital the question will arise as to sources of additional funds. Among the possibilities are: the selling off of existing investments which have become seasoned, the public issue of securities of individual project companies or of ADELA itself, and the raising of additional capital from initial subscribers. At some stage, it may be desired to bring into the capital structure of ADELA substantial Latin American equity funds, if they are available. The charter of ADELA would assure that no initial participant would be obligated to provide additional funds unless he desired to.

IV. The broader results

As has been indicated, the ADELA Investment Co. will be launched with a structure of control and organization which will assure its adherence to the principles of private activity. The management will seek to protect its investments, maintain close restraint on overhead expenses, and earn adequate yield.

In this type of operation it would be unrealistic to count on a rapid development of earnings. However, over a period of years a satisfactory return should be developed; perhaps a very good return. Capital is needed and scarce in Latin America and its fundamental economic yield is high.

The fundamental reason for launching the company, however, is the need to bring added strength to the private sector of Latin America. The broader effects which can be hoped for include the following:

1. *Capital injection.*—When the full initial financial plan is realized, a considerable resource will have been made available. If $40 million of Northern Hemisphere equity capital is mobilized, it may be able to bring roughly the same order of local capital into activity, including funds which have temporarily fled the area. A total equity capital of $80 million would mobilize an even larger sum of loan capital; the total of equity and loan might be as much as $200 million. The effect of this much added capital, dedicated to private undertakings, would be material.

2. *Technical and managerial know-how.*—By bringing into life ventures which would otherwise not be borne, the company will be able to help develop new entrepreneurial skills and experience in Latin American. Furthermore, the fundamental ADELA concept, whereby many Northern Hemisphere corporations join in a private investment activity in Latin America, may well offer a framework around which can be built some new concepts for accelerating the modernization of the area's techniques and management. For example, a structure of technical and consulting activities, related to the ADELA Investment Co., may be possible. Studies of this possibility are being undertaken.

3. *Bringing in Europe.*—The ADELA Investment Co. will unquestionably increase the attention of European business toward the Latin American area—a prime focus of the original Javits initiative—and as an indirect result will exert influence upon European governments in the direction of more liberal policies toward Latin America, in regard to trade and the extent and terms of public development assistance.

4. *Preventing vacuums.*—As the national and integration movement planning procedures mature, there will be many specific development projects identified for private sector investment. If private funds are not immediately available, a vacuum is created, likely to be filled by the public sector. The ADELA capital, with its flexibility as to field of activity, will be uniquely suited to help launch these projects on a private basis.

5. *Investment climate.*—When the ADELA Investment Co. grows in importance, it will be able to speak with considerable effect in persuading Latin American governments of the conditions essential for a vigorous and expanding private sector. As the history of the establishment of IADB emphasizes, the fact of ADELA's specifically Latin American dedication will increase its acceptance and influence. It can be a useful forum for communication between the Northern Hemisphere business community and the structure of inter-American organizations as well as with the individual countries. Its choices of one investment location against another because of investment climate considerations will, by reason of its very broad multinational backing, have growing effect.

In presenting the ADELA program to North American and European business leaders during September and October, the directors will be seeking from them letters of intent for financial participation in the ADELA Investment Co. on the scale indicated.

In November or December of this year, it is planned to hold a relatively small meeting in Europe of key people from the three continents. At this meeting, it is intended to receive the report of the executive directors and, assuming that adequate financial commitments have been received from the United States and

Europe, to take the decision for establishment of the ADELA Co. At this meeting, also, an interim organizing company or group may be formed to complete legal and other details, write the statutes, draft the final prospectus and organization plan, and receive additional capital subscriptions.

If this plan can be carried out so that early in 1964 the undertaking will start functioning, the response to the challenge of the private sector of the Atlantic Community will have again been proven.

[Memorandum—December 27, 1963]

COMMENTS ON THE AVAILABILITY OF EQUITY INVESTMENT OPPORTUNITIES IN LATIN AMERICA

1. The proposed creation of the ADELA Investment Co. brings up the question, often raised, of whether there are enough sound projects in the Latin American private sector. International development agencies are known to have complained about the dearth of private projects adequate for external financing, and some concern has ben voiced over the possibility that the ADELA Investment Co. may meet the same obstacle in its operations.

2. It should be remembered, however, that present sources of external financing, almost without exception, offer dollar loans. The reluctance of Latin American entrepreneurs to commit themselves to long-term indebtedness in foreign currency, in the face of uncertain prospects on the value of their own national currencies, appears quite reasonable, particularly if production is aimed at the internal market.

3. Although a high debt-equity ratio is appealing to stockholders for the leverage it provides, it can be safety stated Latin American companies, by and large, are undercapitalized, with an unduly high portion of their financial structure being represented by commercial bank credits.

4. The possibility of obtaining long-term financing in the form of equity investments from abroad, therefore, should represent a welcome solution to Latin American entrepreneurs, especially if control of the company is to remain in domestic hands.

5. Of course, the situation above described is characteristic more of medium- and small-size enterprises than of large concerns which are able to approach adequate sources of financing, either at home or abroad. It is precisely with this type of firms that the ADELA Investment Co. envisages dealing.

6. On the other hand, the process of industrialization follows a well-defined pattern, starting with the production of consumer goods substitution of imported consumer durables, and ending with export capabilities in consumer as well as capital goods. Most of the Latin American countries can be classified in the first two stages described.

7. Consequently,it is easy to determine theoretically the industrial subsectors in which an equity investment company such as ADELA could be active in Latin America. Production facilities of consumer goods and of components for consumer durables, especially those utilizing domestic or regional inputs, appear to be those meriting priority attention.

8. The importance of the agricultural sector in Latin America both from a viewpoint of employment and of the obvious need of increasing the availability of low-cost foodstuffs reveals a natural priority for the food processing industries. Milling, canning, packaging, production of edible oils, starch, chocolate, and so forth, are industrial activities which would provide an assured market for farm production, contributing thus indirectly to improved conditions in rural areas. Ecuador, Peru, Bolivia, and Paraguay, for instance, do not have as yet well-developed food industries.

9. A similar argument can be made for industries utilizing other agricultural raw materials (textiles and hard fibers) as well as for those producing agricultural inputs (fertilizers, insecticides, etc.)

10. Wood processing and production of building materials (cement. etc.) also provide interesting investment opportunities intimately tied in with the development plans of many countries, such as Chile, Colombia, and Venezuela.

11. Furthermore, the metallurgical subsector is the one where a great many integration-oriented industries can be developed with a view toward industrial complementarity on a regional basis. The manufacture of components for the automotive industry is perhaps the best example. Brazil, Argentina, Mexico,

and Chile appear to be suitable sites for this type of industrial investments at present.

12. The chemical industry is just starting in many Latin American countries. Availability of raw materials at little or no opportunity cost (salt beds, petroleum gas, and so forth) as well as rapidly growing internal consumption for many chemical products (caustic soda, inputs for the manufacture of plastics, etc.) forecast the initiation of many new ventures in this field in the near future.

13. In conclusion, from the list of examples given (which does not attempt to be and should not be considered all inclusive), it appears that industrial investment opportunities in Latin America are quite ample. Moreover, equity investments, as planned by the ADELA Investment Co., should constitute an appropriate form of external financing for Latin American entrepreneurs; as a matter of fact, concrete expressions of interest have been received already from an automobile plant in Brazil, a papermill in Argentina, a textile factory in Peru, and so forth.

14. The operating difficulties that may be encountered by the ADELA Investment Co. (and others of similar characteristics) will, in all likelihood, be a matter of mechanics rather than principle. How to contact entrepreneurs? How to promote a project? How to exploit obvious industrial opportunities? These are questions to which the management of ADELA will have to provide answers.

15. Close cooperation with the IDB, as well as with development institutions to which the IDB has granted a line of credit should prove extremely fruitful in this respect for ADELA.

Summary Report of ADELA Conference, January 10–11, 1964, Chateau de la Muette (Headquarters of the Organization for Economic Cooperation and Development), Paris, France

REPORT ON MEETING OF JANUARY 10

The meeting of January 10 was attended by 102 leading personalities from the private sectors and international organizations of Western Europe, Latin and North America, and Japan. Approximately one-half of the participants represented private firms or organizations while the other half was taken from international public organizations.

The principal speakers were Dr. Thorkil Kristensen, Secretary General of the Organization for Economic Cooperation and Development (OECD); Dr. Felipe Herera, President of the Inter-American Development Bank (IADB); Dr. José Mora, Secretary General of the Organization of American States (OAS); Senator Jacob K. Javits, and Dr. Aurelio Peccei, executive director for Europe for ADELA. M. Henri Burnier, chairman of the Banque Francaise et Italienne, and Mr. Emilio G. Collado, vice president and director of the Standard Oil Co. (New Jersey), served as chairmen of the morning and afternoon sessions respectively.

Among the chief personalities taking an active part in the morning and afternoon discussions were Mr. L. B. Wolters, president of Petrofina; Mr. George Moore, president of the First National City Bank of New York; Mr. Hugo Lindgren, assistant vice president of Enskilda Bank; M. Jacques Oudiette, director of the Banque Nationale pour le Commerce et l'Industrie; the Count de Vogue, president of St. Gobain and chairman of the Comite Europeen pour la Cooperation avec l'Amerique Latine; Mr. Adelbert Krieger Vasena, former Finance Minister of Argentina and member of the National Academy of Economic Sciences; Mr. Andres Aguilar, personal representative of President Betancourt of Venezuela; Mr. Kunio Miki, managing director of the Bank of Tokyo; Mr. Pinhero Neto, corporation lawyer from Brazil; Mr. Arthur Dean, senior partner of Sullivan & Cromwell; Mr. Gianni Agnelli, vice chairman of Fiat; Mr. Evence Coppee, Societe Evence Coppee of Belgium; Mr. Walter McKee, director of the Latin American Division of the Ford Motor Co.; Mr. Claudio Segre, Director for Economic and Financial Affairs of the European Economic Community; and Mr. Willard H. Thorp, chairman of the Development Assistance Committee.

Basic support for the ADELA concept of a coordinated private sector initiative for the economic and social development of Latin America was expressed by the speakers and by the participants in the discussions. Both the Latin American and Northern Hemisphere representatives felt that it would contribute importantly to the revitalization of the Latin American private sector. Other issues considered included the need for measures to protect private investments,

and the advisability of considering the rescheduling of foreign debts of certain Latin American countries. Recommendations for broadening the initial support of the proposed ADELA Investment Co. were also discussed.

Senator Javits, at the conclusion of the meeting, summarized the consensus favoring positive steps for the formation of the company. These steps were initiated the following day.

SUMMARY OF MINUTES OF JANUARY 11, 1964, BUSINESS MEETING

A group of private banking and industrial representatives who participated at the January 10 ADELA Conference in Paris met on January 11. As a result of this meeting, an interim organizing committee (IOC) was established and charged with developing the structure of the proposed multinational private investment company which would undertake equity investments and serve as a catalytic agent for private enterprise in Latin America.

The eight-member IOC is cochaired by Mr. Gianni Agnelli, vice chairman of FIAT, and Mr. Emilio G. Collado, vice president and director of the Standard Oil Co. (New Jersey). Banking and industrial firms from Belgium, Italy, Japan, Switzerland, and the United States are represented on the IOC. Expansion of the IOC is provided for when firms from other major nations commit themselves to participation in the proposed investment company.

ADELA CONFERENCE JANUARY 10–11, 1964, LIST OF PARTICIPANTS

Gianni Agnelli, Vice President, FIAT.
Andrès Aguilar, Représentant du Président Bétancourt (Vénézuela).
Mr. Akiyama, Representing the Mitsubishi Bank.
T. Altafer, Representing the International Confederation of Free Trade Unions (ICFTU).
John B. Arnold, Senior Vice President, First National City Bank.
Mr. Arnold.
Cavendish Bentinck, Director, APPI.
Herbert J. Blitz, Executive Secretary, ADELA.
Mr. Bosc.
Charles E. Bourbonniere, Secrétaire Général, BIAC.
Henry Burnier, Président de la Banque Française et Italienne.
Yves Bricard, Représentant à Paris de la Bank of Mexico.
Franklin O. Canfield, Standard Oil Company (New Jersey).
Mr. Cherie Ligniere, President, FIAT-France.
Takashi Chiba, General Affairs Specialist, Hitachi, Düsseldorf.
Emilio G. Collado, Vice President and Director, Standard Oil Company (New Jersey).
Pierre-Edouard Coquelin, Secrétaire Général de la Banque Worms.
Evence Coppee, Société Evence Coppée, Bruxelles.
Jean Cottier, Secrétaire Général adjoint, OCDE.
Peter Cusick, Assistant to Senator Javits.
Arthur Dean, Senior Partner, Sullivan & Cromwell.
Alain Debiez, Commission des Nations Unies pour l'Amérique Latine.
Ambassador Dowling, Atlantic Institute, Paris.
Mr. Ebe, Director, Bank of Tokyo.
Luciano Elejalde, Corporacion Financeria Nacional, Colombia.
Edward Eller, Chase Manhattan Bank, Paris.
Henri Emmet, Irving Trust, Paris.
Sherwood Fine, Directeur de la Section Finance du Développement, OCDE.
Helmuth Fuhrer, Head of the Financial Policies Division, Development Department, OECD.
Egidio Gavazzi, Administrateur de la Pirelli à Milan.
Jean-Louis Gillieron, Représentant de la Société de Banques Suisses.
Luciano Giretti, Adjoint au Secrétaire Général, chargé du Départment du Développement, OCDE.
E. F. Goldfuss, Vice President, IBM.
Julio Gonzalez Del Solar, Directeur Executif, ADELA.
Herbert E. Gray, Member de la Chambre des Communes, Ottawa.
Jorge Grieve, Committee of Nine, OAS.
Maurice Guernier, Directeur du Bureau de Paris, ADELA.
Felipe Herrera, Président de la Banque Inter-Américaine de Développement.

Guillermo Herrera Carrizosa, Président de la Corporacion Colombiana al Desarrollo Industrial.
Jacob K. Javits, United States Senator.
Bent Jorgensen, Economics Directorate, NATO.
A. M. Kemps, Directeur Général, SYBETRA, Bruxelles.
Tom Killefer, U.S. Director, IADB.
Peider Konz, Secretary of the Council and Head of the Legal Service, OECD.
Adelbert Krieger Vasena, Membre de l'Académie Nationale des Sciences Economiques, Argentine.
Thorkil Kristensen, Secrétaire Général de l'OCDE.
O. van H. Labberton, Secrétaire Executif de la Conférence des Parlementaries de l'Otan.
Mr. de Lapparent, Sous-Directeur du siège de la Société Générale.
J. G. Lejeune, Secrétaire Général de CECAL.
E. W. B. Lewis, Vice President in charge of Finance, Westinghouse.
Mr. de Liedekerke, Lazard Frères.
Hugo Lindgren, Assistant Vice President, Stockholms Enskilda Bank.
Eric Lindroth, Assistant to Mr. Collado, Standard Oil Company (New Jersey).
Louis Louvet, Financial Policies Division, Development Department, OECD.
Walter McKee, Director, Latin American Division of the Ford Motor Company.
Philippe Magnan de Bornier, Comptoir National d'Escompte de Paris.
Robert Menapace, Financial Adviser, Inter-American Development Bank, Washington.
Angel Meschi, Représentant à Paris de Corfo, Chili.
Kunio Miki, Administrateur délégué de la Bank of Tokyo à Tokyo.
John D. Miller, Director, European Office, IBRD, IFC.
Thierry Monnier, Chef de la Division des Relations Extérieures de l'Ocde.
George S. Moore, President, First National City Bank of New York.
José Mora, Secrétaire Général de l'Organisation des Etats-Américains.
Mr. Muller.
Forrest D. Murden, Director, Allen, Murden, Nystrom & Armstrong, Inc.
George Nahoum, Paris Representative, Bank of London and South America.
Octavio Nizzola, Lugano, Switzerland and Peru, Director, Lima Light & Power.
M. Obanda.
Mr. Ogasawara, Fuji Bank.
Jacques Oudiette, Directeur, BNCI.
Ernest C. Parsons, Head of the Economic Development Division, Development Department, OECD.
Aurelio Peccei, Directeur Exécutif, ADELA.
M. Pierre, Banque Worms.
M. Polti, Banque de Paris.
Claude Popelin, Conseil National du Patronat Français.
Mr. Pinhero Neto, Avocat, São Paolo, Brésil.
Paolo Rogers, Olivetti.
Claude Roux, Assemblée Nationale, France.
Seymour Rubin, U.S. Representative on the D.A.C.
Jorge Mejia Salazar, Président du Comité de Direction et Président du Banco de Bogota.
M. Schweinitz, Directeur, GHH, Essen.
Walter Sedwitz, Assistant Secrétaire Général, OAS.
Claudio Segre, Economic and Financial Affairs, EEC.
Thédore Seiler, Directeur Général de la Société de Banques Suisses.
Joseph Slater, Directeur-associé des Programmes des Affaires Internationales.
J. R. Stevenson, Sullivan & Cromwell.
Willard H. Thorp, Président du Comité d' Assistance due Développement, OCDE.
Antonio Tonello, Istituto Mobilare Italiano.
M. Trotta, Délégation Italienne auprés OCDE.
N. Ullman, Atlantic Institute.
M. Urrutia, IADB, Paris.
Lazard Frères Valensi.
Guiseppe Vedovato.
UNIAPAC Vermeire.
Arnaud de Vogué, president du CECAL (Comite Européen pour la Cooperation avec l'Amérique Latine).
J. Vulliod, Directeur du Crédit Lyonnais.
Warren Wilhelm, Directeur Exécutif ADELA.
L. B. Walters, Pétrofina.
Eduardo Zuleta, Ancien Président des Nations Unies.

Representative CURTIS. Mr. Chairman, before I question the witness, I would like to have unanimous consent to place in yesterday's record, rather than having it confuse today's, a colloquy between Senator Hickenlooper and Senator Morse on November 13, 1963, entitled, "Recent Developments in Argentina," which bears on some of the matters we were discussing yesterday. This was called to my attention, and I think it would be very helpful if it were put in the record.

Senator SPARKMAN. Without objection, that insertion will be made in yesterday's record.

(The material referred to appears on p. 108 at the conclusion of the record of hearing, January 14.)

Representative CURTIS. First, I just want to say that this has been very valuable and interesting testimony. Certainly, the future of ADELA is going to be watched with a great deal of concern. It can make a great contribution.

Rather than getting into the details of that and let it be confused, I would like to raise a collateral question that could be asked of any of the witnesses. I think we have been talking a great deal about Government policy in Latin America as far as capital investment is concerned. I have been equally concerned, and I know you gentlemen are, too, with the aspects of what I would term the immigration policy of these countries. Here we are confronted with the big problem of available skills. As this country developed, to a large degree, we imported our skills from Western Europe. This is one of the lines of interrogation I conducted during this subcommittee's visit to the various Latin American countries. Not only did I fail to get what I would regard as satisfactory answers, but I got the impression that there had been very little thought directed toward obtaining skills in this fashion.

In Argentina, I recall, in order to move forward in some of the projects, they imported certain skills mainly from Italy in large numbers. Instead of staying and settling, however, most of these people returned to Italy or their country of origin.

Now, before I pose the question, there is one other point I would like to make.

In the supplemental views to this subcommittee report which I prepared, I tried to point out what I thought was a very basic matter that had received very little attention. As I see it, there is a distinction between two types of undeveloped countries in the world today, on the basis of population per square mile. One group contains those countries which are heavily populated—Indonesia, India, and China come to mind. In contrast, there are a great number of countries that are acually underpopulated, for example, those of Latin America. There are very few sections of Latin America—you could identify them as the island of Jamaica, Puerto Rico, and possibly Cuba—where there is what you might call overpopulation or a full population. I think perhaps one reason we have not thought of Latin America in this context is that attention has been directed to the very recent increases in population and the birth rate.

But I note, in following through the figures, that this population explosion in Latin America has not yet hit their labor market. These people are still in the age brackets before they move into the labor market.

So I think we probably have a problem here of underpopulation. Thus in your concept of investing there, the question arises of how you would obtain your skills. Is part of your scheme to bring skilled people to these areas who might stay? What is the attitude of the various Latin American countries toward this approach?

Would you comment on that general problem?

Mr. PECCEI. Sir, my experience in Latin America, and as the thing would be, would show that the requirement of immigration would be limited to a small number for each enterprise of the more specialized people, and possibly it will not be for permanent or a very long stay. I think that if, by bringing up new undertakings and developing the market, we also will achieve the objective of having more Europeans interested in going into Latin America, that will be a very good thing for many areas.

But I think in our own specific fields, we should only try to have from Japan or Europe or even the United States a small number of people considering also the cost that each enterprise has to bear if it relies heavily on importing of people.

Representative CURTIS. So your answer would tend to be that you will concentrate on training the people already in the country in these skills, rather than bringing them in, colonizing them, and making them citizens of that country?

Mr. PECCEI. Yes, Congressman, and the experience, I know, shows that that is a very good method and the results are rather good.

Representative CURTIS. I have one other question. You have Japanese interests in your group. I tried to pin this down but I have been unable to because I just did not pursue it. I have heard that the Japanese people have been moving into Brazil, for example, settling and becoming citizens. Is that true to any degree, do you know? Have your Japanese partners thought at all along the line of bringing in skills in that fashion?

Mr. PECCEI. Yes; there have been to my knowledge also recently some schemes to bring more Japanese into some areas, into Brazil, Uruguay, Peru, where there is already a colony of Japanese and where they may settle.

Representative CURTIS. They certainly have become splendid citizens in California and a real part of our economy there and in Hawaii. If the premise is correct, and I think it is, that we are dealing with underpopulated as well as underdeveloped countries, I would hope that some more attention could be directed to immigration as a real possibility of moving these economies forward, particularly in this period when they badly need skills. It takes time, of course, to train people in skills, and if you can import them, I again emphasize, like the United States did, why, you are that much ahead of the game.

Thank you.

Senator JAVITS. Mr. Chairman, may I just note, if I may, and I will be finished?

Senator SPARKMAN. Yes.

Senator JAVITS. In response to Congressman Curtis' statement about being kept informed, I have reported to the Senate constantly on this since it started and I will continue to do so.

Senator SPARKMAN. Thank you very much.

Thank you, gentlemen. You have given us something that is quite thought provoking and interesting and we will follow it with a great deal of interest from time to time. We wish you well in it.

Thank you very much.

Now we have two other witnesses this morning on closely related subjects—Dr. Fatouros, who will discuss Government guarantee programs in general, and Mr. Rublee, who treats specifically of such programs as they have been set up and operated by the U.S. Government.

Dr. Fatouros is a professor at the University of Chicago Law School, also author of "Government Guaranties to Foreign Investors."

Mr. Rublee is Assistant General Counsel for Private Enterprise, Agency for International Development, Department of State.

If you gentlemen will come forward, we will proceed in a panel.

We have a joint session of Congress at 12:30 in order to hear from the President of Italy and both Houses will accordingly meet at 12.

I don't want to hurry this hearing up unduly, but if we can move right along, I would appreciate it, so that we can adjourn at 12 o'clock.

You gentlemen both have papers, do you not?

Mr. FATOUROS. Yes.

Senator SPARKMAN. Let me say, as I have to other witnesses, your papers will be printed in full in the record. You may proceed as you wish, either to read it or discuss it.

Mr. Fatouros?

STATEMENT OF A. A. FATOUROS, VISITING ASSISTANT PROFESSOR, UNIVERSITY OF CHICAGO LAW SCHOOL, AND GEORGE RUBLEE, ASSISTANT GENERAL COUNSEL FOR PRIVATE ENTERPRISE, AGENCY FOR INTERNATIONAL DEVELOPMENT

Mr. FATOUROS. Mr. Chairman, members of the subcommittee, I am very honored to appear before you today.

My name is A. A. Fatouros, and I am visiting assistant professor at the University of Chicago Law School. I'll summarize my statement, dealing chiefly with the general characteristics of guarantees and with the conclusions of my study.

The guarantees we are dealing with are intended to counteract the relative lack of security and legal stability, a factor which affects direct private foreign investment in less-developed countries. They have certain common general features. They are issued by governments, not by private agencies. Also, they relate to direct private investment, not indirect investment; that is, investment in foreign securities. Though this is outside my present topic, I should like to add that there is great need today for indirect private investment in the less-developed countries. It would be useful to study the possible ways by which such investment could be encouraged, partly through various guarantee devices. Such devices have been used in the past, but they may have to be adjusted to modern conditions and new methods or combinations of methods may have to be devised.

The guarantees we are dealing with here, the so-called investment guarantees, generally relate to direct investment. One partial exception, of course, is that of the AID guarantees. It is with the purpose

of encouraging direct investment that these kinds of investment guarantees have been devised.

These guarantees provide generally for the indemnification of the investors. But a basic part of their main function is to prevent the occurrence of events injuring the investors' interests. They have a deterrent function, a preventive function, rather than a mere compensatory one.

Finally, they cover risks which are not usually covered by any kind of business or commercial insurance. They cover noncommercial risks which relate in fact to the possibility of unforeseen changes in the legal conditions under which the enterprises established by foreign investment would operate. In most cases they relate to the change of these conditions; that is, what the enterprises are told is that if the conditions change, then they will be indemnified or, more commonly, they are promised that the conditions will not change. But closely related to that kind of promise is the promise, very common in the industrial promotions statutes, for instance, in Latin America, that if the enterprise comes into the country, it will be given certain tax exemptions. This is an attempt to improve the investment climate by eliminating certain difficulties rather than merely assuring that there will be no change detrimental to the investors' interests.

There have been several suggestions recently for an investment code, a multilateral international convention which would embody certain principles by which capital-importing countries would agree to operate, especially the protection of private property, or provisions for permission to repatriate capital, and so on. The proposals are still unofficial. No government has fully adopted such a proposal yet.

Apart from the fact that such a code seems extremely difficult—apart from the fact, rather, that it is highly doubtful that such a code would be adopted by the majority of the capital-importing and capital-exporting countries, it is doubtful that even if adopted, it would be effective. Chances are that the language of such a code would be so watered down by specific exemptions to take into account important aspects, important in their particular context, that by the time it would be adopted, it would become almost counter, in effect, to what is intended. Finally, there are certain dangers in attempting to bring a code into existence. Negotiations on such subjects might lead to adoption of rigid positions, in the beginning, perhaps, for bargaining purposes but which are retained afterward. This is a danger that cannot be ignored.

There have been other proposals for the establishment of a system for the settlement of disputes between investors and host governments. These proposals are quite different from those mentioned before. They do not attempt to establish legal principles by which the host countries would treat foreign investment. Such proposals have been studied for some time now by the staff of the World Bank and it does seem that if such a system could be devised, if it could operate successfully, and even if it could operate at all, it would serve a very useful function.

The United States, as you know, has concluded a number of bilateral investment treaties, friendship, commerce, and navigation treaties. Since 1949, when the new type of treaty was fully developed, 21 such treaties have been signed, of which 18 have entered into force. Of

these, about eight have been concluded with countries which can be considered as economically underdeveloped. With Latin American States, four such treaties have been signed, but only one has come into effect. The other three have not yet come into force, though in at least two of these cases, it seems that the reasons for the nonratification are unrelated to the treaty's provisions on investment.

The other major capital-exporting countries have by now concluded very similar treaties. The Federal Republic of Germany has concluded two FCN treaties with the Dominican Republic and Greece, which follow very closely the American model. Germany has also concluded eight other investment treaties which are somewhat more specialized and deal exclusively with foreign investments. They are the equivalent to, though their content is fairly different from the intergovernmental guarantee agreements concluded under the investment guarantee program of the United States. Switzerland has very recently concluded four investment agreements, being somewhat shorter FCN treaties and known as agreements concerning trade, protection of investments and technical cooperation with African States. Japan has concluded recently two FCN treaties with other countries and the United Kingdom has concluded one with Iran.

Of course, the bilateral treaties are a flexible instrument, since they can be adapted to the particular country with which the treaty is concluded. So for instance, navigation provisions have been excluded from some treaties when there were problems with respect to navigation. Or the content of particular provisions may change; the provisions relating to exchange restrictions, for instance, in the treaty with the Federal Republic of Germany are different from the provisions on the same topic in the treaty with Greece or in the treaties with other countries.

The problem, of course, is that the language of these treaties remains still fairly general and that very few such treaties have been concluded with less-developed countries.

I will not go at any length into the investment insurance program of the United States, because, of course, it will be covered with much greater competence by Mr. Rublee. I will only mention that such systems operate today on lines very similar to that of the United States in Germany and Japan. The principal difference seems to be that the Japanese program operates without being based on a network of intergovernmental agreements, as the U.S. program is. The German program is in between, in the sense that it may operate without such agreements, but the German Government is actively promoting the conclusion of such agreements and has already concluded eight. Also, the German agreements are far more elaborate than the U.S. ones.

Related to these programs, though not the same thing, are the export credit insurance programs, which operate in most developed countries, including Australia, Canada, the United Kingdom, and France, which do not have investment guarantee programs. To some extent, investors may take advantage of the facilities of the export credit insurance programs.

There have been proposals recently, very recently this time, for the establishment of a multilateral investment insurance program, a program similar to that, let's say, of the United States operated by AID, but established by capital-importing and capital-exporting states,

and operated by an international agency, most probably the World Bank or an affiliate of it. There are several proposals of this type. Again, I will not go into the matter at length, because there is an excellent study by the staff of the World Bank on this and any comment I would make would repeat their observations.

There are serious problems, though, in trying to establish such a program. For instance, the risks against which the program would insure would have to be defined much more precisely than they are today defined in the U.S. program, because this would be a multinational program and therefore each nation would have to be sure as to what it is agreeing upon. This, of course, presents difficulties.

Finally, many of the capital-importing countries—in fact, the great majority—have enacted investment statutes, either directed exclusively to foreign investment, or directed to promotion of investment in certain fields, especially industry. The Latin American countries, for example, the great majority of them—15 out of 20—have industrial promotion statutes, while only 8 have foreign investment statutes. The difference between the two is pretty small in some cases. Investment statutes often tend to emphasize exchange restrictions—well, privileges with respect to repatriation of profits, while industrial promotion statutes tend to emphasize tax exemptions. But this is simply a matter of degree.

Usually, the investor is required to apply for approval or for registration, so-called, which comes to the same thing. And after a certain stage where negotiations are most often conducted between the appropriate agency of the host government and the investor, an instrument of approval or a certificate, or sometimes a contract, is issued, where the particular assurances given to the investor are spelled out, sometimes with great precision. He is told how much foreign currency he can take out each year and so on. This is, in fact, the great advantage of these instruments.

First of all, of course, they do indicate the willingness of the host country to accept and encourage foreign investment.

Secondly, they give to the investor very precise promises which are especially useful with respect to minor government officials. If you have to deal with a minor official in the host country it helps if you have an instrument, sometimes in the form of a statute or at least in the form of a decree, which contains elaborate and precise indications as to what exactly you are promised.

Of course, these instruments are subject to change. It is impossible to say that if the regime of the host country changes, or sometimes, though very rarely, if the government changes, the promises will be faithfully kept. Still, in the great majority of the cases, these promises have been kept. We have instances where the courts of the host country have protected the investor, solely on the basis of the instrument of approval which approved his investment, giving him certain promises.

It is very difficult to speak of the results of these guarantees, because they are very new; even where these guarantees have been operating for some time, which is the exception, in most cases this is less than 10 years. Even in this case, it is very difficult to isolate the effects of the guarantees from the effects of other factors—political, social, and so on.

Still, it is necessary to point out that such guarantees have definite limitations. The security of the investment is only one of several factors which the investor takes into account and even its actual value as a factor depends a great deal on other things. Moreover, no guarantee, no legal guarantee can fully provide security. There are certain objective conditions which are far more important.

Now, the existing programs and forms of guarantees, given through the insurance programs of capital-exporting countries, bilateral agreements and guarantees given by the capital-importing countries, give different kinds of protection to the investor so that the ideal situation would be to have all three in the same country, which does in fact happen in some cases. These guarantees are complementary. The guarantees given by the host country are precise, concrete. The FCN treaty as a background makes it more certain that these guarantees will be kept. The investment insurance programs help in assuring that even if they are not kept, the investor will not be injured, or will be injured to a small extent.

Well, I will limit myself to these very general comments.

Senator SPARKMAN. Thank you.

(The complete statement of Mr. Fatouros is as follows:)

AN APPRAISAL OF PROGRAMS OF GOVERNMENT GUARANTEES TO FOREIGN INVESTORS

(By A. A. Fatouros, visiting assistant professor, University of Chicago Law School)

One of the factors which affect direct private foreign investment in less developed countries is the relative lack of security and legal stability. It is not the only factor, nor is it the most important in most cases; economic considerations generally play a much more important role. Still, it is a factor of considerable significance and, even where it does not determine the basic issue whether to invest or not in a particular country, it often affects the field of investment chosen, its form and amount, the rate of return sought, etc.

Government guarantees are intended to counteract this particular factor. The term "guarantees" is used here in a very broad sense; it includes various kinds of promises and assurances as well as "guarantees" in a strict sense.

GENERAL FEATURES

The common characteristics of the guarantees under study are:

(1) They are issued by governments and not by private agencies;

(2) They relate to direct private foreign investment, i.e., investment in enterprises abroad controlled by the investor (indirect foreign investment, i.e., investment in foreign securities, and the related guarantees present quite distinct problems with which we are not dealing here; it should be noted that the bulk of private foreign investment in the developing countries today is direct in form);

(3) Like all guarantees, they often provide for the indemnification of the investor whenever certain specified events occur, but, unlike most private guarantees, their main function is to assure the investor that the events feared will not occur; in other words, they are chiefly intended to prevent such events, rather than merely compensate for the losses they may cause;

(4) They generally cover risks of a peculiar character, not the "ordinary" business risks normally faced by investors but risks which relate to the political and economic conditions in the country of investment.

Generally speaking, these guarantees are calculated to protect foreign investors from unforeseen changes (or from the effects of changes) in the legal conditions under which the enterprises established abroad operate. In our days, such changes have been more frequent and more far reaching than they have in the past. The desire of the less developed countries to promote their rapid economic development, nationalistic feelings in newly liberated nations, fear of foreign domination, political or economic, and revolutionary changes of political regimes are some of the forces that have been behind the increased incidence of

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such changes. The changes may be radical in character; e.g., they may consist in the taking of the foreign investor's property, or they may be less far reaching, though still damaging to the investor; e.g., restrictions on the entry of capital in certain fields of the economy, restrictions on the employment of aliens, limitations on the foreign exchange to be imported or exported by the enterprise, or changes in the amount of taxes to be paid by it.

The existing rules of international law are generally inadequate to deal with such changes, either because the changes occur in fields which, according to traditional international law, belong to each state's virtually absolute jurisdiction (e.g., exchange control, employment of aliens) or because the rules themselves are not clear in their exact content or in their application (e.g., nationalization of foreign-owned property). The need arises, therefore, for specific assurances to the foreign investors to the effect that certain favorable legal conditions will exist or will continue to exist. Most of the guarantees here studied are basically assurances that certain conditions existing at the time of investment will not be changed (or that, if they are changed, the investor's interests will not suffer). In some cases, the guarantees are really inducements; i.e., assurances of special treatment or of the elimination of certain existing conditions; the chief example is the offer of tax exemptions. These two kinds of promises are different, but they are often found together; the difference between them is perhaps of degree rather than of substance.

The following general types of guarantees may be distinguished:

(1) Assurances of fair treatment embodied in a single multilateral international convention, to be concluded among all or a great number of capital-exporting and capital-importing states;

(2) Guarantees given by means of a system of bilateral treaties concluded between capital-exporting and capital-importing states and setting down principles of treatment of foreign investors;

(3) Investment insurance given to individual foreign investors by the country of their nationality (i.e., a capital-exporting country);

(4) Investment insurance given to individual foreign investors by a single international agency set up by capital-exporting and capital-importing countries; and

(5) Guarantees given to individual foreign investors by the capital-importing country in which the investment is made.

INVESTMENT CODE PROPOSALS

It has been suggested that, to assure the legal security of foreign investment, all or most of the countries concerned, capital importing as well as capital exporting, should adopt a multilateral convention which would embody a code of legal rules for the fair treatment of foreign investors. Such proposals have come mainly from nongovernmental private groups representing the interests of actual or potential investors. In the early postwar years, related provisions were included in two international agreements dealing with economic matters; namely, the Charter of the International Trade Organization (Havana, March 1948) and the Inter-American Economic Agreement of Bogotá (May 1948). Both these treaties were not ratified by the United States and never became effective, partly because of acute disagreements among the signatory states concerning the investment-protection provisions. Since then, several governmental and nongovernmental bodies, including several organs of the United Nations and of the Council of Europe, have discussed the idea of an investment code, some expressing their support and others stressing the need for more study.

The most important of the recent efforts in this direction is the draft convention on the protection of foreign property released about a year ago by the Organization for Economic Cooperation and Development. This draft was prepared by the OECD staff and delegates from some member states, on the basis of proposals submitted by the Governments of Switzerland and Western Germany. It is not endorsed, in principle or in content, by the Organization itself or by the member states, and it has been released for the express purpose of obtaining the comments of governments and other interested parties. The draft provides for the "fair and equitable" treatment of foreign property, the respect of any undertakings given by a state to other states or to foreign investors, and the prohibition of direct or indirect takings of foreign-owned property, except under strict conditions (measures taken in the public interest and under due process of law, not discriminatory or in violation of specific undertakings and

accompanied by provision for the payment of "just" compensation). The draft further provides for the settlement by arbitration of any disputes under the proposed convention.

The idea of an investment code is attractive because of its simplicity and generality. Any other method is bound to appear in comparison too complicated and detailed. However, it is no accident that despite repeated efforts no such code has come into effect. There are several compelling reasons.

In the first place, it is highly doubtful that such a code would be adopted by a sufficient number of states. There is no indication that most of the capital-importing ones are willing to enter into an arrangement which would tend to limit their present freedom of action in economic matters. From the capital-importing countries' point of view, the adoption of an investment code is neither a necessary nor a sufficient condition for a significant increase in the amount of capital invested in them; economic factors may keep such capital out, even in the presence of such a code, and the same factors may induce its investment, in the absence of a code. Moreover, most of the codes proposed up to now are one-sided in that they contain rules stating the investors' rights and the duties of the countries of investment, without providing for the protection of the host states' interests or for the foreign investors' duties. It is reasonable to argue that an investment code, to be valuable, should be balanced and should provide a comprehensive framework for the legal relations between host states and foreign investors. Given this situation, an investment code might still be adopted if all major capital-exporting states were prepared to exercise strong pressures on the capital-importing countries, to the possible detriment of other foreign policy objectives. Again, there is no indication that they are so prepared; in fact, as already noted, at least some of the capital-exporting states are reluctant to bind themselves to such an arrangement.

It might have been worthwhile to disregard these difficulties and press for the adoption of an investment code if the code showed any promise of being effective. This is far from being so. Experience with past attempts is instructive: Both the Havana Charter of the International Trade Organization and the Bogotá Economic Agreement contained provisions on the protection of investments which were unsatisfactory to both private investors and host countries. They were vague and general, and their effect depended on the construction of such terms as "appropriate," "unreasonable," "justified," or "equitable." Any international investment convention would have to be couched in general and often vague terms, because it would have to cover many kinds of investments and many sorts of political, legal, and economic conditions and measures. Another reason for a code's probable lack of effectiveness is that it would tend to regulate only those matters as to which there exists some agreement at least among the capital-exporting countries, and leave out any provision which might affect the interests, or make necessary changes in the policies, of these countries. This seems to have happened, for instance, to the OECD Draft Convention whose scope has been progressively limited. The protection afforded the foreign investor is correspondingly restricted; such important matters as exchange control or the employment of foreign personnel are left outside the convention.

Finally, any serious attempt to induce a great number of less developed countries to enter into such an arrangement involves serious dangers. The necessary negotiations and discussions may well result in the adoption of extreme and rigid positions and thus lead to an intensification of existing tensions and differences which would eventually harm foreign investors as well as the relations between developed and underdeveloped countries.

It is necessary to distinguish between the proposals for the conclusion of a convention which would contain certain legal principles of "fair treatment" of foreign investors from other suggestions of joint international action for the establishment of a system of arbitration or conciliation for the settlement of disputes between governments and foreign investors. There have been several proposals of the latter type with a number of variations, and the staff of the World Bank is currently working on the text of a detailed draft convention. These proposals present considerable merits, even though they cannot be considered as providing the solution to all problems of legal security of investments. Three particular elements seem necessary for the successful operation of such a system of dispute settlement: First, recourse to it must retain its voluntary character, since a general agreement for compulsory arbitration seems highly improbable; secondly, emphasis should be placed not only on the procedure of arbitration on the basis of legal principles, but also on the procedures of concili-

ation and arbitration on an equitable basis (ex aequo et bono, in international law terminology); and thirdly, the body charged with the system's administration must be impartial and sufficiently well informed in technical, economic, and financial matters. The World Bank and its affiliates and associates certainly fulfill this last condition.

BILATERAL INVESTMENT TREATIES

The difficulty, if not impossibility, of concluding a satisfactory multilateral investment convention is one of the factors that have led the United States and other capital-exporting countries to favor the conclusion of bilateral treaties dealing with the protection of foreign investment. The instruments used are the traditional comprehensive commercial treaties "of friendship, commerce, and navigation" (FCN treaties) which have been adjusted to include a number of provisions dealing with investment and the position of foreign investors. Since 1949, when the new type of treaty was fully developed, the United States has concluded 21 FCN treaties, of which 18 have entered into force; of these, only 8 have been concluded with countries which may be considered as economically underdeveloped. Four FCN treaties have been concluded with Latin American countries, but only one of them (with Nicaragua) has become effective. The other three (with Uruguay, Colombia, and Haiti) have not yet come into force, though signed from 9 to 15 years ago. However, in at least two of these cases, the reasons for the nonratification appear to be unrelated to the treaties' provisions on investment protection.

The other major capital-exporting countries have also concluded a number of investment treaties with less developed countries. West Germany has concluded two FCN treaties, on the United States model, and eight more of a specialized type dealing exclusively with the protection and promotion of foreign investments. Switzerland has concluded four agreements concerning trade, protection of investments, and technical cooperation with African states. The United Kingdom has concluded one FCN treaty and Japan another two.

The United States FCN treaties cover several subjects in addition to investment; they deal with matters of navigation, trade, establishment of U.S. nationals not engaged in business activities, etc. Their investment protection provisions are fairly extensive. U.S. nationals and companies are accorded national treatment in many fields of business activity and most-favored-nation treatment in others. They are permitted to own property and establish companies, though under certain possible limitations, and to employ the personnel of their choice, though again subject to possible immigration and other limitations. Exchange restrictions are to be imposed only in certain specified situations and, where such restrictions are in force, foreign investors are to be accorded high priority in transferring abroad their profits and, with some restrictions, their capital. The property of foreign investors is subject to expropriation only for purposes of public utility and against payment of prompt, adequate, and effective compensation. Finally, all related disputes must be submitted, in the absence of an agreement providing otherwise, to the International Court of Justice. As already noted, the German FCN treaties follow closely the U.S. pattern; those of the United Kingdom and Switzerland have similar provisions though with differences in phraseology and substance.

The German "treaties for the promotion and protection of investments" are connected with the German investment insurance program (discussed below) and thus are more specialized in their contents. They focus on investments, and their provisions, though basically similar to those in FCN treaties, are more detailed and concrete. When forbidding discriminatory measures, for instance, a number of measures which are to be considered discriminatory are listed. The repatriation of profits and capital is "guaranteed" in unconditional terms. Their provisions on the settlement of disputes are also very elaborate and detailed.

The bilateral treaty program of the United States (as well as that of Western Germany) has evidently fared better than the unofficial proposals for a multilatertal investment code. The bilateral treaty is certainly a more flexible instrument than the multilateral convention, if only because there are fewer interests and points of view to be reconciled. Looking at the U.S. treaties, one notices that in some cases the form of the treaty is altered to fit the other contracting party's special conditions, in other cases, some provisions are omitted, and finally, the contents of specific articles vary from treaty to treaty. The German example of "treaties for the promotion and protection and investment" may be an indication that the elimination of the trade, navigation, and other

provisions which are not directly related to investment might help in inducing some less-developed countries to enter into such agreements.

The bilateral approach has its limitations, too. The U.S. Department of State has been unsuccessful in its efforts to conclude such treaties with many less-developed countries, especially most of the Latin American countries. Many States are unwilling to commit themselves with respect to matters of domestic economic policy. Basically, there are differences between the attitudes (and the interests) of developed and underdeveloped countries which cannot be eliminated by means of a legal formula where full mutual understanding is lacking. Moreover, though no serious problems seem to have arisen under any of the United States or German FCN treaties, the possibility of disputes on the interpretation of their provisions cannot be excluded, since their language is rather general and abstract. From the point of view of the investor, this lack of certainty, coupled with his inability to enforce the rights accorded under the treaty without the intervention of the Department of State, constitutes a serious disadvantage of the treaty approach.

INVESTMENT INSURANCE BY CAPITAL-EXPORTING COUNTRIES

Since 1948, the United States has undertaken to insure the foreign investments of its nationals against certain risks. Today, new investments by U.S. nationals in more than fifty underdeveloped countries can be insured against the dangers of inconvertibility, expropriation, and damage caused by war, revolution or insurrection, while some investments of high priority (and in particular housing projects in Latin America) may be insured against all risks, commercial and noncommercial. On the surface, the program operates on the lines of a private insurance agency: A contract is concluded between the investor and the administering agency (now, the AID), the investor pays a premium and he receives compensation for his losses, should any losses occur. Closer scrutiny, however, shows the intimate relationship of the program with public policy considerations. To be eligible for insurance, investments must be made in countries which have concluded special agreements with the United States. Present legislation allows the issuance of guarantees for investments in countries with which no formal agreement has been concluded, but this has been construed as applying to exceptional cases only and the Government is still promoting actively the conclusion of international guarantee agreements. Generally, and in many cases on the basis of express provisions in the agreements, the particular investment must also be approved by the government of the host country.

Programs very similar to that of the United States are in operation in Japan (since 1956) and the Federal Republic of Germany (since 1959). The principal difference between these programs relates to the degree of their dependence on a network of international guarantee agreements. The Japanese system operates without any such agreements. The German program may and has done so, but the German Government is actively promoting the conclusion of agreements. In this, the German system resembles that of the United States, but the two programs differ in the kind of agreement involved. The U.S. agreements are simple and limited: they specify the particular risks covered by reference to the U.S. legislation and provide for the subrogation of the U.S. Government to the investor's rights in the case of payment on a claim. The German agreements are more elaborate and deal with questions of substance; they are, in fact, short investment treaties and they have already been referred to in that context.

It should also be noted that in all developed countries (including the United Kingdom, France, Australia, Canada, Germany, and Japan) the function of export credit insurance programs which insure exporters (and in many cases foreign importers) against commercial and noncommercial risks in connection with export transactions involving the extension of credit, is closely related to that of investment guarantees. In the United States, such insurance is extended to exporters by the Export-Import Bank of Washington, either by itself or in association with the Foreign Credit Insurance Association. It is evident that some investors may take advantage of these programs, though they are directed at encouraging exports rather than investment as such.

For about the first 10 years of its operation, the U.S. investment guarantee program was little used by the investors. Since then, however, there has been a remarkable increase in their interest in and use of the program. On the other hand, in 1962 and 1963 the AID had to pay out for the first time compensation

for losses, though the total amount paid was very small and the final loss to the Agency will be even smaller.

Though basically a domestic program, operating under municipal law, the investment guarantee program of the United States can be better described as quasi-international in character, in view of the role of the international guarantee agreements and the necessity of continuing cooperation between the governments of the United States and of the countries of investment. The network of international agreements is certainly part of the strength of the program, since it gives to the insurer (the U.S. Government) and to the investors the assurance that the investment of private foreign capital in the particular country is welcomed or even encouraged. At the same time, the emphasis on these agreements imposes a definite limitation on the program, in view of the continuing unwillingness of several less developed countries to conclude such agreements with the United States. The reasons for this reluctance seem to be chiefly the fear that the provision for direct negotiations with the U.S. Government and the consequent bypassing of the international law requirements for seeking local redress as well as the power vested in the agencies of the U.S. Government to judge the character of specific measures of the capital-receiving country and determine whether they constitute expropriation or render a currency nonconvertible (though this determination is obviously not binding on the host country's government), constitute infringements of the host country's sovereignty. These fears seem to be progressively dispelled and in the last few years a number of countries which appeared previously to have such reservations have concluded guarantee agreements with the United States. Still, there remain several less-developed countries which have not concluded such agreements, or the agreements with which cover only one or two of the three categories of specific risks. The increased (though not indiscriminate) use of the statutory permission to issue guarantees even in the absence of intergovernmental agreements seems indicated to remedy this limitation on the program's operation, along with a continuing effort to secure the conclusion of more such agreements.

It is of interest to compare the language of the investment guarantee contracts with investors and that of the related general agreements between governments. The latter do not give any definition of the risks covered beyond referring to the U.S. legislation on the matter. The investor contracts, however, are fairly detailed in their description of the conditions under which a claim can be raised. There is then a possibility that in some cases certain measures of the capital-receiving country's government may be considered by that government as falling outside the agreement and by the relevant U.S. agency as justifying the payment on a claim. This should be seen as a calculated risk which the United States assumes, because a detailed agreement appropriately covering all possible points of dispute would be not only very difficult to prepare, but most probably quite unacceptable to many of the capital receiving countries. To the extent that investment guarantees cover risks which may not be covered in the intergovernmental guarantee agreements, they are an indirect and conditional subsidy to encourage private investment abroad.

MULTILATERAL INVESTMENT INSURANCE

In the past 2 years, attention has been devoted to the possibility of establishing a multilateral investment insurance program. Several nongovernmental agencies and private persons as well as some organs of the Council of Europe have made studies or suggestions on the matter, and the whole question was reviewed last year in an important study by the staff of the World Bank, which is now under consideration by the Development Assistance Committee of the OECD.

The individual proposals vary in their details, but most of them provide for an international agency, preferably the World Bank, in which both capital-importing and capital-exporting states would participate, and which would insure new private foreign investments in underdeveloped countries against the risks of inconvertibility, expropriation, and war losses. Some of the proposals go further and include among the risks those caused by indirect state action and revolution or civil war. The investor would pay premiums to the agency and he would be a self-insurer for at least 10 to 20 percent of the loss.

The idea is attractive. A multilateral investment insurance program would lead to considerable administrative simplification, would eliminate in great part the national political element in the existing programs, would make possible the insurance of joint investments by nationals of several states, and would result in the wider distribution of the risk of loss. However, several serious problems

will have to be resolved before it is realized. The delimitation of the risks to be covered presents difficulties, because in a multilateral instrument they will have to be described in detail. It is evident that many of the less developed countries (and even some of the developed) may object to too broad a definition, especially of the political risks. Generally, the participation of the capital-receiving countries in such a scheme is problematical: Why should they participate and thus share part of the risk when the national investment insurance systems now in operation offer them most of the advantages that are to be had? Even the agreement and continuing cooperation of all capital-exporting countries cannot be taken for granted; each of these countries has its own policies and interests with respect to foreign investment and to the less developed countries, in general. Finally, the successful operation of a multilateral insurance program presents several practical difficulties which may not be easily solved. National schemes possess considerable advantages in this connection because they do not have to solve their problems on the basis of a wide international consensus.

GUARANTEES BY CAPITAL-IMPORTING COUNTRIES

The guarantees most widely in use today are those offered to foreign investors by the governments of less developed countries. There is a great variety of devices and methods and wide differences in culture, politics, and economics between the countries using them, but it is possible to make certain generalizations which apply to the majority of the less developed countries, even if some details do not fit one or the other particular country.

The method that has been increasingly favored in recent years is the enactment of "foreign investment statutes"; that is, statutes specifically designed to provide protection and encouragement to foreign investment. Sometimes, the same kind of assurances is given by means of an official statement of policy concerning foreign investment, but this method has not been favored by the majority of less developed nations as well as by many of the foreign investors. Closely related to foreign investment statutes are the industrial promotion statutes, intended to encourage the investment of private capital, domestic as well as foreign, in certain fields of the economy (especially in industry). Such instruments are widely used in Latin America, together with or instead of foreign investment statutes. From the viewpoint of the foreign investor, the differences between the two kinds of statutes often appear unimportant, though he finds foreign investment statutes generally better suited to his needs and concerns. A recent United Nations compilation gives a total of over 55 states in which investment statutes (of either or both kinds) are in force; to these should be added at least 8 states where official policy statements are serving the same function. Thus, legislation designed to encourage foreign investment is today in effect in all of the French-speaking and most of the English-speaking new African States, in virtually all of Latin America and in many Asian and Middle Eastern States.

A definite pattern for investment statutes can be said to have emerged. The statute generally provides for the creation of a special governmental agency (an "investment center") charged with its implementation, to which prospective foreign investors submit their investment plans for "approval" or "registration." The agency studies the projected investment and examines its feasibility, its effects on the economy and on the balance of payments, its relationship to the operation of the national economic plan, wherever such a plan exists, and it approves, rejects, or, more often, asks the investor to modify the original plans. The final approval is usually marked by the issuance of an "instrument of approval" (or "certificate" or "contract") whereby the state promises to the investor some or all of the assurances provided for in the statute and the investor undertakes certain obligations regarding the form, amount, duration, and other particulars of his investment.

The specific assurances given to investors vary greatly. They generally include, in addition to the permission to proceed with the investment, promises of nondiscrimination, of free transfer abroad (sometimes within certain limits) of the profits and capital of the enterprise, exemptions from various kinds of taxes and charges (especially from import and export duties and restrictions) or, sometimes, a "freezing" of the income tax rates in effect at the time of investment. In many cases, the investor is also assured that his enterprise is not going to be expropriated by the government (often this assurance covers a specified length of time only) or that, if it is taken over, full compensation will be paid.

Assurances of this sort may be given in other ways, too. They may be included in a mining or petroleum concession contract or in a special agreement (sometimes in the form of a statute) between the host state and the investor. These alternative methods were more common in the past; today instruments of approval or similar instruments based on foreign investment laws are generally preferred, though with many variations in their form and content.

Foreign investment statutes present definite and important advantages for the foreign investor. First, they give him a chance for preliminary negotiations with a single competent agency of the host government, rather than a multitude of ministries and officials. He is able thus to find out the host government's attitude and intentions regarding the particular kind of investment and adjust to them (or refrain from investing) at an early stage and in an atmosphere of consultation rather than dispute or antagonism. Then the assurances given to the investor are specific and concrete; they apply to the particular investment involved and can generally form the basis for reasonable predictions. Since they are expressed in specific terms or figures, they are less subject to differences of interpretation, especially where minor officials of the host government are involved. Generally, the very fact that the investment has been properly "approved" or registered means that any action in violation or derogation of the assurances in the instrument of approval will have to be taken at a high governmental level and this generally is to the advantage of the investor. Moreover, he can have recourse to local tribunals to seek the implementation of the assurances given him and this again eliminates some possibilities of unfair treatment. Finally, and this is perhaps the most important consideration, through the conclusion of a contractual or semicontractual instrument of this sort, a whole system of legal relations between the host state and the foreign investor comes into being. Its breakdown, though possible, is more difficult than formal legal considerations might indicate. Given some adaptability and good faith on the part of both parties, such a system may operate under stress and adjust successfully to changing conditions. Instruments of approval or guarantee contracts then should not be understood as final, immutable agreements but rather as instruments outlining a kind of relationship and establishing a frame of reference for future developments.

Of course, investment laws and the procedures they establish are not perfect, nor are they always perfectly applied. The investor often meets confusion and inconsistency on the part of the agencies charged with the administration of the investment laws. He has sometimes to deal with a governmental bureaucracy antagonistic to foreign investors, rigid, arbitrary, and in some cases incompetent in the application of the statute. Official inquiries into the projected enterprise's plans and prospects are sometimes detailed to the point of absurdity and the standards of valuation of machinery or patents unfair to the investors. These faults can be corrected in time; there are other problems whose elimination is more difficult. Investment statutes and policies are subject to change, not only whenever the host country faces serious economic difficulties but also with a change of regime or even of government. The possibility of radical changes of this sort undoubtedly exists, though its probability is sometimes exaggerated. There is a strong contractual element in the instruments of approval or certificates given to the investor, an element sometimes stressed by the issuing government precisely because it generally affords to the investor greater protection. Despite some well-known cases, most successor governments do respect the previous governments' undertakings, if only because to violate them would result in serious international problems and in a decrease of the inflow of foreign capital. Under certain conditions, the violation of such an instrument may result in an act which is unlawful in public international law but there is considerable controversy and doubt as to exactly what these "certain conditions" are. The investor will find cold comfort in being the hero of a controversial and perhaps precedent setting international law case.

CONCLUDING OBSERVATIONS

In recent years, governments, international agencies, and private persons and associations have made great efforts to devise means by which the security of foreign investments in underdeveloped countries can be assured. It is not possible, at this stage, to give even a tentative assessment of the results of these efforts. The whole complex of means and methods is of quite recent origin. But even where certain guarantees have been in use for some time (at most about a decade), it is not easy to isolate the effects of the factors which

relate to the security of investments from other factors. The conclusion of a bilateral investment treaty or the enactment of an investment law has not brought about automatically an increase in the amount of foreign capital invested in a particular country. This is no indication of failure or uselessness, but it shows the complexity of the whole problem and also that there are certain limitations to the efficacy of all the guarantees discussed above. Awareness of these limitations is necessary for an appraisal of their value.

The assumption underlying the efforts and proposals of guarantees is that an increase in the amount of capital invested in less developed areas can be brought about by the provision of assurances regarding the security of investments. There is a great deal of truth in this proposition, but certain qualifications are necessary. First, the security of the investment is only one of several factors which the investor takes into account and probably it is not the most important. Security by itself, in the absence of other favorable factors, is not sufficient to induce the investor to bring his capital in a country. The actual value of the security factor will depend in each particular case on a variety of other factors. Secondly, to the extent that lack of security is a factor, no legal guarantee or scheme can fully eliminate it. The insecurity of foreign investments in the less developed countries is due largely though not solely, to certain objective conditions (such as social unrest or economic instability) which can be affected only to a limited extent by legal devices. Finally, legal devices of the kind examined here are only one kind of factor which affect the real security of the investment. Other factors such as the political stability in a particular country or the extent to which the investor can use self-help in protecting his own investment, are of importance and in many cases are controlling.

These considerations serve to qualify the potential role and present importance of investment guarantees. All-embracing schemes, such as the proposals for an investment code, are not only much more difficult to realize but also much less effective than less ambitious but more realistic programs. Of the multilateral schemes proposed, those relating to the establishment of a system for the settlement of disputes between investors and host states have the best chance of success. Such a system would be very useful in solving present disputes and setting the foundation for a future body of law and practice on investment matters. The proposals for multilateral investment insurance are more difficult to put into effect, but at least there are no serious dangers in attempting to realize them, as there are in the case of an investment code.

No multilateral guarantee program is today in operation, but guarantees in other forms—FCN treaties, investment insurance by capital-exporting countries, assurances through investment laws in capital-importing countries—are in use and have been used for some time. Though any final assessment of their success or failure is not yet possible, they can be studied in operation and their advantages and disadvantages compared.

The investment insurance programs of capital-exporting countries operate more smoothly than any other guarantee program. Within their limitations, they provide a high degree of certainty to the investor and they have the additional advantage of operating in a manner and an atmosphere which is familiar to him. Their main disadvantage, compared to the other forms of guarantee, is that their preventive or deterrent effect is limited. With respect to inconvertibility of currency and war losses, they cannot be said to provide anything more than insurance (not that this in itself is an insignificant function) though a certain element of deterrence does exist with respect to the expropriation risk. This limits their appeal to investors in certain situations.

Bilateral investment treaties, in their various forms, are international instruments, binding upon the parties. Their guarantees are thus backed by the existing machinery of public international law, such as it is. From the investor's point of view, their usefulness is limited by their restricted geographic coverage, the possibility of differences in the interpretation of their abstract and general language, and the need to have recourse to the Department of State and diplomatic proceedings for the enforcement of any right under the treaty. Still, these treaties are very useful as an indication that the capital-importing state is seriously concerned with attracting foreign investment and is conscious of the need for providing legal security. They constitute thus the background of any other more specific action of either state.

The chief virtue of the guarantees given by capital-importing states through instruments of approval and the like is that the content of the assurances is as a rule precisely determined with reference to the particular investment involved. Moreover, such guarantees often offer to the investor preferential treat-

ment, thus adding to the economic attractiveness of the investment. The real effect of the particular promises on the host country is not yet fully studied. Recent studies suggest, for instance, that tax incentives may not be as profitable to the host country's economy as they are often thought to be. However that may be, the effectiveness of such guarantees is limited, from the viewpoint of the investor, because they are to an important extent subject to state action on the part of the guaranteeing government. The probability of such action is a question of fact, which varies with each country.

These three forms of guarantee are not exclusive of one another. Rather, they are complementary: each one of them performs certain functions better than the others, but performs certain other functions worse; each one offers a different kind of protection to the investor. Thus, the guarantees contained in an instrument of approval provide to the investor a high degree of certainty with respect to the normal operation of his enterprise in the host country. Their value is enhanced when an FCN treaty is in existence since then it becomes more probable that the host state's specific promises to the investor will be carried out. At the same time, the investment guarantees given by the capital-exporting state provide insurance against damage suffered because of exceptional economic or political conditions (inconvertibility, war loss) or because of radical measures directed against the investor (expropriation). It is clear that all three of these forms of guarantee are useful and there is ground for the promotion and improvement of each one of them.

It is also necessary, however, to look further and examine the underlying factors, the very causes of instability and insecurity. There is much that can be done for the improvement of attitudes and objective conditions on both sides, on the part of the private investors as well as on the part of the less developed countries. Legal problems and legal considerations should not be allowed to obscure the realities behind them. The legality of a measure is quite distinct from its usefulness or appropriateness. The host country may have the "right" to nationalize a foreign enterprise but the real question is whether it should do so; measures which are fully legal may well create a climate of insecurity. On his part, the investor could do well to consider whether it would pay in the long run to seek to enforce a particular right at some particular point. Moreover, it should be fully understood that it is at the time of investment that the competent authorities of host countries and the prospective foreign investors can work out a useful framework for future relations. Neither side wins by striking an initial "good bargain"; it is to the continuing relationship based on the community of interests of investor and host country that their attention should be focused. It is by study of and respect and concern for the realities behind the legal appearances that security for foreign investments can be achieved in the long run. Guarantees and other devices are useful as stopgap measures for perhaps a considerable length of time and as factors contributing to the establishment of such security.

Senator SPARKMAN. Now, Mr. Rublee, will you present your discussion?

STATEMENT OF GEORGE RUBLEE, ASSISTANT GENERAL COUNSEL FOR PRIVATE ENTERPRISE, AGENCY FOR INTERNATIONAL DEVELOPMENT

Mr. RUBLEE. Thank you, Mr. Chairman. Mr. Chairman and members of the subcommittee, it is an honor to appear here today.

My principal assignment in the Agency for International Development for the last 2 years has been the specific risk investment guarantee program—one of the programs for encouraging private participation in economic development which are under the operation and control of Mr. Seymour Peyser, who, unfortunately, could not be here today because he is in the hospital.

We hope to have him back on the job very soon.

Mr. Chairman, your kind letter of last week indicated that the committee would like some information on the scope and importance of U.S. private investment guarantees.

I think statistics tell us this better than anything else. In my statement, there are some figures which show that between 1949, when the specific risk investment guarantee program started, and December 31, 1961, guarantees had been issued amounting to slightly over $600 million.

In 1962, guarantees amounting to more than $400 million had been issued. These are calendar years.

In 1963, guarantees amounting to more than $360 million were issued. In the last 2 years, this program has more than doubled the activity in the preceding 12 years.

The committee is interested in Latin America. In the last 3 months, October, November, December of 1963, specific risk guarantees amounting to over $158 million were issued covering new U.S. investment, private investment in Latin America. That compares with coverage amounting to $72 million in the preceding 15 months.

I think it is fair to conclude that the program is of significant interest to U.S. investors, particularly with respect to activities in Latin America.

I would like to summarize, if I might, the purpose of these guarantees. What exactly do they try to cover? I will touch also on the intergovernmental agreements which establish the guarantee program.

The oldest form of investment guarantee currently in use is the specific risk guarantee. These cover certain abnormal political risks that might otherwise prevent investors from evaluating a business opportunity in developing countries. The risks are the possibility of inconvertibility of currency, expropriation, physical damage from war, revolution, and insurrection.

This program was available in the Marshall plan countries until 1959, when its availability was limited to the developing countries. It is presently available in 55 countries. (I wrote that on Friday and it is 56 today, because another one came in on the weekend.) In Latin America, the program is now available in 17 of the 21 American Republics that receive some economic assistance from the United States and we are talking with the governments of the other 4. We have some indications that we are going to be successful, that this exercise of persuasion is going to result in the program being instituted.

The agreement that we seek with another government in order to set up the guarantee program provides for the right of the United States in connection with property transferred to the United States by investors who receive compensation. For example, an inconvertibility guarantee protects the interests of a private U.S. businessman in the country whose dollar reserves are so short that he cannot transfer his foreign currency earnings into dollars. The United States purchases such local currency, and under the intergovernmental agreement the foreign government recognizes that, first, the United States may freely use the currency locally, and second, that the United States may sell

the local currency for dollars when private U.S. investors in that country can again freely convert.

We get an undertaking by the host countries to recognize the transfer of assets to the United States and the right of the United States to transfer good title to businesses and to land. We get an undertaking that any international law problem arising out of the foreign government's treatment of a guaranteed U.S. investor will be a fit subject for intergovernmental discussion and if not satisfactorily resolved in that discussion, will be settled by arbitration. There is a deadline on that. The arbitration is to be in accordance with international law principles. This is really the heart of our agreement, because this undertaking on the part of a host country represents an undertaking to have their treatment of a private investment measured against international law standards. This is a very significant thing, and it improves the climate for private investment sufficiently so that some private investors will invest in such countries without the guarantees.

We have an extended risk guarantee program which is a credit guarantee. We guarantee repayment of a portion of the principal of a loan. We don't care what the cause of the failure of the borrower to repay was—if it was not the result of misconduct of the investor or if it was not a result of normally insurable risks such as fire or damage.

There is a special version of the extended risk guarantee with respect to Latin American housing, reflecting the enormous priority attached to the development of housing in the Latin American countries. Both these extended risk programs have recently started to move and the housing program is moving particularly quickly.

I have included in my prepared statement some suggestions by business groups for improvements in the program. I won't go through those one by one. I will say simply that we have carried out most of the suggestions that have been made to us. If you have any questions, I will be delighted to answer them.

Senator SPARKMAN. Thank you very much. As I stated, your statement and suggestions also will be printed in full.

(The complete prepared statements of Mr. Rublee and a statement on private enterprise in the Alliance for Progress follow:)

AID INVESTMENT GUARANTEES WITH SPECIAL REFERENCE TO LATIN AMERICA

(By George Rublee, Assistant General Counsel for Private Enterprise, Agency for International Development)

Mr. Chairman and members of the committee, it is an honor to appear here today. It is regrettable that Mr. Seymour Peyser, who is in operational charge of most of our foreign aid programs designed to encourage private participation in the task of economic development, is in the hospital. As Mr. Peyser's lawyer in these programs I shall try to give you the information that he would have presented had his health permitted.

Specific risk guarantees.—The most frequently used U.S. governmental guarantees of new investment in the developing countries are the so-called specific risk guarantees. These protect investment and earnings thereon equal to the amount of the original investment against loss from inconvertibility of foreign currency, from expropriation, and from war, revolution, and insurrection.

Brief history.—The specific risk program started in 1949 as part of the Marshal plan. In 1959 Congress stopped the issuance of any more guarantees for investment in most of the Marshal plan countries. That year the foreign aid legislation was amended to limit the program to the developing countries. (A list of these wherein the program is presently available appears in the attached exhibit A.)

Geographic availability.—At the present time the investment guarantee program has been instituted in 55 of the developing countries. The program now is effectively available in 17 of the 21 Latin American Republics that receive economic assistance from the United States.

The four remaining Latin American Republics are Peru, Uruguay, Brazil, and Mexico. Peru has agreed to the part of the guarantee program protecting against inconvertibility of earnings, and in fact nearly $12 million of such guarantee coverage is presently outstanding for U.S. private investment in Peru. Further there have been active negotiations with the Peruvian Government concerning instituting the full program. These are still going on.

Uruguay has signed the agreements to institute the program, but under Uruguayan law these cannot be implemented until ratified.

There have been negotiations with the Government of Brazil going into the details of the agreement to set up the program. Last spring, the Government of Mexico requested copies of the draft agreement.

Intergovernmental agreements.—A brief description of the nature of and reasons for the intergovernmental agreements setting up the guarantee program may be helpful.

The agreements, in essence, contain the following:

A recital that the purpose of the guarantee program is to further the development of the economy of the host country;

An undertaking by the United States not to guarantee investment in a project which has not been approved by the host country;

An undertaking by the host country to recognize the validity of transfers of assets from guaranteed investors to the United States in return for compensation under a guarantee;

An undertaking by the United States not to convert local currency acquired pursuant to inconvertibility guarantees until private U.S. investors in the host country can again effect conversion;

Undertakings by both the host country and the United States to resolve differences between them on whether the treatment accorded guaranteed investments complies with international law standards, first, through negotiation and if agreement is not promptly achieved there, then by reference to an impartial arbitral tribunal.

Not the least important reason for having these agreements is that their existence alone, without more, frequently serves to improve the climate for private investment. Since the agreements express a willingness on the part of the host country to have its treatment of foreign investment tested against international law standards, some investors go forward on that basis alone and invest without seeking guarantees.

The agreements, in addition to establishing a procedure for the resolution of international law questions arising from the treatment of guaranteed investors, also work out arrangements for the subrogation of the United States to the property, including claims, of guaranteed investors.

The project approval procedure provides a mechanism to discover in advance of investment whether the project is favorably or unfavorably regarded by the host country government.

Finally, the agreements are required by U.S. statute.

Extended risk guarantees.—In addition to the specific risk guarantees, new U.S. investment in the developing countries may be guaranteed against such additional risks as the President may determine, provided, that no more than 75 percent of the investment (other than loans for housing) may be covered, and provided further that coverage will not apply to loss from normally insurable risks like fire and theft or to loss resulting from the investor's own misconduct.

Several months ago the first of these guarantees was issued to cover investment in a petrochemical complex in Argentina. If the investment goes through,

it will result in the largest privately financed project outside of the industrialized countries.

Discussion of this project for a moment may indicate some aspects of the usefulness of guarantee programs.

Financing arrangements for the project had been put together several years ago. About half the potential investors were from countries which do not have investment guarantee programs. Not being U.S. citizens or firms, they were not eligible for our guarantees. Subsequent to those financing arrangements the value of the Argentine currency depreciated by 50 percent; there were also several revolutions. Most of the unguaranteed investors withdrew; those holding specific risk guarantees have stayed; the extended risk guarantees have been offered to investors who will replace the dropouts.

Latin American housing guarantees.—There is a third type of U.S. governmental investment guarantee. This provides extended risk coverage for up to 90 percent of long-term mortgage financing made available by U.S. investors for housing projects in Latin America. Two of these guarantees covering $9,360,000 have been issued, and eight covering $44 million have been approved.

Specific risk performance.—The specific risk investment guarantee program has been in existence since 1949 and is the principal source of experience with governmental guarantees of investment.

Between 1949 and December 31, 1961, guarantees had been issued amounting to $631,872,073. In 1962, 138 guarantees were issued amounting to $440 million. In 1963, 167 guarantees were issued amounting to $362 million. The activity of the past 2 years has more than equaled that of the preceding 12 years.

Turning to Latin America, we see that in the period June 30, 1962, to September 30, 1963, the amount of outstanding guarantee coverage increased by $72,200,000 from $170,600,000 to $242,800,000.

In the last 3 months of calendar year 1963, however, guarantee coverage of $158,432,131 was issued for U.S. investment in Latin America. This would indicate that investments covered by guarantees are a significant portion of total new U.S. investment being made in Latin America.

The guarantee program has nonetheless reached only a small way toward its potential effectiveness for Latin America.

Evaluation of the 1963 figures should, for example, take into account that the guarantee program has really just started in both Colombia and Venezuela. It is not yet really underway in Chile where the intergovernmental agreement establishing the full program was reached in December. In Colombia and in Venezuela lack of procedures to approve projects in which U.S. investment is to be guaranteed has held up the issuance of guarantees and in a number of cases held up the making of investments.

Colombia finally established its project approval procedures last summer. Although the amount of guarantee coverage being sought for U.S. investment in Colombia on September 30, 1963, was $223,300,000, not one guarantee had been issued by that date. Only two guarantees providing coverage of $1,010,000 have been issued subsequently.

In Venezuela the project approval procedure started last spring. As of September 30, 1963, guarantee coverage sought was $103,600,000. Outstanding guarantee coverage on that was $1 million. This was increased by $30,550,000 of coverage issued in the final quarter of 1963.

In Chile, which signed the agreement in December, requests for guarantee coverage on September 30, 1963, amounted to $106,200,000. Naturally no guarantee coverage was then outstanding, and none has yet been issued.

In all three of those countries, unless something extremely unexpected happens, the amount of investments and the amount of guarantees should increase substantially in 1964.

It has been stated earlier that execution of the agreement setting up the program in and of itself arouses investor interest. The Colombian experience supports this. On September 30, 1962, the investment guarantee coverage sought for Colombia was $137 million. Even though Colombia had not until mid-1963 started to implement the guarantee program, requests for coverage increased by $90 million during the year following signing of the agreement.

Investor criticism.—There is much that the U.S. Government has done and should continue to do to improve its handling of the investment guarantee program. The most recent written evaluation of the program by users of it is contained in the report of the Commerce Committee for the Alliance for Progress. That report made seven recommendations which are set out below with comment.

"1. Extension of investment guarantees to all less developed countries of the Western Hemisphere."

As discussed above, the program has been agreed to by 17 of the 21 Latin American Republics. We are continually working to broaden its availability. Mr. Bell has testified before the Clay Committee and before the committees of Congress dealing with the foreign aid legislation that this task is a matter of persuasion, of overcoming emotional prejudices. Progress has been made. Of those 17 Latin American countries that have agreed to the program, Argentina, Colombia, Chile, the Dominican Republic, Jamica, Trinidad-Tobago, and Venezuela signed agreements instituting the full program within the last 15 months.

"2. Broadened application of extended risk coverage."

As indicated above in the discussion of the petrochemical project in Argentina, the extended risk guarantee authority has now been put to use. Operational responsibility for this program has also in the past month been shifted from the AID regional bureaus to Mr. Peyser's Private Enterprise Office which also administers the specific risk guarantee program.

"3. Extension of war risk coverage, including revolution and insurrection, to also include damages resulting from riots and civil disturbances."

In the past year contracts have been issued providing the expanded coverage authorized in 1961. This new coverage includes loss from revolution and insurrection with loss from war. Congress had been reluctant in prior years to go as far as it did in 1961. Commercial insurance policies are available for property damage arising out of riots and civil disturbances. It is our belief that a broad interpretation of revolution and insurrection to include damage resulting from acts of Communist groups and other organized revolutionary forces should meet the primary need not now covered by commercial insurance. It would be our opinion that most of the damage that has occurred in Venezuela recently is of the type that would be covered under our present form of guarantee against loss from revolution and insurrection.

"4. Revision of present contract procedures and fee schedules to provide for a multirisk contract where an investor elects to take two or more specific-risk guarantees."

During the past year we have been working on a revision of the guarantee contract. The revised contract would lump all three specific risk contracts together unless the investor elected not to take a certain coverage or unless the intergovernmental arrangements with the host country did not permit a certain coverage. A revision in the fee is being studied in connection with the revision of the basic guarantee contract form.

"5. Standardization and simplification for contract language."

Frequently investors or their counsel suggest, in the process of discussing draft guarantee contracts, language which does simplify and clarify prior provisions. A number of these suggestions have been incorporated in the current contract forms. In addition these suggestions are being put into the major revision of the contracts which has been underway for a year and which we expect to test out with investors in the near future.

"6. Increase in the authorized statutory limits of different kinds of guarantees."

The 1963 amendments to the Foreign Assistance Act would increase the statutory limits on the outstanding amounts of specific risk and Latin American housing guarantee coverage. The general extended risk ceiling was not raised although authority to issue extended risk guarantees was advanced from June 30, 1964, to June 30, 1965.

The present statutory limits and present outstanding amounts are shown below:

Type of guarantee	Statutory limit	Outstanding coverage
Specific risk	$2,500,000,000	$1,125,900,000
Extended risk (general)	180,000,000	8,325,000
Latin American housing	150,000,000	9,460,000

"7. Recommendation that processing fee, if adopted, be credited against initial fee payable by investors entering into final contract."

This recommendation relates to a suggestion that AID should begin to charge a processing fee as one step to clear away the thicket of pending applications. The idea of the processing fee is that it would eliminate some applications which never will be perfected. Approximately two of every three applications have in the past lapsed, generally because the investment was not made.

While AID is not now seriously examining adopting a processing fee, if one is adopted, the above recommendation will certainly be considered.

Application handling.—One principle should be kept in mind when evaluating the process of handling guarantee applications. The principle is that guarantees are available only for new investments. (New investment is defined to include expansion or modernization of existing facilities.)

The immediate result of this principle is that a routine had to be devised for distinguishing new from old investments. This routine has consisted of an investor informing AID prior to being committed to an investment that he contemplates it. AID then replies with a waiver letter which tells the investor that the investment he subsequently becomes committed to make will be considered on its merits as a new investment by the Investment Guaranties Division. Adherence to this routine has resulted in the awesome backlog figures which, despite the increased rate at which guarantees are issued, have grown from $2 billion to $5 billion in the last 2 years. Not very many of those applicants are in fact ready for guarantees.

Another aspect of the processing is that the applications generally lie dormant for several years and then spring to life with a considerable sense of urgency. This is going to remain true so long as the guarantee program remains, as it should, responsive to investors' needs.

In recognition of the fact that applications should be reviewed and potential investors given certain advice long before the pressure of deadlines and closings arises, the Investment Guaranties Division is organized into an application branch and several contract issuing branches. The application branch processes requests for waivers, assists investors in getting project approval from the host country and obtains U.S. field reaction to the project.

The contract issuing branches then take over the application, draft guarantee contracts, obtain clearance of the draft contracts from the General Counsel's office and discuss the contracts with the investor. These branches also keep up the work on outstanding guarantees. This includes reviewing progress reports concerning the project, responding to requests by the investor for changes in coverage as the amount of investment at risk changes, and processing assignments.

AID has in the past year added staff to this operation and plans to increase that still further. The introduction of machine records is being studied. As mentioned earlier the forms of guarantee contracts are being revised and consolidated. These are steps designed to make the guarantee program quickly responsive to investors' needs.

General goals.—In concluding it seems appropriate to state the general goals of the investment guarantee programs, particularly regarding the Alliance for Progress.

The Clay Committee report of last March eloquently stated the importance to the Alliance of private participation:

"We must continue to assume leadership with Latin Americans in stimulating the offering of incentives to the private sector which are required if Latin American development goals are to be attained. Impediments to the growth of private enterprise must be identified and treated, the shallowness and harm of doctrinaire biases against responsible private enterprise exposed, new sources of credit opened to medium and small Latin American businessmen, and foreign investment encouraged in the confidence that all governments now have means to protect themselves against potential abuses. * * * Latin America must be encouraged to see its essential choice between totalitarian, inefficient, state-controlled economies and societies on the one hand, and an economically and politically freer system on the other, realizing that a society must begin to accumulate wealth before it can provide an improved standard of living for its members. We believe the increasing acknowledgment that proper incentives to the private sector are required for dynamic growth must be accompanied by sustained U.S. and Latin American efforts and decisions at all levels of government policy and action. With such as basis, a more progressive Latin American private enterprise spirit, substantial foreign investment which receives no more and no less than fair treatment, and other Alliance aid, the development of Latin America would be assured."

Investment guarantees are specific measures for obtaining private participation in the developmental process not only in terms of the money and skills required for individual projects but also in terms of judgments on the desirable areas of new economic activity. The specific risk guarantees by blocking out the abnormal risks of inconvertibility, expropriation, war, revolution, and insurrection, permit private investors to evaluate normal business risks. The selection process of free enterprise is thus allowed to operate.

Private enterprise can contribute much to the attainment of the basic national objectives that have led the United States to start and to continue its foreign aid programs. These are, first, the goal of mutual security, to provide economies of sufficient strength to support stable governments which can resist Communist infiltration. Next, the moral goal, to see societies in which men may be free. Third, the desire to improve our economic self-interest by improving the abilities of other countries to trade with us on a mutually advantageous basis.

All three of the basic objectives call for improvement of the economies in the developing countries. We have too frequently and too recently seen in this century the vulnerability to dictatorship of countries whose economies are either disrupted by war or which have never been developed. Responsible governments, stable governments have great difficulty in surviving when large portions of the country's populace do not have the opportunity to obtain for their work remuneration which is adequate to maintain life and hope. Finally the United States as an exporter of food and manufactured goods cannot sell these to countries which do not have the capacity to earn the dollars to pay for them.

Today when a major goal of the foreign aid program is to phase itself out as soon as its objectives have been accomplished, private investment is increasingly important not only to assist in the phaseout but to provide a continuing mutually beneficial economic relationship when aid has terminated.

27-779—64——12

EXHIBIT A

INVESTMENT GUARANTIES DIVISION,[1] OFFICE OF DEVELOPMENT FINANCE, AGENCY FOR INTERNATIONAL DEVELOPMENT, WASHINGTON, D.C.

Countries where investment guarantees are available, Jan. 15, 1964

Convertibility	Expropriation	War risk
Afghanistan.	Afghanistan.	Afghanistan.
Argentina.	Argentina.	Argentina.[1]
Bolivia.	Bolivia.	
Chile.	Chile.	Chile.[1]
China, Republic of	China, Republic of	China, Republic of.[1]
Colombia.	Colombia.	Colombia.[1]
Congo (Brazzaville).	Congo (Brazzaville).	Congo (Brazzaville).[1]
Congo (Léopoldville).	Congo (Léopoldville).	Congo (Léopoldville).[1]
Costa Rica.	Costa Rica.	
Cyprus.	Cyprus.	Cyprus.[1]
Dominican Republic.	Dominican Republic.	Dominican Republic.[1]
Ecuador.	Ecuador.	Ecuador.[1]
El Salvador.	El Salvador.	
Ethiopia.	Ethiopia.	
Gabon.	Gabon.	Gabon.[1]
Ghana.	Ghana.	
Greece.	Greece.	Greece.[1]
Guatemala.	Guatemala.	
Guinea.	Guinea.	Guinea.[1]
Haiti.	Haiti.	
Honduras.	Honduras.	
India.	India.	
Iran.	Iran.	
Israel.	Israel.	Israel.[1]
Ivory Coast.	Ivory Coast.	Ivory Coast.[1]
Jamaica.	Jamaica.	Jamaica.[1]
Jordan.	Jordan.	Jordan.[1]
Korea.	Korea.	Korea.
Liberia.	Liberia.	Liberia.
Malagasy, Republic of.	Malagasy, Republic of.	Malagasy, Republic of.[1]
Malaya, Federation of.	Malaya, Federation of.	
Morocco.	Morocco.	Morocco.[1]
Nepal.	Nepal.	Nepal.[1]
Nicaragua.	Nicaragua.	Nicaragua.
Niger.	Niger.	Niger.[1]
Nigeria.	Nigeria.	
Pakistan.	Pakistan.	
Panama.	Panama.	Panama.
Paraguay.	Paraguay.	
Peru.		
Philippines.	Philippines.	
Portugal.	Portugal.	
Senegal.	Senegal.	Senegal.[1]
Sierra Leone.	Sierra Leone.	Sierra Leone.[1]
Spain.	Spain.	
Sudan.	Sudan.	Sudan.
Tanganyika.	Tanganyika.	Tanganyika.[1]
Thailand.	Thailand.	Thailand.
Togo.	Togo.	Togo.[1]
Trinidad-Tobago.	Trinidad-Tobago.	Trinidad-Tobago.[1]
Tunisia.	Tunisia.	Tunisia.[1]
Turkey.	Turkey.	
United Arab Republic (Egypt).	United Arab Republic (Egypt).	United Arab Republic (Egypt).[1]
Uruguay.[2]	Uruguay.[2]	
Venezuela.	Venezuela.	Venezuela.[1]
Vietnam.	Vietnam.	Vietnam.[1]
Somalia.	Somalia.	Somalia.[1]

[1] Including also guarantees against loss due to revolution and insurrection; also extended risk.
[2] Although applications will be accepted for Uruguay, guarantees cannot be processed until agreement is ratified by country's legislative body.

Although the Mutual Security Act of 1959 excluded economically developed countries for purposes of the investment guaranty program, guarantees are still available for the underdeveloped oversea dependencies of the following countries:

Convertibility:	Expropriation:
Denmark	Denmark
France	France
Netherlands	Netherlands
Norway	Norway
United Kingdom	

The following countries also have signed the agreement to participate in the investment guaranty program but due to the Mutual Security Act of 1959 guarantees may no longer be issued for investments there:

Austria	Italy
Belgium	Japan
Finland	Luxembourg
Germany, Federal Republic of	Yugoslavia
Ireland	

Cuba signed the agreement in 1957 for convertibility and expropriation but due to conditions existing in that country the program is inoperative there.

Supplemental Statement by Mr. Rublee on Investment Guarantees and Other Incentives to Private Enterprise in Latin America

I. General

The success of the Alliance for Progress can be insured only if there is an effective synthesis of private investment with government assistance and the contributions of voluntary, noncommercial organizations. The Charter of Punta del Este, signed by all Alliance member nations, stressed the need for private capital participation—internal and external—if the Alliance is to fulfill its mission.

Increased participation of private enterprise is required since—

(1) Private enterprise possesses a vast amount of the technical know-how which must be mobilized in the industrial and agricultural growth efforts of the Latin American countries.

(2) Public capital resources are far from sufficient in themselves to meet the demands of economic development in Latin America. It has been estimated that substantial new private investment must flow from the United States and other industrialized nations to Latin America, to meet the goals of the Alliance Charter for development programs.

(3) Private investment provides important stimuli for economic democracy, contributing to the distribution of wealth and material resources, and through competition, to the provision of more varied and better quality products. This contribution of private enterprise is essential for giving meaning to development along democratic lines.

(4) It will be largely the task of private initiative to maintain growth in these countries when the Alliance's basic goals have been achieved and the foreign aid program as such is phased out.

The U.S. Government, in cooperation with the Latin American nations has implemented a number of practical programs to encourage private sector growth.

The investment guarantee program has been available to U.S. private investors since 1948. As of December 31, 1963, guarantees of U.S. investment against certain risks in Latin America totaled $438 million. About 86 percent of the total dollar amount issued for Latin America has been committed since the inception of the Alliance for Progress.

Last year the Congress authorized an all-risk insurance program. Eleven guarantees, totaling nearly $61 million, have been approved through January 20, 1964, for housing projects in Argentina, Chile, Colombia, Peru, Mexico, Honduras, El Salvador, and Panama.

The guarantee of U.S. investment in Latin America contributes to Latin American development and encourages U.S. business to participate in that development. Just as significant, the principle serves to make Latin American governments acutely aware of the need to provide a secure climate for their own investors,

thereby reducing capital flight and directing investment toward development needs.

AID was granted authority under section 231 of the Foreign Assistance Act to participate in up to 50 percent of the cost of investment surveys. These explore the feasibility of contemplated private investments which will contribute to the achievement of AID objectives in the developing countries. As of December 9, 1963, 29 applications with a total possible cost to AID of $261,000, had been approved for surveys in Latin America in such industries as building materials, automobiles, food processing, and wood and paper. Only if the investment is not finally made would AID reimburse the sponsor for one-half the cost of the survey. If the investment is made, the entrepreneur must bear the full cost of the survey. Approvals to date could result in a total private investment of about $83 million (of which about $16 million would be U.S. investors' equity).

U.S. private enterprise also is benefiting from the so-called Cooley loans—which are extended out of the local currency funds generated by the sale of U.S. surplus commodities under Public Law 480. From the inception of the program through June 30, 1963, 56 of these Cooley loans, amounting to the equivalent of almost $20 million, had been authorized for use in Latin America.

AID may also make dollar loans to either U.S. or foreign private borrowers or joint ventures, if other financing is not available.

AID has put increasing emphasis on loans to intermediate credit institutions in Latin America, which relend to private firms or individuals for projects contributing to economic growth, for housing, and for supervised credit to help farmers increase their yields through more efficient techniques. Such loans which are now active or recently authorized total more than $270 million.

For Latin American business, there is an industry loan program designed to stimulate expansion of existing plants or establishment of new ones. Since the beginning of the Alliance for Progress, the Export-Import Bank has made loans to private enterprise totaling over $70 million. The Social Progress Trust Fund administered by the Inter-American Development Bank (IDB) for the United States, has made loans to private enterprise or to intermediate credit institutions totaling more than $50 million.

II. INVESTMENT GUARANTEE ACTIVITY IN LATIN AMERICA

Guarantees issued

As of December 31, 1963, guarantees issued for investments in Latin America totaled approximately $438 million—$285 million against inconvertibility of currency, $142 million against expropriation, and $11 million against war risks. Of these, approximately $400 million remain outstanding.

In the quarter from September 30 to December 31, 1963, $158 million in guarantees was issued for Latin America, almost doubling the activity of the previous 15 months.

Eighty-six percent of the total dollar amount of guarantees issued for Latin America has been committed since the inception of the Alliance for Progress program—approximately $377 million issued in 30 months, against $61 million in the previous 13 years of the guarantee program.

It should be noted that in a number of cases, the same investment has been guaranteed against several risks and thus, total figures would be greater than would be the total amount of investment involved.

Applications in process

As of September 30, 1963, applications were in process for all of the participating Latin American countries, as well as for Uruguay. The total for all guarantees under consideration for Latin America as of September 30, was close to $3 billion. During the quarter ended December 31, 1963, an additional 94 applications were received with a total value of close to $800 million.

Analysis of specific risk investment guarantees issued—Latin America

[In millions]

	Total	Convertibility	Expropriation	War risk
Cumulative (from beginning of guarantee program) through Dec. 31, 1963	$438.0	$285.1	$141.5	$11.4
Total since inception of Alliance (fiscal year 1962) to Dec. 31, 1963	376.7	253.1	112.2	11.4
Fiscal year 1963 guarantees	68.7	66.5	2.2	
Fiscal year 1964 guarantees to Sept. 30, 1963	19.9	17.3	2.6	
Sept. 30 to Dec. 31, 1963	158.2	47.9	98.9	11.4

Specific risk investment guarantees issued beginning of guarantee program through Dec. 31, 1963—Latin America

[A total of $438,000,000 in guarantees has been issued for Latin American investment, from the inception of the program through Dec. 31, 1963. Most of this activity has occurred since the inception of the Alliance for Progress. Guarantees issued, by country and type of risk covered, follow]

[In millions]

Country	Total	Convertibility	Expropriation	War risk
Argentina	$311.5	$235.7	$75.8	
Bolivia	21.3	1.2	20.1	
Colombia	1.0	.5	.5	
Costa Rica	1.4	.4	1.0	
Ecuador	7.7	4.0	3.7	
El Salvador	2.4	1.2	1.2	
Guatemala	3.2	.4	2.8	
Haiti	4.5	2.0	2.5	
Honduras	11.3	1.6	9.7	
Jamaica	.2	.2		
Paraguay	10.8	3.9	6.9	
Peru	13.4	13.4		
Trinidad-Tobago	17.7	17.7		
Venezuela	31.5	2.9	17.3	$11.4
Total	438.0	285.1	141.5	11.4

NOTE.—Columns may not add to totals due to rounding.

Investment guarantee availability

[Investment guarantees are available for investment in 18 Latin American countries. The risks presently covered in the participating countries follow]

	Convertibility	Expropriation	War risk
Argentina	X	X	X.[1]
Bolivia	X	X	
Chile	X	X	X.[1]
Colombia	X	X	X.[1]
Costa Rica	X	X	
Dominican Republic	X	X	X.[1]
Ecuador	X	X	X.[1]
El Salvador	X	X	
Guatemala	X	X	
Haiti	X	X	
Honduras	X	X	
Jamaica	X	X	X.[1]
Nicaragua	X	X	X.
Panama	X	X	X.
Paraguay	X	X	
Peru	X		
Trinidad-Tobago	X	X	X.[1]
Uruguay [2]	X	X	
Venezuela	X	X	X.[1]

[1] Includes also extended-risk guarantees and loss due to revolution and insurrection.
[2] Although applications will be accepted for Uruguay, guarantees cannot be processed until agreement is ratified by Uruguay's legislative body.

Specific risk investment guarantees applications in process, Sept. 30, 1963—Latin America

[In millions]

	Convertibility	Expropriation	War risk
Argentina	$379.5	$467.5	$218.0
Bolivia	6.7	7.1	----------
Chile	106.2	----------	----------
Colombia	223.3	182.4	112.4
Costa Rica	53.2	50.0	----------
Dominican Republic	59.5	53.8	30.6
Ecuador	10.9	9.6	0.5
El Salvador	23.7	17.7	1.2
Guatemala	40.6	42.5	----------
Haiti	15.8	14.7	----------
Honduras	20.1	31.1	----------
Jamacia	45.8	40.8	25.2
Nicaragua	19.7	20.9	9.2
Panama	11.2	18.1	9.5
Paraguay	5.4	14.4	----------
Peru	84.9	----------	----------
Trinidad	43.8	43.7	40.3
Uruguay	5.5	4.7	----------
Venezuela	103.6	117.3	69.6
Total	1,259.4	1,136.3	516.5
Grand total	2,912.2		

NOTE.—With French, Netherlands, and British dependencies added, the grand total comes to $2,926.6.

Senator SPARKMAN. Let me ask a question. You used the date 1949. Is that when we started the guarantee program in the Marshall plan?

Mr. RUBLEE. Yes, sir; the Marshall plan, of course, was started in 1948. The guarantee program came in the next year.

Senator SPARKMAN. Yes; and it has been going ever since, and we have been adding to it from year to year?

Mr. RUBLEE. Yes, sir.

Senator SPARKMAN. As a matter of fact, you mentioned the stepup over the last couple of years. That was really brought about by our stepped-up guarantee program, particularly in the Latin American area, was it not?

Mr. RUBLEE. I think the enormous increase in the amount of guarantees is attributable to the desire of U.S. businessmen to cover themselves in Latin America. Nobody had taken out this insurance policy, if you will, in Cuba. There was not one single penny of U.S. private investment guaranteed against expropriation under this program in that country although the program was available to them. A great many investors decided that this mistake would not be made again.

Senator SPARKMAN. Let me ask, and this will be my final question, because I want my colleagues to have some time—before the guarantee becomes effective in any country, there has to be a treaty between that country and this country, an agreement; is that not true?

Mr. RUBLEE. The statute authorizing these guarantees requires that there be an agreement between the United States and the host country to have the program operating. The statute also requires that there be suitable arrangements to protect the interest of the United States in connection with its position after paying compensation under a guarantee. These later provisions do not have to be incorporated into a formal agreement. Mr. Frank Coffin's testimony 2 years ago when the statute was revised on this point indicated that suitable arrangements need not be incorporated in a formal agreement, that they

could even be found in the history of the host country, a good record of treatment of private investment.

Senator SPARKMAN. Mrs. Griffiths?

Representative GRIFFITHS. How do you set the rate? How do you determine the rates?

Mr. RUBLEE. We inherited the rates. The rates, incidentally, are half a percent of the amount of coverage in force and a quarter of a percent of the amount of potential coverage beyond that in force. Most investment goes in in increments, and people don't take out the maximum amount of insurance in the beginning.

The American Actuarial Association was called in a year and a half ago to study whether an actuarial basis for the rates could be found in the nature of the risks, the nature of the program. As you know, we constantly shift from one area, when a fire has been put out, to another area where a fire is raging. The shift from the Western European countries to the developing countries was not the kind of shift insurance companies would make. The actuaries said "You are really not selling insurance. It might look like insurance, but there is no actuarial basis. You are constantly intensifying your risk. That is the reason you exist, because most insurance companies could not do that."

We are carefully evaluating the occasional criticisms we get from investors as to the fees. It has not been our experience that we have actually driven away any investor with these fees. I think it is appropriate for an investor to pay some fee. It keeps away a frivolous use of the program and covers part of the cost of administering the program.

Representative GRIFFITHS. Have you lost any money?

Mr. RUBLEE. An incredibly small amount, compared to the amount of liability. There was $650,000 paid out to U.S. banks as a result of a Development Loan Fund guarantee, a predecessor agency guarantee. On the specific risk program, less than $20,000 has been paid out to the same company in the Congo, an American businessman in the Congo. He is able to operate. We are buying his Congolese francs. We buy his francs at 95 percent of the going rate and sell them to other agencies in the U.S. Government who are buying them otherwise from the Congo Government at 100 percent. The United States is getting the benefit of the 5-percent markdown. We have not shown any losses.

Representative GRIFFITHS. What is the total value of the insured now?

Mr. RUBLEE. Outstanding coverage on December 31, 1963, was $1,125.900,000 on the specific risk program; $8,325,000 on the general program; and $9,460,000 on the Latin American housing program.

Representative GRIFFITHS. What is the 9 in relation to the amount of money that you figure is invested by the U.S. firms in Latin America? What percentage does that $9 million represent?

Mr. RUBLEE. On the housing? That probably represents close to the actual investment, because what we are doing there, we are guaranteeing loans. I believe that we are covering about a year's interest in these, so the total coverage is close to the principal amount.

Representative GRIFFITHS. Thank you very much.

Senator SPARKMAN. Mr. Curtis?

Representative CURTIS. What I am concerned about are your fees. On this $1.125 billion outstanding, what do you collect annually in fees?

Mr. RUBLEE. I believe the annual fee collections on the specific risk program are going to be near $4 million for 1963.

Representative CURTIS. I wonder if you can supply the actual figures for the record?

Mr. RUBLEE. We shall be glad to. We do give that to Congress, of course, when we report——

Representative CURTIS. Oh, sure. I am not suggesting you are hiding them. I simply want them for the record here.

Mr. RUBLEE. The total fee accumulation in the whole history of the program is around $12 million.

(Subsequently, the following information was supplied:)

ACCUMULATED GUARANTEE FEES

During calendar year 1963, the fees paid for investment guarantee coverage amounted to $3,992,040.13.

The total amount of fees collected as a result of investment guarantees from the beginning of the guarantee program through December 31, 1963, was $15,118,235.30.

Representative CURTIS. If you are not paying out any claims, I can see one explanation: One reason why you are not getting any business is that your fee schedule does not recognize varying risks. If the terms of your policies recognized differences in real risks then your services would be in demand and you would be paying claims. That is what I want to know.

Is this a flat fee regardless of the country?

Mr. RUBLEE. Yes, sir; it is the same fee that was charged in Western Europe.

Representative CURTIS. I understand. You told me that. But that is a pretty flat answer, isn't it, for something that we are trying to move forward? Does the fact that you had something 15 years ago mean you need some legislative changes in order to use some imagination?

Mr. RUBLEE. No, sir; I indicated that a few moments ago. We have been considering suggestions and comments about the fee. Now, we do not get a good deal of criticism on the fee.

Representative CURTIS. You are getting it now and I will give you more, if that is what you are waiting for.

Mr. RUBLEE. No.

Representative CURTIS. I would think this record that you have presented to us right now, just on the bare bones of it, would be enough to make you shamefaced enough—not you as an individual, but your agency—to come in here with some ideas of your own, instead of waiting for criticism.

Mr. RUBLEE. We do have some ideas. For example, one of the techniques being worked on right now is a package contract which will provide the three risks and which will have a lower fee for the three risks combined.

Representative CURTIS. But what will it do? Will it do anything toward having a differentiation in respect to the country involved, so that you are reflecting the real risks?

Mr. RUBLEE. Mr. Curtis, we have checked with experts from the insurance actuarial field on this. They say it is impossible to make anything other than an arbitrary judgment about the nature of the risks from country to country. These are political risks——

Representative CURTIS. Let me give you one reading that you can put in right away: those countries with which you have no agreement and those with which you do have an agreement.

Mr. RUBLEE. This is a thought that has been seriously studied.

(Subsequently, the following information was supplied:)

UNIFORM FEE SCHEDULE

The fee schedule for investment guarantees is as follows:

Amount of coverage in force: One-half of 1 percent.

Standby coverage: One-fourth of 1 percent.

The above fees are charged with respect to each of the specific risk coverages taken out by the investor; namely, inconvertibility, expropriation, or war (which includes revolution and insurrection). The fees are the same in each of the countries where the guarantees are available.

There are several reasons for not employing different fees for each type of risk, for each country or for each type of project.

In the first place, professional actuaries who have examined the problem say that there is no actuarial basis for employing different fees, that variations would have to be arbitrary.

In the second place, with fees at the present levels of one-half percent and one-fourth percent significant variations could not be made without raising the fees. AID is studying lowering the guarantee fees. Raising them would not improve the usefulness of the guarantees to private investors.

Representative CURTIS. I have no doubt it is. I have been after this for many years and never could quite understand why, on the basic idea that was put in here, there was no further development. I can see the answer very clearly from your testimony, and again it is no reflection on you as an individual—you are testifying on behalf of an agency. But I think probably rather than waste the time of the record I will prepare a list of questions directed to your Agency and ask that they be answered. If your Agency is waiting for criticism and that is why it has not moved forward, let's make right here and now about as strong a criticism as could be directed against it. I think this has been lacking in imagination. I just don't think you achieved anything to speak of at all. This could be, I think, a real program.

Just to give you an idea of some of the possibilities, if you were doing a proper job here in insurance, you could give credit to those who lower their risks. I am talking about countries, and a country that conforms to your best standard ought to have a lower premium. That becomes a matter of credit to them and something to shoot for. So you would be getting better cooperation from the countries if you related your premium charges to what they have been willing to agree with and their experience rating of losses.

Then, I would look around the other side to see if this is such a safe area of investment. Apparently it seems to be, if you have paid out no claims——

Mr. RUBLEE. Mr. Curtis, most of the insurance was covering invesments in Western Europe.

Representative CURTIS. You have said that, but this is a hearing on Latin America.

Mr. RUBLEE. Right.

Representative CURTIS. Apparently there has been very little movement in this area.

Mr. RUBLEE. Our experience with the developing countries has been recent. We have only gotten about 2 years of real experience—no; 3 years of real experience with developing countries.

Representative CURTIS. By "developing countries," do you mean Latin America, Africa, and so forth?

Mr. RUBLEE. Yes, sir.

Representative CURTIS. I want to be sure here, because I have been free with my criticism of your Agency. I don't want to put that out of context. Maybe you need some corrections in the laws, but I think the laws were such that you could have moved into this field of undeveloped countries; could you not? Was there any restriction in the laws——

Mr. RUBLEE. No, sir; there were not. The choice of where the investment is made is, of course, the investors.

Representative CURTIS. That is what I thought.

Mr. RUBLEE. To the extent that there was investment going into developing countries, we certainly have some covered in Africa. We had some programs going in Latin America. There was fairly substantial resistance to the guarantee programs by the major countries in Latin America, a resistance which we——

Representative CURTIS. Let me get this straight. I thought you could and did have insurance available in a country even though they had not entered into an agreement. Did I misunderstand you?

Mr. RUBLEE. Under certain circumstances, where their record——

Representative CURTIS. Why use the country's failure to do something as a defense for not doing something yourself?

Mr. RUBLEE. That discretion, sir, to start the program without full formal agreement was given to us in 1961. Since 1961, we have used this discretion. We have broken through to some extent in Latin America. There were seven countries who refused to institute guarantee programs in Latin America. We have gotten four of them to——

Representative CURTIS. Let me illustrate this specifically, and then I will have finished here, because I don't think we are getting anywhere.

You can charge higher premiums to those countries that refuse, and indeed, you should. Those countries which cooperate should be related to the risk, because if you have some sort of agreement from the country, the risk should be cut down considerably. Now, obviously, if this were in a field where private money could go, private insurance companies would be there. So you are tackling a tougher problem than they are willing to tackle in the private sector. But that, in my judgment, is no reason to throw out the window the concept of doing the best you can considering risks, particularly in view of the advice of relating your premiums to cooperation that you receive from the countries.

Well, maybe there is somebody in your organization who could present a paper with more imagination, because, I must confess, this is about as disturbing a situation as I have seen. I can easily see why you don't move forward in these programs when you have a report like this. This is shameful.

Mr. Chairman, I would like permission to address a series of questions to the organization, and to others who might want to answer them in regard to these programs.

(The questions propounded by Representative Curtis and the answers thereto follow:)

QUESTIONS BY REPRESENTATIVE CURTIS CONCERNING GOVERNMENT GUARANTEES TO PRIVATE INVESTORS AND AID'S ANSWERS

I. Classification by types of businesses, public utility, manufacturing, mining, etc., of (1) guarantees applied for, (2) guarantees undertaken, (3) losses paid, or (4) guarantees "in trouble."

Of the 287 projects throughout the world in which U.S. private investment had been guaranteed through June 30, 1963, the majority were industrial. There were 180 industrial projects, 44 of an agricultural or food processing nature, 25 commercial, 23 oil, 16 mining, and 2 public utility. Pending applications are distributed in about the same way.

The losses that have been paid were in connection with a shipyard and with a plywood manufacturing plant.

The guarantees in trouble are investment in one mining project, two manufacturing projects (one large and one small) and one commercial project.

II. What in general has been the behavior of the U.S. guaranteeing agency when faced with a potential loss under a guarantee program?

1. Payoff on certification and include amount of loss in appropriation request?
2. Use the claimant's subrogated position as a basis for diplomatic negotiation?

Only three projects have given rise to claims that have been processed under the guarantee programs. A $650,000 claim was paid under a DLF guarantee of repayment of a loan from New York banks to a privately owned company operating a shipyard in Taiwan. Upon proof of default in payment, the United States made the payment and became subrogated to the rights of the banks as creditors against the assets of the shipyard company. The United States has brought suit in the United States to recover assets here of the defaulting company and also the United States is asserting liens against assets of the company in Taiwan.

The U.S. investor in a plywood company operating in the Congo has presented several claims under a guarantee against inconvertibility. Here the United States in accordance with the guarantee has purchased the investor's holdings of Congolese currency which he was unable to transfer into dollars. The United States has used this currency for its expenses in the Congo. In this case, the investor submitted evidence that Congolese authorities had refused to sell him dollars or other hard currencies for Congolese francs.

The third claimant, a manufacturer of metal products in a Far Eastern country alleged that he was unable to convert his foreign currency earnings except at a discriminatory rate. The evidence he submitted in support of the claim showed that the alleged discriminatory rate was in fact the rate commonly in use for almost all the exchange transactions taking place in the country. The claim was denied and is now in litigation in the U.S. Court of Claims.

There have been occasions when an investor insured against expropriation informed the agency administering the guarantee program that foreign governmental action seemed likely to become expropriatory. In several of these occasions, the U.S. Government has through diplomatic negotiations discussed the proposed action with the foreign government and the action has stopped. The U.S. Government would probably have done this whether or not the investment had been guaranteed.

To date no claim of expropriation, other than a recent claim in the Near East where the facts are still being developed, has been presented.

III. To what extent does (or must) the insuring Government agency approve wisdom of original investment and either control or supervise operations in order to make sure that subsequent loss is not a result of bad private policy or administration? That is to say, how much of the business risk can be shifted by the capital investor to the guaranteeing agency?

In connection with investment guarantees against loss from inconvertibility, expropriation or war, revolution, or insurrection, the insuring Government agency does not examine into the business risks nor does it seek to control the business operations of the enterprise in which the investment is made. The purpose of these investment guarantees is to block out abnormal

risks but leave business risks to be evaluated and borne by the private investor. None of that business risk is assumed by the guaranteeing Government agency.

Under the extended risk guarantee, a portion of the investment is guaranteed against business risks by the Government agency issuing the guarantee. Here such business risks are evaluated by the agency as though it were making a loan. The degree of agency supervision and control over the operations of the enterprise in which the investment is made depends on the degree to which the private investment is not covered by the U.S. Government's guarantee.

IV. How do the guarantee programs treat so-called industrial property such as patents, trademarks, licensing agreements, etc.?

Patents are eligible for guarantees and licensing agreements permitting the use of patented processes are thus also eligible for guarantees. Trademarks, trade names and good will have not been covered by guarantees for several reasons. They are very difficult to evaluate, and the original possessors of them generally would not wish to see them transferred to third parties in the event of a takeout by reason of expropriation. Where the licenser and licensee have bargained at arm's length the guarantee covers the value they have put upon the patent.

V. How do the guarantee programs deal with U.S. interests in joint ventures in which local capital either supplies a large part or the majority of funds and control?

The guarantee programs are limited to guaranteeing the investments of U.S. investors in foreign businesses in the developing countries. If the foreign business is a joint venture in which there is a large part of local capital, only the U.S. interest in the joint venture will be covered by the U.S. guarantee programs. Thus if a business 50 percent owned by U.S. investors were nationalized, the U.S. investor would be protected by the guarantees against loss of the original U.S. investment plus half the subsequent reinvested profits of the foreign enterprise up to an amount equalling that original investment.

VI. If, under a bilateral arrangement the United States is to be indemnified by the host government, is not the "incurred" risk in reality the good faith of the host government?

The bilateral agreements establishing the guarantee programs do not provide for indemnification of the U.S. Government by the host country government. Such a provision would probably greatly diminish the willingness of host country governments to permit private U.S. investment to come in with coverage under the guarantee program. The bilateral arrangements do secure from host country governments undertakings to have the propriety of their treatment of guaranteed U.S. investment tested against international law standards by an impartial arbitral tribunal.

Oh, yes; there is one thing I want to add. Could you supply for the record the application form for assistance from your organization?

Mr. RUBLEE. Yes, sir.

Representative CURTIS. Is that a standard form or is there a series of standard forms? What is it?

Mr. RUBLEE. There is a standard form.

Representative CURTIS. One form?

Mr. RUBLEE. Yes, sir.

(See pp. 186–187.)

Representative CURTIS. One other thing. Is there a standard form of policy that you issue when you accept an application?

Mr. RUBLEE. Yes, sir. There are several standard forms.

Representative CURTIS. There are several standard forms. For the record, would you tell us the exact number?

Mr. RUBLEE. There are five basic standard forms.

Representative CURTIS. Would you supply those basic standard forms for us? We ought also have copies of any basic information which you give out to businessmen who might be interested in oversea guarantee programs.

Mr. RUBLEE. Yes, sir.

(The basic forms referred to appear at the end of this day's testimony. See p. 239.)

Senator SPARKMAN. Senator Javits, before calling on you, I would like to ask Mr. Rublee just for a very brief comment as to what you think of the guarantee program as it has been worked out in our AID programs.

Mr. RUBLEE. We think it is an extremely important——

Senator SPARKMAN. No; I meant Mr. Fatouros.

Mr. FATOUROS. Well, I think that it should be realized the program is a domestic one. It is not basically an international program; this, of course, makes it more effective in the United States but on the other hand, limits the extent to which it can have a preventive effect on the taking of measures which might affect foreign investors. The United States may guarantee any investment it wants to guarantee, but this will affect the policies of the country of investment only indirectly.

On the other hand, because of exactly these reasons, this program can be tailored more easily to the domestic problems and requirements than an international program, and this has great advantages. It is a program which operates in a context familiar to the foreign investor. He doesn't have to go to a foreign country. He goes to the administration, which may seem a stranger to him sometimes, but still he knows how to deal with it. These are basic advantages to the program.

However, I think that not too much should be expected of it in two ways: First, as to eliminating the risks in the foreign countries. The risks cannot be eliminated through a guarantee program. Only the degree of the risk can be made somewhat lower.

Secondly, it is a problem to which no positive or negative answer has been given, whether the program is really an incentive to foreign investment. There is really no proof—again I say no proof positive or negative—that the availability of investment guarantees does induce foreign investment. There is a good chance that the investment might have been made, whether guarantees were available or not. Now, as I say, there is really no indication one way or the other. I am not saying there is proof that the investment would have been made anyway, but there is no proof that it wouldn't have.

So the investment guarantee program is useful, but I think it should be seen within its limitations. It cannot solve all the problems of private foreign investment. Unfortunately, only developments in the host countries and in the relationships of the host countries and the investors and the capital-exporting countries, only these can really solve the problems. The investment guarantee program can help by providing some assurance to the individual investor.

Senator SPARKMAN. Senator Javits?

Senator JAVITS. I had just one or two questions, Mr. Chairman. I would like to ask them of Mr. Rublee. I notice that the extended risk guarantees have been very little used: $180 million authorized; $8.325 million used. Now, what is the reason?

Mr. RUBLEE. The reasons are several. The authority itself is a rather complicated authority. The agency spent a good deal of time deciding how they were going to use it. You recall General Clay and his Committee expressed some doubt about using the authority at all.

PLEASE COMPLETE PAGES 1 & 2 — **PAGE 1 OF 2**

AID-20-2 (11-60)

BUDGET BUREAU NO 24-R-033.4

DATE

INVESTMENT GUARANTY APPLICATION*

1 NAME AND ADDRESS OF APPLICANT

2 CITIZENSHIP

a. If individual indicate method of obtaining U.S. Citizenship ☐ Birth ☐ Naturalization

Other ______

b. If corporation name State where incorporated ______ . Year Incorporated ______

(Must be U.S. Citizen or U.S. Corporation)

3. STOCK OWNERSHIP OF APPLICANT:

% Common stock known or believed to be owned by U.S. citizens ______

% Preferred stock known or believed to be owned by U.S. citizens ______

Does Applicant have substantial foreign creditors? ______ YES OR NO

(If yes, describe on separate sheet.)

4. AUTHORIZED REPRESENTATIVES OF APPLICANT FOR PURPOSES OF THIS APPLICATION

NAME	ADDRESS	TELEPHONE NUMBER

5. DESCRIPTION OF APPLICANT'S BUSINESS

6 NAME AND ADDRESS OF FOREIGN CONCERN OR BRANCH RECEIVING INVESTMENT *(If now known)*:

7. BRIEF DESCRIPTION OF FOREIGN CONCERN'S BUSINESS:

8. APPROXIMATE DATE WHEN ENTERPRISE WAS OR WILL BE FORMED

9. LEGAL FORM OF ORGANIZATION *(Corporation, etc.)*

10. APPROXIMATE DATE INVESTMENT WILL BE MADE

11. DESCRIBE IN GENERAL TERMS NATURE AND PURPOSE OF PROPOSED PROJECT *(the investment)* AND INDICATE PROBABLE BENEFITS OF THE PROJECT TO THE ECONOMY OF THE FOREIGN COUNTRY.

*Send FOUR copies to Investment Guaranties Division, Agency for International Development, Washington 25, D. C., in accordance with Appendix "A" of the Investment Guaranty Handbook. *(Where additional information is attached, refer to item number in this application.)*

CONTINUED FROM PAGE 1

12. PROPOSED INVESTMENT

a. CASH *(Amount)*	b. MACHINERY, EQUIPMENT, MATERIALS *(Value)*	c. PATENTS, PROCESSES AND TECHNIQUES *(Value)*	d. SERVICES *(Value)*
$	$	$	$

13. INDICATE BASIS FOR DETERMINING VALUE, FOR INSTANCE, BY APPRAISAL, ETC. *(If cash is other than U.S. funds give details on separate sheet.)*

14. STATE WHAT APPLICANT WILL RECEIVE FOR INVESTMENT - STOCK, NOTES, ROYALTY AGREEMENT OR OTHER INSTRUMENT AS COMPENSATION OR EVIDENCE OF OWNERSHIP. IN CASE THE PROJECT IS A BRANCH, INDICATE. DESCRIBE THE INVESTMENT PLAN.

(Use separate sheet if necessary. If draft of the investment instrument is available copies should be attached.)

15. GUARANTIES REQUESTED:	CONVERTIBILITY*	EXPROPRIATION	WAR RISK**
Equity	$	$	$
Loan	$	$	$
Royalty	$	$	$
Other	$	$	$
No. of years			

16. IF FINANCIAL SOURCE OF INVESTMENT IS OTHER THAN TREASURY FUNDS OR USUAL BANKING ARRANGEMENTS BY THE INVESTOR WITH AMERICAN INSTITUTIONS, DESCRIBE FULLY.

17. INDICATE ANY CONTRACTUAL AGREEMENTS WITH THE FOREIGN CONCERN NOT GOVERNED BY THE INVESTMENT INSTRUMENT.

18. STATE THE ARRANGEMENTS UNDER WHICH YOU WILL BE ABLE TO REMIT INCOME AND TO REPATRIATE INVESTMENT.

19. SIGNATURE	TITLE

*Up to 200% of investment

**Up to 90% of value of physical property guarantied. Attach description of physical property, if available.

GPO 928130

The program was divided among the four regions of the agency, where this fairly complicated program competed for attention with development loans, development grants. Finally, we did adopt basic policies which would enable the agency to put the thing in use. The Latin American region was the first one to use it. They used it on a very interesting project in Argentina. We hope that that project will go forward as a result of these guarantees. The financing of the project had been arranged with European investors and American investors. With the declining value of the Argentine currency and with the unrest there, the Europeans who did not have guarantees withdrew. We hope that the extended risk guarantee will enable the managers of that project to find U.S. investors as substitutes.

Senator JAVITS. How much is that?

Mr. RUBLEE. The total project is $72 million. The amount of financing involved here is about $14 million. This is just——

Senator JAVITS. When on my suggestion the Senate increased in 1962 the amount of extended risk guarantees that may be issued to $25 million in the case of a loan, I laid before the Senate as its reason a project of the International Telephone & Telegraph in Chile, which involved, I think, $25 million. Whatever happened to that?

Mr. RUBLEE. The intergovernmental agreement instituting the full guarantee program which was necessary to issue the all-risk guarantee, was signed last month. The Chitelco application is being considered by the Latin American region——

Senator JAVITS. I don't quite get it. The agreement was signed in December of 1963, only last month.

Mr. RUBLEE. Yes, sir.

Senator JAVITS. Let's have the rest of it. I didn't hear you.

Mr. RUBLEE. Chitelco, the subsidiary of I.T. & T. C-h-i-t-e-l-c-o, the subsidiary of I.T. & T. that had applied for the risk guarantee, so far as I know has maintained that application. The application has been with the Latin American region, which has been processing it——

Senator JAVITS. What is the Latin American region? Is that in your office?

Mr. RUBLEE. No, sir; it is in the Alliance for Progress.

Senator JAVITS. Where is it? Is it in the State Department?

Mr. RUBLEE. It is in the State Department. I would have to supply for the record where it stands with them.

Senator JAVITS. Do you ask us, then, to understand that you don't give any guarantee in AID unless the State Department approves it?

Mr. RUBLEE. I am sorry, sir. The Alliance for Progress is part of, was part of AID in the last 2 years. It is physically located, as is most of AID, in the State Department. The application for guarantee that we are talking about rests with the AID personnel, the capital project analysts, in the Alliance.

Senator JAVITS. AID gives the guarantee?
Mr. RUBLEE. Yes, sir.
Senator JAVITS. But you give it only if the Alliance for Progress organization approves it?
Mr. RUBLEE. Yes, sir. They are part of AID.
Senator JAVITS. Do you have to approve it, too?
Mr. RUBLEE. No, sir.
Senator JAVITS. In other words, if they say give it, you give it?
Mr. RUBLEE. Yes, sir.
Senator JAVITS. You do not exercise independent discretion?
Mr. RUBLEE. That is correct.
Senator JAVITS. Is that true of any extended risk guarantee in Latin America?
Mr. RUBLEE. It is true of those that have been worked on by the Latin American region. In the last month, December 21, Mr. Bell transferred the operational responsibility for the all-risk program to Mr. Peyser.
Senator JAVITS. The what program?
Mr. RUBLEE. The extended risk guarantee program.
Senator JAVITS. For Latin America, too?
Mr. RUBLEE. Yes, sir.
Senator JAVITS. And took it away from the Alliance for Progress?
Mr. RUBLEE. Under 221(b)(2). Not the housing guarantees. They remain in the Alliance. The authority to issue the guarantees has been transferred on extended risk guarantees to Mr. Peyser. The authority for specific risk guarantees has always been with Mr. Peyser.
Senator JAVITS. When you say the authority to issue, I want you to speak as a lawyer. The authority to issue was always in AID, wasn't it?
Mr. RUBLEE. Yes, sir.
Senator JAVITS. Now he is transferred some other authority than the authority to issue?
Mr. RUBLEE. The authority to approve and issue extended risk guarantees has been delegated by Mr. Bell to Mr. Peyser.
Senator JAVITS. But you always had the authority to issue, didn't you? You have never lost it?
Mr. RUBLEE. Mr. Bell had always had it. It had been delegated to Ambassador Moscoso. It has now been delegated to Mr. Peyser. It is to put the guarantee programs under one roof, the private enterprise roof, instead of having the agency develop——
Senator JAVITS. How many applications do you have pending for extended risk guarantee?
Mr. RUBLEE. Our survey is not yet complete, Senator Javits, because the things have been in our regions. We have a man physically going around getting the applications from the regions now. This is the thing that Mr. Peyser's office was engaged in yesterday.

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Senator JAVITS. All right. Will you submit for the record two things, then:

The status of the I.T. & T. situation on the extended risk guarantee. I feel personally responsible for that, in a sense. I put it up to the Senate very frankly and the Senate did it. So we ought to have a report, Mr. Chairman.

Secondly, the roundup of all the guarantee applications you have pending.

Mr. RUBLEE. Yes, sir.

Senator JAVITS. Thank you very much.

(Subsequently, the following two exhibits were submitted:)

STATUS OF I.T. & T. SITUATION RE EXTENDED RISK GUARANTEES

The application for extended risk guarantees by I.T. & T. for a proposed investment in Chile has been examined by AID personnel both in the Alliance for Progress and in the Office of Development Finance and Private Enterprise. Because negotiations between I.T. & T. and the Chilean Government affecting the investment have not yet been concluded, action on the application awaits receipt of further information from I.T. & T.

SUMMARY OF PENDING APPLICATIONS FOR EXTENDED RISK GUARANTEES

Four applications for extended risk guarantees are pending for projects in Latin America. The projects involved are a poultry farm, a telecommunications system, a sawmill, and an industrial plant. The industrial plant application is under intensive review by AID's Office of Development Finance and Private Enterprise. Action on the other applications awaits receipt of further information from the prospective investors.

No applications for extended risk guarantees are currently pending for projects in either the Near East, south Asia, or the Far East.

Nine applications for extended risk guarantees are pending for projects in Africa. Four of these relate to hotels, four to housing projects, and one to a development bank. Where the AID African Bureau had commenced work on the applications, continued responsibility for their processing remains with the Bureau. Those applications which are still at a preliminary stage have been transferred to the Office of Development Finance and Private Enterprise.

Projects have not been identified by country or by amount, since generally pending applications for investment guarantee coverage contain business information of commercial value whose premature disclosure might adversely affect the costs of the projects.

Representative CURTIS. I just want to put this in the record. Maybe what needs to be done is to put this program in the Department of Commerce, which is interested in the private enterprise system. Furthermore, I see that the possible difficulty here is that AID and these Government programs would prefer to use Government money, because anything that would encourage the use of private money would be in the form of competition. Now, that is a nasty suggestion, but I must confess I can't understand the report that has been submitted here. I do think maybe the Department of Commerce should take the program and handle it. I think your agency will probably have some comments on that, so I'll relieve you of the burden of doing this now.

Mr. RUBLEE. Sir, we have been working on this program. I think by more than doubling the guarantee program in the last 2 years, I would think that would show we are interested.

Representative CURTIS. If you had a good basis to start with, that might be true.

Senator JAVITS. Will the Congressman yield?

Representative CURTIS. Yes.

Senator JAVITS. You know that there is a provision in the Foreign Assistance Act of 1963 for an Advisory Committee on Private Enterprise to determine what can be done about escalating the private enterprise participation in foreign aid, the Committee of Nine. I would like to join with Congressman Curtis in the urgent recommendation of a report on the use of the guarantees, who administers them, what success has been had, and so forth. It would certainly be looked upon by this committee as a very important subject.

Representative CURTIS. Thank you.

Senator SPARKMAN. Thank you very much, gentlemen. We appreciate your presentation.

The committee will stand recessed until 10 o'clock tomorrow morning.

(Whereupon, at 12:10 p.m., the committee recessed, to reconvene Thursday, January 16, 1964, at 10 a.m.)

(The following exhibits were ordered placed in the record during the foregoing proceedings:)

UNITED STATES GOVERNMENT

Memorandum

TO : BUSINESSMEN

FROM : STATE DEPT. — AGENCY FOR INTERNATIONAL DEVELOPMENT

SUBJECT: AIDS TO BUSINESS (OVERSEAS INVESTMENT)

FOREWORD

The Congress of the United States recognizes the vital role of free enterprise in achieving rising levels of production and standards of living essential to economic progress and development . . .

In order to encourage and facilitate participation by private enterprise to the maximum extent practicable in achieving any of the purposes of this Act, the President shall—

(1) make arrangements to find, and draw the attention of private enterprise to, opportunities for investment and development in less-developed friendly countries and areas; . . .

(4) wherever appropriate carry out programs of assistance through private channels and to the extent practicable in conjunction with local private or governmental participation, including loans under the authority of section 201 to any individual, corporation, or other body of persons.

(From Section 601, Foreign Assistance Act of 1961)

It is the clearly established policy of the United States Government to foster, encourage and promote participation by private enterprise in foreign economic development.

Over the years, Congress has provided a number of specific programs to assist and encourage U. S. business to undertake investments in less-developed friendly countries and to assist local businesses in these nations to prosper. For fifteen years there has been an investment guaranty program covering political risks. For five years a local currency Cooley loan program has been in operation. For five years our government has made direct dollar development loans to private firms.

All of these aids to investment—along with several new programs—are now administered by the Agency for International Development (A.I.D.).

A.I.D. was established on November 4, 1961, under the Foreign Assistance Act of 1961. This Act terminated the International Cooperation Administration and the Development Loan Fund and transferred their functions, along with the Export-Import Bank's Cooley loan program to A.I.D. So, now, virtually all of the government's foreign economic aid activities, including U.S. participation in the Alliance for Progress, have been centralized and coordinated in a single agency—A.I.D.

A.I.D. is placing a greater emphasis than predecessor foreign assistance agencies upon sound country plans and self-help measures as pre-conditions for development assistance. It encourages, in particular, those investment proposals which will do the most to speed development of the friendly less-developed countries. There are far greater resources at the disposal of private enterprise than can ever be applied to such development by governments.

A.I.D. favors joint-venture type investments with local capital because this type of enterprise is most likely to result in a transfer of entrepreneurial, technical and management skills to the country itself. Further, A.I.D. believes it is wisest in the long run for U. S. investors to identify their interests closely with those of the citizens of the country in which they operate. In view of the desire to mobilize scarce foreign exchange resources, those investments which are accompanied by dollar capital, in addition to management and technical know-how, are preferred. The sale of packaged plants, or the provision of so-called "turn-key" jobs, usually takes a lower priority position than those proposals in which there is a sizeable private equity contribution in relation to debt.

Consistent with A.I.D.'s objectives, several programs of particular interest to businessmen are receiving immediate attention and emphasis:

1. **Sharing the cost of conducting investment surveys undertaken by U.S.-owned business firms.**
2. **Authorizing dollar development loans to private borrowers.**
3. **Administering the PL 480 local currency (Cooley) loan program formerly handled by the Export-Import Bank.**
4. **Administering the broadened investment guaranty program.**

A newly created Office of Development Finance and Private Enterprise is the initial point of contact within A.I.D. for private businessmen interested in overseas investment. It aims to encourage private enterprise to play an even larger development role than it does at present, while insuring adherence to sound standards for development financing.

Among the chief functions of the Office of Development Finance and Private Enterprise are: (1) to meet with business groups and individual businessmen to explain the A.I.D. private enterprise program, and (2) to work with the regional administrators for Latin America, the Near East and South Asia, the Far East, and Africa to promote those private enterprise projects which will particularly further the A.I.D. program. The regional administrators implement the specific proposals pertaining to their geographical areas, and have ultimate operational responsibility for all these activities except specific-risk investment guaranties.

We believe this booklet will answer many questions which American businessmen have asked about how A.I.D. can, and does, assist United States companies contemplating making a productive investment in less-developed countries or wishing to expand already existing foreign operations. The booklet outlines the Congressional tools which now enable A.I.D. to enlist American business collaboration in our foreign aid program.

Each chapter describes a separate program—who is eligible to participate, the terms and conditions, and how to apply to A.I.D. The exhibits which follow include a discussion of some of the programs administered by other U.S. and international financial institutions.

Seymour M. Peyser
Assistant Administrator for
Development Finance and Private Enterprise
Agency for International Development

January 1963

SUBJECT: Investment Surveys

A.I.D. seeks to increase investment by United States private enterprise in the economies of friendly less-developed countries by sharing with U.S.-owned firms the cost of conducting surveys of investment opportunities.

THE PROGRAM

The purpose of the investment survey program is to encourage potential investors to identify specific investment opportunities in less-developed friendly countries which they might not otherwise investigate.

A.I.D. has authority, under Section 231 of the Foreign Assistance Act of 1961, to participate in up to 50 per cent of the cost of approved surveys which explore the feasibility of contemplated private investments in developing countries which will contribute to the achievement of A.I.D. objectives.

If the prospective investor then proceeds with the investment (following the survey), he will repay A.I.D. those funds which may have been advanced to him. The investor will retain exclusive rights to the survey.

But if the prospective investor *does not* undertake the investment studied, the survey will then become the property of the United States Government. In this case, the investor is entitled to A.I.D. participation, providing he has complied with the terms and conditions of the participation agreement. He is then under no obligation to repay any such advances to A.I.D.

Note: A.I.D. participation in an investment survey in no way implies that the U. S. Government will provide the investor with further financial assistance. Subsequent applications from the same investor for loans or guaranties will be considered separately, on the basis of their respective merits.

ELIGIBILITY

Prospective investors eligible to participate in the A.I.D. investment survey program are persons who are citizens of the United States or any corporation, partnership or other association substantially beneficially owned by U.S. citizens. The survey may be made either by the prospective investor or by a qualified independent contractor engaged by the prospective investor.

TERMS AND CONDITIONS

Within the limits of funds available, A.I.D. may participate in the financing of investment surveys which meet the following criteria:

1. There must be reasonable prospects that the survey will result in an investment.

2. The investment must contribute to the achievement of A.I.D.'s objective of furthering economic development of a less-developed friendly nation.
3. The investment must be consistent with the host country's development program.

NATURE OF SURVEYS

Surveys will normally explore and analyze the economic and technical feasibility of proposed investments. They will usually include analyses of the potential market, plant location, raw materials availability, labor supply, availability of qualified personnel, profitability and other financial considerations (capital requirements), and potential contribution of the investment to the host country's economy.

Surveys of extraction opportunities—including those ascertaining the existence, location, extent or quality of any deposit of ore, oil, gas, or other mineral, and those determining the feasibility of mining or other extraction of any such mineral or the processing of it to the stage of commercial marketability—are *not* eligible for A.I.D. participation.

HOW A.I.D. SHARES IN SURVEY FINANCING

For acceptable investment survey proposals, A.I.D. will normally share in the financing on the following basis:

- A.I.D. will undertake to reimburse the prospective investor an amount not to exceed 50 per cent of the total allowable cost of an approved investment survey, as defined in the investment survey grant document. Total allowable cost, which may include both dollar and local currency expenditures, may include (a) salaries of personnel at their normal rate of pay for the time spent on the survey, (b) expenditures for subsistence and travel, (c) communications and (d) indirect costs which A.I.D. agrees are allocable to the survey.

- Payment may be made after the survey is completed, or if appropriate, provision may be made in the grant document for interim payments (pay-as-you-go).

- The grant document will provide an appropriate period of time after completion of the survey for the investor to decide whether to invest.

- If, within the agreed period of time, the decision is made to proceed with the investment, the costs may not be shared by A.I.D. (and the prospective investor will reimburse A.I.D. any funds paid to him by A.I.D.).

• If, within the agreed period of time, the potential investor has decided *not* to invest (or has not decided to invest by the end of this period), he shall provide A.I.D. with copies of a professionally acceptable survey which then becomes the property of the U.S. Government. In such event, A.I.D. also shall have access to, and obtain copies as desired of, relevant underlying correspondence, memoranda, working papers, documents and other materials gathered in connection with the survey. A.I.D. may then utilize the survey for any appropriate purpose.

HOW TO APPLY

Inquiries regarding the program in general should be directed to: Office of Development Finance and Private Enterprise, A.I.D., Washington 25, D. C. Inquiries regarding investment surveys in a specific country should be directed to the appropriate regional office of A.I.D., Washington 25, D. C. (See Exhibit I for a listing with addresses, by regions, of the United States A.I.D. Missions and the A.I.D. regional offices in Washington.)

Letters of application (there is no special application form) for A.I.D. participation in investment surveys should be addressed to the appropriate regional office of A.I.D., Washington 25, D. C. Send four (4) copies of the application. The letter of application should be submitted at least 30 days prior to the contemplated start of the survey and should include the following information:

1. Applicant's full legal name, address, nature (whether corporation, partnership, etc.), and the country in which organized or incorporated.
2. Description of projected investment.
3. Scope of survey and estimated cost (breakdown of principal components).
4. Names and qualifications of persons who will conduct survey.
5. Proposed plans for the implementation of the investment project.
6. Statement indicating the ability of potential investor to finance the investment opportunity to be surveyed.
7. Proposed time schedule, including date by which investment decision will be made.
8. To the extent known, relationship of investment project to the overall economy and development program of the host country.

SUBJECT: Dollar Loans

A.I.D. seeks to increase investment by private enterprise in the economies of friendly less-developed countries by helping to finance high-priority projects which promote economic development.

THE PROGRAM

A.I.D. has authority, under Section 201 of the Foreign Assistance Act of 1961, to make dollar loans to private (as well as public) enterprise, both U. S. and foreign. It is A.I.D. policy to encourage those investments which contributed to the economic development of a less-developed friendly country in which the investment is to be made, with emphasis on assisting long-range development plans.

Dollar development loans may be made only where there are reasonable prospects of repayment. Normally, U. S. dollar loans are to be used to cover the U. S. procurement component of the project, with few exceptions permitted.

As required by statute, the Administrator of A.I.D., before authorizing loans, must take into account the availability of financing from other free world sources on reasonable terms. So, a prospective borrower should investigate a number of private and other public institutions before making formal application to A.I.D.

In general, the other public agencies also require that the borrower first seek financing from *private* financial sources. Hence, potential borrowers should initially consult their regular banking relationships. (A list of those private U. S. financial institutions which have been authorized by the Federal Reserve System to participate in loans and/or ownership in international ventures—the so-called Edge Act Corporations—is contained in Exhibit II. Current listings of Edge Act Corporations are periodically published by the Federal Reserve Bank, Washington 25, D. C. In addition, there are a number of investment banking and other privately financed long-term lending institutions which may provide dollar financing for foreign investments.)

Assuming that financing from private sources is not available on reasonable terms, contact should first be made with the Export-Import Bank of Washington (Eximbank), 811 Vermont Avenue, N. W., Washington, D. C. The Eximbank makes dollar loans to finance the export of capital equipment and contract services for engineering or supervisory purposes for development projects. Eximbank will also insure exporters against certain political and credit risks in collaboration with private insurance companies and banks, including coverage of relatively small exporter transactions. (Exhibit III gives a brief description of the three Eximbank programs mentioned above.)

Besides the Eximbank, there are other public financial institutions to which application may be made:

- The International Finance Corporation, an arm of the World Bank, formed to encourage productive *private* enterprise in the countries of its members.
- The World Bank itself, if the project to be financed is one which clearly falls within the category of basic infra-structure—power, transportation, heavy industry, etc.
- The Inter-American Development Bank (IDB) if the proposed investment is in one of the Latin American countries. The United States has made available substantial dollar funds to the IDB, which administers three distinct programs of development lending for Latin America. (A brief description of the programs of each of these institutions is also given in Exhibit III.)

Development banks are another potential source of dollar financing to qualified borrowers. A.I.D., the World Bank, IFC and IDB have made substantial loans to a number of development banks, which in turn may relend to private individuals. Many of these banks can also assist borrowers in the preparation of feasibility studies and the identification of prospective joint-venture partners, among other services. (See Exhibit IV for a list of development banks.)

ELIGIBILITY

If dollar financing is *not* available on reasonable terms from private or other public sources as outlined above, then application to A.I.D. may be made by private firms or individuals.

Loans may be made to private firms or individuals seeking to expand existing enterprises and to firms or individuals planning to establish new enterprises. Applicants need not be residents of the country where the enterprise is located.

The projected new investment, or expansion or diversification must be acceptable to the government of the country in which it will be made, and it must clearly contribute to the economic development of the country. Therefore, it is advisable to discuss acceptability of the project with both the host country government and the A.I.D. Mission in that country in advance of making formal application to A.I.D. In countries where the government require prior licenses or other approvals of an industrial enterprise, prospective applicants should obtain such assurances from the appropriate government ministries *before* submitting their application to A.I.D.

TERMS AND CONDITIONS

1. The project must give reasonable promise of contributing to the development of economic resources and/or increasing the productive capacities of the country concerned.
2. It must be consistent with the other development activities being undertaken or planned for the country. Necessarily, A.I.D. is limited to financing only those activities which occupy a relatively high priority position in a country's development program.
3. The project must be economically and technically sound, with reasonable prospects that it will pay out satisfactorily.
4. The project must not compete (within the meaning of section 620(d) of the Foreign Assistance Act, 22 U.S.C. Sec. 2370(d)) with U.S. enterprises, especially with enterprises in areas of the U.S. with substantial labor surpluses.
5. The proceeds of the loan must be used to finance the dollar costs of the project except where, for good cause, A.I.D. agrees otherwise.
6. Procurement will be limited to goods and services of United States origin, with few exceptions permitted.
7. Loans are generally made directly by A.I.D. to the private borrower at an interest rate of 5¾ per cent. While principal and interest are owed in dollars, arrangements may be made for repayment of principal and interest in local currency (dollar denominated) to the local government which, in turn, arranges to pay A.I.D. in dollars.
8. Borrowers must agree to follow normal commercially acceptable business practices to assure that the prices paid for goods financed under A.I.D. loans are reasonable and that contracts are awarded on an appropriate competitive basis.

HOW TO APPLY

Inquiries regarding the program in general should be directed to: Office of Development Finance and Private Enterprise, A.I.D., Washington 25, D. C. Inquiries regarding dollar development loans to private borrowers for operations in a specific country should be addressed to the appropriate U. S. A.I.D. Mission or to the proper regional office of A.I.D., Washington 25, D. C. (See Exhibit I for a listing with addresses, by region, of the United States A.I.D. Missions and the A.I.D. regional offices in Washington.)

Letters of application (there is no special application form) must be in English. Six (6) copies should be sent to the U.S. A.I.D. Mission in the appropriate country or to the proper regional office of A.I.D., Washington 25, D. C.

The letter of application should include the following, where applicable:

1. Applicant's full legal name, address, nature (whether corporation, partnership, etc.), and the country in which organized or incorporated.
2. A brief biographical sketch of the principal owners, directors, officers, and managers, including the percentage of U.S. and other ownership. Indicate the extent of management's experience and qualifications.
3. The amount of the loan requested from A.I.D. and a statement showing the specific uses to be made of the funds to be borrowed—buildings, machinery, services and equipment, etc.
4. The desired repayment period (in the form of a tentative repayment schedule).
5. If the enterprise is already in operation, submit (a) a current balance sheet and balance sheets for the prior three years, including statements of surplus, (b) a profit and loss statement for the past five years, (c) a statement of sources and uses of funds, and (d) a current cash flow statement, together with similar statements for the past three years. All financial statements should be audited if possible. Otherwise, they should be signed by an officer of the applicant.
6. All applicants must submit pro-forma balance sheets, and profit and loss and cash flow statements estimated for future years until operations become fully developed with debt servicing stabilized. Such statements should indicate clearly the assumptions made in the projections and the bases of these assumptions.
7. The name(s) of the applicant's bank(s).
8. The total cost of the proposed project (including all equity investment contemplated), and the amount of, sources of, security for, and repayment terms for all proposed borrowing and other financing.

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9. Any preliminary engineering, economic, and market studies already made which are pertinent to the proposed loan, including (a) the volume and kind of end products or services which would be produced, (b) the source of the required raw materials, (c) the markets to be supplied, and the competition, if any, (d) the transportation available for raw materials and finished products, and (e) a forecast of production costs.
10. A description of the efforts which have been made to raise the required capital from other free-world sources and the terms, if any, on which such capital is available.

In short, a request for a dollar loan for a project should be supported by any and all information necessary to determine the equity participation, economic justification, technical feasibility, and cost; by a description of how the engineering, purchasing, construction, and management of the project will be carried out, and by appropriate financial projections. It should be made clear whether it is planned that consulting services will be utilized, and, if not, the reasons why should be stated.

The length of time required by A.I.D. to process an application will vary, depending upon the nature of the proposal. However, as a general rule, the more completely documented the submission, the more quickly processing will be completed.

In the light of the large volume of applications to A.I.D., and in view of the limits on its resources, it is obvious that A.I.D. will not be able to extend credit for all the worthwhile proposals submitted to it for consideration. But all applications will be acknowledged after they have been subjected to preliminary review by the appropriate regional office within A.I.D. and by the United States A.I.D. Mission in the field. If an application cannot be considered within a reasonable time, the applicant will be so notified.

SUBJECT: Local Currency Loans

A.I.D. seeks to stimulate economic activity by private enterprise in friendly less-developed countries by lending to private firms local currencies generated from the sale of U. S. surplus agricultural commodities.

THE PROGRAM

Under Section 104(e), Title I of Public Law 480, the Agricultural Trade Development and Assistance Act of 1954, up to 25 per cent of the foreign currencies received by the U.S. Government in payment for surplus agricultural commodities may be lent to qualified borrowers to develop business and expand trade. These local currency loans, usually referred to as "Cooley loans," are named after Congressman Harold D. Cooley, who sponsored the amendment to Public Law 480 setting aside some of the proceeds of certain surplus sales for relending to U. S. private businesses. This program, formerly administered by the Export-Import Bank of Washington, was transferred to A.I.D. on January 1, 1962.

ELIGIBILITY

Local currencies may be loaned to (1) U. S. firms or their branches, subsidiaries, or affiliates for business development and trade expansion in the foreign country, or (2) either U. S. firms or firms of the local country for expanding markets for, and consumption of, U. S. agricultural products abroad.

TERMS AND CONDITIONS

The currencies are available in countries where the U. S. has sold surplus agricultural commodities. The currencies may be used by the borrower to develop his business and to expand trade by financing such local costs as expansion of plant and equipment, land acquisition, working capital (in most of the countries), industrial training, and other normal costs of operations.

Cooley loans may *not* be made for the manufacture of products which would be exported to the United States in competition with U.S.-made products, and they may *not* be made for the production of commodities which would be marketed in competition with U. S. agricultural commodities. Cooley loans to foreign firms (non U.S.-affiliated borrowers) may *only* be made if they will be used to expand markets for U. S. agricultural products.

A.I.D. Cooley loans usually bear interest at rates comparable to those charged by local development banks. Maturities are related to the purposes of financing. Loans are repayable in the currency borrowed, without maintenance of value. In some cases, a guaranty of loan repayment may be required.

In countries where there are not sufficient Cooley funds to meet the demand, A.I.D. may impose priorities. Data on the

availability of Cooley funds are periodically published in A.I.D. press releases. Persons wishing to receive these releases regularly may request that their names be included on the mailing list by writing to: Office of Development Finance and Private Enterprise, A.I.D., Washington 25, D. C.

HOW TO APPLY

Inquiries regarding the Cooley fund program in general or the availability of Cooley funds in a given country, should be directed to: Office of Development Finance and Private Enterprise, A.I.D., Washington 25, D. C. Inquiries regarding Cooley loans to private borrowers for operations in a specific country should be addressed to the appropriate U. S. A.I.D. Mission or to the proper regional office of A.I.D., Washington 25, D. C. (See Exhibit I for a listing with addresses, by region, of the United States A.I.D. Missions and the A.I.D. regional offices in Washington.)

Letters of application (there is no special application form) must be in English. Three (3) copies should be sent to the U.S. A.I.D. Mission in the appropriate country or to the proper regional office of A.I.D., Washington 25, D. C.

The letter of application should include the following, where applicable:

1. Applicant's full legal name, address, nature (whether corportation, partnership, etc.), and the country in which organized or incorporated.
2. A brief biographical sketch of the principal owners, directors, officers and managers, including the percentage of U.S. and other ownership. Indicate the extent of management's experience and qualifications.
3. The amount of the loan requested from A.I.D. and a statement showing the specific uses to be made of the funds to be borrowed. If the loan is to finance the procurement of fixed assets, break down such procurement by categories—land, buildings, machinery, services and equipment, etc. If it is to provide working capital, break down into general purposes—inventory, installment sales or receivables, refinancing, payrolls, general expenses, etc.
4. The desired repayment period (in the form of a tentative repayment schedule).

5. If the enterprise is already in operation, submit (a) a current balance sheet and balance sheets for the prior three years, including statements of surplus, (b) a profit and loss statement for the past five years, (c) a statement of sources and uses of funds, and (d) a current cash flow statement, together with similar statements for the past three years. All financial statements should be audited if possible. Otherwise, they should be signed by an officer of the applicant.

6. All applicants must submit pro-forma balance sheets, and profit and loss and cash flow statements estimated for future years until operations become fully developed with debt servicing stabilized. Such statements should indicate clearly the assumptions made in the projections and the bases of these assumptions.

7. The name(s) of applicant's bank(s).

8. The total cost of the proposed project (including all equity investment contemplated), and the amount of source of, security for, and repayment terms for all proposed borrowing and other financing.

9. Pertinent economic data, including market studies, indicating the benefits which the proposed activity would yield to the enterprise and to the country.

10. If the activity will produce items for export, an estimate of the value of such exports and the probable markets.

11. If the applicant is not a U. S. firm or affiliate, an account of how the proposed activity will expand markets for U. S. agricultural commodities.

12. The name and address of any proposed guarantor, together with an audited, or signed, current financial statement of the guarantor.

SUBJECT: Investment Guaranties

A.I.D. seeks to increase investment by United States private enterprise in the economies of friendly less-developed countries by guarantying investors against certain political and business risks.

THE PROGRAMS

As described earlier, A.I.D. will make dollar and local currency loans, and share the cost of conducting investment surveys. The Agency will also enter into a contract with a firm that is planning to make a new investment or expand an existing investment in order to guaranty the firm against some of the political risks and, in certain cases, against a portion of the business risks inherent in foreign investment.

The purpose of the guaranty programs is to encourage and facilitate those private U. S. investments abroad which further the development of the economic resources and productive capacities of a less-developed country. Thus, guaranties are generally available only for new investment rather than for existing investments or investments which have been irrevocably committed before an application for a guaranty has been filed. Guaranties are available for additions to existing investments.

The role of the United States Government is to encourage desirable investment in those countries in which the investment guaranty program applies and then to act solely as a guarantor.

Under Sections 221 and 224 of the Foreign Assistance Act of 1961, Congress has authorized three investment guaranty programs:

1. The specific political risk guaranties against (a) inconvertibility of foreign currency, (b) expropriation or confiscation, (c) loss due to war, revolution or insurrection;
2. The extended risk guaranties which cover a portion of both political and business risks;
3. The extended risk guaranties covering losses on pilot or demonstration private housing projects in Latin America.

The specific political risk guaranty program has been in operation almost 15 years. The other two programs are new, and the policies and procedures governing them are, therefore, less refined.

THE SPECIFIC (POLITICAL) RISK PROGRAM

Guaranties are now available in forty-eight less-developed countries (and a number of overseas dependencies of the developed countries) against one, two, or all three of the following political risks:

- Inability to convert into dollars foreign currency representing earnings on, or return of, capital.

- Loss due to expropriation or confiscation.
- Loss due to war, revolution or insurrection.

(A list of the countries in the Specific-Risk Investment Guaranty Program, with the risks currently covered in each, is contained in Exhibit V.)

Agreements with Foreign Governments

Before guaranties can be issued for investments in a particular country or area, an agreement between the United States and the foreign government is signed to institute the guaranty program.

Primarily, this agreement provides the understandings between the two governments as to procedures, the status of local currency, and other claims which may be acquired by the United States when contracts of guaranty are invoked. This agreement also provides, in advance, orderly procedures for the handling of such currencies and claims.

Negotiations with countries not now in the guaranty program are currently underway, and it is therefore anticipated that additional countries will enter the program. Discussions are also being held with those countries which have so far only agreed to cover one or two of the specific risks described above, in the hope that they may agree to authorize additional coverage.

The agreement with the foreign government does not provide for special treatment by the host government of guarantied investments. Guaranties, however, provide the investor with the United States Government's assurance that he will be protected up to the amount specified in the guaranty from inconvertibility or from loss due to expropriation, confiscation, war, revolution or insurrection.

The Contract

After an agreement has been signed with the government, and the investment guaranty program is put into effect, guaranties are issued to the investor in the form of a contract between the investor and A.I.D.

The contract provides that payments due thereunder to investors shall be made from funds provided by the Congress. No obligations are placed on the investor other than those necessary in the administration of the guaranties. There is no interference in the operation of the business of the investor (or in the business of the recipient of the investment). However, the United States Government will, in accordance with good business practice—upon paying a claim to the guarantied investor—acquire the

currency or claim on which the payment is based. All the agreements between the United States Government and the investor are set forth in a contract. Each contract is negotiated in the light of the special circumstances of the investment concerned, and this contract governs the relationship between the investor and the United States Government.

Eligibility

To be eligible for guaranties the investment must be made by a citizen of the United States or a corporation, partnership, or other association created under the laws of the United States or of any state or territory, and substantially beneficially owned by citizens of the United States. Ordinarily, a company organized under United States law will be considered an eligible investor if more than one-half of the total value of all classes of its stock is owned by United States citizens.

In 1961, Congress also extended eligibility for investment guaranties to the wholly-owned foreign subsidiaries of eligible U. S. corporations.

It should be noted that there is no fixed form which an investment must take to be eligible for coverage.

Investment Contributions

Whether in the form of equity, loan, royalty (or leasing agreement), the investment contribution may be any of the following:

Cash: If cash is to be invested, it must be dollars or credits in dollars, or foreign currency (a) purchased with dollars for the purpose of the investment, or (b) otherwise acquired or owned by the investor, and freely transferable into dollars.

Materials or Equipment: Both new and used materials or equipment may be considered to be investment contributions. If new, material or equipment will ordinarily be valued at its cost to the investor. If used, it will ordinarily be valued at the value determined by an independent appraisal.

Patents, Processes or Techniques: Congress has made these intangible assets eligible for guaranty because of the desirability of encouraging the spread of advanced technological methods. However, the licensing of trade names, trademarks and good will, often closely associated with the licensing of patents, processes and techniques, is

not eligible for guaranty. It should also be understood that, to be eligible for guaranty, the patents, processes and techniques included in the investment should represent predominantly a body of information and experience already in existence.

Services: Contributions of engineering and management services will usually be considered investments only when performed for the purpose of transmitting other eligible investments, such as processes and techniques, and provided, of course, that the services are not to be currently and separately paid for. The cost of engineering surveys in advance of construction, and before the commitment for the investment is made, can be included as a part of the total investment if essential to the project for which the guaranty is sought—if such costs have been incurred for the express purpose of making construction of the project possible.

Loan Guaranties: In addition to the above types of investment contributions, guaranties of repayment given by investors on loans made by financial institutions may be considered to be eligible investments. This type of investment raises special problems. So, at the earliest opportunity, investors should write to: Investment Guaranties Division, A.I.D., Washington 25, D.C., outlining the proposed transaction.

Terms and Conditions

In general, guaranties must be approved by A.I.D. as furthering the economic development and productive capacities of an economically less-developed friendly country. This includes most projects which promote trade, increase production, raise standards of living, improve technical efficiency, etc.

At the present time, there is no restriction as to size of the investments which may be guaranteed. Guaranty contracts have been written for as little as $1,000 and for as much as $60 million.

Guaranty contracts may be written for a maximum term of twenty years from the date of issuance.

Before any investment guaranty contract is issued, A.I.D. requires the investor to secure approval from the foreign government for the inclusion of his project under the investment

guaranty agreement between the foreign government and the United States. This is done to (1) assure that the project is within the scope of the inter-governmental agreement, and (2) protect the interests of the United States, should a claim arise.

It must be emphasized that it is the responsibility of the investor to present to the foreign government the plan and details of the investment, to fulfill the foreign government's requirements regarding the investment, and to request the foreign government's written expression to the A.I.D. Mission or American Embassy of the approval of the project for investment guaranty purposes.

When the investor has obtained approval from the foreign government for inclusion of his project under the investment guaranty program, and when the terms of the proposal are clearly understood and found by A.I.D. to meet the criteria determining the availability of investment guaranties, a draft of a guaranty contract will be sent to the applicant for his approval. Each contract is drafted to meet the particular circumstances of the investment and the needs of the investor. After agreement is reached with the investor on the terms of the contract, the proposed contract and the application are submitted to the Administrator of A.I.D. or his delegate for final approval. If approved, the guaranty contract is then executed on behalf of the United States Government by A.I.D.

Fees

A fee is charged of ½ per cent of the amount of each coverage in force in any given contract year. There is also an annual fee of ¼ per cent of the amount of standby coverage—that is, the difference between the amount in force and the maximum amount which the investor may elect to have put in force. For the purpose of measuring fees there are three types of specific risk coverage: (1) inconvertibility, (2) expropriation and confiscation, (3) war, revolution and insurrection.

How to Apply

When a prospective investor's plans have been sufficiently developed to make it possible for him to do so, **but before he has made the investment or committed himself to make it,** he may file an application for an investment guaranty. Such an application need not be complete and final in every detail but should contain the *essential facts* about the proposed investment.

Where it is desirable for an investor to make an investment, or to enter into a firm commitment to make an investment, before an investment guaranty contract is issued, the investor may request that A.I.D. issue an assurance against prejudice on his application.

Such an assurance, sometimes called a "waiver" (or "no prejudice") letter, provides that the investor may proceed with his investment plans or enter into contracts without prejudicing his application for a guaranty. This assurance is usually valid for six months and may be extended.

This assurance, of course, does not commit A.I.D. to issue a guaranty contract, nor indicate that the foreign government will approve the project, nor assure the investor that further information about the proposed investment may not make it ineligible for guaranty. It merely avoids any subsequent objection that the application is untimely.

Inquiries regarding the specific-risk investment guaranty program should be sent directly to: Investment Guaranties Division, A.I.D., Washington 25, D. C.

Details on "How to Apply" are given in the A.I.D. "Investment Guaranty Handbook" which may be obtained without charge from the Investment Guaranties Division. U.S. Department of Commerce Field Offices are also generally familiar with the Investment Guaranty Program and can usually provide information and copies of the Investment Guaranty Handbook.

THE EXTENDED-RISK PROGRAMS

In addition to the specific-risk guaranties described on preceding pages, Congress has authorized A.I.D. to issue guaranties which cover commercial risks as well as political risks. These guaranties are issued in special and specific cases which occupy high-priority positions in the host country's development.

Two extended-risk guaranties are now offered. One type—General—may be applied in less-developed friendly countries to cover certain losses of private investment in priority projects. The other type (discussed under Extended-Risk Latin American Housing Guaranties later in this chapter) is specifically limited to guarantying private investment in self-liquidating pilot or demonstration housing projects in Latin America.

Extended-Risk General Guaranties

Eligibility

The rules governing eligibility for specific-risk guaranties also apply to the extended-risk "general" guaranties.

Terms and Conditions

1. Extended-risk guaranties will be considered only for projects where it can be clearly demonstrated that the private investment would not otherwise be made.
2. This type of guaranty will be issued only to investments in industries, or other areas of economic activity, which have been identified by A.I.D. as being of sufficient importance to qualify for a development loan. Emphasis shall be placed upon projects which further social progress and the development of small independent business enterprises.
3. Guaranties are available for loans as well as for equity investment.
4. Ordinarily, a fee of 2 per cent per annum of the face value will be charged for an extended-risk guaranty.
5. No individual guaranty shall exceed $25 million for a loan, $10 million otherwise.
6. The guaranty coverage will not extend to loss resulting from fraud or misconduct for which the investor is responsible or from normally insurable risks.

How to Apply

Inquiries regarding this program should be directed to: Office of Development Finance and Private Enterprise, A.I.D., Washington 25, D. C. This office will then advise prospective applicants of the procedure to be followed.

Extended-Risk Latin American Housing Guaranties

The Foreign Assistance Act of 1961 also authorized A.I.D. to guaranty private United States investment in self-liquidating pilot or demonstration private housing projects in Latin America.

This program is intended to stimulate private home ownership for middle and lower-middle income families by means of guaranties of long-term mortgage-type financing of housing projects, suitable for conditions in Latin America, and similar to those provided in the United States by the Federal Housing Administration. Guaranties may not be granted for investment in rental housing projects.

Since the housing guaranty program is designed to stimulate the development of demonstration housing projects which would

not have been undertaken without a guaranty, only applications for new housing projects will be considered.

Eligibility

Guaranties for Latin American housing projects are limited to U.S. capital investments made by U.S. citizens or U.S. business entities which are substantially beneficially owned by U.S. citizens.

Terms and Conditions

While A.I.D. may not fully guaranty an investment, it is permissible for an investor to obtain security from other sources for all or any part of the portion of the investment not guarantied by A.I.D.

Mortgages may not be held directly by U.S. investors under the guaranty program. An appropriate fiduciary in the host country should hold and service the individual mortgages for the benefit of the U.S. investor.

A fee, based upon the amount of the investment guaranteed, will be charged by A.I.D. for the guaranty. Such fee would not exceed 2 per cent of the amount of that portion of the investment guarantied.

No individual guaranty shall exceed $10 million.

How to Apply

Inquiries regarding this program should be directed to: Housing Guaranties Division, Office of Capital Development, Bureau for Latin America, A.I.D., Washington 25, D. C.

SUBJECT: Exhibits

Pertinent information which will be useful to United States private enterprise seeking investment opportunities in the economies of friendly less-developed countries, including a discussion of some other programs administered by other U. S. and international institutions.

EXHIBIT I

Addresses — A.I.D. Regional Offices Washington, and USAID Missions

(a) AID REGIONAL OFFICES, WASHINGTON:

For countries listed in Exhibit I(b) under **Africa-Europe:**

Office of Capital Development and Finance
Bureau for Africa-Europe
Agency for International Development
Washington 25, D. C.

For countries listed in Exhibit I(b) under **Far East:**

Capital Development and Finance Staff
Bureau for Far East
Agency for International Development
Washington 25, D. C.

For countries listed in Exhibit I(b) under **Latin America:**

Assistant Administrator
Bureau for Latin America
Agency for International Development
Washington 25, D. C.

For countries listed in Exhibit I(b) under **Near East and South Asia:**

Office of Capital Development and Finance
Bureau for Near East and South Asia
Agency for International Development
Washington 25, D. C.

(b) USAID MISSION ADDRESSES:

Sample: USAID to Afghanistan
c/o American Embassy
Kabul, Afghanistan

COUNTRY	CITY
AFRICA-EUROPE	**USAID c/o American Embassy**
Cameroon	Yaounde
Central African Republic	Bangui
Chad	Fort Lamy
Congo, Republic of	Brazzaville
Congo, Republic of the	Leopoldville
Dahomey	Cotonou
Eritrea	Asmara
Ethiopia	Addis Ababa
Gabon, Republic of	Libreville
Ghana	Accra
Guinea	Conakry
Ivory Coast	Abidjan

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COUNTRY	CITY
AFRICA—EUROPE	USAID c/o American Embassy
Kenya	Nairobi
Liberia	Monrovia
Libya	Tripoli
Malagasy Republic	Tananarive
Mali	Bamako
Morocco	Rabat
Niger	Niamey
Nigeria	Lagos
Rhodesia and Nyasaland (Federation of)	Salisbury
Senegal	Dakar
Sierra Leone	Freetown
Somalia	Mogadiscio
Sudan	Khartoum
Tanganyika	Dar-es-Salaam
Togo	Lome
Tunisia	Tunis
Uganda	Kampala
Upper Volta	Ouagadougou
FAR EAST	
Burma	Rangoon
Cambodia	Phnom Penh
China	Taipei
Indonesia	Djakarta
Korea	Seoul
Laos	Vientiane
Philippines	Manila
Thailand	Bangkok
Vietnam	Saigon
LATIN AMERICA	
Argentina	Buenos Aires
Bolivia	La Paz
Brazil	Rio de Janeiro
British Guiana	Georgetown
British Honduras	Belize
Chile	Santiago
Colombia	Bogota
Costa Rica	San Jose
Dominican Republic	Santo Domingo
Ecuador	Quito
El Salvador	San Salvador
Guatemala	Guatemala City
Haiti	Port-au-Prince
Honduras	Tegucigalpa
Jamaica	Kingston
Mexico	Mexico City
Nicaragua	Managua
Panama	Panama City
Paraguay	Asuncion
Peru	Lima
Surinam	Paramaribo

COUNTRY	CITY
LATIN AMERICA	**USAID c/o American Embassy**
Trinidad and Tobago	Port-of-Spain
Uruguay	Montevideo
Venezuela	Caracas
NEAR EAST AND SOUTH ASIA	
Afghanistan	Kabul
Ceylon	Colombo
Cyprus	Nicosia
Greece	Athens
India	New Delhi
Iran	Tehran
Iraq	Baghdad
Israel	Tel Aviv
Jordan	Amman
Lebanon	Beirut
Nepal	Kathmandu
Pakistan	Karachi
Syrian Arab Republic	Damascus
Turkey	Ankara
United Arab Republic	Cairo
Yemen	Taiz

EXHIBIT II

Edge Act Corporations*

FINANCING CORPORATION:	OWNED BY
Bamercial International Financial Corporation	Bank of America National Trust & Savings Assn., San Francisco, Cal.
Bankers International Financing Company, Inc.	Bankers Trust Company New York, N.Y.
Boston Overseas Financial Corporation	First National Bank of Boston Boston, Mass.
Chase International Investment Corporation	Chase Manhattan Bank New York, N.Y.
Chemical International Finance, Ltd.	Chemical Bank New York Trust Company, New York, N.Y.
Continental International Finance Corporation	Continental Illinois National Bank and Trust Company of Chicago, Chicago, Ill.
First National City Overseas Investment Corporation	First National City Bank New York, N.Y.
First Pennsylvania Overseas Finance Corporation	First Pennsylvania Banking & Trust Company, Philadelphia, Pa.
Manufacturers Hanover International Finance Corp.	Manufacturers Hanover Trust Company, New York, N.Y.
Morgan Guaranty International Finance Corporation	Morgan Guaranty Trust Company New York, N.Y.
Philadelphia International Investment Corporation	Philadelphia National Bank Philadelphia, Pa.
BANKING CORPORATION:	
Bank of America (International)	Bank of America National Trust & Savings Assn., San Francisco, Cal.
Bankers International Corporation	Bankers Trust Company, New York, N.Y.
Chase Manhattan Overseas Banking Corporation	Chase Manhattan Bank, New York, N.Y.
Chemical International Banking Corporation	Chemical Bank New York Trust Company, New York, N.Y.
Continental Bank International	Continental Illinois National Bank and Trust Company, Chicago, Ill.
The First Bank of Boston International	The First National Bank of Boston Boston, Mass.
Manufacturers Hanover International Banking Corp.	Manufacturers Hanover Trust Company, New York, N.Y.
Morgan Guaranty International Banking Corp.	Morgan Guaranty Trust Company New York, N.Y.
Western Bancorporation International Bank	The Philadelphia National Bank Philadelphia, Pa.

* The Edge Act and applicable regulations provide for two kinds of U.S. financial institutions authorized to do business outside the United States. Broadly defined: one, a banking corporation, may engage in commercial banking activities, but may not make equity investments; the other, a financing corporation, may not receive deposits but may make equity investments.

EXHIBIT III
Other International Financial Agencies

THE EXPORT-IMPORT BANK OF WASHINGTON

The Export-Import Bank of Washington (Eximbank, Washington 25, D. C.) is the oldest international finance agency of the United States Government. It seeks to stimulate and facilitate U.S. foreign trade by making (1) direct dollar loans for the purchase of U.S. goods and services, (2) guarantees and writing insurance on export transactions, and (3) medium-term exporter credits. It can assist export sales to customers in both developed and less-developed countries.

Established in 1934, Eximbank has authorized loans of more than $12,000,000,000 for the sale of United States products abroad. Most of the loans have covered the sale of capital equipment, agricultural machinery, and commodities such as cotton.

The Export-Import Bank is especially interested in making its facilities available for small transactions as well as large. Its smallest transaction to date has been $500. In 1961 more than 80 per cent of its exporter transactions were for less than $100,000, and 25 per cent were for less than $10,000.

Eximbank will not give its help in any undertakings for which, in its judgment, private capital is available on reasonable terms.

Eximbank welcomes and encourages commercial banks and other private institutions as participants in new loans and as purchasers of existing loans from its portfolio.

Direct Dollar Loans

Eximbank may finance up to 100 per cent of the dollar cost of loans to a public or private purchaser of equipment in a foreign country. Terms range from 5 to 20 years. The interest rate is currently 5¾ per cent per annum. There must be a finding of "reasonable assurance of repayment," with such repayment to be made in U.S. dollars.

Guarantees and Insurance

A new Eximbank program, designed in collaboration with private institutions, seeks to provide political and credit risk protection for American exporters and to make it easier for them to enlist private commercial bank participation in overseas transactions. The Foreign Credit Insurance Association (FCIA), through private insurance brokers and agents, issues to American exporters comprehensive policies covering both the political and the commercial risks of export sales. A consortium (union) of private United States insurance companies issues the policies with Eximbank covering the political component.

Medium-Term Exporter Credits

Another new Eximbank program has been designed to encourage commercial banks to extend more medium-term credit to exporters. This program offers guarantees directly to banks to cover their exposure when they finance medium-term export sales transactions without recourse to the exporter. The commercial bank assumes the commercial risk in the early maturities, which amounts to from 30 to 50 per cent of the total financing while Eximbank takes the rest.

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (WORLD BANK)

The International Bank for Reconstruction and Development (World Bank, 1818 H Street, N. W., Washington 25, D. C.) is currently owned by 91 member countries (see list on page 37), each subscribing to its capital stock in accordance with that country's own economic strength. The World Bank makes loans to governments, governmental agencies, and private enterprises of member countries mainly for undertakings directed toward helping the member countries build the infra-structure foundations of their economic growth.

The Bank, founded in 1946, turned from post-war reconstruction to development lending in 1948. Since then, an increasing proportion of its loans has been directed to the less-developed areas of the world. Its development loans have been for electric power, transportation and general industrial and agricultural development purposes.

If the borrower is not a government, the Bank requires the guarantee of the member government concerned. Normally, it finances only the foreign exchange costs involved in the purchase of imported goods and services and expects the borrower

to meet local costs, usually more than half the total, out of other resources.

The loans made by the Bank are amortized over a period of years determined by the type of project being financed. The Bank lends at the current cost of borrowed money, plus a 1 per cent per annum special reserve charge and about 1/4 per cent per annum for administrative expenses. The rate has varied from 3 per cent to 6 1/4 per cent, and currently is 5 3/4 per cent. The Bank does not distinguish between borrowers as to the rate of interest charged. There have been no losses on loans to date.

The World Bank also enlists the direct participation of private investors in its loans. By getting them to participate in new loans and selling them portions of loans from its portfolio, it has replenished its funds available for development financing. Sales to private participants are without recourse to the Bank.

INTERNATIONAL FINANCE CORPORATION

The International Finance Corporation (IFC, 1818 H Street, N. W., Washington 25, D. C.) is a unique public international corporation formed and owned by member governments (see list on page 37) to encourage productive *private* enterprise in member countries, particularly in the less-developed areas. It was established in July 1956, with authorized capital of $100,000,000.

IFC participates in projects in association with nationals of the country in which the project is located, or with foreign private investors, or a combination of the two. It does not invest in government-owned or government-operated undertakings, but its participation in an enterprise in which some public funds have been invested is not precluded if the project is essentially private in character.

Any enterprise in which IFC invests must be designed to make a useful contribution to the development of the economy of the member country in which it is located. IFC requires assurance that private investors will put up most of the necessary capital and that sufficient investment funds are not available elsewhere on reasonable terms. IFC does not engage in operations that are essentially for purposes of refunding or refinancing, nor does it finance exports or imports. And IFC does not invest in public utilities, such as electric power and transportation, in real estate development, such as housing and hotels, nor in irrigation, reclamation or drainage projects.

As a rule, IFC's share of the required financing is limited to 50 per cent of the total. The agency usually keeps its investment within the $500,000-$4,000,000 range. It may invest without tangible security. As a matter of principle, it will not exercise voting rights on stock it holds, and ordinarily does not seek representation on a company's board of directors.

IFC has no uniform interest rates for its loans. The rate for each investment is governed by relevant circumstances, such as the risks involved and the prospective over-all return on the investment. The agency charges a commitment fee of 1 per cent per annum of the undisbursed portion of its obligation.

Member Countries of the IBRD and IFC

The following countries are members of the World Bank. Those designated by an asterisk are *not* members of its subsidiary, the International Finance Corporation.

Afghanistan
Argentina
Australia
Austria
Belgium
Bolivia
Brazil
Burma
Cameroon
Canada
Central African Rep.*
Ceylon
Chad *
Chile
China *
Colombia
Congo (Brazzaville) *
Costa Rica
Cyprus
Denmark
Dominican Republic
Ecuador
El Salvador
Ethiopia
Finland
France
Gabon *
Germany
Ghana
Greece
Guatemala
Guinea *
Haiti
Honduras
Iceland
India
Indonesia *
Iran
Iraq
Ireland
Israel
Italy
Ivory Coast
Jamaica *
Japan
Jordan
Korea
Kuwait
Laos *
Lebanon
Liberia
Libya
Luxembourg
Malaya
Mexico
Morocco *
Nepal *
Netherlands
New Zealand
Nicaragua
Niger
Nigeria
Norway
Pakistan
Panama
Paraguay
Peru
Philippines
Portugal *
Saudi Arabia
Senegal
Sierra Leone
Somalia
South Africa
Spain
Sudan
Sweden
Syrian Arab Republic
Thailand
Tanganyika
Togo
Tunisia *
Turkey
United Arab Republic
United Kingdom
United States
Upper Volta
Uruguay *
Venezuela
Vietnam *
Yugoslavia *

INTER-AMERICAN DEVELOPMENT BANK

The United States and every country in Latin America, except Cuba, are members of the Inter-American Development Bank (IDB, 808 17th Street, N. W., Washington 6, D. C.). The IDB is a hemispheric version of the World Bank, but has a more diversified lending pattern.

The IDB, organized in 1959 to accelerate the economic development of the Latin American member countries, originally offered assistance through (1) its ordinary capital resources and (2) a Fund for Special Operations. On June 19, 1961, the agency added a third operation when it began to administer (3) a Social Progress Trust Fund that the U.S. Government entrusted to it to finance social development projects in Latin American countries. This fund consists of $394,000,000 of the $500,000,000 special fund that our Government set up in 1961 to speed social development in Latin America.

The funds from these three sources are held, and used, separately from one another. The IDB also provides technical assistance to borrowers in preparing development plans and projects.

Authorized ordinary capital of IDB is over $800 million. From these resources the Bank extends loans, repayable in the currencies lent, to private enterprises and public entities. The interest rate is currently 5¾ per cent per annum, of which 1 per cent represents a commission allocated to a special reserve. Terms for the most part are from 10 to 20 years, including grace periods. Commercial banks are participating in the early maturities of some of these loans, with no IDB guarantee.

During 1961 the Bank authorized 40 loans totaling almost $130 million from its ordinary capital. These included 10 loans for just under $50 million to development agencies for re-lending to private enterprise; 16 for $23 million directly to private enterprise; 12 for $55.8 million to governments and government entities, primarily for water supply, irrigation, and electric power; and 2 for $1.1 million to governments for technical assistance activities. Procurement anywhere in the free world is permitted.

Fund for Special Operations

The Bank lends from this fund on terms and conditions adapted to special circumstances arising in specific countries or in connection with specific projects; these conditions include re-

payment in the currency of the borrower. Interest rates run from 4 per cent to 5¾ per cent per annum. Terms for the most part are from 10 to 20 years, including grace periods. Procurement anywhere in the free world is allowed.

Social Progress Trust Fund

The IDB administers this fund under an agreement with the United States Government. The resources of the Trust Fund are used to bring about improvements in land settlement and land use, low-cost housing, community water supply and sanitation facilities, and advanced education and training.

Loans are in dollars, generally repayable in the currency of the borrower's nation. The rates of interest were from 1¼ to 2¾ per cent per annum as of March 31, 1962. An additional service charge of ¾ per cent a year is payable in dollars, however. Maturities have varied from 20 years to 30 years.

The above are major U. S. government and international agencies which make development loans to private borrowers as well as to governments.* However, there are other sources, also, including the European Development Fund and the public and private development banks in the developing countries as well as the Edge Act corporations and investment banking houses.

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* Two other agencies, the International Monetary Fund and the International Development Association, deal only with specialized areas of inter-governmental finance not of general interest to the business community. The Commodity Credit Corporation of the Department of Agriculture has a limited, specialized credit program to promote additional exports of U.S. surplus agricultural products in the CCC inventory.

EXHIBIT IV

Development Banks and Other Intermediate Credit Institutions to Which A.I.D. Has Authorized U.S. Dollar Loans and Guaranties (G)

(September 1, 1962)

COUNTRY OF OPERATION	NAME AND PRINCIPAL ADDRESS OF INSTITUTION
DEVELOPMENT BANKS	
AFRICA—EUROPE	
Ethiopia	Development Bank of Ethiopia P. O. Box 1900 Addis Ababa, Ethiopia
Liberia (G)	Bank of Monrovia Monrovia, Liberia
Morocco (G)	Banque Nationale pour le Development Economique Rabat, Morocco
Niger	Niger Development Bank Niamey, Niger
Somalia	Credito Somalo Mogadiscio, Somalia
Sudan	The Industrial Bank of Sudan Khartoum, Sudan
Tunisia	La Societe Tunisienne de Banque (STB) Palais Consuelaire 1 Ave. Habib Thameur Tunis, Tunisia
Uganda	Uganda Development Corporation Post Office Box 442 Kampala, Uganda

COUNTRY OF OPERATION	NAME AND PRINCIPAL ADDRESS OF INSTITUTION
DEVELOPMENT BANKS	
FAR EAST	
Korea	Reconstruction Bank of Korea Seoul, Korea
Philippines	Central Bank of the Philippines Manila, Philippines
Taiwan	China Development Corporation 181-5 Chung Shan Road, North Sec. Taipei, Taiwan
	Land Bank of Taiwan 25 Haiang Yang Road Taipei, Taiwan
	SMALL INDUSTRY FUND
	(1) First Commercial Bank of Taiwan 30 Chung Kung So. Road, Section 1 Post Office Box 56 Taipei, Taiwan
	(2) Chang Hua Commercial Bank 53 Tsu Yu Road Taichung, Taiwan
	(3) Hua Nan Commercial Bank, Ltd. 38 South Chung-King Road Taipei, Taiwan
	(4) Central Trust of China 96 Po-Ai Road Taipei, Taiwan
LATIN AMERICA	
Central America	Central American Bank for Economic Integration, Tegucigalpa, Honduras
Chile	CORFO (Corporación de Fomento de la Producion) Santiago, Chile
Ecuador	National Securities Commission Quito, Ecuador
Peru (G)	PERUINVEST (Peruano Suiza De Fomento E Inversiones SA.) Lima, Peru

COUNTRY OF OPERATION	NAME AND PRINCIPAL ADDRESS OF INSTITUTION
DEVELOPMENT BANKS	
NEAR EAST-SOUTH ASIA	
Egypt	Industrial Bank of Egypt El Galaa Street Cairo, Egypt
India	The Industrial Credit & Investment Corporation of India, Ltd. (ICICI) 163 Backbay Reclamation Bombay 1, India
	Industrial Finance Corporation of India (IFCI) Reserve Bank Building Parliament Street New Delhi, India
	National Small Industries Corporation 5-c Rani Jhansi Road New Delhi, India
Iran	Industrial & Mining Development Bank of Iran 204 Boulevard Abe-Karodj Post Office Box 1801 Teheran, Iran
Israel	Industrial Development Bank of Israel 22 Rothschild Boulevard Tel Aviv, Israel
Greece	National Bank of Greece 86 Eolou Street Athens, Greece
	Economic Development and Financing Organization (EDO) 8 Dragataanion Street Athens, Greece
Lebanon	Banque de Credit Agricole Industriel et Foncier (BCAIF) Riod El Solh Street Post Office Box 3696 Beirut, Lebanon
Nepal	Industrial Development Corporation of Nepal Judha Road Katmandu, Nepal

COUNTRY OF OPERATION	NAME AND PRINCIPAL ADDRESS OF INSTITUTION
DEVELOPMENT BANKS	
NEAR EAST—SOUTH ASIA	
Pakistan	Pakistan Industrial Credit & Investment Corporation, Ltd. (PICIC) Jubilee Insurance House McLeod Road Karachi, Pakistan
Syria	Industrial Bank of Syria Damascus, Syrian Arab Republic
Turkey	Industrial Development Bank Anadolu Sigorta Han Galata, Istanbul, Turkey
HOUSING INSTITUTIONS	
LATIN AMERICA	
Chile	Caja Central de Ahorros y Prestamos (Central Savings & Loan Bank) Santiago, Chile
Colombia	Instituto de Credito Territorial Bogota, Colombia
Colombia (G)	Las Americas Housing Project Cali, Colombia
Ecuador	Banco Ecuatoriano de la Vivienda (Ecuadorian Housing Bank) Quito, Ecuador
Honduras	SITRATERCO (Sindicato de Trabajadores de la Tela Railroad Co.) La Lima, Honduras
Panama	Caja de Ahorros Panama City, Panama
Peru	Association Mutual de Creditos para Vivienda "Peru" Jiron Huanacavelica 331 Lima, Peru
	Fondo Nacional para la Vivienda (Central Home Loan Bank) Lima, Peru

COUNTRY OF OPERATION	NAME AND PRINCIPAL ADDRESS OF INSTITUTION
HOUSING INSTITUTIONS	
LATIN AMERICA	
Venezuela	Fundacion de la Vivienda Popular (Foundation for Peoples Housing) Edificio las Fundaciones Avenida Andres Bello Local No. 6 Caracas, Venezuela
	Banco Obrero (National Housing Institute) Caracas, Venezuela
AGRICULTURAL CREDIT INSTITUTIONS	
AFRICA—EUROPE	
Tunisia	Banque Nationale Agricole (BNA) 19 Avenue de Paris Tunis, Tunisia
LATIN AMERICA	
Colombia	Caja de Credito Agrario Bogota, Colombia
Costa Rica	Banco Nacional de Costa Rica San Jose, Costa Rica
Guatemala	Banco de Guatemala Ciudad de Guatemala Guatemala
Mexico	Nacional Financiera, S. A. de Mexico Venustiano Carranza No. 25 Mexico 1, D. F.
Peru	Institute of Agrarian Reform and Colonization Lima, Peru
Venezuela	Agricultural Livestock Bank (Banco Agricola y Pecuario) Caracas, Venezuela

EXHIBIT V
Specific-Risk Investment Guaranty Program

Countries and Coverages Available—(January 1, 1963)

Country	Convertibility	Expropriation	War Risk
Afghanistan	Yes	Yes	Yes
Argentina	Yes	No	No
Bolivia	Yes	Yes	No
Chile	Yes	No	No
China, Republic of	Yes	Yes	Yes
Colombia	Yes	Yes	Yes
Congo (Brazzaville)	Yes	Yes	Yes
Congo (Leopoldville)	Yes	Yes	Yes
Costa Rica	Yes	Yes	No
Dominican Republic	Yes	Yes	Yes
Ecuador	Yes	Yes	No
El Salvador	Yes	Yes	No
Ethiopia	Yes	Yes	Yes
Ghana	Yes	Yes	No
Greeoe	Yes	Yes	No
Guatemala	Yes	Yes	No
Guinea	Yes	Yes	Yes
Haiti	Yes	Yes	No
Honduras	Yes	Yes	No
India	Yes	Yes	No
Iran	Yes	Yes	No
Israel	Yes	Yes	Yes
Ivory Coast	Yes	Yes	Yes
Jordan	Yes	Yes	Yes
Korea	Yes	Yes	Yes
Liberia	Yes	Yes	Yes
Malaya, Federation of	Yes	Yes	No
Morocco	Yes	Yes	Yes
Nepal	Yes	Yes	Yes
Nicaragua	Yes	Yes	Yes
Niger	Yes	Yes	Yes
Nigeria	Yes	Yes	No
Pakistan	Yes	Yes	No
Panama	Yes	Yes	Yes
Paraguay	Yes	Yes	No
Peru	Yes	No	No
Philippines	Yes	Yes	No
Portugal	Yes	Yes	No
Sierra Leone	Yes	Yes	Yes
Spain	Yes	Yes	No
Sudan	Yes	Yes	Yes
Thailand	Yes	Yes	Yes
Togo	Yes	Yes	Yes
Tunisia	Yes	Yes	Yes
Turkey	Yes	Yes	No
Uruguay	Yes*	Yes*	No
Venezuela	Yes	Yes	Yes
Vietnam	Yes	Yes	Yes
Yugoslavia	Yes	Yes	No

* Agreement in force when ratified by Uruguay's legislative body.

EXHIBIT VI

U.S. Department of Commerce Investment Programs and Services

While the Department of Commerce does not provide financial assistance to U. S. firms for the purpose of facilitating overseas investment, it does support extensive programs and provides services which can be of assistance in other ways.

These programs and services include: the network of Commercial Officers who are assigned to most of our diplomatic and/or consular establishments abroad; field offices in 34 cities of the United States (see page 46); the Office of Regional Economics which provides the Overseas Business Report; a pamphlet covering basic and authoritative information on specific countries needed by exporters, importers, investors, manufacturers, researchers, and all who are concerned with international trade and economic conditions throughout the world; the Commercial Intelligence Division which can furnish World Trade Directory Reports which contain commercial and financial information on specific foreign firms and individuals; the Business and Defense Services Administration which provides advice and analyses of the economic factors attendant to the sale, purchase, marketing of and/or investment in a specific commodity in foreign countries; Checklist, a bibliography and handy reference to the hundreds of published reports available to the U. S. business community interested in world trade and investment; and International Commerce, the principal weekly periodical published in the International Affairs area of the Department of Commerce. International Commerce contains practical and concise international marketing information, news and reports explaining potential advantages to U. S. businessmen in profitable international sales of U. S. products, and lists of many investment opportunities from around the world.

Detailed information relative to investment opportunities abroad is available to U. S. firms through the Office of International Investment, Bureau of International Commerce, U. S. Department of Commerce, Washington 25, D. C.

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SPECIMEN CONTRACT FORMS

SPECIMEN
A.I.D. CONTRACT OF GUARANTY
NO.________________

CONTRACT OF GUARANTY (CONVERTIBILITY-LOAN)

Contract of Guaranty made and entered into by and between the AGENCY FOR INTERNATIONAL DEVELOPMENT (hereinafter called "A.I.D."), an agency of the United States of America, and /Firm Name/ (hereinafter called "Investor"), a corporation organized and existing under the laws of /Place of Incorporation/ , having its principal place of business at /Street, City, Zone, State/

/ Brief description of Investor's business. /

/Name of the foreign firm which will receive the investment./ , (hereinafter called the "Foreign Enterprise") is a / corporation, limited company, etc., as applicable / organized and existing under the laws of / place of charter or incorporation /. The Foreign Enterprise / brief description of the business of the Foreign Enterprise and the purpose of the investment /.

/ List and incorporate any investment approvals given by the government of the country where the investment will be made./

/ Description of the notes which the Investor will receive from the Foreign Enterprise. / Said notes (hereinafter called the "Notes") will be issued to the Investor by the Foreign Enterprise / against payment of, in exchange for, etc., as applicable / the Investment, as hereinafter defined.

The Investor has filed with A.I.D. pursuant to the provisions of Section 221(b) of the Foreign Assistance Act of 1961, as amended, (hereinafter called the "Act") and to the rules and regulations prescribed by the Administrator of A.I.D. thereunder, an application for a guaranty of convertibility of investment earnings and return of capital.

A.I.D. and the Government of /Name of the country where the investment will be made/ have each approved the Project, as hereinafter defined.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, A.I.D. and the Investor hereby agree as follows:

ARTICLE I
Definitions

Wherever used in this contract:

I-A. The term "Date of This Contract" means that date, shown on the last page of this contract, on which this contract was executed for A.I.D.

I-B. The term "Contract Period" means:

1. the year beginning on the Date of This Contract, such Contract Period being hereinafter called the First Contract Period, and
2. periods of one year in length, each commencing on the successive anniversaries of the Date of This Contract.

I-C. The term "Investment Earnings" means, on any date, the amounts received by the Investor subsequent to the Date of This Contract as payments of interest on the Notes and redemption premiums, if any, which the Foreign Enterprise may owe the Investor in connection with the Notes acquired as a result of the Investment and in the Investor's possession on such date.

Investment Earnings are, by the terms of the Notes, to be paid in the United States of America in United States dollars. For purposes of this contract, however, if the Foreign Enterprise is unable, by operation of any law, decree, regulation or administrative determination recognized as being then in effect by the governing authorities of the Project Country, as hereinafter defined, to obtain the United States dollars required to discharge its obligations on the Notes, and subsequently attempts to discharge its then obligations on the

Notes by making payments in Local Currency, as hereinafter defined, and such payments are accepted by the Investor in lieu of United States dollar payments, such Local Currency payments are to be included in the term "Investment Earnings".

I-D. The term "Return of Capital" means, on any date, the amounts received by the Investor subsequent to the Date of This Contract as payments of principal of the Notes acquired as a result of the Investment and in the Investor's possession on such date.

Return of Capital is, by the terms of the Notes, to be paid in the United States of America in United States dollars. For purposes of this contract, however, if the Foreign Enterprise is unable, by operation of any law, decree, regulation or administrative determination recognized as being then in effect by the governing authorities of the Project Country, to obtain the United States dollars required to discharge its obligations on the Notes, and subsequently attempts to discharge its then obligations on the Notes by making payments in Local Currency, as hereinafter defined, and such payments are accepted by the Investor in lieu of United States dollar payments, such Local Currency payments are to be included in the term "Return of Capital".

I-E. The term "Guaranty Period" means (a) the period of twenty years plus two months from the date, shown on the last page of this contract, on which this contract was executed and issued, or (b) if terminated pursuant to Article IV or IX, then to and including the effective date of such termination.

I-F. The term "Date of Application" means the date of delivery to A.I.D. of an application for transfer hereunder.

I-G. The term "Local Currency" means currency recognized when received by the Investor as legal tender in the Project Country, as hereinafter defined, by the governing authorities thereof.

I-H. The term "Life of This Contract" means (a) a period of twenty years from the date, shown on the last page of this contract, on which this contract was executed and issued; or (b) if terminated pursuant to Article IV or IX, then to and including the effective date of such termination.

I-I. The term "Reference Date" means (a) in any case where the Investor makes application for transfer of Local Currency hereunder on the ground that such currency is eligible under clause 2 of Article V, the date which is sixty (60) consecutive days before the Date of Application, and (b) in all other cases, the date which is thirty (30) consecutive days before the Date of Application.

I-J. The term "Date of Notice" means the date of delivery to A.I.D. of the notice specified for the purpose of Article VII hereof of submission of an application for transfer of Local Currency to that agency of the governing authorities of the Project Country, as hereinafter defined, which legally or under color of law controls the transfer of Local Currency into U. S. dollars.

I-K. The term "Reference Rate of Exchange" means, on any day specified herein, the rate of exchange certified by the Federal Reserve Bank of New York to the Secretary of the Treasury for such day for the purpose of computing the U. S. dollar amounts of duties on commodities imported into the United States from the Project Country, as hereinafter defined, as required by the U. S. customs laws, provided that one, but not more than one, such rate is certified to the Secretary of the Treasury for such purpose as of such date.

If no one such rate or value is certified to the Secretary of the Treasury on such date, the rate to be used for purposes of this Article I-K shall be the average effective rate which, on the day specified herein, is lawfully charged under the laws of the Project Country, as hereinafter defined, to residents of said Project Country, exclusive of governmental entities, for that group of commodity exports from the United States to said Project Country, the U. S. dollar value of which during the one-year period preceding such day constituted a larger amount than the value of any other group of such exports to which a differenct single rate is applicable on such day. In determining the relative U. S. dollar value of groups of such exports to which a different rate may be applicable, statistics of the U. S. Bureau of the Census covering the most recent one-year period available will be conclusively presumed to be the best available evidence, provided that statistics necessary for this purpose were being maintained on a current basis on the day specified herein.

I-L. The term "Project Country" means the territory presently under the jurisdiction of ______________________.

I-M. The term "Maximum Amount of the Guaranty" means:

____.

Such amount shall be progressively reduced by any amounts received by the Investor as transfers under this contract, such reduction to take effect as of the first day of the Contract Period next succeeding the Contract Period in which the applicable Reference Date occurred. Such amount shall also be subject to reduction by the Investor as provided in Article IX-B hereof.

A.I.D. shall refund to the Investor the portion of the Fee(s) for This Contract, as hereinafter defined, paid for the amount by which the Maximum Amount of the Guaranty is reduced during the Contract Period(s) commencing with the effective date of the reduction.

I-N. The term "Face Amount of the Guaranty" means the following amounts for the Contract Periods indicated:

1. During the First Contract Period; ______________________

   ____

2. During the Second Contract Period and each succeeding Contract Period; any amount elected by the Investor as provided in Article IX-B hereof but not greater than the Maximum Amount of the Guaranty as of the first day of each Contract Period.

Such amount shall be progressively reduced by any amounts received by the Investor as transfers under this contract, each such reduction to take effect as of the applicable Reference Date.

I-O. The term "Fee for This Contract" means the amount of $________________ for the First Contract Period payable on or before the Date of This Contract, and an amount payable on or before the first day of each Contract Period thereafter during the Life of This Contract, which amount shall be equal to the sum of:

1. one-half of one percent (½%) of the Face Amount of the Guaranty for the respective ensuing Contract Period and
2. one-quarter of one percent (¼%) of the amount, if any, by which the Maximum Amount of the Guaranty exceeds the Face Amount of the Guaranty for such respective ensuing Contract Period.

ARTICLE II
Guaranty

Subject to the terms and conditions of this contract, A.I.D. hereby guarantees to the Investor, upon application, the transfer into United States dollars, up to the Face Amount of the Guaranty as of the applicable Reference Date, of Local Currency which is received by the Investor during the Life of This Contract as Return of Capital or Investment Earnings and which, during the Guaranty Period, is eligible for transfer under Article V of this contract.

ARTICLE III
Representations and Covenants

The Investor hereby represents to A.I.D. that, as of the date on which this contract is executed by the Investor:

III-A. The Investor is a corporation created under the laws specified in the first paragraph on page 1 of this contract, and is substantially beneficially owned by citizens of the United States.

III-B. The Investor has disclosed to AID all then existing arrangements and agreements of whatever nature, with respect to the transfer from the Project Country of U.S. dollars, Local Currency or other currencies, and credits in any of the foregoing, to be received by the Investor as Investment Earnings or Return of Capital subsequent to the Date of This Contract.

The Investor hereby covenants with A.I.D. that:

III-C. The Investor will make payment to A.I.D. of the Fee for This Contract in the amount and manner specified in Article I.

III-D. The Investor will continue during the Guaranty Period to be a corporation created under the laws of the United States, or of one of the states or territories of the United States. In the event that the Investor shall during such period cease to be substantially beneficially owned by citizens of the United States, the Investor shall give prompt notice of that fact to A.I.D. and A.I.D. shall have the rights of termination or refusal to make transfers as provided under paragraph A of Article IV in the case of breach of covenant.

III-E. The Investor will disclose promptly to A.I.D. in detail all arrangements and agreements of whatever nature which, during the Guaranty Period are entered into by the Investor with respect to the transfer from the Project Country of U.S. dollars, Local Currency or other currencies, and credits in any of the foregoing, received by the Investor as Investment Earnings or Return of Capital subsequent to the Date of This Contract.

III-F. The Investor during the Guaranty Period will submit to A.I.D. at least thirty (30) days prior to each date upon which the Fee for this Contract shall be due beginning with the second Contract Period a progress report in duplicate, in such form as A.I.D. may specify, indicating the amount of the Investment, made, all sums received as Return of Capital in U.S. dollars, Local Currency or other currencies, and credits in any of the foregoing, and such other information as A.I.D. shall reasonably require. The first such report shall cover the period from the Date of This Contract until thirty (30) days prior to its due date, and subsequent reports shall cover the respective successive 12-month periods.

III-G. The Investor will maintain in a place accessible to A.I.D. or its duly authorized representatives, books of account and other records, in accordance with generally accepted accounting principles, covering the amount of the Investment, Investment Earnings, Return of Capital, and all other receipts, expenditures and transactions by the Investor in U.S. dollars, Local Currency or other currencies, and credits in any of the foregoing, in the Project

Country or elsewhere, in connection with the Investment. During the Guaranty Period, and for five years thereafter, the Investor will permit A.I.D. or its duly authorized representatives, to inspect, examine and audit said accounts and records, whether they be located in the Project Country or elsewhere. During the Guaranty Period and for five years thereafter, the Investor will use its best efforts to enable the duly authorized representatives of A.I.D. to examine, audit and copy for the purpose of this contract any books and records of the Foreign Enterprise, and to inspect its properties, whether in the Project Country or elsewhere, and the Investor will render every reasonable assistance in connection therewith.

III-H. The Investor will not assign, transfer, pledge or make other disposition of this contract or of any of the rights of the Investor hereunder without first obtaining the consent of A.I.D. thereto in writing.

III-I. No member of or delegate to Congress or resident commissioner shall be admitted to any share or part of this contract or to any benefit that may arise therefrom, but this provision shall not be construed to extend to this contract if made with a corporation for its general benefit.

III-J. Unless A.I.D. first agrees otherwise in writing, the Investor will, to the extent of Investor's ability, cause the Investment to be made substantially in accordance with this Contract of Guaranty and with the material representations submitted in obtaining this contract of Guaranty.

ARTICLE IV
Misrepresentation and Breach of Covenant

IV-A. In the event that the Investor shall have made a material misrepresentation of any fact stated in paragraph A or B of Article III hereof, or shall breach any covenant contained in paragraphs D, E, H or I of said Article, A.I.D. shall have the right to terminate this contract at any time by written notice given to the Investor, and, with or without exercising such right of termination, shall have the right to refuse to make any transfer for the Investor hereunder.

IV-B. In the event that the Investor shall breach any covenant contained in any paragraph of Article III other than paragraphs D, E, H or I thereof, A.I.D. may, at its option, do any or all of the following:

1. terminate this contract by giving not less than thirty (30) days written notice to the Investor. Such notice shall contain a statement of A.I.D.'s intention to terminate, the reason upon which the termination is based, and the date upon which the termination is effective. Unless the Investor shall have cured such breach prior to said date, all obligations of A.I.D. hereunder shall terminate on said date, except as to any rights of the Investor which have accrued prior to such breach and with respect to which any application or applications are then pending;

2. refuse to make any transfer for the Investor based upon an application filed subsequent to the breach unless the Investor shall cure the breach within thirty (30) days after A.I.D. shall give notice to the Investor of the existence of the breach;

3. make such arrangements as it deems proper with the Investor to provide for the cure of the breach.

IV-C. In the event of any termination of this contract by A.I.D. all rights, liabilities and obligations under this contract, except as expressly continued by paragraph B of this Article, shall cease, except the following obligations of the Investor:

1. to comply with the covenants and agreements contained in paragraphs G and H of Article III hereof; and

2. to make any repayment required by paragraph E of this article IV.

IV-D. In the event of misrepresentation or breach giving rise to the right of A.I.D. to terminate this contract as hereinabove provided, neither the acceptance of any fee by A.I.D. after the occurrence of such misrepresentation or breach, nor the fact that A.I.D. shall have had knowledge, actual or constructive, of the occurrence of such misrepresentation or breach and shall have failed to exercise its right of termination, shall operate as a waiver of the right of A.I.D. to terminate this contract or to refuse to make a transfer for the Investor hereunder unless the Investor is fully carrying out arrangements agreed to pursuant to IV-B3.

IV-E. If A.I.D. shall have made any transfer for the Investor hereunder and shall thereafter ascertain that, prior to such transfer, the Investor misrepresented any fact stated in paragraph A or B of Article III, or, prior to the date of such transfer, breached any covenant in paragraph D, E, H, I, or J of Article III, or made any material misstatement of fact in the application for such transfer, then, on demand of A.ID., contained in a written notice given to the Investor within one year after ascertaining that any such misrepresentation or breach has occurred or such misstatement was made, the Investor shall immediately repay A.I.D. the amount of U. S. dollars so paid to the Investor, and upon receiving such repayment A.I.D. shall effect repayment to the Investor of the amount of the Local Currency received from the Investor in any such transfer, provided, however, A.I.D. may not assert such demand after the expiration of the period of five (5) years immediately succeeding the misrepresentation, breach or misstatement occasioning the demand.

IV-F. In the event and to the extent that A.I.D. shall without sufficient legal cause have refused to make any transfer hereunder, A.I.D. shall not be liable to the Investor for damages beyond the amount herein expressly provided to be paid by A.I.D. with respect to such transfer.

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ARTICLE V
Local Currency Eligible for Transfer

Local Currency received by Investor as Investment Earnings or as Return of Capital during the Life of This Contract and not held by Investor for more than eighteen (18) months shall be eligible for transfer under this contract:

1. if the Investor is prevented for a period of thirty (30) consecutive calendar days from effecting the transfer of such Local Currency into U. S. dollars by operation of any law, decree, regulation or administrative determination recognized as being in effect by the governing authorities of the Project Country, which regulates the transfer of Local Currency into U. S. dollars; or
2. if the Investor is prevented from effecting the transfer of such Local Currency into U. S. dollars by the failure by that agency of the governing authorities of the Project Country which legally or under color of law controls the transfer of Local Currency into U. S. dollars, to grant an application made to such agency by the Investor for the transfer of such Local Currency, provided such application has been pending for at least sixty (60) consecutive calendar days; or
3. if the Investor is unable to transfer such Local Currency into U. S. dollars in any market or through any channel through which dollar exchange transactions

are then being legally and normally effected except at a rate of exchange which, at the close of business on each of the thirty (30) consecutive calendar days immediately preceding the Date of Application hereunder, is less favorable to the Investor than the rate determined as of each of such days in accordance with the provisions of Article VI hereof;

provided, however, (a) that the Investor has taken all reasonable steps required to effect such transfer under such laws, decrees, regulations or administrative determinations, (b) that the inability of the Investor to effect such transfer does not result from the operation of any law, decree, regulation or administrative determination which is recognized as being in effect by the governing authorities of the Project Country on the Date of This Contract and of which the Investor can reasonably be expected to have knowledge, and (c) that, with respect to Local Currency in its possession, the Investor has made reasonable efforts to comply with all laws, decrees, regulations or administrative determinations of which it can reasonably be expected to have knowledge and which regulate the transfer of Local Currency investment receipts into U. S. dollars.

ARTICLE VI
Rate of Exchange for Transfers

Transfers of Local Currency into U. S. dollars under this contract by A.I.D. shall be made at a rate which shall yield ninety-five percent (95%) of the U.S. dollars which would be yielded as of the Reference Date, by applying the Reference Rate of Exchange.

ARTICLE VII
Application for Transfer

VII-A. If the Investor has made application for the transfer of Local Currency to that agency of the governing authorities of the Project Country which legally or under color of law controls the transfer of such currency, the Investor may give written notice thereof to A.I.D. provided that with such notice the Investor shall submit any and all documents or other evidence which the Investor may then have with respect to its right subsequently to file an application for transfer with A.I.D. hereunder.

VII-B. At one or more times during the Guaranty Period, application under this contract may be made by the Investor for the transfer of Local Currency which is eligible for transfer into U.S. dollars under this contract. Each application shall be submitted to A.I.D. in a form satisfactory to A.I.D. The Investor shall submit such evidence as A.I.D. may reasonably require in order to enable it to determine whether and to what extent the Investor is entitled by the provisions of this contract to the transfer for which application has been made.

VII-C. The Investor shall sumbit a draft drawn to the order of A.I.D. or any agent designated by A.I.D., upon a depository acceptable to A.I.D., for the Local Currency which is eligible for transfer into U.S. dollars under this contract and for which application for transfer is made. Such draft shall be submitted at the time of the filing of an application hereunder or at any time thereafter provided that, in any event, it shall be submitted within a reasonable period after the Date of Application, or within five (5) days after

receipt of written demand by A.I.D.; any such Local Currency not covered by a draft thus submitted shall be thereafter ineligible for transfer under said application.

VII-D. In any case, an application for transfer shall expire at the end of a period of six (6) months from the date of its receipt by A.I.D. unless a draft for the Local Currency covered thereby has been previously received by A.I.D.; provided, however, that nothing herein shall be deemed to impair the effectiveness of any subsequent applications which the Investor may file with respect to the transfer of the same currency or of other Local Currency eligible for transfer.

VII-E. A.I.D. shall have a reasonable period not in excess of sixty (60) consecutive calendar days from the date of receipt of the draft or drafts referred to in the previous paragraph to make such transfer in whole or in part or to refuse to make such transfer in whole or in part; provided, that if the Investor's application is based on clause 2 of Article V and if the Investor has given written notice to A.I.D. that it has filed an application for transfer of Local Currency with that agency of the governing authorities of the Project Country which legally or under color of law controls the transfer of such currency, such sixty (60) day period shall be reduced by a period equivalent to the number of days between the Date of Notice and the Date of Application; provided further that such sixty (60) day period shall in no event be reduced to less than thirty (30) days. In no instance shall the receipt by A.I.D. of an application, statement or other evidence operate to create any presumption in favor of the Investor that it shall be entitled by the terms of this contract to receive the transfer into U.S. dollars for which application has been made.

VII-F. A.I.D. shall consult with the Investor or otherwise afford the Investor a reasonable opportunity to present its views on any question of fact which A.I.D. must resolve in determining whether and to what extend any transfer applied for shall be made.

VII-G. If and to the extent that A.I.D. shall refuse to make transfer pursuant to application hereunder, it shall return to the Investor any draft or drafts submitted in connection with such application and any portion of the Local Currency proceeds from such drafts with respect to which transfer into dollars under this contract has been refused.

ARTICLE VIII
Funds Available for Payment of Guaranty

VIII-A. The only funds which will be available to A.I.D. for the purpose of discharging liability under this and all other contracts of guaranty which may have been or may hereafter be entered into pursuant to the authority of Section 221(b) of the Act, Sections 202(b) and 413(b)(4) of the Mutual Security Act of 1954, as amended, and Section 111(b)(3) of the Economic Cooperation Act of 1948, as amended (exclusive of informational media guaranties), are (i) those specified in Section 222 of the Act, and (ii) other funds, if any, which may be available at any time hereafter for the aforesaid general purpose, pursuant to the laws of the United States.

VIII-B. The Investor shall have no right or claim arising out of this contract against any other asset of A.I.D.

ARTICLE IX
Termination and Reduction

IX-A. The Investor shall have the right to terminate this contract effective on the first day of any Contract Period by written notice given to A.I.D. on or prior to such day. Such termination shall, from its effective date, relieve the Investor of all further obligations to pay the Fee for This Contract, but it shall not discharge or affect any other right, liability or obligation of either party which has accrued prior to the effective date of the termination of this contract or which, by the terms of this contract, is to survive the Guaranty Period.

IX-B. Prior to the first day of any Contract Period the Investor may by giving written notice to A.I.D.:

(1) Elect a Face Amount of the Guaranty for the ensuing Contract Period.

(2) Reduce the Maximum Amount of the Guaranty for the remaining Contract Periods.

Election under (1) shall be in effect only for the Contract Period requested by the Investor and reduction under (2) shall be permanent and may not be reinstated. Reductions pursuant to this Article shall become effective on the first day of any Contract Period immediately following delivery to A.I.D. of written notice thereof and shall not affect the amount of the fee payable, or the retention by A.I.D. of any fee paid, for any period prior to the date on which such reductions become effective.

ARTICLE X
Modification

Any provision(s) of this contract may be modified, supplemented or otherwise altered by mutual agreement in writing.

ARTICLE XI
Notices

XI-A. Written notice to the respective parties may be delivered by:

1. making personal delivery of such notice to the Investment Guaranties Division, Agency for International Development, or to one of the representatives of the Investor, authorized pursuant to Article XII hereof,

   or

2. depositing such notice in the U.S. Post Office by registered mail enclosed in an envelope, postage prepaid, addressed to the party concerned at the address below specified, or to such other address as may be specified in writing from time to time:

   To: INVESTMENT GUARANTIES DIVISION
   AGENCY FOR INTERNATIONAL DEVELOPMENT

   At: WASHINGTON 25, D. C.

   To: THE INVESTOR

   At: The address stated in the first paragraph on page 1 of this contract

XI-B. The date of delivery under A.1. shall be the date on which the notice is received and under A.2. shall be the date on which the item was registered.

ARTICLE XII
Authority of Representatives

Prior to and as a condition of receiving any payment under this contract the Investor shall furnish A.I.D. with evidence of the authority of the persons who will act as representatives of the Investor in connection with the operation of this contract. A.I.D. shall be entitled to rely on such evidence of authority until A.I.D. shall receive written notice from the Investor that such persons are no longer authorized so to act; and in the event of such notice, the Investor will promptly furnish A.I.D. with evidence of the authority of persons authorized to act in their place and stead.

ARTICLE XIII
Disclaimer

The approval of A.I.D. of this Investment for guaranty purposes is not to be construed as an acknowledgement of the legality of the agreements or arrangements constituting or relating to this Investment, or of any acts in pursuance thereof, under the laws, including the antitrust laws, of the United States or of the Project Country.

ARTICLE XIV
Arbitration

Any question which shall arise as to the obligation of either party under this contract or the interpretation of any provision thereof, if not settled by mutual agreement, shall, at the option of either party and, upon written notice to the other party, be settled by arbitration. The arbitration shall be held at Washington, D. C., and shall be conducted in accordance with the then prevailing rules of the American Arbitration Association. In any such arbitration A.I.D. shall appoint one arbitrator, the Investor shall appoint another, and the two so appointed shall appoint a third arbitrator; provided, however, that if any arbitrator or arbitrators are not appointed in accordance with the foregoing provisions of this Article within sixty (60) days after notice for arbitration has been given, such arbitrator or arbitrators shall be appointed in accordance with the rules above mentioned.

The controversy shall be submitted to the arbitrators in such manner as they shall deem appropriate, consistent with the then prevailing rules of the American Arbitration Association, and the decision of a majority of the arbitrators, rendered in writing, shall be final and conclusive and binding on the parties.

Each party shall pay its own expenses in connection with the arbitration, but the compensation and expenses of the arbitrators shall be borne in such manner as may be specified in the decision of the arbitrators.

Each party shall, in any arbitration hereunder, have the right to appear and be heard and present evidence before the arbitrators.

IN WITNESS WHEREOF, the parties hereto have caused this contract to be duly executed and issued in duplicate at Washington, District of Columbia, United States of America, as of the date, shown below, on which this contract was executed for A.I.D.

AGENCY FOR INTERNATIONAL DEVELOPMENT

By________________________
Assistant Administrator

Date______________________

NAME OF COMPANY OR INDIVIDUAL

By________________________

Date______________________

A.I.D. CONTRACT OF GUARANTY

No. (Specimen)

CONTRACT OF GUARANTY (CONVERTIBILITY-EQUITY)

Contract of Guaranty made and entered into by and between the AGENCY FOR INTERNATIONAL DEVELOPMENT (hereinafter called "A.I.D."), an agency of the United States of America, and ______________________________ (hereinafter called "Investor"), a corporation organized and existing under the laws of ____________________, having its principal place of business at ____.

The Investor is a corporation substantially beneficially owned by citizens of the United States and is engaged in _______________________ ____ ____.

The Investor proposes to invest in ______________________________ ________________________ (hereinafter called the "Foreign Enterprise"), a corporation organized and existing under the laws of _________________, which was formed for the purposes of _____________________________ ____.

The Investor contemplates a total investment of U. S. $_____________, of which amount approximately U. S. $_______________ will be utilized for the purchase of ____________ percent (%) of the equity shares of the Foreign Enterprise. The investment will be utilized for _________________ ____

The Investor has filed with A.I.D. pursuant to the provisions of Section 221(b) of the Foreign Assistance Act of 1961, as amended, (hereinafter called the "Act"), and to the rules and regulations prescribed by the Administrator of A.I.D. thereunder, an application for a guaranty of convertibility of investment earnings and return of capital.

A.I.D. and the Government of _______________ have each approved the Project, as hereinafter defined.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, A.I.D. and the Investor hereby agree as follows:

ARTICLE I
Definitions

Wherever used in this contract:

I-A. The term "Date of This Contract" means that date, shown on the last page of this contract, on which this contract was executed for A.I.D.

I-B. The term "Contract Period" means:

1. the year beginning on the Date of This Contract, such Contract Period being hereinafter called the First Contract Period, and

2. periods of one year in length, each commencing on the successive anniversaries of the Date of This Contract.

I-C. The term "Investment Earnings" means the amounts received subsequent to the Date of This Contract by the Investor as dividends on the Equity Shares held by the Investor as a result of the Investment, as hereinafter defined, but exclusive of dividends paid in complete or partial liquidation of said Equity Shares.

I-D. The term "Return of Capital" means the amounts received by the Investor subsequent to the Date of This Contract as dividends paid in complete or partial liquidation of the Equity Shares held by the Investor as a result of the Investment, as hereinafter defined, or as proceeds from the sale or transfer in the Project Country, as hereinafter defined, of all or any part of the Equity Shares held by the Investor as a result of the Investment.

I-E. The term "Guaranty Period" means (a) the period of twenty years plus two months from the date, shown on the last page of this contract, on which this contract was executed and issued, or (b) if terminated pursuant to Article IV or IX, then to and including the effective date of such termination.

I-F. The term "Date of Application" means the date of delivery to A.I.D. of an application for transfer hereunder.

I-G. The term "Local Currency" means currency recognized when received by the Investor as legal tender in the Project Country, as hereinafter defined, by the governing authorities thereof.

I-H. The term "Life of This Contract" means (a) a period of twenty years from the date, shown on the last page of this contract, on which this contract was executed and issued; or (b) if terminated pursuant to Article IV or IX, then to and including the effective date of such termination.

I-I. The term "Reference Date" means (a) in any case where the Investor makes application for transfer of Local Currency hereunder on the ground that such currency is eligible under clause 2 of Article V, the date which is sixty (60) consecutive days before the Date of Application, and (b) in all other cases, the date which is thirty (30) consecutive days before the Date of Application.

I-J. The term "Date of Notice" means the date of delivery to A.I.D. of the notice specified for the purpose of Article VII hereof of submission of an application for transfer of Local Currency to that agency of the governing authorities of the Project Country, as hereinafter defined, which legally or under color of law controls the transfer of Local Currency into U.S. dollars.

I-K. The term "Reference Rate of Exchange" means on any date:

First, the effective (including for example exchange taxes, transfer taxes or margins however designated) free market rate of exchange applicable to the purchase in the Project Country of United States dollars with Local Currency on such date by a private investor or investors remitting earnings or capital or a private borrower servicing United States dollar debt, or if no single such rate can be determined, then the average of such rates on such date as obtained from a representative group of banks in the Project Country, but if no such rate exists on such date then;

Second, the most depreciated (that is requiring the greatest amount of Local Currency per United States dollar) effective rate of exchange published or used by the central bank of the Project Country on such date for sale of United States dollars to private residents of the Project Country for imports into the Project Country.

In the event either A.I.D. or the Investor regard the above rates as either inapplicable or achieving an inequitable result in the sense of unfairly distorting the relative value between Local Currency and United States dollars, the question of an equitable Reference Rate of Exchange to be employed will be negotiated, and if agreement cannot be reached within sixty (60) days between A.I.D. and the Investor, the question of an equitable Reference Rate of Exchange will be referred to arbitration for settlement at the request of either A.I.D. or the Investor.

I-L. The term "Project Country" means the territory presently under the jurisdiction of

I-M. The term "Maximum Amount of the Guaranty" means:

______________________________ dollars (U.S. $________________________).

Such amount shall be progressively reduced by any amounts received by the Investor as transfers under this contract, such reduction to take effect as of the first day of the Contract Period next succeeding the Contract Period in which the applicable Reference Date occurred. Such amount shall also be subject to reduction by the Investor as provided in Article IX-B hereof.

A.I.D. shall refund to the Investor the portion of the Fee(s) for This Contract, as hereinafter defined, paid for the amount by which the Maximum Amount of the Guaranty is reduced during the Contract Period(s) commencing with the effective date of the reduction.

I-N. The term "Face Amount of the Guaranty" means the following amounts for the Contract Periods indicated:

1. During the First Contract Period;

    ______________________ dollars (U.S. $______________).

2. During the Second Contract Period and each succeeding Contract Period; any amount elected by the Investor as provided in Article IX-B hereof but not greater than the Maximum Amount of the Guaranty as of the first day of each Contract Period.

Such amount shall be progressively reduced by any amounts received by the Investor as transfers under this contract, each such reduction to take effect as of the applicable Reference Date.

I-O. The term "Fee for This Contract" means the amount of U. S. $________________ for the First Contract Period payable on or before the Date of This Contract, and an amount payable on or before the first day of each Contract Period thereafter during the Life of This Contract, which amount shall be equal to the sum of:

1. one-half of one percent (1/2%) of the Face Amount of the Guaranty for the respective ensuing Contract Period and

2. one-quarter of one percent (1/4%) of the amount, if any, by which the Maximum Amount of the Guaranty exceeds the Face Amount of the Guaranty for such respective ensuing Contract Period.

I-P. The term "Project" means the installation, establishment and expansion of the facility and activities with the participation of the

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Investor for the processing and refining of petroleum and its products, including the distribution and marketing thereof.

I-Q. The term "Investment" means a percent equity interest in the Foreign Enterprise evidenced by shares of the authorized capital stock and acquired by the payment or payments by the Investor of obtained by the Investor through transfer of U.S. Dollars at the rate of exchange prevailing at the time of acquiring the shares.

ARTICLE II
Guaranty

Subject to the terms and conditions of this contract, A.I.D. hereby guarantees to the Investor, upon application, the transfer into United States dollars, up to the Face Amount of the Guaranty as of the applicable Reference Date, of Local Currency which is received by the Investor during the Life of This Contract as Return of Capital or Investment Earnings and which, during the Guaranty Period, is eligible for transfer under Article V of this contract.

ARTICLE III
Representations and Covenants

The Investor hereby represents to A.I.D. that, as of the date on which this contract is executed by the Investor:

III-A. The Investor is a corporation created under the laws specified in the first paragraph on page 1 of this contract, and is

substantially beneficially owned by citizens of the United States.

III-B. The Investor has disclosed to A.I.D. all then existing arrangements and agreements of whatever nature, with respect to the transfer from the Project Country of U.S. dollars, Local Currency or other currencies, and credits in any of the foregoing, to be received by the Investor as Investment Earnings or Return of Capital subsequent to the Date of This Contract.

The Investor hereby covenants with A.I.D. that:

III-C. The Investor will make payment to A.I.D. of the Fee for This Contract in the amount and manner specified in Article I.

III-D. The Investor will continue during the Guaranty Period to be a corporation created under the laws of the United States, or of one of the states or territories of the United States. In the event that the Investor shall during such period cease to be substantially beneficially owned by citizens of the United States, the Investor shall give prompt notice of that fact to A.I.D. and A.I.D. shall have the rights of termination or refusal to make transfers as provided under paragraph A of Article IV in the case of breach of covenant.

III-E. The Investor will disclose promptly to A.I.D. in detail all arrangements and agreements of whatever nature which, during the Guaranty Period, are entered into by the Investor with respect to the transfer from the Project Country of U.S. dollars, Local Currency or other currencies, and credits in any of the foregoing, received by the Investor as Investment Earnings or Return of Capital subsequent to the Date of This Contract.

III-F. The Investor during the Guaranty Period will submit to A.I.D. at least thirty (30) days prior to each date upon which the Fee for This Contract shall be due beginning with the second Contract Period a progress report in duplicate, in such form as A.I.D. may specify, indicating the amount of the Investment made, all sums received as Return of Capital in U.S. dollars, Local Currency or other currencies, and credits in any of the foregoing, and such other information as A.I.D. shall reasonably require. The first such report shall cover the period from the Date of This Contract until thirty (30) days prior to its due date, and subsequent reports shall cover the respective successive 12-month periods.

III-G. The Investor will maintain in a place accessible to A.I.D. or its duly authorized representatives, books of account and other records, in accordance with generally accepted accounting principles, covering the amount of the Investment, Investment Earnings, Return of Capital, and all other receipts, expenditures and transactions by the Investor in U.S. dollars, Local Currency or other currencies, and credits in any of the foregoing, in the Project Country or elsewhere, in connection with the Investment. During the Guaranty Period, and for five years thereafter, the Investor will permit A.I.D. or its duly authorized representatives, to inspect, examine and audit said accounts and records, whether they be located in the Project Country or elsewhere. During the Guaranty Period and for five years thereafter, the Investor will use its best efforts to enable the duly authorized representatives of A.I.D. to examine, audit and copy for the purpose of this contract any books and records of the Foreign Enterprise, and to inspect its

properties, whether in the Project Country or elsewhere, and the Investor will render every reasonable assistance in connection therewith.

III-H. The Investor will not assign, transfer, pledge or make other disposition of this contract or of any of the rights of the Investor hereunder without first obtaining the consent of A.I.D. thereto in writing.

III-I. No member of or delegate to Congress or resident commissioner shall be admitted to any share or part of this contract or to any benefit that may arise therefrom, but this provision shall not be construed to extend to this contract if made with a corporation for its general benefit.

III-J. Unless A.I.D. first agrees otherwise in writing, the Investor will, to the extent of Investor's ability, cause the Investment to be made substantially in accordance with the material representations relating thereto submitted in obtaining this Contract of Guaranty and in accordance with this Contract of Guaranty.

ARTICLE IV
Misrepresentation and Breach of Covenant

IV-A. In the event that the Investor shall have made a material misrepresentation of any fact stated in paragraph A or B of Article III hereof, or shall breach any covenant contained in paragraphs D, E, H or I of said Article, A.I.D. shall have the right to terminate this contract at any time by written notice given to the Investor, and, with or without exercising such right of termination, shall have the right to refuse to make any transfer for the Investor hereunder.

IV-B. In the event that the Investor shall breach any covenant contained in any paragraph of Article III other than paragraphs D, E,

H or I thereof, A.I.D. may, at its option, do any or all of the following:

1. terminate this contract by giving not less than thirty (30) days written notice to the Investor. Such notice shall contain a statement of A.I.D.'s intention to terminate, the reason upon which the termination is based, and the date upon which the termination is effective. Unless the Investor shall have cured such breach prior to said date, all obligations of A.I.D. hereunder shall terminate on said date, except as to any rights of the Investor which have accrued prior to such breach and with respect to which any application or applications are then pending;
2. refuse to make any transfer for the Investor based upon an application filed subsequent to the breach unless the Investor shall cure the breach within thirty (30) days after A.I.D. shall give notice to the Investor of the existence of the breach;
3. make such arrangements as it deems proper with the Investor to provide for the cure of the breach.

IV-C. In the event of any termination of this contract by A.I.D. all rights, liabilities and obligations under this contract, except as expressly continued by paragraph B of this Article, shall cease, except the following obligations of the Investor:

1. to comply with the covenants and agreements contained in paragraphs G and H of Article III hereof; and

2. to make any repayment required by paragraph E of this Article IV.

IV-D. In the event of misrepresentation or breach giving rise to the right of A.I.D. to terminate this contract as hereinabove provided, neither the acceptance of any fee by A.I.D. after the occurrence of such misrepresentation or breach, nor the fact that A.I.D. shall have had knowledge, actual or constructive, of the occurrence of such misrepresentation or breach and shall have failed to exercise its right of termination, shall operate as a waiver of the right of A.I.D. to terminate this contract or to refuse to make a transfer for the Investor hereunder unless the Investor is fully carrying out arrangements agreed to pursuant to paragraph B-3 of this Article IV.

IV-E. If A.I.D. shall have made any transfer for the Investor hereunder and shall thereafter ascertain that, prior to such transfer, the Investor misrepresented any fact stated in paragraph A or B of Article III, or, prior to the date of such transfer, breached any covenant in paragraph D, E, H, I, or J of Article III, or made any material misstatement of fact in the application for such transfer, then, on demand of A.I.D., contained in a written notice given to the Investor within one year after ascertaining that any such misrepresentation or breach has occurred or such misstatement was made, the Investor shall immediately repay to A.I.D. the amount of U. S. dollars so paid to the Investor, and upon receiving such repayment A.I.D. shall effect repayment to the Investor of the amount of the Local Currency received from the Investor in any such transfer, provided, however, A.I.D. may not assert such demand after the

expiration of the period of five (5) years immediately succeeding the misrepresentation, breach or misstatement occasioning the demand.

IV-F. In the event and to the extent that A.I.D. shall without sufficient legal cause have refused to make any transfer hereunder, A.I.D. shall not be liable to the Investor for damages beyond the amount herein expressly provided to be paid by A.I.D. with respect to such transfer.

ARTICLE V
Local Currency Eligible for Transfer

Local Currency received by Investor as Investment Earnings or as Return of Capital during the Life of This Contract and not held by Investor for more than eighteen (18) months shall be eligible for transfer under this contract:

1. if the Investor is prevented for a period of thirty (30) consecutive calendar days from effecting the transfer of such Local Currency into U.S. dollars by operation of any law, decree, regulation or administrative determination recognized as being in effect by the governing authorities of the Project Country, which regulates the transfer of Local Currency into U.S. dollars; or
2. if the Investor is prevented from effecting the transfer of such Local Currency into U.S. dollars by the failure by that agency of the governing authorities of the Project Country which legally or under color

of law controls the transfer of Local Currency into U.S. dollars, to grant an application made to such agency by the Investor for the transfer of such Local Currency, provided such application has been pending for at least sixty (60) consecutive calendar days; or

3. if the Investor is unable to transfer such Local Currency into U.S. dollars in any market or through any channel through which dollar exchange transactions are then being legally and normally effected except at a rate of exchange which, at the close of business on each of the thirty (30) consecutive calendar days immediately preceding the Date of Application hereunder, is less favorable to the Investor than the rate determined as of each of such days in accordance with the provisions of Article VI hereof;

provided, however, (a) that the Investor has taken all reasonable steps required to effect such transfer under such laws, decrees, regulations or administrative determinations, (b) that the inability of the Investor to effect such transfer does not result from the operation of any law, decree, regulation or administrative determination which is recognized as being in effect by the governing authorities of the Project Country on the Date of This Contract and of which the Investor can reasonably be expected to have knowledge, and (c) that, with respect to Local Currency in its possession, the Investor has made reasonable efforts to comply with all laws, decrees, regulations or administrative determinations of which it can reasonably be expected to have knowledge and

which regulate the transfer of Local Currency investment receipts into U.S. dollars.

ARTICLE VI
Rate of Exchange for Transfers

Transfers of Local Currency into U.S. dollars under this contract by A.I.D. shall be made at a rate which shall yield ninety-five percent (95%) of the U.S. dollars which would be yielded as of the Reference Date, by applying the Reference Rate of Exchange.

ARTICLE VII
Application for Transfer

VII-A. If the Investor has made application for the transfer of Local Currency to that agency of the governing authorities of the Project Country which legally or under color of law controls the transfer of such currency, the Investor may give written notice thereof to A.I.D. provided that with such notice the Investor shall submit any and all documents or other evidence which the Investor may then have with respect to its right subsequently to file an application for transfer with A.I.D. hereunder.

VII-B. At one or more times during the Guaranty Period, application under this contract may be made by the Investor for the transfer of Local Currency which is eligible for transfer into U.S. dollars under this contract. Each application shall be submitted to A.I.D. in a form satisfactory to A.I.D. The Investor shall submit such evidence as A.I.D. may reasonably require in order to enable it to determine whether and to what extent the Investor is entitled by the provisions of this contract to the transfer for which application has been made.

VII-C. The Investor shall submit a draft drawn to the order of A.I.D. or any agent designated by A.I.D., upon a depository acceptable to A.I.D., for the Local Currency which is eligible for transfer into U.S. dollars under this contract and for which application for transfer is made. Such draft shall be submitted at the time of the filing of an application hereunder or at any time thereafter provided that, in any event, it shall be submitted within a reasonable period after the Date of Application, or within five (5) days after receipt of written demand by A.I.D.; any such Local Currency not covered by a draft thus submitted shall be thereafter ineligible for transfer under said application.

VII-D. In any case, an application for transfer shall expire at the end of a period of six (6) months from the date of its receipt by A.I.D. unless a draft for the Local Currency covered thereby has been previously received by A.I.D.; provided, however, that nothing herein shall be deemed to impair the effectiveness of any subsequent applications which the Investor may file with respect to the transfer of the same currency or of other Local Currency eligible for transfer.

VII-E. A.I.D. shall have a reasonable period not in excess of sixty (60) consecutive calendar days from the date of receipt of the draft or drafts referred to in the previous paragraph to make such transfer in whole or in part or to refuse to make such transfer in whole or in part; provided, that if the Investor's application is based on clause ~~2 of Artic~~le V and if the Investor has given written notice to A.I.D. that it has filed an application for transfer of Local Currency with that agency of the governing authorities of the

Project Country which legally or under color of law controls the transfer of such currency, such sixty (60) day period shall be reduced by a period equivalent to the number of days between the Date of Notice and the Date of Application; provided further that such sixty (60) day period shall in no event be reduced to less than thirty (30) days. In no instance shall the receipt by A.I.D. of an application, statement or other evidence operate to create any presumption in favor of the Investor that it shall be entitled by the terms of this contract to receive the transfer into U.S. dollars for which application has been made.

VII-F. A.I.D. shall consult with the Investor or otherwise afford the Investor a reasonable opportunity to present its views on any question of fact which A.I.D. must resolve in determining whether and to what extent any transfer applied for shall be made.

VII-G. If and to the extent that A.I.D. shall refuse to make transfer pursuant to application hereunder, it shall return to the Investor any draft or drafts submitted in connection with such application and any portion of the Local Currency proceeds from such drafts with respect to which transfer into dollars under this contract has been refused.

ARTICLE VIII
Funds Available for Payment of Guaranty

VIII-A. The only funds which will be available to A.I.D. for the purpose of discharging liability under this and all other contracts of guaranty which may have been or may hereafter be entered into pursuant to the authority of Section 221(b) of the Act, Sections 202(b) and 413(b)(4) of the Mutual Security Act of 1954, as amended, and Section 111(b)(3) of the Economic Cooperation Act of 1948, as amended (exclusive

of informational media guaranties), are (i) those specified in Section 222 of the Act, and (ii) other funds, if any, which may be available at any time hereafter for the aforesaid general purpose, pursuant to the laws of the United States.

VIII-B. The Investor shall have no right or claim arising out of this contract against any other asset of A.I.D.

ARTICLE IX
Termination and Reduction

IX-A. The Investor shall have the right to terminate this contract effective on the first day of any Contract Period by written notice given to A.I.D. on or prior to such day. Such termination shall, from its effective date, relieve the Investor of all further obligations to pay the Fee for This Contract, but it shall not discharge or affect any other right, liability or obligation of either party which has accrued prior to the effective date of the termination of this contract or which, by the terms of this contract, is to survive the Guaranty Period.

IX-B. Prior to the first day of any Contract Period the Investor may by giving written notice to A.I.D.:

(1) Elect a Face Amount of the Guaranty for the ensuing Contract Period.

(2) Reduce the Maximum Amount of the Guaranty for the remaining Contract Periods.

Election under (1) shall be in effect only for the Contract Period requested by the Investor and reduction under (2) shall be permanent and may not be reinstated. Reductions pursuant to this Article shall become effective on the first day of any Contract Period immediately

following delivery to A.I.D. of written notice thereof and shall not affect the amount of the fee payable, or the retention by A.I.D. of any fee paid, for any period prior to the date on which such reductions become effective.

ARTICLE X
Modification

Any provision(s) of this contract may be modified, supplemented or otherwise altered by mutual agreement in writing.

ARTICLE XI
Notices

XI-A. Written notice to the respective parties may be delivered by:

1. making personal delivery of such notice to the Investment Guaranties Division, Agency for International Development, or to one of the representatives of the Investor, authorized pursuant to Article XII hereof, or
2. depositing such notice in the U.S. Post Office by registered mail enclosed in an envelope, postage prepaid, addressed to the party concerned at the address below specified, or to such other address as may be specified in writing from time to time:

To. INVESTMENT GUARANTIES DIVISION
AGENCY FOR INTERNATIONAL DEVELOPMENT

At: WASHINGTON 25, D.C.

To: THE INVESTOR

At: The address stated in the first paragraph on
page 1 of this contract

XI-B. The date of delivery under A.1. shall be the date on which the notice is received and under A.2. shall be the date on which the item was registered.

ARTICLE XII
Authority of Representatives

Prior to and as a condition of receiving any payment under this contract the Investor shall furnish A.I.D. with evidence of the authority of the persons who will act as representatives of the Investor in connection with the operation of this contract. A.I.D. shall be entitled to rely on such evidence of authority until A.I.D. shall receive written notice from the Investor that such persons are no longer authorized so to act; and in the event of such notice, the Investor will promptly furnish A.I.D. with evidence of the authority of persons authorized to act in their place and stead.

ARTICLE XIII
Disclaimer

The approval of A.I.D. of this Investment for guaranty purposes is not to be construed as an acknowledgment of the legality of the agreements or arrangements constituting or relating to this Investment, or of any acts in pursuance thereof, under the laws, including the antitrust laws, of the United States or of the Project Country.

ARTICLE XIV
Arbitration

Any question which shall arise as to the obligation of either party under this contract or the interpretation of any provision thereof, if not settled by mutual agreement, shall, at the option of either party and, upon written notice to the other party, be settled by arbitration. The arbitration shall be held at Washington, D.C., and shall be conducted in accordance with the then prevailing rules of the American Arbitration

Association. In any such arbitration A.I.D. shall appoint one arbitrator, the Investor shall appoint another, and the two so appointed shall appoint a third arbitrator; provided, however, that if any arbitrator or arbitrators are not appointed in accordance with the foregoing provisions of this Article within sixty (60) days after notice for arbitration has been given, such arbitrator or arbitrators shall be appointed in accordance with the rules above mentioned.

The controversy shall be submitted to the arbitrators in such manner as they shall deem appropriate, consistent with the then prevailing rules of the American Arbitration Association, and the decision of a majority of the arbitrators, rendered in writing, shall be final and conclusive and binding on the parties.

Each party shall pay its own expenses in connection with the arbitration, but the compensation and expenses of the arbitrators shall be borne in such manner as may be specified in the decision of the arbitrators.

Each party shall, in any arbitration hereunder, have the right to appear and be heard and present evidence before the arbitrators.

IN WITNESS WHEREOF, the parties hereto have caused this contract to be duly executed and issued in duplicate at Washington, District of Columbia, United States of America, as of the date, shown below, on which this contract was executed for A.I.D.

AGENCY FOR INTERNATIONAL DEVELOPMENT

By______________________________
Assistant Administrator

Date______________________________

By______________________________

Date______________________________

SPECIMEN (10/1/62)

AID CONTRACT OF GUARANTY
NO.____________

CONTRACT OF GUARANTY (EXPROPRIATION-LOAN)

Contract of Guaranty made, entered into and dated as of the ________ day of ____________, 196 , by and between AGENCY FOR INTERNATIONAL DEVELOPMENT (hereinafter called "A.I.D."), an agency of the United States of America, and ____ (hereinafter called "Investor"), a corporation organized and existing under the laws of the State of ____________ having its principal place of business at ____________________________________.

The Investor is engaged in, among other things, (brief description of the Investor's business; brief description of the foreign enterprise or other business in which the proposed investment is to be made; and brief description of the contemplated investment). ____

The Investor has filed with A.I.D. pursuant to the provisions of Section 221(b) of the Foreign Assistance Act of 1961, as amended, (hereinafter called the "Act") and to the rules and regulations prescribed by the Administrator of A.I.D. thereunder, an application for a guaranty against loss on the Investment, as hereinafter defined, by reason of expropriation.

A.I.D. and the Government of ____________ have each approved the Project, as hereinafter defined.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, A.I.D. and the Investor hereby agree as follows:

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ARTICLE I
Definitions

Wherever used in this contract:

I-A. The term "Date of This Contract" means that date, shown on the last page of this contract, on which this contract was executed for A.I.D.

I-B. The term "Contract Period" means:

1. the year beginning on the Date of This Contract, such Contract Period being hereinafter called the First Contract Period, and
2. periods of one year in length, each commencing on the successive anniversaries of the Date of This Contract.

I-C. The term "Investment Earnings" means, on any date, the amounts received by the Investor subsequent to the Date of This Contract as payments of interest on the Notes, and redemption premiums, if any, which the Foreign Enterprise may owe the Investor in connection with the Notes acquired as a result of the Investment and in the Investor's possession on such date.

Investment Earnings are, by the terms of the Notes, to be paid in the United States of America in United States dollars. For purposes of this contract, however, if the Foreign Enterprise is unable, by operation of any law, decree, regulation or administrative determination recognized as being then in effect by the governing authorities of the Project Country, as hereinafter defined, to obtain the United States dollars required to discharge its obligations on the Notes, and subsequently attempts to discharge its then obligations on the

Notes by making payments in Local Currency, as hereinafter defined, and such payments are accepted by the Investor in lieu of United States dollar payments, such Local Currency payments are to be included in the term "Investment Earnings".

I-D. The term "Return of Capital" means, on any date, the amounts received by the Investor subsequent to the Date of This Contract as payments of principal of the Notes acquired as a result of the Investment and in the Investor's possession on such date.

Return of Capital is, by the terms of the Notes, to be paid in the United States of America in United States dollars. For purposes of this contract, however, if the Foreign Enterprise is unable, by operation of any law, decree, regulation or administrative determination recognized as being then in effect by the governing authorities of the Project Country, to obtain the United States dollars required to discharge its obligations on the Notes, and subsequently attempts to discharge its then obligations on the Notes by making payments in Local Currency, as hereinafter defined, and such payments are accepted by the Investor in lieu of United States dollar payments, such Local Currency payments are to be included in the term "Return of Capital".

I-E. The term "Government of the Project Country" means the present or any succeeding governing authority (without regard to the method of its succession or to whether it is recognized by the United States), or authorized agents thereof, in effective control of all or any part of the Project Country, as hereinafter defined, or of any political or territorial subdivision thereof; provided, however, that in no event shall the Government of the United States of America, or any military government or command in which it participates, be included within the meaning of this paragraph.

I-F. The term "Guaranty Period" means (a) the period of twenty years from the date, shown on the last page of this contract, on which this contract was executed and issued, or (b) if terminated pursuant to Article IV or IX, then to and including the effective date of such termination.

I-G. The term "Date or Expropriation" means the first day of the one-year period referred to in paragraph J of this Article.

I-H. The term "Local Currency" means currency recognized when received by the Investor as legal tender in the Project Country, as hereinafter defined, by the governing authorities thereof.

I-I. The term "Net Investment" means, on any date, the sum of the principal then outstanding and the interest then accrued in connection with the Notes acquired by the Investor as a result of the Investment and in Investor's possession on such date.

I-J. The term "Expropriatory Action" means any action, other than an exchange control action, which is taken, authorized, ratified or condoned by the Government of the Project Country commencing during the Guaranty Period, with

or without compensation therefor, and which for a period of one year necessarily results in preventing:

1. the Investor from receiving payment in United States Dollars when due of the principal amounts of or the interest on the Notes acquired as a result of the Investment, or redemption premiums due, if any, or other amounts, if any, which the Foreign Enterprise owes the Investor in connection with the Notes acquired as a result of the Investment; or
2. the Investor from effectively exercising its rights with respect to the Foreign Enterprise either as shareholder or as creditor, as the case may be, acquired as a result of the Investment, as hereinafter defined; or
3. the Investor from disposing of the Notes acquired as a result of the Investment, as hereinafter defined, or any rights accruing therefrom; or
4. the Investor from repatriating amounts received as Investment Earnings or Return of Capital which action commences within the eighteen (18) months immediately succeeding such receipt, provided, however, that if such action is essentially regulatory or revenue producing in nature, such action shall not be deemed to be an "Expropriatory Action".

Notwithstanding the foregoing, no such action shall be deemed an Expropriatory Action if it occurs, or continues in effect during the aforesaid period of one year, as a result of:

a. enforcement by the Government of the Project Country of any law, decree, regulation or administrative determination violated by the Investor or the Foreign

Enterprise, unless such law, decree, regulation or administrative determination shall have been enacted or promulgated with a primary object of divesting any or all of the then existing shareholders or creditors of the Foreign Enterprise of their respective interest therein; or

b. failure on the part of the Investor or the Foreign Enterprise to take all reasonable measures under then available administrative and judicial procedures in the Project Country to prevent or postpone such action; or

c. provocation by the Investor or the Foreign Enterprise of such action; or

d. insolvency of or creditors' proceedings against the Foreign Enterprise other than an insolvency or a creditors' proceeding directly resulting from acts of the Foreign Enterprise which could have been restrained under applicable law and which the Investor attempted to restrain but was prevented from so doing for a period of one year by action taken, authorized, ratified or condoned by the Government of the Project Country during the Guaranty Period.

Provided further, that any action which would be considered to be an Expropriatory Action if it were to continue to have any of the effects described in 1, 2, or 3 above for one year may be considered to be an Expropriatory Action at an earlier time if A.I.D. shall determine that such action has caused or permitted a dissipation or destruction of the assets of the Foreign Enterprise sufficient to destroy the value of the Foreign Enterprise as a going concern.

I-K. The term "Reference Rate of Exchange" means, on any day specified herein, the rate of exchange certified by the Federal Reserve Bank of New York to the Secretary of the Treasury for such day for the purpose of computing the U. S. dollar amounts of duties on commodities imported into the United States from the Project Country, as hereinafter defined, as required by the U. S. customs laws, provided that one, but not more than one, such rate is certified to the Secretary of the Treasury for such purpose as of such date.

If no one such rate or value is certified to the Secretary of the Treasury on such date, the rate to be used for purposes of this Article I-K shall be the average effective rate which, on the day specified herein, is lawfully charged under the laws of the Project Country, as hereinafter defined, to residents of said Project Country, exclusive of governmental entities, for that group of commodity exports from the United States to said Project Country, the U. S. dollar value of which during the one-year period preceding such day constituted a larger amount than the value of any other group of such exports to which a differenct single rate is applicable on such day. In determining the relative U. S. dollar value of groups of such exports to which a different rate may be applicable, statistics of the U. S. Bureau of the Census covering the most recent one-year period available will be conclusively presumed to be the best available evidence, provided that statistics necessary for this purpose were being maintained on a current basis on the day specified herein.

I-L. The term "Project Country" means the territory presently under the jurisdiction of the Government of ____________.

I-M. The term "Maximum Amount of the Guaranty" means:

________________________________ Dollars ($________).

Such amount shall be progressively reduced by any amounts received by the Investor as compensation under this contract, such reduction to take effect as of the first day of the Contract Period next succeeding the Contract Period in which the applicable Date of Expropriation occurred. Such amount shall also be subject to reduction by the Investor as provided in Article IX-B hereof.

A.I.D. shall refund to the Investor the portion of the Fee(s) for This Contract, as hereinafter defined, paid for the amount by which the Maximum Amount of the Guaranty is reduced during the Contract Period(s) commencing with the effective date of the reduction.

I-N. The term "Face Amount of the Guaranty" means the following amounts for the Contract Periods indicated:

1. During the First Contract Period;

   __________ Dollars ($________).

2. During the Second Contract Period and each succeeding Contract Period; any amount elected by the Investor as provided in Article IX-B hereof but not greater than the Maximum Amount of the Guaranty as of the first day of each Contract Period.

Such amount shall be progressively reduced by any amounts received by the Investor as compensation under this contract, each such reduction to take effect as of the applicable Date of Expropriation.

I-O. The term "Fee for This Contract" means the amount of $________ for the First Contract Period payable on or before the Date of This Contract, and an amount payable on or before the first day of each Contract Period thereafter during the Life of This Contract, which amount shall be equal to the sum of:

1. one-half of one percent (½%) of the Face Amount of the Guaranty for the respective ensuing Contract Period and
2. one-quarter of one percent (¼%) of the amount, if any, by which the Maximum Amount of the Guaranty exceeds the Face Amount of the Guaranty for such respective ensuing Contract Period.

I-P. The term "Project" means ____
____
____

I-Q. The term "Investment" means an amount or amounts not exceeding in aggregate ________ Dollars ($________) paid over or to be paid over by the Investor to the Foreign Enterprise as a loan to the Foreign Enterprise for use in connection with the Project. The Investment will be evidenced by the Notes in an aggregate principal amount equal to the amount of the Investment.

ARTICLE II
Guaranty

Subject to the terms and conditions of this contract, A.I.D. hereby guarantees to the Investor, upon application, compensation in United States dollars up to the limit provided for in Article V hereof for losses determined in accordance with Article VI hereof resulting from Expropriatory Action taken during the Guaranty Period.

ARTICLE III
Representations and Covenants

The Investor hereby represents to A.I.D. that, as of the date on which this contract is executed by the Investor:

III-A. The Investor is a corporation created under the laws specified in the first paragraph on page 1 of this contract, and is substantially beneficially owned by citizens of the United States.

III-B. The Investor has not entered into any arrangements or agreements of whatever nature with respect to compensation by the Project Country for any loss on the Investment by reason of Expropriatory Action.

The Investor hereby covenants with A.I.D. that:

III-C. The Investor will make payment to A.I.D. of the Fee for This Contract in the amount and manner specified in Article I.

III-D. The Investor will continue during the Guaranty Period to be a corporation created under the laws of the United States, or of one of the states or territories of the United States. In the event that the Investor shall during such period cease to be substantially beneficially owned by citizens of the United States, the Investor shall give prompt notice of that fact to A.I.D. and A.I.D. shall have rights of termination or refusal to make compensation as provided under paragraph A of Article IV in the case of breach of covenant.

III-E. The Investor will disclose promptly to A.I.D. in detail all arrangements and agreements of whatever nature which, during the Guaranty Period, are entered into by the Investor with respect to compensation by the Project Country for any loss on the Investment by reason of Expropriatory Action by the Government of the Project Country and will not, without obtaining the permission of A.I.D.,

enter into any such arrangements or agreements or accept any such compensation for any loss with respect to which an application for compensation is submitted hereunder.

III-F. The Investor will notify A.I.D. promptly in writing of any action which it has reason to believe may become or has become an Expropriatory Action.

III-G. The Investor during the Guaranty Period will submit to A.I.D. at least thirty (30) days prior to each date upon which the Fee for This Contract shall be due beginning with the second Contract Period a progress report in duplicate, in such form as A.I.D. may specify, indicating the amount of the Investment made, all sums received as Return of Capital in U. S. dollars, Local Currency or other currencies, and credits in any of the foregoing, and such other information as A.I.D. shall reasonably require. The first such report shall cover the period from the Date of This Contract until thirty (30) days prior to its due date, and subsequent reports shall cover the respective successive 12-month periods.

III-H. The Investor will maintain in a place accessible to A.I.D. or its duly authorized representatives, books of account and other records, in accordance with generally accepted accounting principles, covering the amount of the Investment, Return of Capital, Investment Earnings, and all other receipts, expenditures, and transactions by the Investor in U. S. Dollars, Local Currency, or other currencies, and credits in any of the foregoing, in the Project Country or elsewhere,

in connection with the Investment. During the Guaranty Period, and for five years thereafter, the Investor will permit A.I.D. or its duly authorized representatives, to inspect, examine and audit said accounts and records, whether they be located in the Project Country or elsewhere. During the Guaranty Period, and for five years thereafter, the Investor will use its best efforts to enable the duly authorized representatives of A.I.D. to examine, audit and copy for the purpose of this contract any books and records of the Foreign Enterprise, and to inspect its properties, whether in the Project Country or elsewhere, and the Investor will render every reasonable assistance in connection therewith.

III-I. The Investor will not assign, transfer, pledge or make other disposition of this contract or of any of the rights of the Investor hereunder without first obtaining the consent of A.I.D. thereto in writing.

III-J. Unless A.I.D. first agrees otherwise in writing, the Investor will, to the extent of Investor's ability, cause the Investment to be made substantially in accordance with this Contract of Guaranty and with the material representations submitted in obtaining this Contract of Guaranty.

III-K. Prior to the completion of the transfers and assignments specified in paragraph O of this Article, the Investor will take all reasonable measures to pursue and preserve any administrative or judicial remedies which may be available in connection with the Expropriatory Action and to maintain and preserve the assets of the Foreign Enterprise.

III-L. The Investor will cooperate in full, and will use its best efforts to cause the Foreign Enterprise to cooperate in full, with the responsible agents of the Government of the United States of America in the administration of any property acquired by the Government under paragraph O of this Article and in the preservation and prosecution of any claims transferred pursuant to said paragraph O, including without limitation the making available of technical and other information necessary to the maintenance of property thus acquired and the making available of evidence, including documents and witnesses, necessary to the prosecution of claims thus acquired. The Investor shall not be obligated by this paragraph to take any action which will incur substantial direct expenses by it unless reimbursement for such expenses by the Government of the United States is made available.

III-M. Within sixty (60) days after the Date of This Contract and on or before the last day of the sixth month of each fiscal year of the Foreign Enterprise during the Guaranty Period, the Investor, to the extent of its ability, shall furnish A.I.D. two copies of a balance sheet, profit and loss statement, analysis of surplus and such other statements as A.I.D. shall reasonable require, prepared or approved by an independent certified public accountant or other accountant, setting forth such data as A.I.D. shall reasonably require pertaining to the operations and the financial condition of the Foreign Enterprise during its preceding fiscal year.

III-N. No member of or delegate to Congress or resident commissioner shall be admitted to any share or part of this contract or to any benefit that may arise therefrom, but this provision shall not be construed to extend to this contract if made with a corporation for its general benefit.

III-O. Subject to the provisions of paragraph C of Article VII hereof, the Investor will, upon receipt of notice from A.I.D. of the amount of compensation determined to be due hereunder, and prior to the payment of any such compensation, assign and transfer to A.I.D. or to any agent designated by A.I.D. to the extent and in the manner requested by A.I.D. which request shall be commensurate with whether compensation is being computed under paragraph A or B of Article VI hereof:

1. the Notes acquired by the Investor as a result of the Investment and in Investor's possession on the Date of Expropriation;
2. any assets, currency or other property received directly or indirectly by the Investor from the Foreign Enterprise, by virtue of the Notes acquired as a result of the Investment, after the Date of Expropriation which the Investor is unable to withdraw from the Project Country;
3. any assets, currency, or other property received directly or indirectly by the Investor as compensation for loss on the Notes as a result of the Expropriatory Action which the Investor is unable to withdraw from the Project Country; and
4. any claims, causes of action or other rights of the Investor existing in connection with any of the foregoing items. To the extent of its ability, the Investor will execute or transfer all documents, and will take all other actions, as A.I.D. may reasonably require, to complete effectively the assignments provided in this paragraph.

ARTICLE IV
Misrepresentation and Breach of Covenant

IV-A. In the event that the Investor shall have made a material misrepresentation of any fact stated in paragraph A or B of Article III hereof, or shall breach any covenant contained in paragraph D, E, F, I, or N of said Article, A.I.D. shall have the right to terminate this contract at any time by written notice given to the Investor, and, with or without exercising such right of termination, shall have the right to refuse to make compensation to the Investor hereunder.

IV-B. In the event that the Investor shall breach any covenant contained in any paragraph of Article III other than paragraph D, E, F, I, or N thereof, A.I.D. may, at its option, do any or all of the following:

1. terminate this contract by giving not less than thirty (30) days written notice to the Investor. Such notice shall contain a statement of A.I.D.'s intention to terminate, the reason upon which the termination is based, and the date upon which the termination is effective. Unless the Investor shall have cured such breach prior to said date, all obligations of A.I.D. hereunder shall terminate on said date, except as to any rights of the Investor which have accrued prior to such breach and with respect to which any application or applications are then pending;

2. refuse to make compensation to the Investor based upon an application filed subsequent to the breach unless the Investor shall cure the breach within thirty (30) days after A.I.D. shall give notice to the Investor of the existence of the breach;

3. make such arrangements as it deems proper with the Investor to provide for the cure of the breach.

IV-C. In the event of any termination of this contract by A.I.D. all rights, liabilities and obligations under this contract, except as expressly continued by paragraph B of this Article, shall cease, except the following obligations of the Investor:

1. to comply with the covenants and agreements contained in paragraphs E, H, I, and L of Article III hereof; and

2. to make any repayment required by paragraph E of this Article IV.

IV-D. In the event of misrepresentation or breach giving rise to the right of A.I.D. to terminate this contract as hereinabove provided, neither the acceptance of any fee by A.I.D. after the occurrence of such misrepresentation or breach, nor the fact that A.I.D. shall have had knowledge, actual or constructive, of the occurrence of such misrepresentation or breach and shall have failed to exercise its right of termination, shall operate as a waiver of the right of A.I.D. to terminate this contract or to refuse to make compensation to the Investor hereunder, unless the Investor is fully carrying out arrangements agreed to pursuant to paragraph B3 of this Article IV.

IV-E. If A.I.D. shall have paid any compensation to the Investor hereunder and shall thereafter ascertain that, prior to such payment, the Investor misrepresented any fact stated in paragraph A or B of Article III, or, prior to the date of such payment, breached any covenant in paragraph D, E, F, I, J, or N of Article III, or made any material misstatement of fact in the application for such compensation, or, subsequent to the payment of such compensation, the Investor breached the covenant contained in paragraph L of Article III, then, on demand of A.I.D., contained in a written notice given to the Investor within one year after ascertaining that any such misrepresentation or breach has occurred or such misstatement was made, the Investor shall immediately repay to A.I.D. the amount of U.S. dollars so paid to the Investor, and upon receiving such repayment A.I.D. shall return to the Investor the rights, title and interests transferred pursuant to paragraph O of Article III hereof, provided, however, A.I.D. may not assert such demand after the expiration of the period of five years immediately succeeding the misrepresentation, breach or misstatement occasioning the demand.

IV-F. In the event and to the extent that A.I.D. shall without sufficient legal cause have refused to pay any compensation hereunder, A.I.D. shall not be liable to the Investor for damages beyond the amount herein expressly provided.

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ARTICLE V
Amount of Compensation

The compensation to be paid hereunder for losses resulting from an Expropriatory Action shall be any or all of:

a. the loss by reason of an Expropriatory Action of the kind described in paragraph J1, J2, or J3 of Article I hereof determined in accordance with paragraph A of Article VI hereof;

b. the loss by reason of an Expropriatory Action preventing the repatriation of receipts or proceeds of the kind described in paragraph J4 of Article I hereof determined in accordance with paragraph B of Article VI hereof,

provided, however, that the amount of such compensation payable for any and all loss resulting from an Expropriatory Action shall not exceed the Face Amount of the Guaranty in effect on the Date of Expropriation.

ARTICLE VI

Computation of Loss by Reason of the Expropriatory Action

VI-A. The loss by reason of an Expropriatory Action of the kind described in paragraphs J1, J2, or J3 of Article I hereof shall be determined, as of the Date of Expropriation, as:

The Net Investment less the U. S. dollar value of any assets, currency or other property not required to be transferred pursuant to paragraph O of Article III hereof which is received, directly or indirectly, by the Investor either as compensation for loss as a result of that Expropriatory Action or as an assignment from the Foreign Enterprise after the Date of Expropriation by virtue of the Net Investment, such value to be determined as of the date or dates such assets, currency or other property, accepted by the Investor, first come into the Investor's possession outside of the Project Country.

VI-B. The loss by reason of an Expropriatory Action preventing the repatriation of receipts or proceeds of the kind described in paragraph J4 of Article I hereof, shall be determined (a) where such receipts or proceeds consist of Local Currency, by the U. S. dollar equivalent thereof on the basis of the Reference Rate of Exchange in effect on or nearest succeeding the Date of Expropriation, and (b) where such proceeds consist of other currencies, the U. S. dollar equivalent at the applicable rate of exchange for such currency certified by the Federal Reserve Bank of New York on or nearest succeeding such date, provided, however, that from such U. S. dollar equivalent shall be deducated the U. S. dollar value of any assets, currency, or other property, not required to be transferred pursuant to paragraph O of Article III hereof, which is received,

directly or indirectly, by the Investor either as compensation for loss as a result of that Expropriatory Action or as an assignment from the Foreign Enterprise by virtue of the Net Investment, such value to be determined as of the date or dates such assets, currency, or other property, accepted by the Investor, first comes into the Investor's possession outside the Project Country.

VI-C. Loss by reason of an Expropriatory Action shall be determined in accordance with accounting principles generally accepted in the United States, and, except as required by the Government of the Project Country, depreciation shall be computed at rates not less than those allowed under then existing regulations of the United States Internal Revenue Service.

ARTICLE VII
Application for Compensation

VII-A. At one or more times the Investor may file with A.I.D. application for compensation hereunder; provided, however, that any such application must be filed not later than six (6) months after the Investor has reason to believe that Expropriatory Action has been taken, and in no event shall any such application be filed more then eighteen (18) months after the expiration of the Guaranty Period. Any such application shall be in a form satisfactory to A.I.D. and shall contain all information reasonably required by A.I.D. to determine the Investor's right to compensation and the amount thereof. A.I.D. thereafter will keep the Investor advised in writing as to any additional evidence which it may deem reasonably necessary to complete the application; provided, however, that:

1. an application will be deemed to be complete, if, at the expiration of three (3) months after the receipt of any evidence from Investor, A.I.D. does not have outstanding a request for additional evidence; and
2. if the Investor fails to respond to a request for evidence within three (3) months after the making thereof, A.I.D. may at its option consider the application as abandoned. A.I.D. may, at its option, reinstate such application upon written request of the Investor.

A.I.D. shall consult with the Investor or otherwise afford the Investor a reasonable opportunity to present its views on any question of fact which A.I.D. must resolve in determining whether and to what extent Investor has incurred loss on the part or all of the Investment as a result of Expropriatory Action within the meaning of this contract. The filing of applications and supporting evidence shall not operate to create any presumption that Investor has incurred such losses.

VII-B. A.I.D. shall have a reasonable period, not in excess of six (6) months after completion of any application, to determine and to notify Investor of its determinations as to (1) whether or not Investor has incurred loss for which compensation is hereby guaranteed, (2) the Date of Expropriation, if any, and (3) the amount of such compensation. Within sixty (60) days (or such longer period as the parties may agree upon in writing) after the delivery to Investor of notice from A.I.D. that compensation is due hereunder, and the amount thereof, Investor shall assign its rights, title and interest to A.I.D. as provided in paragraph O of Article III hereof, and A.I.D.,upon the completion of such assignment shall make immediate payment to the Investor of the amount of compensation due.

VII-C. Nothing in this agreement shall prevent Investor from withdrawing any application at any time prior to the time of the assignment to A.I.D. of Investor's rights, title and interest as provided in paragraph O of Article III hereof.

ARTICLE VIII
Funds Available for Payment of Guaranty

VIII-A. The only funds which will be available to A.I.D. for the purpose of discharging liability under this and all other contracts of guaranty which may have been or may hereafter be entered into pursuant to the authority of Section 221(b) of the Act, Sections 202(b) and 413(b)(4) of the Mutual Security Act of 1954, as amended, and Section 111(b)(3) of the Economic Cooperation Act of 1948, as amended (exclusive of informational media guaranties), are (i) those specified in Section 222 of the Act, and (ii) other funds, if any, which may be available at any time hereafter for the aforesaid general purpose, pursuant to the laws of the United States.

VIII-B. The Investor shall have no right or claim arising out of this contract against any other asset of A.I.D.

ARTICLE IX
Termination and Reduction

IX-A. The Investor shall have the right to terminate this contract effective on the first day of any Contract Period by written notice given to A.I.D. on or prior to such day. Such termination shall, from its effective date, relieve the Investor of all further obligations to pay the Fee for This Contract, but it shall not discharge or affect any other right, liability or obligation of either party which has accrued prior to the effective date of the termination of this contract or which, by the terms of this contract, is to survive the Guaranty Period.

IX-B. Prior to the first day of any Contract Period the Investor may by giving written notice to A.I.D.:

(1) Elect a Face Amount of the Guaranty for the ensuing Contract Period.

(2) Reduce the Maximum Amount of the Guaranty for the remaining Contract Periods.

Election under (1) shall be in effect only for the Contract Period requested by the Investor and reduction under (2) shall be permanent and may not be reinstated. Reductions pursuant to this Article shall become effective on the first day of any Contract Period immediately following delivery to A.I.D. of written notice thereof and shall not affect the amount of the fee payable, or the retention by A.I.D. of any fee paid, for any period prior to the date on which such reductions become effective.

ARTICLE X
Modification

Any provision(s) of this contract may be modified, supplemented or otherwise altered by mutual agreement in writing.

ARTICLE XI
Notices

XI-A. Written notice to the respective parties may be delivered by:

1. making personal delivery of such notice to the Investment Guaranties Division, Agency for International Development, or to one of the representatives of the Investor, authorized pursuant to Article XII hereof,

   or

2. depositing such notice in the U.S. Post Office by registered mail enclosed in an envelope, postage prepaid, addressed to the party concerned at the address below specified, or to such other address as may be specified in writing from time to time:

   To: INVESTMENT GUARANTIES DIVISION
   AGENCY FOR INTERNATIONAL DEVELOPMENT

   At: WASHINGTON 25, D. C.

   To: THE INVESTOR

   At: The address stated in the first paragraph on page 1 of this contract

XI-B. The date of delivery under A.1. shall be the date on which the notice is received and under A.2. shall be the date on which the item was registered.

ARTICLE XII
Authority of Representatives

Prior to and as a condition of receiving any payment under this contract the Investor shall furnish A.I.D. with evidence of the authority of the persons who will act as representatives of the Investor in connection with the operation of this contract. A.I.D. shall be entitled to rely on such evidence of authority until A.I.D. shall receive written notice from the Investor that such persons are no longer authorized so to act; and in the event of such notice, the Investor will promptly furnish A.I.D. with evidence of the authority of persons authorized to act in their place and stead.

ARTICLE XIII
Disclaimer

The approval of A.I.D. of this Investment for guaranty purposes is not to be construed as an acknowledgement of the legality of the agreements or arrangements constituting or relating to this Investment, or of any acts in pursuance thereof, under the laws, including the antitrust laws, of the United States or of the Project Country.

ARTICLE XIV
Arbitration

Any question which shall arise as to the obligation of either party under this contract or the interpretation of any provision thereof, if not settled by mutual agreement, shall, at the option of either party and, upon written notice to the other party, be settled by arbitration. The arbitration shall be held at Washington, D. C., and shall be conducted in accordance with the then prevailing rules of the American Arbitration Association. In any such arbitration A.I.D. shall appoint one arbitrator, the Investor shall appoint another, and the two so appointed shall appoint a third arbitrator; provided, however, that if any arbitrator or arbitrators are not appointed in accordance with the foregoing provisions of this Article within sixty (60) days after notice for arbitration has been given, such arbitrator or arbitrators shall be appointed in accordance with the rules above mentioned.

The controversy shall be submitted to the arbitrators in such manner as they shall deem appropriate, consistent with the then prevailing rules of the American Arbitration Association, and the decision of a majority of the arbitrators, rendered in writing, shall be final and conclusive and binding on the parties.

Each party shall pay its own expenses in connection with the arbitration, but the compensation and expenses of the arbitrators shall be borne in such manner as may be specified in the decision of the arbitrators.

Each party shall, in any arbitration hereunder, have the right to appear and be heard and present evidence before the arbitrators.

IN WITNESS WHEREOF, the parties hereto have caused this contract to be duly executed and issued in duplicate at Washington, District of Columbia, United States of America, as of the day of , 1962.

AGENCY FOR INTERNATIONAL DEVELOPMENT

By______________________________

Date______________________________

Investor's Name

By______________________________

Date______________________________

SPECIMEN (10/1/6)

AID CONTRACT OF GUARANTY
NO.__________

CONTRACT OF GUARANTY (EXPROPRIATION-EQUITY)

Contract of Guaranty made, entered into and dated as of the __________ day of __________, 196 , by and between AGENCY FOR INTERNATIONAL DEVELOPMENT (hereinafter called "AID"), an agency of the United States of America, acting for the Administrator of AID (hereinafter called "Administrator") under authority contained in the Foreign Assistance Act of 1961, as amended, (hereinafter called the "Act") and duly delegated to the Administrator and ______ ______________________(hereinafter called "Investor"), a corporation organized and existing under the laws of ______________having its principal place of business at ____.

The Investor is engaged in, among other things, (brief description of the Investor's business; brief description of the foreign enterprise or other business in which the proposed investment is to be made; brief description of the contemplated investment) ____
____
____
____.

The Investor has filed with AID pursuant to the provisions of Section 221(b) of the Act and to the rules and regulations prescribed by the Administrator thereunder, an application for a guaranty against loss on the Investment, as hereinafter defined, by reason of expropriation. AID and the Government of ____________________have each approved the Project.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, AID and the Investor hereby agree as follows:

ARTICLE I
Definitions

Wherever used in this contract:

I-A. The term "Date of This Contract" means that date, shown on the last page of this contract, on which this contract was executed for A.I.D.

I-B. The term "Contract Period" means:

(a) the year beginning on the Date of This Contract, such Contract Period being hereinafter called the First Contract Period, and

(b) periods of one year in length, each commencing on the successive anniversaries of the Date of This Contract.

I-C. The term "Investment Earnings" means the amounts received subsequent to the Date of This Contract by the Investor as dividends on the Equity Shares held by the Investor as a result of the Investment, as hereinafter defined, but exclusive of dividends paid in complete or partial liquidation of said Equity Shares.

I-D. The term "Return of Capital" means the amounts received by the Investor subsequent to the Date of This Contract as dividends paid in complete or partial liquidation of the Equity Shares held by the Investor as a result of the Investment, as hereinafter defined, or as proceeds from the sale or transfer in the Project Country, as hereinafter defined, of all or any part of the Equity Shares held by the Investor as a result of the Investment, as hereinafter defined..

I-E. The term "Government of the Project Country" means the present or any succeeding governing authority (without regard to the method of its succession or to whether it is recognized by the United States), or authorized agents thereof, in effective control of all or any part of the Project Country, as hereinafter defined, or of any political or terriotrial subdivision thereof; provided, however, that in no event shall the Government of the United States of America, or any military government or command in which it participates, be included within the meaning of this paragraph.

I-F. The term "Guaranty Period" means (a) the period of twenty years from the date, shown on the last page of this contract, on which this contract was executed and issued, or (b) if terminated pursuant to Article IV or IX, then to and including the effective date of such termination.

I-G. The term "Date of Expropriation" means the first day of the one-year period referred to in paragraph J of this Article.

I-H. The term "Local Currency" means currency recognized as legal tender in the Project Country, as hereinafter defined, by the governing authorities thereof.

I-I. The term "Net Investment" means, on any date, the amount of the Investment, expressed in U. S. dollars, expended by the Investor for those Equity Shares, acquired by the Investor as a result of the Investment and in Investor's possession on such date.

I-J. The term "Expropriatory Action" means anv action, other than an exchange control action, which is taken, authorized, ratified or condoned by the Government of the Project Country during the Guaranty Period with or

without compensation therefor, and which for a period of one year necessarily results in preventing:

1. the Foreign Enterprise from exercising substantial control on the use and disposition of its property; or
2. the Investor from effectively exercising its rights of participation in the control of the Foreign Enterprise acquired as a result of the Investment, as hereinafter defined, or
3. the Investor from disposing of its Equity Shares acquired as a result of the Investment, as hereinafter defined, or any rights accruing therefrom; or
4. the Investor from repatriating amounts received as Investment Earnings or Return of Capital which action commences within the eighteen (18) months immediately succeeding such receipt, provided, however, that if such action is essentially regulatory or revenue producing in nature, such action shall not be deemed to be an "Expropriatory Action".

Notwithstanding the foregoing, no such action shall be deemed an Expropriatory Action if it occurs, or continues in effect during the aforesaid period of one year, as a result of:

a. enforcement by the Government of the Project Country of any law, decree, regulation or administrative determination violated by the Investor or the Foreign Enterprise, unless such law, decree, regulation or

administrative determination shall have been enacted or promulgated with a primary object of divesting any or all of the then existing shareholders or creditors of the Foreign Enterprise of their respective interest therein; or

b. failure on the part of the Investor or the Foreign Enterprise to take all reasonable measures under then available administrative and judicial procedures in the Project Country to prevent or postpone such action; or

c. provocation by the Investor or the Foreign Enterprise of such action; or

d. insolvency of or creditors' proceedings against the Foreign Enterprise other than an insolvency or a creditors' proceeding directly resulting from acts of the Foreign Enterprise which could have been restrained under applicable law and which the Investor attempted to restrain but was prevented from so doing for a period of one year by action taken, authorized, ratified or condoned by the Government of the Project Country during the Guaranty Period.

provided further, that any action which would be considered to be an Expropriatory Action if it were to continue to have any of the effects described in 1, 2, or 3 above for one year may be considered to be an Expropriatory Action at an earlier time if A.I.D. shall determine that such action has caused or permitted a dissipation or destruction of the assets of the Foreign Enterprise sufficient to destroy the value of the Foreign Enterprise as a going concern.

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I-K. The term "Reference Rate of Exchange" means, on any day specified herein, the rate of exchange certified by the Federal Reserve Bank of New York to the Secretary of the Treasury for such day for the purpose of computing the U. S. dollar amounts of duties on commodities imported into the United States from the Project Country, as hereinafter defined, as required by the U. S. customs laws, provided that one, but not more than one, such rate is certified to the Secretary of the Treasury for such purpose as of such date.

If no one such rate or value is certified to the Secretary of the Treasury on such date, the rate to be used for purposes of this Article I-K shall be the average effective rate which, on the day specified herein, is lawfully charged under the laws of the Project Country, as hereinafter defined, to residents of said Project Country, exclusive of governmental entities, for that group of commodity exports from the United States to said Project Country, the U. S. dollar value of which during the one-year period preceding such day constituted a larger amount than the value of any other group of such exports to which a differenct single rate is applicable on such day. In determining the relative U. S. dollar value of groups of such exports to which a different rate may be applicable, statistics of the U. S. Bureau of the Census covering the most recent one-year period available will be conclusively presumed to be the best available evidence, provided that statistics necessary for this purpose were being maintained on a current basis on the day specified herein.

I-L. The term "Project Country" means the territory presently under the jurisdiction of the Government of __________.

I-M. The term "Maximum Amount of the Guaranty" means:

__________ Dollars ($).

Such amount shall be progressively reduced by any amounts received by the Investor as compensation under this contract, such reduction to take effect as of the first day of the Contract Period next succeeding the Contract Period in which the applicable Date of Expropriation occurred. Such amount shall also be subject to reduction by the Investor as provided in Article IX-B hereof.

A.I.D. shall refund to the Investor the portion of the Fee(s) for This Contract, as hereinafter defined, paid for the amount by which the Maximum Amount of the Guaranty is reduced during the Contract Period(s) commencing with the effective date of the reduction.

I-N. The term "Face Amount of the Guaranty" means the following amounts for the Contract Periods indicated:

1. During the First Contract Period; ________________ __________ Dollars ($).
2. During the Second Contract Period and each succeeding Contract Period; any amount elected by the Investor as provided in Article IX-B hereof but not greater than the Maximum Amount of the Guaranty as of the first day of each Contract Period.

Such amount shall be progressively reduced by any amounts received by the Investor as compensation under this contract, each such reduction to take effect as of the applicable Date of Expropriation.

I-O. The term "Fee for This Contract" means the amount of $_________ for the First Contract Period, payable on or before the Date of This Contract, and an amount payable on or before the first day of each Contract Period thereafter during the Guaranty Period, which amount shall be equal to the sum of:

1. one-half of one percent (½%) of the Face Amount of the Guaranty for the respective ensuing Contract Period, and
2. one-quarter of one percent (¼%) of the amount, if any, by which the Maximum Amount of the Guaranty exceeds the Face Amount of the Guaranty for such respective ensuing Contract Period.

I-P. The term "Project" means____
____
____.

I-Q. The term "Investment" means an amount, totaling not in excess of
____
____
____

ARTICLE II
Guaranty

Subject to the terms and conditions of this contract, A.I.D. hereby guarantees to the Investor, upon application, compensation in United States dollars up to the limit provided for in Article V hereof for losses determined in accordance with Article VI hereof resulting from Expropriatory Action taken during the Guaranty Period.

ARTICLE III
Representations and Covenants

The Investor hereby represents to A.I.D. that, as of the date on which this contract is executed by the Investor

III-A. The Investor is a corporation created under the laws specified in the first paragraph on page 1 of this contract, and is substantially beneficially owned by citizens of the United States.

III-B. The Investor has not entered into any arrangements or agreements of whatever nature with respect to compensation by the Project Country for any loss on the Investment by reason of Expropriatory Action.

The Investor hereby covenants with A.I.D. that:

III-C. The Investor will make payment to A.I.D. of the Fee for This Contract in the amount and manner specified in Article I

III-D. The Investor will continue during the Guaranty Period to be a corporation created under the laws of the United States, or of one of the states or territories of the United States. In the event that the Investor shall during such period cease to be substantially beneficially owned by citizens of the United States, the Investor shall give prompt notice of that fact to A.I.D. and A.I.D. shall have rights of termination or refusal to make compensation as provided under paragraph A of Article IV in the case of breach of covenant.

III-E. The Investor will disclose promptly to A.I.D. in detail all arrangements and agreements of whatever nature which, during the Guaranty Period, are entered into by the Investor with respect to compensation by the Project Country for any loss on the Investment by reason of Expropriatory Action by the Government of the Project Country and will not, without obtaining the permission of A.I.D.

enter into any such arrangements or agreements or accept any such compensation for any loss with respect to which an application for compensation is submitted hereunder.

III-F. The Investor will notify A.I.D. promptly in writing of any action which it has reason to believe may become or has become an Expropriatory Action.

III-G. The Investor during the Guaranty Period will submit to A.I.D. at least thirty (30) days prior to each date upon which the Fee for This Contract shall be due beginning with the second Contract Period a progress report in duplicate, in such form as A.I.D. may specify, indicating the amount of the Investment made, all sums received as Return of Capital in U. S. dollars, Local Currency or other currencies, and credits in any of the foregoing, and such other information as A.I.D. shall reasonably require. The first such report shall cover the period from the Date of This Contract until thirty (30) days prior to its due date, and subsequent reports shall cover the respective successive 12-month periods.

III-H. The Investor will maintain in a place accessible to A.I.D. or its duly authorized representatives, books of account and other records, in accordance with generally accepted accounting principles, covering the amount of the Investment, Return of Capital, Investment Earnings, and all other receipts, expenditures, and transactions by the Investor in U. S. Dollars, Local Currency, or other currencies, and credits in any of the foregoing, in the Project Country or elsewhere,

in connection with the Investment. During the Guaranty Period, and for five years thereafter, the Investor will permit A.I.D., or its duly authorised representatives, to inspect, examine and audit said accounts and records, whether they be located in the Project Country or elsewhere. During the Guaranty Period, and for five years thereafter, the Investor will use its best efforts to enable the duly authorised representatives of A.I.D. to examine, audit, and copy for the purpose of this contract any books and records of the Foreign Enterprise, and to inspect its properties, whether in the Project Country or elsewhere, and the Investor will render every reasonable assistance in connection therewith.

III-I. The Investor will not assign, transfer, pledge or make other disposition of this contract or of any of the rights of the Investor hereunder without first obtaining the consent of A.I.D. thereto in writing.

III-J. Unless A.I.D. first agrees otherwise in writing, the Investor will, to the extent of Investor's ability, cause both the Project to be carried out and the Investment to be made substantially in accordance with the material representations relating thereto submitted in obtaining this Contract of Guaranty and in accordance with this Contract of Guaranty.

III-K. Prior to the completion of the transfers and assignments specified in paragraph O of this Article, the Investor will take all reasonable measures to pursue and preserve any administrative or judicial remedies which may be available in connection with the Expropriatory Action and to maintain and preserve the assets of the Foreign Enterprise.

III-L. The Investor will cooperate in full, and will use its best efforts to cause the Foreign Enterprise to cooperate in full, with the responsible agents of the Government of the United States of America in the administration of any property acquired by the Government under paragraph O of this Article and in the preservation and prosecution of any claims transferred pursuant to said paragraph O, including without limitation the making available of technical and other information necessary to the maintenance of property thus acquired and the making available of evidence, including documents and witnesses, necessary to the prosecution of claims thus acquired. The Investor shall not be obligated by this paragraph to take any action which will incur substantial direct expenses by it unless reimbursement for such expenses by the Government of the United States is made available.

III-M. Within sixty (60) days after the Date of This Contract and on or before the last day of the sixth month of each fiscal year of the Foreign Enterprise during the Guaranty Period, the Investor, to the extent of its ability, shall furnish A.I.D. two copies of a balance sheet, profit and loss statement, analysis of surplus and such other statements as A.I.D. shall reasonable require, prepared or approved by an independent certified public accountant or other accountant, setting forth such data as A.I.D. shall reasonably require pertaining to the operations and the financial condition of the Foreign Enterprise during its preceding fiscal year.

III-N. No member of or delegate to Congress or resident commissioner shall be admitted to any share or part of this contract or to any benefit that may arise therefrom, but this provision shall not be construed to extend to this contract if made with a corporation for its general benefit.

III-O. Subject to the provisions of paragraph C of Article VII hereof, the Investor will, upon receipt of notice from A.I.D. of the amount of compensation determined to be due hereunder, and prior to the payment of any such compensation, assign and transfer to A.I.D. or to any agent designated by A.I.D. to the extent and in the manner requested by A.I.D. which request shall be commensurate with whether compensation is being computed under paragraph A or B of Article VI hereof:

1. the Equity Shares acquired by the Investor as a result of the Investment and in Investor's possession on the Date of Expropriation;
2. any assets, currency or other property received directly or indirectly by the Investor from the Foreign Enterprise, by virtue of the Equity Shares acquired as a result of the Investment, after the Date of Expropriation which the Investor is unable to withdraw from the Project Country;
3. any assets, currency, or other property received directly or indirectly by the Investor as compensation for loss on the Equity Shares as a result of the Expropriatory Action which the Investor is unable to withdraw from the Project Country; and
4. any claims, causes of action or other rights of the Investor existing in connection with any of the foregoing items. To the extent of its ability, the Investor will execute or transfer all documents, and will take all other actions, as A.I.D. may reasonably require, to complete effectively the assignments provided in this paragraph.

ARTICLE IV
Misrepresentation and Breach of Covenant

IV-A. In the event that the Investor shall have made a material misrepresentation of any fact stated in paragraph A or B of Article III hereof, or shall breach any covenant contained in paragraph D, E, F, I, or N of said Article, A.I.D. shall have the right to terminate this contract at any time by written notice given to the Investor, and, with or without exercising such right of termination, shall have the right to refuse to make compensation to the Investor hereunder.

IV-B. In the event that the Investor shall breach any covenant contained in any paragraph of Article III other than paragraph D, E, F, I, or N thereof, A.I.D. may, at its option, do any or all of the following:

1. terminate this contract by giving not less than thirty (30) days written notice to the Investor. Such notice shall contain a statement of A.I.D.'s intention to terminate, the reason upon which the termination is based, and the date upon which the termination is effective. Unless the Investor shall have cured such breach prior to said date, all obligations of A.I.D. hereunder shall terminate on said date, except as to any rights of the Investor which have accrued prior to such breach and with respect to which any application or applications are then pending;

2. refuse to make compensation to the Investor based upon an application filed subsequent to the breach unless the Investor shall cure the breach within thirty (30) days after A.I.D. shall give notice to the Investor of the existence of the breach;

3. make such arrangements as it deems proper with the Investor to provide for the cure of the breach.

IV-C. In the event of any termination of this contract by A.I.D. all rights, liabilities and obligations under this contract, except as expressly continued by paragraph B of this Article, shall cease, except the following obligations of the Investor:

1. to comply with the covenants and agreements contained in paragraphs E, H, I, and L of Article III hereof; and

2. to make any repayment required by paragraph E of this Article IV.

IV-D. In the event of misrepresentation or breach giving rise to the right of A.I.D. to terminate this contract as hereinabove provided, neither the acceptance of any fee by A.I.D. after the occurrence of such misrepresentation or breach, nor the fact that A.I.D. shall have had knowledge, actual or constructive, of the occurrence of such misrepresentation or breach and shall have failed to exercise its right of termination, shall operate as a waiver of the right of A.I.D. to terminate this contract or to refuse to make compensation to the Investor hereunder, unless the Investor is fully carrying out arrangements agreed to pursuant to paragraph B3 of this Article IV.

IV-E. If A.I.D. shall have paid any compensation to the Investor hereunder and shall thereafter ascertain that, prior to such payment, the Investor misrepresented any fact stated in paragraph A or B of Article III, or, prior to the date of such payment, breached any covenant in paragraph D, E, F, I, J, or N of Article III, or made any material misstatement of fact in the application for such compensation, or, subsequent to the payment of such compensation, the Investor breached the covenant contained in paragraph L of Article III, then, on demand of A.I.D., contained in a written notice given to the Investor within one year after ascertaining that any such misrepresentation or breach has occurred or such misstatement was made, the Investor shall immediately repay to A.I.D. the amount of U.S. dollars so paid to the Investor, and upon receiving such repayment A.I.D. shall return to the Investor the rights, title and interests transferred pursuant to paragraph O of Article III hereof, provided, however, A.I.D. may not assert such demand after the expiration of the period of five years immediately succeeding the misrepresentation, breach or misstatement occasioning the demand.

IV-F. In the event and to the extent that A.I.D. shall without sufficient legal cause have refused to pay any compensation hereunder, A.I.D. shall not be liable to the Investor for damages beyond the amount herein expressly provided.

ARTICLE V
Amount of Compensation

The compensation to be paid hereunder for losses resulting from an Expropriatory Action shall be any or all of:

a. the loss by reason of an Expropriatory Action of the kind described in paragraph J1, J2, or J3 of Article I hereof determined in accordance with paragraph A of Article VI hereof;

b. the loss by reason of an Expropriatory Action preventing the repatriation of receipts or proceeds of the kind described in paragraph J4 of Article I hereof determined in accordance with paragraph B of Article VI hereof,

provided, however, that the amount of such compensation payable for any and all loss resulting from an Expropriatory Action shall not exceed the Face Amount of the Guaranty in effect on the Date of Expropriation.

ARTICLE VI
Computation of Loss by Reason of the Expropriatory Action

VI-A. The loss by reason of an Expropriatory Action of the kind described in paragraph J1, J2, or J3 of Article I hereof shall be determined, as of the Date of Expropriation, as:

The Adjusted Value of the Equity Shares, as hereinafter defined, less: the U. S. dollar value of any assets, currency or other property not required to be transferred pursuant to paragraph O of Article III hereof which is received, directly or indirectly, by the Investor either as compensation for loss as a result of that Expropriatory Action or as an assignment from the Foreign Enterprise after the Date of Expropriation by virtue of the Investment in Equity Shares, such value to be determined as of the date or dates such assets, currency or other property, accepted by the Investor, first come into the Investor's possession outside of the Project Country.

For the purposes of this paragraph A the term "Adjusted Value of the Equity Shares" shall mean the sum of:

1. the Net Investment on the Date of Expropriation; and

2. the United States dollar equivalent of an amount determined by subtracting from the Investor's Share of any net income (including net capital gains or losses) after taxes, realized by the Foreign Enterprise from the date of the Investment to the Date of Expropriation, the sum of:

a. the Investor's Share of any net losses (including net capital gains or losses) after taxes, realized by the Foreign Enterprise from the date of the Investment to the Date of Expropriation; and

b. the Investor's Share of any dividends declared and paid on the Equity Shares from the date of the Investment to the Date of Expropriation.

The Investor's Share shall be determined on the basis of those Equity Shares in Investor's possession on the Date of Expropriation in connection with the Net Investment on such date. The United States dollar equivalent of said amount shall be obtained by applying a rate of exchange which shall be the average of the Reference Rates of Exchange on the last day of each month, or part thereof, from the Date of This Contract to the Date of Expropriation.

VI-B. The loss by reason of an Expropriatory Action preventing the repatriation of receipts or proceeds of the kind described in paragraph J4 of Article I hereof, shall be determined (a) where such receipts or proceeds consist of Local Currency, by the U. S. dollar equivalent thereof on the basis of the Reference Rate of Exhange in effect on or nearest succeeding the Date of Expropriation, and (b) where such proceeds consist of other currencies, the U. S. dollar equivalent at the applicable rate of exchange for such currency

certified by the Federal Reserve Bank of New York on or nearest succeeding such date, provided, however, that from such U. S. dollar equivalent shall be deducted the U. S. dollar value of any assets, currency, or other property, not required to be transferred pursuant to paragraph 0 of Article III hereof, which is received, directly or indirectly, by the Investor either as compensation for loss as a result of that Expropriatory Action or as an assignment from the Foreign Enterprise by virtue of the Investment in the Equity Shares, such value to be determined as of the date or dates such assets, currency, or other property, accepted by the Investor, first comes into the Investor's possession outside the Project Country.

VI-C. Loss by reason of an Expropriatory Action shall be determined in accordance with accounting principles generally accepted in the United States, and depreciation shall be computed at rates not less than those allowed under then existing regulations of the United States Internal Revenue Service. Further if the books and records of the Foreign Enterprise showing Adjusted Value of the Equity Shares on the Date of Expropriation are not available, such value or values shall be determined as of that date on the basis of the best available evidence.

ARTICLE VII
Application for Compensation

VII-A. At one or more times the Investor may file with A.I.D. application for compensation hereunder; provided, however, that any such application must be filed not later than six (6) months after the Investor has reason to believe that Expropriatory Action has been taken, and in no event shall any such application be filed more then eighteen (18) months after the expiration of the Guaranty Period. Any such application shall be in a form satisfactory to A.I.D. and shall contain all information reasonably required by A.I.D. to determine the Investor's right to compensation and the amount thereof. A.I.D. thereafter will keep the Investor advised in writing as to any additional evidence which it may deem reasonably necessary to complete the application; provided, however, that:

1. an application will be deemed to be complete, if, at the expiration of three (3) months after the receipt of any evidence from Investor, A.I.D. does not have outstanding a request for additional evidence; and
2. if the Investor fails to respond to a request for evidence within three (3) months after the making thereof, A.I.D. may at its option consider the application as abandoned. A.I.D. may, at its option, reinstate such application upon written request of the Investor.

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A.I.D. shall consult with the Investor or otherwise afford the Investor a reasonable opportunity to present its views on any question of fact which A.I.D. must resolve in determining whether and to what extent Investor has incurred loss on the part or all of the Investment as a result of Expropriatory Action within the meaning of this contract. The filing of applications and supporting evidence shall not operate to create any presumption that Investor has incurred such losses.

VII-B. A.I.D. shall have a reasonable period, not in excess of six (6) months after completion of any application, to determine and to notify Investor of its determinations as to (1) whether or not Investor has incurred loss for which compensation is hereby guaranteed, (2) the Date of Expropriation, if any, and (3) the amount of such compensation. Within sixty (60) days (or such longer period as the parties may agree upon in writing) after the delivery to Investor of notice from A.I.D. that compensation is due hereunder, and the amount thereof, Investor shall assign its rights, title and interest to A.I.D. as provided in paragraph O of Article III hereof, and A.I.D.,upon the completion of such assignment shall make immediate payment to the Investor of the amount of compensation due.

VII-C. Nothing in this agreement shall prevent Investor from withdrawing any application at any time prior to the time of the assignment to A.I.D. of Investor's rights, title and interest as provided in paragraph O of Article III hereof.

ARTICLE VIII
Funds Available for Payment of Guaranty

VIII-A. The only funds which will be available to A.I.D. for the purpose of discharging liability under this and all other contracts of guaranty which may have been or may hereafter be entered into pursuant to the authority of Section 221(b) of the Act, Sections 202(b) and 413(b)(4) of the Mutual Security Act of 1954, as amended, and Section 111(b)(3) of the Economic Cooperation Act of 1948, as amended (exclusive of informational media guaranties), are (i) those specified in Section 222 of the Act, and (ii) other funds, if any, which may be available at any time hereafter for the aforesaid general purpose, pursuant to the laws of the United States.

VIII-B. The Investor shall have no right or claim arising out of this contract against any other asset of A.I.D.

ARTICLE IX
Termination and Reduction

IX-A. The Investor shall have the right to terminate this contract effective on the first day of any Contract Period by written notice given to A.I.D. on or prior to such day. Such termination shall, from its effective date, relieve the Investor of all further obligations to pay the Fee for This Contract, but it shall not discharge or affect any other right, liability or obligation of either party which has accrued prior to the effective date of the termination of this contract or which, by the terms of this contract, is to survive the Guaranty Period.

IX-B. Prior to the first day of any Contract Period the Investor may by giving written notice to A.I.D.:

(1) Elect a Face Amount of the Guaranty for the ensuing Contract Period.

(2) Reduce the Maximum Amount of the Guaranty for the remaining Contract Periods.

Election under (1) shall be in effect only for the Contract Period requested by the Investor and reduction under (2) shall be permanent and may not be reinstated. Reductions pursuant to this Article shall become effective on the first day of any Contract Period immediately following delivery to A.I.D. of written notice thereof and shall not affect the amount of the fee payable, or the retention by A.I.D. of any fee paid, for any period prior to the date on which such reductions become effective.

ARTICLE X
Modification

Any provision(s) of this contract may be modified, supplemented or otherwise altered by mutual agreement in writing.

ARTICLE XI
Notices

XI-A. Written notice to the respective parties may be delivered by:

1. making personal delivery of such notice to the Investment Guaranties Division, Agency for International Development, or to one of the representatives of the Investor, authorized pursuant to Article XII hereof,

   or

2. depositing such notice in the U.S. Post Office by registered mail enclosed in an envelope, postage prepaid, addressed to the party concerned at the address below specified, or to such other address as may be specified in writing from time to time:

   To: INVESTMENT GUARANTIES DIVISION
   AGENCY FOR INTERNATIONAL DEVELOPMENT

   At: WASHINGTON 25, D. C.

   To: THE INVESTOR

   At: The address stated in the first paragraph on page 1 of this contract

XI-B. The date of delivery under A.1. shall be the date on which the notice is received and under A.2. shall be the date on which the item was registered.

ARTICLE XII
Authority of Representatives

Prior to and as a condition of receiving any payment under this contract the Investor shall furnish A.I.D. with evidence of the authority of the persons who will act as representatives of the Investor in connection with the operation of this contract. A.I.D. shall be entitled to rely on such evidence of authority until A.I.D. shall receive written notice from the Investor that such persons are no longer authorized so to act; and in the event of such notice, the Investor will promptly furnish A.I.D. with evidence of the authority of persons authorized to act in their place and stead.

ARTICLE XIII
Disclaimer

The approval of A.I.D. of this Investment for guaranty purposes is not to be construed as an acknowledgement of the legality of the agreements or arrangements constituting or relating to this Investment, or of any acts in pursuance thereof, under the laws, including the antitrust laws, of the United States or of the Project Country.

ARTICLE XIV
Arbitration

Any question which shall arise as to the obligation of either party under this contract or the interpretation of any provision thereof, if not settled by mutual agreement, shall, at the option of either party and, upon written notice to the other party, be settled by arbitration. The arbitration shall be held at Washington, D. C., and shall be conducted in accordance with the then prevailing rules of the American Arbitration Association. In any such arbitration A.I.D. shall appoint one arbitrator, the Investor shall appoint another, and the two so appointed shall appoint a third arbitrator; provided, however, that if any arbitrator or arbitrators are not appointed in accordance with the foregoing provisions of this Article within sixty (60) days after notice for arbitration has been given, such arbitrator or arbitrators shall be appointed in accordance with the rules above mentioned.

The controversy shall be submitted to the arbitrators in such manner as they shall deem appropriate, consistent with the then prevailing rules of the American Arbitration Association, and the decision of a majority of the arbitrators, rendered in writing, shall be final and conclusive and binding on the parties.

Each party shall pay its own expenses in connection with the arbitration, but the compensation and expenses of the arbitrators shall be borne in such manner as may be specified in the decision of the arbitrators.

Each party shall, in any arbitration hereunder, have the right to appear and be heard and present evidence before the arbitrators.

IN WITNESS WHEREOF, the parties hereto have caused this contract to be duly executed and issued in duplicate at Washington, District of Columbia, United States of America, as of the ________________ day of ________________, 1962.

AGENCY FOR INTERNATIONAL DEVELOPMENT

By________________________

____

By________________________

Date:________________________

A.I.D. CONTRACT OF GUARANTY

No. ______________________

CONTRACT OF GUARANTY-WAR RISK (LOAN AND EQUITY)

Contract of Guaranty made, entered into by and between the AGENCY FOR INTERNATIONAL DEVELOPMENT (hereinafter called "A.I.D."), an agency of the United States of America, and ____________________ (hereinafter called "Investor"), a corporation organized and existing under the laws of ______________________________ having its principal place of business at the ____

The Investor is a corporation substantially beneficially owned by citizens of the United States and is engaged in the United States and abroad in the ____ ____

The Investor proposes to invest in the ____________________ (hereinafter called the "Foreign Enterprise"), a corporation organized and existing under the laws of ____________________ which was formed for the purpose of ____ ______________ The total authorized capital of the Foreign Enterprise is ________________ (U.S. $______________ equivalent at the present rate of exchange).

The Investor contemplates a total investment of U.S. __________ of which approximately U.S. __________ will be utilized for the purchase of __________ percent _____ of the equity shares of the Foreign Enterprise and the remainder of which will be made in the form of long term United States dollar loans to the Foreign Enterprise.

________________ percent _____ of the equity shares of the Foreign

Enterprise will be owned by ______________________________

The Investment will be utilized for the installation and expansion of the Foreign Enterprise's ______________________________
____
____
____
____
________.

A Basic Agreement between the Investor and the Foreign Enterprise was concluded ______________ the establishment of the Project, as hereinafter defined, a copy of which is annexed to A.I.D. Contract of Guaranty No. ____________. Pursuant to the Basic Agreement, a Stock Subscription Contract setting out the details of the investment to be made by the Investor by way of its purchase of equity shares of the Foreign Enterprise was concluded ________________ a copy of which is annexed to A.I.D. Contract of Guaranty No. ______________. Further pursuant to the Basic Agreement, a Loan Contract setting out the details of the loans and the provisions regarding repayment including the form of the promissory notes (hereinafter called "Notes"), was concluded ________________ between the Investor and the Foreign Enterprise, a copy of which is annexed to A.I.D. Contract of Guaranty No. ___________.

The Investor has filed with A.I.D. pursuant to the provisions of Section 221(b) of the Act and to the rules and regulations prescribed the the Administrator thereunder, an application for a guaranty against loss on the Investment, as hereinafter defined, by reason of war,

revolution or insurrection. A.I.D. and the Government of ____________ ________ have each approved the project.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, A.I.D. and the Investor hereby agree as follows:

ARTICLE I

Definitions

Wherever used in this contract:

I-A. The term "Date of This Contract" means that date, shown on the last page of this contract, on which this contract was executed for A.I.D.

I-B. The term "Contract Period" means:

1. the year beginning on the Date of This Contract, such Contract Period being hereinafter called the First Contract Period, and
2. periods of one year in length, each commencing on the successive anniversaries of the Date of This Contract.

I-C. The term "Government of the Project Country" means the present or any succeeding governing authority (without regard to the method of its succession or to whether it is recognized by the United States), or authorized agents thereof, in effective control of all or any part of the Project Country, as hereinafter defined, or of any political or territorial subdivision thereof; provided, however, that

in no event shall the Government of the United States of America or any military government or command in which it participates, be included within the meaning of this paragraph.

I-D. The term "Guaranty Period" means (a) the period of twenty years from the date, shown on the last page of this contract, on which this contract was executed and issued, or (b) if terminated pursuant to Article IV or IX, then to and including the effective date of such termination.

I-E. The term "Investment" means the sum of:

(a) an amount not in excess of ________________ (U.S. __________) expended to acquire a ________ percent ____ equity interest in the Foreign Enterprise evidenced by ________ shares of the authorized capital stock of the Foreign Enterprise, plus

(b) the principal amount of the loan made by the Investor to the Foreign Enterprise in an amount not exceeding in aggregate the greater of either ________________ ________ (U.S. __________ or the difference between ____ and the dollar amount expended by the Investor in acquiring __________ percent of the equity shares of the Foreign Enterprise, evidenced by the Notes given the Investor by the Foreign Enterprise.

I-F. The term "Net Investment" means, on any date, the sum of:

(a) the book value of the equity shares of the Foreign

Enterprise which were acquired by the Investor as a result of the Investment and which were owned by the Investor on such date plus

(b) the unpaid principal on such date of the Notes of the Foreign Enterprise acquired by the Investor as a result of the Investment and which were owned by the Investor on such date.

I-G. The term "Project Country" means the territory presently under the jurisdiction of the Government of ______________________

I-H. The term "Maximum Amount of the Guaranty" means:

______________________________ dollars (U.S.$____________________).

Such amount shall be progressively reduced by any amounts received by the Investor as compensation under this contract, such reduction to take effect as of the first day of the Contract Period next succeeding the Contract Period in which the Damage occurred. Such amount shall also be subject to reduction by the Investor as provided in Article IX-B hereof.

A.I.D. shall refund to the Investor the portion of the Fee(s) for this Contract, as hereinafter defined, paid for the amount by which the Maximum Amount of the Guaranty is reduced during the Contract Period(s) commencing with the effective date of the reduction.

I-I. The term "Face Amount of the Guaranty" means the following amounts for the Contract Periods indicated:

1. During the First Contract Period:

______________________________________ dollars

(U.S. $____________________).

2. During the Second Contract Period and each succeeding Contract Period; any amount elected by the Investor as provided in Article IX-B hereof but not greater than the Maximum Amount of the Guaranty as of the first day of each Contract Period.

Such amount shall be progressively reduced by any amounts received by the Investor as compensation under this contract, each such reduction to take effect as of the date of Damage. Such reduction shall not entitle the Investor to a reduction in the Fee for This Contract, as hereinafter defined.

I-J. The term "Fee for This Contract" means the amount of U.S. $________________________ for the First Contract Period payable on or before the Date of This Contract, and:

(1) an amount payable on or before the first day of each of the succeeding nine (9) Contract Periods thereafter, which amount shall be equal to the sum of:

(a) one-half of one percent (1/2%) of the Face Amount of the Guaranty, for the respective ensuing Contract Period, and

(b) one-quarter of one percent (1/4%) of the amount, if any, by which the maximum amount of the Guaranty exceeds the Face Amount of the Guaranty for such respective ensuing Contract Period.

(2) an amount to be fixed by A.I.D., at least thirty (30) days prior to the beginning of the eleventh and each succeeding Contract Period, in the light of experience of the Administrator in the writing of war risk guarantees and which shall be payable by the Investor on or before the beginning of each such Contract Period, said amount however, not to exceed four percent (4%) of the Face Amount of the Guaranty for such Contract Period.

I-K. The term "Covered Property" means the tangible property of the Foreign Enterprise located in the Project Country at the time of Damage, as hereinafter defined. The term does not include accounts, bills, currency, deeds, evidences of debt, money, securities, bullion or manuscripts.

I-L. 1. The term "Damage" means injury to the physical condition of or destruction of Covered Property directly caused by insurrection, revolution or war (whether or not under formal declaration and thus encompassing any hostile act by any national or international organized force) and includes injury to the physical condition of or destruction of Covered Property as a direct result of actions taken in hindering, combatting or defending against a pending or expected hostile act whether in a war, revolution or insurrection. The term does not include injury to the physical condition or destruction of Covered Property directly caused by civil strife of a lesser degree than revolution or insurrection, but does include such destruction or injury

directly caused by hostile acts of organized revolutionary or insurrectionary forces including acts of sabotage.

2. An event shall be deemed to have directly caused injury to the physical condition of or destruction of Covered Property if there is an unbroken chain of causes and effects, starting with the event and ending with the injury or destruction, and if the injury or destruction would not have been sustained had the event not transpired, even though another event actively contributed to the injury or destruction (except as contemplated in II-B and III-P hereto) and was of itself sufficient to produce the injury or destruction.

I-M. The term "Investor's Share" means the ownership interest of the Investor in the Covered Property acquired by reason of the Investment. Such ownership interest, on any date, is the fraction the numerator of which shall be the Net Investment, as herein defined, on such date and the denominator of which shall be the sum of all the liabilities (other than the current liabilities) plus the equity capital and the surplus of the Foreign Enterprise on such date. The terms and the making of the Investment may not be varied without A.I.D.'s prior consent thereto in writing which shall not unreasonably be withheld, but which shall be conditioned upon an appropriate revision of the Investor's Share.

I-N. The term "Local Currency" means currency recognized as legal tender in the Project Country, as hereinafter defined, by the governing authorities thereof.

I-O. The term "Actual Cash Value" means, for any item of

Covered Property, the value immediately prior to the event of Damage, established on the books of account of the Foreign Enterprise kept in accordance with Article VII-H hereof, after any allowances for depreciation or amortization, adjusted, as necessary, to reflect the fair value of the item at the time of acquisition by the Foreign Enterprise and the actual physical condition of the item immediately prior to the event of Damage.

I-P. The term "Reference Rate of Exchange" shall mean on any date, with respect to currencies other than United States dollars:

First, the effective (including, for example, exchange taxes, transfer taxes, or margins, however designated) free market rate of exchange recognized or used by the Central Bank of the country issuing such currency, or if no single such free market rate can be determined then the average of such rates on such date recognized or used by the Central Bank of said country,

Second, the effective (including, for example, exchange taxes, transfer taxes, or margins, however designated) rate of exchange applicable to the purchase in the country issuing such currency of United States dollars with such currency on such date by a private investor or investors remitting earnings or capital or a private borrower servicing United States dollar debt, or if no single such rate can be determined, then the average of such rates on such date as obtained from a representative group of banks in said country, but if no such rate exists on such date,

Then, the most depreciated (that is, requiring the greatest amount of such currency per United States dollar) effective

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(including, for example, exchange taxes, transfer taxes, or margins, however designated) rate of exchange published or used by the Central Bank of the country issuing such currency on such date for sale of United States dollars to private residents of said country for imports into said country.

In the event either A.I.D. or the Investor regard the above rates as inapplicable or achieving an inequitable result in the sense of unfairly distorting the relative value between such currency and United States dollars, the question of an equitable Reference Rate will be settled by negotiation and if not resolved within sixty (60) days after delivery of a request for negotiation, shall be, at the request of either A.I.D. or the Investor, referred to arbitration for settlement.

I-Q. The term "Other Compensation" means any compensation of any kind for Damage to Covered Property received by the Investor or the Foreign Enterprise from any source other than under this Contract of Guaranty no matter whether such other source characterized the cause of said Damage as other than war, revolution or insurrection. The term "Other Compensation" further includes all sums received by the Foreign Enterprise or the Investor for the sale of damaged Covered Property less the costs of making such sale provided such costs do not exceed the sales proceeds.

ARTICLE II

Guaranty

II-A. Subject to the terms and conditions of this contract,

A.I.D. hereby guarantees to the Investor, upon application, compensation in U.S. dollars in the amount provided for in Article V hereof and occurring during the Guaranty Period; provided, however, that the Investor shall have no claim under this contract if the amount of compensation for Damage, computed as aforesaid, does not exceed $10,000 or 1% of the Face Amount of the Guaranty, whichever is smaller, and provided further that if such amount does exceed $10,000 or 1% of the Face Amount of the Guaranty, the Investor shall be entitled to compensation without deduction of the said minimal amount.

II-B. A.I.D. shall not be liable under this Contract of Guaranty for loss caused directly or indirectly by neglect of the Investor or the Foreign Enterprise to use all reasonable measures to save and preserve the Covered Property from Damage.

ARTICLE III

Representations and Covenants

The Investor hereby represents to A.I.D. that, as of the date on which this contract is executed by the Investor:

III-A. The Investor is a corporation created under the laws specified in the first paragraph on page 1 of this contract, and is substantially beneficially owned by citizens of the United States.

III-B. The Investor has not entered into any arrangements or agreements of whatever nature with respect to compensation by the Project Country for any loss on the Investment by reason of Damage.

The Investor hereby covenants with A.I.D. that:

III-C. The Investor will make payment to A.I.D. of the Fee for This Contract in the amount and manner specified in Article I.

III-D. The Investor will continue during the Guaranty Period to be a corporation created under the laws of the United States, or of one of the states or territories of the United States. In the event that the Investor shall during such period cease to be substantially beneficially owned by citizens of the United States, the Investor shall give prompt notice of that fact to A.I.D. and A.I.D. shall have rights of termination or refusal to make compensation as provided under paragraph A of Article IV in the case of breach of covenant.

III-E. The Investor will disclose promptly to A.I.D. in detail all arrangements and agreements of whatever nature which, during the Guaranty Period, are entered into by the Investor with respect to compensation of any kind by the Government of the Project Country for any Damage (no matter whether such government characterized the cause of said Damage as other than war, revolution, or insurrection) and will not, without obtaining the permission of A.I.D., enter into any such arrangements or agreements or accept any such compensation for any Damage with respect to which an application for compensation is submitted hereunder.

III-F. The Investor will notify A.I.D. promptly in writing of any action which it has reason to believe may cause or has caused Damage.

III-G. The Investor will, during the Guaranty Period, submit

to A.I.D. an annual financial report in duplicate, prepared in accord with accounting principles generally accepted in the United States and in such form as A.I.D. may reasonably request, indicating the amount of the Investment, the amount of the Net Investment, all sums received therefrom in U.S. Dollars, Local Currency or other currencies, and credits in any of the foregoing; the Actual Cash Value of the Covered Property; and such other information as A.I.D. shall reasonably require. The first such report shall cover the period to the end of the month in which the Date of This Contract falls, and subsequent reports shall cover the respective successive years. Each report shall be due within ninety (90) days after the end of the year reported.

III-H. The Investor will maintain in a place accessible to A.I.D. or its duly authorized representatives, books of account and other records, in accordance with accounting principles generally accepted in the United States, covering the amount of the Investment; the amount of the Net Investment; the Actual Cash Value of the Covered Property; and all other receipts, expenditures, and transactions by the Investor in U.S. Dollars, Local Currency, or other currencies, and credits in any of the foregoing, in the Project Country or elsewhere in connection with the Investment. During (i) the Guaranty Period, (ii) any period after the Guaranty Period when the Investor has an application for compensation hereunder pending, and (iii) for five years after payment of any compensation hereunder:

(a) the Investor will permit A.I.D., or its duly authorized representatives, to inspect, examine

and audit said accounts and records, whether they be located in the Project Country or elsewhere; and

(b) the Investor will use its best efforts to enable the duly authorized representatives of A.I.D. to examine, audit, and copy for the purpose of this contract any books and records of the Foreign Enterprise, and to inspect its properties, whether in the Project Country or elsewhere, and the Investor will render every reasonable assistance in connection therewith.

III-I. The Investor will not assign, transfer, pledge or make other disposition of this contract or of any of the rights of the Investor hereunder without first obtaining the consent of A.I.D. thereto in writing.

III-J. Unless A.I.D. first agrees otherwise in writing, the Investor will, to the extent of Investor's ability, cause both the Project to be carried out and the Investment to be made substantially in accordance with the material representations relating thereto submitted in obtaining this Contract of Guaranty and in accordance with this Contract of Guaranty.

III-K. Prior to the completion of the transfers and assignments specified in Paragraph III-O, the Investor shall take all reasonable measures to pursue and preserve any and all administrative or judicial remedies available in connection with the loss and to maintain and preserve the Covered Property.

III-L. The Investor will cooperate in full, and will use its best efforts to cause the Foreign Enterprise to cooperate in full, with

the responsible agents of the Government of the United States of America in the preservation and prosecution of any claims transferred pursuant to said Paragraph O, including without limitation the making available of evidence, including documents and witnesses, necessary to the prosecution of claims thus acquired. The Investor shall not be obligated by this paragraph to take any action which will incur substantial direct expenses by it unless reimbursement for such expenses by the Government of the United States is made available.

III-M. Within sixty (60) days after the Date of This Contract and on or before the last day of the sixth month of each fiscal year of the Foreign Enterprise during the Guaranty Period, the Investor, to the extent of its ability, shall furnish A.I.D. two copies of a balance sheet, profit and loss statement, analysis of surplus or Investor's investment account and such other statements as A.I.D. shall reasonably require pertaining to the operations and the financial condition of the Foreign Enterprise during its preceding fiscal year.

III-N. No member of or delegate to Congress or resident commissioner shall be admitted to any share or part of this contract or to any benefit that may arise therefrom, but this provision shall not be construed to extend to this contract if made with a corporation for its general benefit.

III-O. The Investor shall, upon receipt of notice from A.I.D. of the amount of compensation determined to be due hereunder, and prior to the payment of any such compensation, assign, transfer, set over and convey to A.I.D., or to any agent designated by A.I.D., in the manner

and to the extent reasonably required by A.I.D., any claims, causes of actions or rights which the Investor may have for compensation from whatever source for Damage to the extent of the compensation to be paid hereunder. To the extent of its ability, the Investor will execute or transfer all documents, and will take all other actions, as A.I.D. may reasonably require, to complete effectively the assignments, transfers, settings over, and conveyances provided in this paragraph.

III-P. The Investor shall take and, to the extent of his ability, cause the Foreign Enterprise to take all reasonable measures to protect the Covered Property from further damage, separate the damaged and undamaged Covered Property, put it in the best possible order, prepare a complete inventory of the lost, destroyed, damaged and undamaged property, showing in detail quantities, costs, Actual Cash Value and amount of loss.

ARTICLE IV

Misrepresentation and Breach of Covenant

IV-A. In the event that the Investor shall have made a material misrepresentation of any fact stated in paragraph A or B of Article III hereof, or shall breach any covenant contained in paragraph D, E, F, I, or N of said Article, A.I.D. shall have the right to terminate this contract at any time by written notice given to the Investor, and, with or without exercising such right of termination, shall have the right to refuse to make compensation to the Investor hereunder. In the event of misrepresentation or breach giving rise to the right of

A.I.D. to terminate this contract as provided in this paragraph IV-A, neither the acceptance of any fee by A.I.D. after the occurrence of such misrepresentation or breach, nor the fact that A.I.D. shall have had knowledge, actual or constructive, of the occurrence of such misrepresentation or breach and shall have failed to exercise its right of termination, shall operate as a waiver of the right of A.I.D. to terminate this contract or to refuse to make compensation to the Investor hereunder.

IV-B. In the event that the Investor shall breach any covenant contained in any paragraph of Article III other than paragraph D, E, F, I, or N thereof, A.I.D. shall, at its option, do one or more of the following:

1. terminate this contract by giving not less than thirty (30) days written notice to the Investor. Such notice shall contain a statement of A.I.D.'s intention to terminate, the reason upon which the termination is based, and the date upon which the termination is effective. Unless the Investor shall have cured such breach prior to said date, all obligations of A.I.D. hereunder shall terminate on said date, except as to any rights of the Investor which have accrued prior to such breach and with respect to which any application or applications are then pending:
2. refuse to make compensation to the Investor based

upon an application filed subsequent to the breach unless the Investor shall cure the breach within thirty (30) days after A.I.D. shall give notice to the Investor of the existence of the breach:

3. make such arrangements as it deems proper with the Investor to provide for the cure of the breach.

In the event of breach giving rise to the right of A.I.D. to terminate this contract as provided in this paragraph IV-B, neither the acceptance of any fee by A.I.D. after the occurrence of such breach, nor the fact that A.I.D. shall have had knowledge, actual or constructive, of the occurrence of such breach and shall have failed to exercise its right of termination, shall operate as a waiver of the right of A.I.D. to terminate this contract or to refuse to make compensation to the Investor hereunder, provided, however, that the Investor shall be given a reasonable opportunity to cure any such breach, and A.I.D. shall not terminate this contract or refuse to make compensation to the Investor hereunder if Investor carries out agreed arrangements for such cure.

IV-C. In the event of any termination of this contract by A.I.D. all rights, liabilities and obligations under this contract, except as expressly continued by paragraph B of this Article, shall cease, except the following obligations of the Investor:

1. to comply with the covenants and agreements contained in paragraphs E, H, I, and L of

Article III hereof; and

2. to make any repayment required by paragraph D of this Article IV.

IV-D. If A.I.D. shall have paid any compensation to the Investor hereunder and shall thereafter ascertain that, prior to such payment, the Investor misrepresented any fact stated in paragraph A or B of Article III, or, prior to the date of such payment, breached any covenant in paragraph D, E, F, I, J, or N of Article III, or made any material misstatement of fact in the application for such compensation, or, subsequent to the payment of such compensation, the Investor breached the covenant contained in paragraph L of Article III, then, on demand of A.I.D., contained in a written notice given to the Investor within one year after ascertaining that any such misrepresentation or breach has occurred or such misstatement was made, the Investor shall immediately repay to A.I.D. the amount of U.S. dollars so paid to the Investor, and upon receiving such repayment A.I.D. shall return to the Investor the rights, title and interests transferred pursuant to paragraph O of Article III hereof, provided, however, A.I.D. may not assert such demand after the expiration of the period of five years immediately succeeding the misrepresentation, breach or misstatement occasioning the demand.

IV-E. In the event and to the extent that A.I.D. shall without sufficient legal cause have refused to pay any compensation hereunder, A.I.D. shall not be liable to the Investor for damage beyond the amount herein expressly provided.

ARTICLE V

Amount of Compensation

V-A. The amount of compensation to be paid hereunder for Damage shall be the lesser of either

(a) the Face Amount of the Guaranty in effect on the Date of Damage, or

(b) ninety percent (90%) of the Investor's Share of the amount of Damage determined in accordance with Article VI less:

1. The United States dollar value of any Other Compensation received by the Investor for the same Damage, and

2. The Investor's Share of the United States dollar value of any such Other Compensation received by the Foreign Enterprise but not by the Investor.

If such Other Compensation is received in currency other than United States dollars, the United States dollar value of such Other Compensation shall be established at the Reference Rate of Exchange on the date of receipt of such Other Compensation. If such Other Compensation is received in kind, the value of such other compensation shall be the fair market value thereof.

V-B. If A.I.D. pays any compensation hereunder for Damage and if, within five (5) years after the Investor has received compensation hereunder, the Investor or the Foreign Enterprise receives Other Compensation for such Damage other than Other Compensation which was taken into account under paragraph V-A in computing the amount of compensation hereunder, the Investor shall promptly repay to A.I.D. a) ninety percent (90%) of any amounts so received by the Investor and/or b) ninety percent (90%) of the Investor's Share of any amounts so received by the Foreign

Enterprise but not by the Investor; provided, however, that the Investor shall not be obligated to make any of the aforesaid repayments in excess of the amount of compensation received by the Investor from A.I.D. hereunder. If A.I.D. so requests as a condition of paying compensation hereunder, the Investor agrees to give A.I.D. appropriate surety or guaranty for any repayment that may be required by this paragraph.

V-C. In the event that A.I.D. has made any compensation hereunder on the basis of the presumption that the percentage of Damage is sixty percent (60%) as provided under paragraph VI-C, any such compensation shall be subject to review for a period extending five (5) years from the date such compensation is made. Further, A.I.D. shall make prompt and reasonable attempts during said five-year period to review the amount of such Damage. In the event such review reveals the Damage to be greater than sixty percent (60%) A.I.D. shall promptly make additional compensation to the Investor equal to the difference between the amount determined by A.I.D. to be due the Investor on the basis of said review and the Investor shall make additional assignments, transfers, settings over and conveyances in accordance with paragraph III-O to the extent of such additional compensation. In the event such review reveals the Damage to be less than sixty percent (60%) the Investor shall, within sixty (60) days of receipt of notice by A.I.D., refund to A.I.D. an amount equal to the difference between the compensation previously made and that determined by A.I.D. to be due the Investor on the basis of said review and A.I.D. shall make an adjustment in the assignments, transfers, settings over and conveyances previously made under paragraph III-O to reflect the reduced compensation actually received by the Investor.

ARTICLE VI
Computation of the Amount of Damage

VI-A. The amount of Damage shall be the Actual Cash Value of the damaged Covered Property, but not exceeding the amount of the reasonable cost of repairing or replacing such Covered Property with property of like kind and quality within a reasonable time after such Damage.

VI-B. In case the Investor and A.I.D. shall fail to agree as to the Actual Cash Value of the damaged Covered Property then, on the written demand of either, a competent and disinterested appraiser shall be appointed by the American Arbitration Association. The appraiser shall then appraise and state separately the Actual Cash Value of each item or property asserted to be damaged Covered Property, the reasonable cost of repairing or replacing each such item, the reasonable sales value of the damaged Covered Property and the reasonable costs of putting the property into such salable condition. An award in writing, so itemized, when filed with A.I.D. shall be prima facie evidence of the amount of Actual Cash Value, reasonable repair or replacement cost, reasonable sales value and costs of putting damaged Covered Property into salable condition. The appraiser and the expenses of appraisal shall be paid by the parties equally.

VI-C. If A.I.D. is unable, after making a reasonable attempt, to determine the amount of Damage because conditions prevailing in the Project Country create a personal hazard for personnel or authorized agents of A.I.D. attempting to assess the amount of Damage or because the Government of the Project Country forbids personnal or authorized agents of A.I.D. from entering the Project Country or travelling therein

as necessary to assess the amount of Damage, then the amount of Damage shall be presumed to be equal to sixty percent (60%) of the Actual Cash Value of the Covered Property on the date of Damage and A.I.D. shall so notify the Investor, unless the Investor has furnished evidence of a different amount of Damage.

ARTICLE VII

Application for Compensation

VII-A. At one or more times the Investor may file with A.I.D. application for compensation hereunder; provided, however, that any such application must be filed not later than six (6) months after the Investor has reason to believe that Damage has occurred. Any such application shall be in a form satisfactory to A.I.D. and shall contain all information reasonably required by A.I.D. to determine the Investor's right to compensation and the amount thereof. A.I.D. thereafter will keep the Investor advised in writing as to any additional evidence which it may deem reasonably necessary to complete the application; provided, however, that:

1. an application will be deemed to be complete, if, at the expiration of three (3) months after the delivery to A.I.D. of any evidence from Investor, A.I.D. does not have outstanding a request for additional evidence;
2. if the Investor, within three (3) months after date of delivery to the Investor of a request by A.I.D. for evidence, either fails to supply such evidence or fails to make reasonable efforts to supply such evidence, A.I.D. may, at

its option, consider the application as abandoned unless the Investor has shown A.I.D. good cause why such evidence should not be supplied or such efforts undertaken. A.I.D. may, at its option, reinstate such application upon written request of the Investor.

A.I.D. shall consult with the Investor or otherwise afford the Investor a reasonable opportunity to present its views on any question of fact which A.I.D. must resolve in determining whether and to what extent Investor has incurred loss on the part or all of the Investment as a result of Damage within the meaning of this contract. The filing of applications and supporting evidence shall not operate to create any presumption that Investor has incurred such losses.

VII-B. Every application for compensation hereunder shall be accompanied by a proof of loss, signed and sworn to by the Investor, stating the knowledge and belief of the Investor as to the following: (i) the time and origin of the Damage, (ii) the interest of the Investor and all others in the damaged Covered Property, (iii) the Actual Cash Value, reasonable cost of repair and replacement, probable sales value and costs of putting into salable condition of each item of damaged Covered Property, (iv) all other contracts of insurance, and other sources of Other Compensation, covering any of said property, and (v) the amount of any Other Compensation already received by the Investor or by the Foreign Enterprise for the Damage.

VII-C. A.I.D. shall have a reasonable period, not in excess of six (6) months after completion of any application, to determine and

to notify Investor of its determinations as to (1) whether or not Damage has been incurred, and if so the amount thereof, (2) the date of Damage, if any, and (3) the amount of compensation so due to the Investor hereunder. If A.I.D. does not make the determinations and give the notification required by this paragraph within six (6) months after completion of any application an arbitrable controversy shall be deemed to exist.

VII-D. Nothing in this agreement shall prevent Investor from withdrawing any application at any time prior to the time of the assignment to A.I.D. of Investor's rights, title and interest as provided in paragraph O of Article III hereof.

VII-E. Within sixty (60) days (or such longer period as the parties may agree upon in writing) after the delivery to Investor of notice from A.I.D. that compensation is due hereunder, and the amount thereof, Investor shall assign its rights, title and interest to A.I.D. as provided in paragraph O of Article III hereof, and A.I.D., upon the completion of such assignment shall make immediate payment to the Investor of the amount of compensation due.

ARTICLE VIII

Funds Available for Payment of Guaranty

VIII-A. The only funds which will be available to A.I.D. for the purpose of discharging liability under this and all other contracts of guaranty which may have been or may hereafter be entered into pursuant to the authority of Section 221(b) of the Act, Sections 202(b) and 413(b)(4) of the Mutual Security Act of 1954, as amended, and

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Section 111(b)(3) of the Economic Cooperation Act of 1948, as amended (exclusive of informational media guaranties), are (i) those specified in Section 222 of the Act, and (ii) other funds, if any, which may be available at any time hereafter for the aforesaid general purpose, pursuant to the laws of the United States.

VIII-B. The Investor shall have no right or claim arising out of this contract against any other asset of A.I.D.

ARTICLE IX

Termination and Reduction

IX-A. The Investor shall have the right to terminate this contract effective on the first day of any Contract Period by written notice given to A.I.D. on or prior to such day. Such termination shall, from its effective date, relieve the Investor of all further obligations to pay the Fee for This Contract, but it shall not discharge or affect any other right, liability or obligation of either party which has accrued prior to the effective date of the termination of this contract or which, by the terms of this contract, is to survive the Guaranty Period.

IX-B. Prior to the first day of any Contract Period the Investor may by giving written notice to A.I.D.:

(1) Elect a Face Amount of the Guaranty for the ensuing Contract Period.

(2) Reduce the Maximum Amount of the Guaranty for the remaining Contract Periods.

Election under (1) shall be in effect only for the Contract Period

requested by the Investor and reduction under (2) shall be permanent and may not be reinstated. Reductions pursuant to this Article shall become effective on the first day of any Contract Period immediately following delivery to A.I.D. of written notice thereof and shall not affect the amount of the fee payable, or the retention by A.I.D. of any fee paid, for any period prior to the date on which such reductions become effective.

ARTICLE X

Modification

Any provision(s) of this contract may be modified, supplemented or otherwise altered by mutual agreement in writing.

ARTICLE XI

Notices

XI-A. Written notice to the respective parties may be delivered by:

1. making personal delivery of such notice to the Investment Guaranties Division, Agency for International Development, or to one of the representatives of the Investor, authorized pursuant to Article XII hereof, or
2. depositing such notice in the U.S. Post Office by registered mail enclosed in an envelope, postage prepaid, addressed to the party concerned at the address below specified, or to such other address as may be specified in writing from time to time:

To: INVESTMENT GUARANTIES DIVISION
AGENCY FOR INTERNATIONAL DEVELOPMENT

At: WASHINGTON 25, D. C.

To: THE INVESTOR

At: The address stated in the first paragraph
on page 1 of this contract

XI-B. The date of delivery under A.1. shall be the date on which the notice is received and under A.2. shall be the date on which the item was registered.

ARTICLE XII

Authority of Representatives

Prior to and as a condition of receiving any payment under this contract the Investor shall furnish A.I.D. with evidence of the authority of the persons who will act as representatives of the Investor in connection with the operation of this contract. A.I.D. shall be entitled to rely on such evidence of authority until A.I.D. shall receive written notice from the Investor that such persons are no longer authorized so to act; and in the event of such notice, the Investor will promptly furnish A.I.D. with evidence of the authority of persons authorized to act in their place and stead.

ARTICLE XIII

Disclaimer

The approval of A.I.D. of this Investment for guaranty purposes is not to be construed as an acknowledgment of the legality of the agreements or arrangements constituting or relating to this

Investment, or of any acts in pursuance thereof, under the laws, including the antitrust laws, of the United States or of the Project Country.

ARTICLE XIV

Arbitration

Any question which shall arise as to the obligation of either party under this contract or the interpretation of any provision thereof, if not settled by mutual agreement, shall, at the option of either party and, upon written notice to the other party, be settled by arbitration. The arbitration shall be held at Washington, D. C., and shall be conducted in accordance with the then prevailing rules of the American Arbitration Association. In any such arbitration A.I.D. shall appoint one arbitrator, the Investor shall appoint another, and the two so appointed shall appoint a third arbitrator; provided, however, that if any arbitrator or arbitrators are not appointed in accordance with the foregoing provisions of this Article within sixty (60) days after notice for arbitration has been given, such arbitrator or arbitrators shall be appointed in accordance with the rules above mentioned.

The controversy shall be submitted to the arbitrators in such manner as they shall deem appropriate, consistent with the then prevailing rules of the American Arbitration Association, and the decision of a majority of the arbitrators, rendered in writing, shall be final and conclusive and binding on the parties.

Each party shall pay its own expenses in connection with the arbitration, but the compensation and expenses of the arbitrators shall

be borne in such manner as may be specified in the decision of the arbitrators.

Each party shall, in any arbitration hereunder, have the right to appear and be heard and present evidence before the arbitrators.

IN WITNESS WHEREOF, the parties hereto have caused this contract to be duly executed and issued in duplicate at Washington, District of Columbia, United States of America, as of the date, shown below, on which this contract was executed for A.I.D.

By________________________________

Date______________________________

AGENCY FOR INTERNATIONAL DEVELOPMENT

By________________________________

Date______________________________

PRIVATE INVESTMENT IN LATIN AMERICA

THURSDAY, JANUARY 16, 1964

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON INTER-AMERICAN ECONOMIC
RELATIONSHIPS OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The subcommittee met, pursuant to recess, at 10:05 a.m., in room 1202, New Senate Office Building, Hon. John Sparkman, presiding.

Present: Senators Sparkman, Pell, Javits, and Jordan, and Representatives Griffiths and Curtis.

Also present: William H. Moore, economist; Hamilton D. Gewehr, administrative clerk; and Donald A. Webster, minority economist.

Senator SPARKMAN. Let the committee come to order, please.

We have a rather heavy schedule this morning, and I think we had better get started. We do know several members are on the way. One member is in the Banking and Currency Committee. I just left that committee myself. Here comes Senator Javits—so at least we have a bipartisan committee to start with.

This is the third day of these hearings. We have had some very profitable and interesting discussions. I feel certain that this morning will be no exception.

We are pleased today to have with us Mr. Francis E. Grimes, vice president, Chase Manhattan Bank, N.Y. Also Mr. Sperry Lea, associate director of research, Canadian-American Committee, National Planning Association, author of "A Canada-United States Free Trade Arrangement." And Mr. William L. Clayton, board of directors, Anderson, Clayton & Co., former Under Secretary of State for Economic Affairs.

We are pleased to have all three of you gentlemen. I have asked the three of you to sit at the table as a panel. Each one may present his own individual views or paper, and then there will be questions directed to any one or all from the members of the committee. In fact, I hope that all of you will feel that they are directed to you and will participate in the answers and discussion, and even ask questions of one another at the panel, if you will.

Our first presentation will be by Mr. Grimes. Mr. Grimes, we have a copy of your paper, and I may say to all of you that your paper will be printed in full in the record regardless of how you treat it. You may read it, summarize it, or discuss the high points in any way that you wish.

Senator JAVITS. Mr. Chairman, first I would like to welcome my own constituent, Mr. Grimes, and thank him for helping the committee by his testimony. And I don't think it would be fitting to allow Will Clayton's appearance to go unnoticed, Mr. Chairman. He

has the bipartisan appreciation and I think the affection of almost everybody here. I am glad to see him here looking so well in his usual role, tossing out provocative ideas.

Senator SPARKMAN. Fine. All right, Mr. Grimes.

STATEMENT OF FRANCIS E. GRIMES, VICE PRESIDENT, AREA EXECUTIVE, LATIN AMERICA, CHASE MANHATTAN BANK, NEW YORK, N.Y.

Mr. GRIMES. Mr. Chairman and gentlemen of the committee, it is indeed a pleasure and an honor to be asked to testify before your subcommittee which has made such an important contribution to a fuller understanding of the myriad problems facing Latin America and U.S. relations with that area.

I have already submitted to the Secretary my paper updating the developments in Latin America, in the two new regional markets in Latin America as we see it at the Chase Manhattan Bank. I presume that you gentlemen of the committee have had a chance to review this material and I would therefore like to submit this written report to you for inclusion in the record and forego the reading of it at this time. Instead, I would like to verbally touch on some of the highlights of the report and attempt to answer any questions which you might have, if that is agreeable to you.

Senator SPARKMAN. Very well, sir.

(The prepared statement and the attached charts referred to are as follows:)

LATIN AMERICAN REGIONAL MARKETS AND THEIR IMPACT ON U.S. DIRECT INVESTMENTS

(Prepared statement of Francis E. Grimes, vice president, the Chase Manhattan Bank)

I. THE LATIN AMERICAN REGIONAL MARKETS AND U.S. PRIVATE INVESTMENTS

This paper discusses some of the influences that the Latin American Free Trade Area (LAFTA) and the Central American Common Market (CACM) may have on U.S. private investments in the area. First, however, it will be useful to describe the two areas, to give a brief historical background, and to point out the differences between the two markets.

These regional developments have already brought several shifts in trading and investment patterns, although they are small in the case of LAFTA. But in looking at these two markets it must be kept in mind that they are both relatively new and that they differ markedly from each other in several important respects.

Furthermore, although encouraged by the highly successful European Common Market (EEC), LAFTA and the CACM are quite different in nature and in purpose from their older European cousin. The EEC is composed of highly industrialized economically mature nations with a tradition of economic interdependence; and the underlying goal of the EEC is political in nature. On the other hand, the Latin American markets consist of unintegrated, low-income, agricultural economies in which intraregional trade is only a small percent of the total; and the primary goal of unification is economic in nature.

II. THE LATIN AMERICAN FREE TRADE ASSOCIATION

Only 3 years old, but with some major accomplishments already to its credit, the Latin American Free Trade Association (LAFTA) seems well on its way toward becoming a permanent and important force in the economic life of Central and South America.

LAFTA has created an effective forum wherein businessmen and government officials from all over the area can explore common problems and opportunities. It has lowered trade barriers among member countries, although it is still too early to say just how far. And despite the many difficulties that lie ahead, the general feeling is that the association will not only hang together but will exert a continuing and growing influence on economic activity in Latin America.

A compelling need

Established by the Treaty of Montevideo in February 1960, LAFTA is a historic step toward the realization of an ancient dream—free trade throughout Latin America. By broadening markets and stimulating investment, free trade in turn is expected to speed industrialization, promote overall economic development, and generate a better life for the area's people.

The need for improvement here is compelling. Latin American living standards are far below those which a growing segment of the population is coming to regard as minimal. And the need to show more rapid progress toward meeting the people's aspirations was one of the prime reasons behind the agreement.

Also pushing the agreement along were several outside developments, among them the immense success of the European Common Market. While serving as a shining example of what international cooperation can accomplish, the Common Market also posed a threat to Latin American exports, largely because of the favored treatment it gives the farm produce of its African associates. What's more, the area's terms of trade had been steadily deteriorating, which brought home in no uncertain fashion the necessity for spurring development of industries to produce items other than traditional raw materials.

A major market

Approving the treaty so far are Argentina, Brazil, Chile, Colombia, Ecuador, Mexico, Paraguay, Peru, and Uruguay. Put together, these countries make up one of the world's major markets. They have a population of 180 million, an area over twice as large as the continental United States, and an annual gross product of about $55 billion. Their yearly imports run around $5.9 billion, their yearly exports around $5.1 billion.

The things they produce range from copper, zinc, iron, and gold to cotton, bananas, coffee, and tobacco; from sheep and cattle to steel ingots, autos and caustic soda. And in many key products, they turn out well over 75 percent of the Central and South American total.

Less tangible than all this, but perhaps of equal importance as a yardstick of the area's potential, is the simple fact that the partners entered into the agreement. This in itself is a significant symbol. It shows a willingness to work together. It likewise shows a strong desire for economic improvement.

How trade is liberalized

Providing for the gradual elimination of tariffs and other trade restrictions over a 12-year period, the treaty requires that members take two steps toward razing trade barriers.

The national schedule: First, each country must negotiate an annual national schedule setting forth the tariff cuts it will grant other members. These talks may be carried on by pairs or groups of countries in line with their various interests. But the reductions given to any one member also apply to all others. This is so all members can compete equally in the country offering the concession.

According to treaty article 5, which at first glance seems entirely straightforward, the weighted average of the duties listed on the national schedule must be reduced each year by not less than 8 percent of the weighted average of the duties applicable to nonmember nations.

The common schedule: Second, each country must agree to a common schedule, which differs from the national schedule in several important ways. Once a product goes on this list it cannot be removed. Also, a definite timetable is set up for the common schedule's growth. It is slated to cover 25 percent of all intraregional trade at the end of the first 3 years, 50 percent after 6 years, 75 percent after 9 years, and substantially all regional trade at the end of 12 years.

Agriculture and new products

But, however loose these general provisions may seem, they are in fact even looser still—the reason being that they are hedged with special exemptions, susceptible to delay, and open to backtracking maneuvers on the part of the participants. All of which had led some critics to claim—quite prematurely—that the treaty isn't up to the job of fashioning a fully functioning free trade area within the 12-year target period.

One major exemption is agriculture. Except to cover deficits at national price levels, members need not buy the farm products of other members. For example, if a country grows enough rice to supply its own domestic market, it can keep its tariffs on rice. And even when it does bring in such products, it can impose levies that raise the price of the imports to the price of domestic products.

Somewhat more unusual is LAFTA's treatment of new products—that is, items not traded within the region at the time the treaty was signed. Although encouraged to do so, members are not required to expand trade by granting concessions on new items. However, an encouraging sign was the recent proposal by one of the member states that a procedure be adopted to eliminate all internal tariffs regardless of whether the products are now traded between the member countries.

The three conferences

But while technically valid perhaps, these criticisms appear overly harsh, obscuring two vitally important points. One, the treaty was apparently the best that could be worked out under admittedly difficult circumstances—and even a weak agreement is preferable to none at all. Two, the broad spirit of the treaty may ultimately overcome its excessively narrow letter.

And at the first LAFTA conference, which got underway in July 1961, there were several signs suggesting that the spirit might prevail. Rules and procedures were adopted promoting the inclusion of new goods, with the negotiations actually covering many such items. What's more, reported duty reductions reached about 25 percent of the weighted overall average, a figure about three times larger than the treaty calls for. This figure must be interpreted with caution, however, since some part of it came from a recognition of preexisting arrangements rather than new cuts.

What can be said with certainty is that the levies on many items were drawn back. A 30-percent duty now applies to meat imports into Chile from Argentina, as against 54 percent from countries outside LAFTA. Razor blades produced in Argentina now enter Brazil with an 8-percent duty, while non-LAFTA countries must pay 84 percent. Also, a sizable chunk of chemical business has been shifted from American to Mexican firms, which are now free from prior deposit rules along with high ad valorem and surcharge duties.

Following the first round of negotiations, some decided changes in trading patterns were clearly observable. Although the area's total imports declined 1.3 percent during 1962, the first year after the concessions, exports inside LAFTA rose a resounding 37 percent, with every member showing an increase. True, the gain came from a very low base, since intra-LAFTA trade accounts for less than 10 percent of the area's total. Still and all, the showing should not be equated to zero—or anywhere near it.

Mexico, which fared better than any other LAFTA country, provides the best example of what can happen when trade walls are lowered. Her manufacturing exports during 1962 rose 150 percent; chemical exports rose 425 percent. In total, her trade with the rest of the zone increased 90 percent, up from $12 to $23 million. It is expected to reach $40 million in 1963.

Scarcely anyone, of course, has interpreted these improvements as meaning that LAFTA is out of the woods and safely home. On the contrary, when the second conference opened in August 1962, in Mexico City, the prevailing mood was one of urgency. The general feeling was that the integration process must be accelerated.

First and foremost, it was widely agreed the concessions already granted weren't being fully used. Mexico's exports to the region, for example, increased 80 percent during the first 7 months of 1962. Yet out of 400 items for which concessions had been obtained, only 70 were exported to the area, compared with exports of 130 products not included in the liberalization.

Many concessions were not sufficient to offer LAFTA exporters a genuinely competitive position. Not enough information had been made available to exporters about the reductions. And in some cases, although theoretically helped by tariff cuts in the countries where they wanted to do business, companies found themselves boxed in by high export duties imposed by their own countries.

Nevertheless, the achievements of the second conference instilled a new breath of life in the organization. And further cuts were also made in intra-area tariffs.

The progress at the third annual conference, which opened in October 1963 at Montevideo, was methodical and deliberate. The bargaining that took place indicated that the members feel the movement toward economic integration

may become irreversible and that concessions should therefore not be granted lightly.

Although the intratrade tariff rates for 1964 are not fully compiled, early indications are that the annual 8-percent reduction will be achieved. The meeting showed that while product-by-product negotiation is cumbersome, across-the-board cuts seem impossible as long as different customs systems are still in force.

The members also agreed to work further toward a common outer tariff and took the first step by instructing the Customs Advisory Committee to consider this subject in a meeting next February. Its first task will be to improve the LAFTA nomenclature to permit useful comparisons among the existing tariffs of member countries. A committee of experts from each country will then prepare a proposal for a common outer tariff to be presented at the fourth conference in Bogotá next fall. This, if successful, will bring the area closer toward its goal of a true common market.

Of considerable importance, a special conference this May was scheduled at which the first common list applicable to all members will be negotiated. The list will cover products that represent 25 percent of intra-LAFTA trade during 1960–62. Once an item has been placed on this list, members are committed to reduce their intra-LAFTA tariffs and other trade restrictions on that item to zero by June 1973.

Problems ahead

One important fact brought out in the second and third conferences is that the negotiation of future concessions will likely get tougher. In the third session it was much more difficult to negotiate concessions than it had been in 1962, when most of the liberated products were raw materials. And now that it is becoming more and more difficult to grant tariff concessions without injuring local producers, the give and take will grow progressively harder.

Poor transportation also continues as a trade deterrent. The geography of the continent, with its vast interior of mountains, jungles, and deserts, makes inland transport difficult and costly. And because cargoes between the members remain small, ocean shipments, too, are expensive. The LAFTA Transportation Commission, which is now wrestling with these problems, is preparing proposals that will promote the complementary development of the transportation industry. But it seems unlikely that the difficulties here can be overcome in the near future.

Another knotty problem, but one that appears on the way to quick solution, has been the lack of medium- and long-term export credit. Last fall the Inter-American Development Bank (IDB) announced a pioneering program to finance exports of capital goods among its Latin American member countries from January 1, 1964. An initial allocation of $30 million has been authorized from the IDB's ordinary resources to finance the program. Under the program, the IDB will make available medium-term loans (6 months to 5 years) to finance the export of capital goods enumerated in a provisional list, which includes equipment for generation of power, electricity, agriculture, offices, metalworking, mining, industry, and railways, machinery and automotive vehicles for industrial and commercial use, aircraft, ships, prefabricated buildings, and manufactured components to be used in the above items.

To be eligible for financing under the program, the capital goods must originate among the Latin American members of the IDB. The total value of constituent materials that are not from Latin America may not exceed 50 percent of the price of the finished goods. Funds provided by the IDB may finance up to 70 percent of the value of any export transaction and the importer must pay at least 20 percent of the invoice value of the export in cash.

Complementarity and insularity

Nor are difficulties in further negotiations, transport, and finance the only causes for concern. There are also the problems of excessive complementarity and insularity.

Complementarity: Two important complementary agreements, under which government officials decide the products that will be produced in each nation and sold throughout the area, covering business machines and copper have already been approved by the LAFTA membership. And a third concerning the creation of a glass factory in Uruguay is now awaiting approval.

In many cases such agreements may work out fine as interim measures, promoting both greater competition and greater efficiency over the long haul. In these arrangements one country trades off its rights to make a certain product in return for an agreement to supply another product to other members.

This, of course, is tantamount to the introduction of new and rigid trade barriers—which is one of the reasons why Latin American economies have not developed in a true complementary fashion in the first place. True complementary development thrives on freedom—the freedom of resources to find their most efficient use. To be sure, resources are "directed," but by customers and suppliers, not government decree.

Insularity: Another major concern is the attitude LAFTA will take toward the rest of the world. If it moves toward high, permanent external barriers and discriminating trading arrangements against the European Common Market, the United States, or others, Latin America's long-term growth prospects will be sorely damaged. On the other hand, LAFTA can serve a constructive purpose if oriented toward the long-term objective of declining external trade barriers and expanding multilateral trade with all the nations of the free world.

The future

But perhaps the hardest problem facing the region in the near future is simply that its major imports cannot be supplied from within the Montevideo countries. Not even the most efficient treaty conceivable can change this fact. So it would be highly unrealistic to suppose that LAFTA can be transformed into a European Common Market overnight. Too much in the way of capital, skill, communication, and tradition are lacking for that.

But given sufficient time—and the area's ability to move away from national protectionism and toward an environment in which industrial growth and trade expansion are determined by the forces of competition—LAFTA can certainly go a long way in that direction.

If the enthusiasm that has sparked the progress made to date continues and if the climate for private capital is favorable, LAFTA could become an increasingly attractive location for investment. This is particularly true of manufacturing industries where large markets are needed. Perhaps an attitude similar to the one that led to the surge of U.S. investments in the European Common Market could develop.

But the main sources of strength for LAFTA is and will remain the efforts of Latin American businesses and Latin American governments—which is as it should be. To become a complete success, however, LAFTA will require not only much additional effort but a willingness on the part of all member nations to overcome a natural tendency to act in defense of purely national interests. But the needs are great, and recognition of those needs is becoming clearer. This is helping to provide the cement that hopefully will bind the LAFTA nations more closely together, and provide an important motive force in their economic development.

III. THE CENTRAL AMERICAN COMMON MARKET

The CACM is much smaller than LAFTA—with a population of about 12 million as compared to 180 million for LAFTA, and an estimated total GNP of $2.3 billion as compared with an estimated $55 billion for LAFTA. However, during the few years since its beginning it has several major accomplishments to its credit. These include the elimination of trade barriers on about half the trade of member countries, with more to be freed by 1965; the standardization of external tariffs on over 80 percent of all commodities; the beginning of a regional development bank; and machinery for resolving disputes arising among members of the new union.

General treaty is the backbone

The General Treaty of Economic Integration, the major treaty of the CACM, was signed by four member countries in Managua, Nicaragua, in 1960. It was then ratified and became operative for El Salvador, Guatemala, and Nicaragua in June of 1961, and for Honduras in August of 1962. Costa Rica signed the general treaty in July of 1962 but has not yet ratified it.

Because of the importance of the general treaty, its major provisions are reviewed below.

A Common Market: The five countries agree to establish a Common Market within 5 years of ratification of the treaty. Until then certain commodities listed in a special annex, are exempted from immediate free trade. Most of the listed products are those of companies that would be harmed by elimination of duties. However, tariffs on this list may be negotiated every year; and with few exceptions, all products will be freely traded by 1966. Products not contained in the special annex were made free of all duties and other restrictions on trade among the member countries.

National treatment: Goods originating in any member state enjoy the same treatment in other member states as the national products of that other member. Certain exceptions are permissible for reasons of health, safety, or enforcement of law and order.

Investments: The industrial development laws and other legislation of the member states related to investments and business activities are to be made as uniform as possible—particularly with respect to special investment incentives.

Financing economic integration: The general treaty provides for the establishment of a Central American bank to finance and promote the economic development of the area. Accordingly, the Central American Bank for Economic Integration was inaugurated on May 30, 1961, at Tegucigalpa, Honduras. A few months later, a Central American clearinghouse was established under the general direction of the CABEI.

Administration of the program:

1. The Central American Economic Council is responsible for the direction and control of economic integration policies. Its membership consists of the ministers of economy of the member governments.

2. The Executive Council applies and administers the general treaty and takes the necessary steps required to achieve economic union. Its membership consists of one principal delegate and an alternate for each of the member countries.

3. The permanent secretariat has juridical responsibility to serve both the Economic Council and the Executive Council. It is directed by a Secretary General, appointed for a 3-year term by the Economic Council.

Arbitration procedures: Differences among the member states in matters of interpretation of the treaty are to be settled by the Economic Council or the Executive Council. All disputes not resolved by these organs will be settled by arbitration.

While the general treaty is the main instrument of the CACA, some provisions of previous agreements continue to be in effect. The general treaty states that any previous agreement between member countries, not contradicted by the general treaty, remains in effect.

CACA faces obstacles

The two major obstacles facing economic integration and industrialization are (1) the existing inequalities in the development levels of the countries, and (2) the dependence on primary commodities for the bulk of their export earnings.

During the 1950's three commodities provided about 80 percent of total export earnings of the area as a whole. These commodities are: coffee (El Salvador, Guatemala, Costa Rica, Nicaragua, and Honduras); cotton (El Salvador, Guatemala, Honduras, and Nicaragua); and bananas (Costa Rica, Guatemala, and Honduras. In recent years, world oversupplies of these goods have tended to depress the value of exports. Thus in each of the member countries, efforts are being made to diversify the farm sector of the economy. Some success has been achieved and several countries are now experimenting with new farm exports: tobacco and cucumbers in Honduras, cattle and frozen meat in Nicaragua, and kenaf in Guatemala.

Inequalities of income poses a difficult problem. There is real concern lest existing inequalities should be augmented rather than diminished. The argument is that labor and capital might tend to migrate to the more industrialized areas, making them even more efficient, raising their incomes even more relative to those in the currently less developed areas. The higher incomes in the rapidly growing centers would mean better markets, providing an additional stimulus to their economic growth, but increasing the disparity between the advanced and the less advanced areas.

Fears of this kind—which may well be exaggerated—have tended to retard the program of the so-called integrated industries. But, at the recent meeting of the economics ministers of the member nations in January of this year, regulations were adopted that clarify the meaning and application of this program. Moreover, two companies were given the coveted designation of "integrated industry."

To qualify as an integrated industry the minimum volume of production that can be achieved at reasonable cost must be greater than the needs of any single member country's market. The company receiving the designation must make certain guarantees as to quality, price, and delivery. In return for such guarantees, an "integrated industry" company is granted a 10-year exemption from import duties on raw materials, a waiver of production taxes, and tariff protection

from third countries. The two companies so far designated as "integrated" include a company to produce caustic soda and chlorinated insecticides in Nicaragua, and a company producing tires and tubes in Guatemala.

Development of economic infrastructure

The economic development of the area will depend to a large degree on construction of basic service and communications networks to bind the area into one single economic unit. In the past, the absence of such integrated services has been far more important in keeping these economies apart than have tariff barriers.

In order to cope with this problem a number of studies are underway with the assistance of the United Nation's Special Fund and the U.N.'s Technical Assistance Board. Plans are being made for a Central American road network; and for a coordinated electric power grid for Central America and Panama.

Another major study nearing completion is a draft project for a Central American telecommunications network. The five countries now have independent telecommunication systems with little connection between them. Not only are some of the systems different technically, most of them are in need of modernization and expansion. The U.N. Special Fund has allocated $770,000 toward the cost of the study, and these funds are administered and disbursed by the World Bank, which acts as executing agency.

The study will include recommendations for each country of the scope, character, estimated cost, and phasing of a telecommunications development program for the internal needs of that country for the next 5 years. Supplementing the study, 18 fellowships will be established to train men in the technical and managerial aspects of the telecommunications industry.

A major problem of full economic integration is that of monetary unification. Recognizing this, a group within the Central American Clearing House is studying the eventual formation of a monetary union among the five member nations. Although no definite time schedule is now being considered, the Clearing House has already adopted the Central American peso—at par with the U.S. dollar—as its basic unit of account.

The beginning

While the framework for the Central American Common Market has been largely put in place, much remains to be done in order to fill it out and thus achieve a fully integrated, operating market in the area. As yet, the general treaty has been in effect to short a time to have had much direct impact. But it has called attention to the areawide market potential. This has not only caused an increase in regional trade, but has aroused the interest of a growing number of foreign companies, many of which are now investing, or planning to invest, on a scale to supply the entire market.

An important weakness of the Central American Common Market—its small amount of mutual trade—is also an important source of strength. Little intraregional trade has meant that few interests strongly oppose economic union. Therefore it has been possible to move ahead very rapidly in reducing potential as well as actual trade barriers, and promote the transportation and communications facilities needed to support a substantial amount of economic integration in the future.

With this start, and assuming that the five nations continue to work in the cooperative spirit that has animated their efforts up to now, the region may well be on the threshold of a new era of rapid economic advance.

IV. U.S. INVESTMENTS IN LATIN AMERICA

Although substantial U.S. investments were made in Latin America during the earlier part of this century, the biggest growth has taken place since World War II. From less than $3 billion at the end of 1945, U.S. direct investments have risen to nearly $9 billion by 1961—representing about a quarter of the U.S. total, worldwide. Looked at as an annual flow rather than a total amount, over the past 10 years these direct investments have contributed 5 to 10 percent of the area's total net capital formation. Moreover, it seems likely that the contribution to the economic growth in the area is more significant than even these figures suggest:

Over a third of Latin America's industrial and mining production comes from U.S. companies in the area.

A third of all Latin American exports originate with these companies.

About a fifth of all Latin American taxes—and a third of the income taxes—are paid by U.S. companies.

Beyond the dollar figures, is the transfer of skills and technical knowledge that accompanies U.S. capital, and the catalytic effect such investments have on the industrial growth of domestic industries in many areas.

Before trying to fully assess the value to Latin America of this capital flow, it may be well to point out three of its characteristics that have important implications both to investors and to host nations:

Although growth of U.S. direct investments to Latin America has been rapid it has slowed relative to other areas—especially since 1958. Thus the area's share of total U.S. oversea investments has fallen—from 38 percent in 1950 to about 23 percent in 1962. There are several reasons for this, but they all boil down to the fact that the security and profitability of investments has been generally higher elsewhere than in Latin America. In some cases this can be traced to the relatively slow expansion of markets for primary commodities. This would include petroleum in recent years, and most nonferrous metals. In other cases the public attitude toward foreign investments has become increasingly cool, leading to uncertainty about the long-run security of the companies involved. In still other cases the relatively slow expansion of domestic markets for manufactured goods has reduced incentives to produce these goods locally.

There have been very important exceptions to these general observations—countries in which markets have expanded, and the investment climate has greatly improved. Yet such cases have not been sufficiently important to fully offset the conditions leading to a slower rate of expansion in other areas.

A second characteristic of U.S. investments is that although they have been made in all Latin American countries, they are unevenly distributed. More than half of such investments in dollar value, are located in Venezuela (30 percent), Brazil (12 percent), and Mexico (10 percent). Next, in order, are Chile (9 percent), Argentina (6 percent), Peru (5 percent), and Colombia (5 percent).

A third feature of the U.S. investment picture is the growing importance of manufacturing. Before World War II most foreign capital in Latin America—from the United States and elsewhere—was devoted either to the extraction of some mineral or agricultural commodity for the export market, or to a basic public service, such as railroads and electric power supply.

Thus, in 1940, mining, petroleum, and public utilities together accounted for almost 75 percent of the book value of U.S. investments in Latin America; public utilities alone accounted for 36 percent. At the same time manufacturing's share of the total was only 8 percent. But by 1962 with public utilities' share down to 9 percent, manufacturing investment had climbed to almost 22 percent of book value.

The outlook for investments

Against this background of declining amounts of new U.S. investments in Latin America, it is pertinent to ask how will the markets affect future investments.

First of all, the decline in foreign investments has been largely due to the economic disorganization and lack of business confidence stemming from political uncertainties. And there has been ample evidence of small but vocal groups in Latin America who do not recognize, or do not care to recognize, the importance of private capital, and who would destroy the conditions it requires to be effective.

And, about the same time as the Cuban Revolution, several of the larger republics experienced the political overthrow of a dictatorial regime. In some cases this was followed by great uncertainties about the economic future, and about the stability of the institutions and laws in which private enterprise must have confidence in order to expand. These political changes heightened the uncertainties about the political evolution of some of the key Latin American countries. This led, in many cases, to flight of local capital and to retrenchment by foreign business enterprises. This resulted in a lower rate of overall investment in all but a few countries—such as Peru and Colombia.

A reversal of these trends—that is, increasing political stability and confidence—as well as the expectation of reasonable profits, would likely lead to greater U.S. investments in Latin America. And of course, if the regional integration movements are successful, this will be accentuated.

IMPACT ON U.S. INVESTMENTS

The formation of the regional markets has already, in a small way, changed the pattern of U.S. investments and trade in the area. For example, imposition a heavy prior deposits in such countries as Brazil and Chile—with no such requirements on imports from other LAFTA members—has forced some buyers to look for new suppliers within the area.

On the side of investments a number of companies have already modified their investment plans to fit the new conditions in LAFTA and CACM. A large sewing machine manufacturer has begun treating the area as a whole. It has full manufacturing facilities in Brazil, Argentina, and Mexico, and assembly plants in Colombia and Peru. The Brazilian plant supplies Chile,
sembly plants in Colombia and Peru. The Brazilian plant supplies Chile,
Uruguay, and Paraguay with finished products and components, it also sells components to Colombia and other countries where they may be needed.

Another large manufacturer of business machinery has also begun to take advantage of the potential of LAFTA. This firm helped devise the first complementarity agreement, by which various components are produced in different countries, and is now setting up operations in Argentina, Brazil, Chile, and Mexico.

Thus, the creation of LAFTA is forcing firms to think in LAFTA-wide terms regarding new investment decisions, and causing firms to consider altering the marketing operations of existing subsidiaries.

While the number of firms that have begun to change their planning marketing or purchasing patterns is still small, indications are that the list is growing.

Where to locate in LAFTA

The emergence of LAFTA has raised the basic question of where foreign firms should locate their facilities inside the market. This problem is complicated by the fact that widely different conditions prevail in almost every member country. And so far, there has been little talk of harmonizing the investment laws, taxes, and similar factors. This situation is quite different in the CACM where steps have been taken to unify within 7 years the incentives to be granted to industries which effectively contribute to the economic development of Central America.

Factors in selecting a manufacturing site

Apart from the general investment climate, the most important factor in locating a plant is nearness to the buyers and the suppliers. LAFTA has two large and growing demand areas: the Buenos Aires-Montevideo-São Paulo-Rio de Janeiro complex, and the Mexico-Colombia arc. While many firms will locate in the more outlying regions—if transportation facilities are good enough—these two regions seem to have the market and supplier advantage. Both provide a relatively substantial internal market. Selling the rest of the LAFTA market would not be a requirement to get a plant going, although such sales might be maximized early for competitive reasons.

Labor cost factors are another broad area where there is comparatively wide diversity. While this will tend to diminish as the market moves toward unity, there will always be some regions where such costs are lower, or where skilled labor is much more available.

In any case, the choice of an investment site is a case-by-case decision for each firm. The only thing that is certain is that Latin America needs a huge inflow of productive and profitable investment, and that the development of an integrated market will make it more practical for foreign firms to produce within the market, providing conditions are otherwise satisfactory.

Investment in the CACM

To encourage investment the CACM has taken many steps of which the largest is the concept of integrated industries, of which the conditions and privileges were mentioned above.

In addition, the member countries have established uniform tax incentives, and they have introduced a system to encourage new investments by giving many of the benefits of integration status.

The progress of the CACM is, of course, much further advanced than its much larger neighbor, LAFTA. Furthermore, it is compact, without great distances between members. Still, the response of foreign investors has been very favorable and there have been a number of new investments made in all of the countries since its inception.

The outlook for investments

It is clear that the two regional markets will increasingly alter the pattern of U.S. investment and trade in the area. It is difficult at this point to say how fast or to tell what the new patterns will be. But the markets are now beginning to function in a more integrated fashion. Given a higher degree of political stability than now exists—it would be reasonable to expect that the total amount of new U.S. investment in Latin America will be increased by this development.

Conclusion

We believe that the growth of regional trading areas in Latin America can be a healthy and forward-looking development. The individual countries' markets are to small, as a general rule, to attract the large-scale investments that can promote the area's economy. We therefore strongly endorse the idea of LAFTA and of CACM as a goal worth a great deal of effort on the part of the nations involved, and we believe, worth the general support of the U.S. Government.

However, we feel that this laudable purpose can be undermined if the regional groupings are used as a mechanism to throw up high protective barriers around the trading blocks, and to promote uneconomic industries both through these protective devices and through other measures that prevent the free movement of resources within the area and thus prevent the most efficient use of those resources. In short, the regional groupings in Latin America have great potential for good, and we support them. But we feel that it is of utmost importance that this potential not be frustrated by excessive use of trade barriers against world competition.

Mr. GRIMES. The two regional markets—the Latin American Free Trade Association and the Central American Common Market—have already brought several changes in trading and investment patterns to the area. But, the markets are both relatively new and differ markedly from each other in several important respects.

Furthermore, although inspired by the highly successful European Common Market, LAFTA and the Central American Common Market are quite different in nature and in purpose from their older European cousin. The EEC is composed of highly industrialized, economically mature nations with a tradition of economic interdependence; and the underlying goal of the EEC is political in nature. On the other hand, the Latin American markets consist of low income, essentially agricultural economies in which intraregional trade is only a small percent of the total; and the primary goal of unification is economic in nature. And Latin American living standards are far below those which a growing segment of the population is coming to regard as minimal; thus, the need to show more rapid progress toward meeting the people's aspirations is urgent.

The Latin American Free Trade Association agreement, established by the Treaty of Montevideo, provides for the gradual elimination of tariffs and other trade restrictions over a 12-year period, and requires that members take two steps toward eliminating trade barriers. First, each country must negotiate an annual "national schedule" setting forth the tariff cuts it will grant other members. Reductions given to any one member also applies to all others.

Second, each country must agree to a "common schedule." Once a product goes on this list it cannot be removed. Also, a definite timetable is set up for the common schedule's growth. It is slated to cover 25 percent of all intraregional trade at the end of the first 3 years, 50 percent after 6 years, 75 percent after 9 years, and substantially all regional trade at the end of 12 years.

But, like the EEC, the treatment of agricultural products presented a special problem. And LAFTA's answer has been to exempt agriculture from the agreement. Except to cover deficits at national price levels, members need not buy the farm products of other members.

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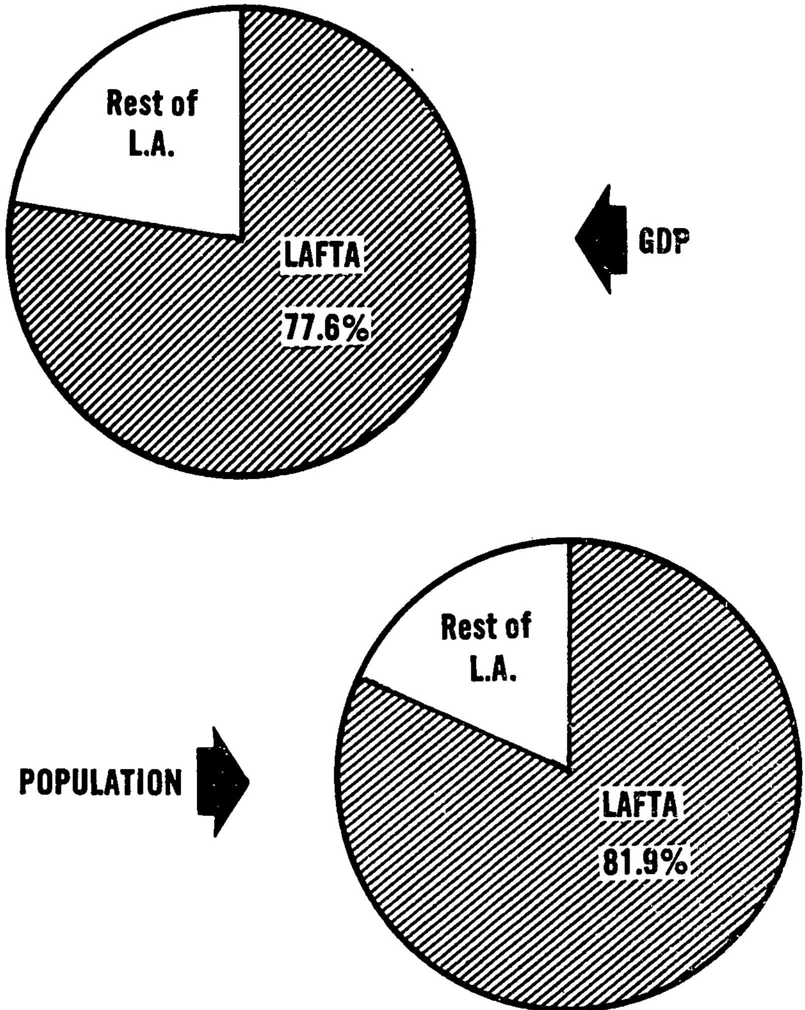
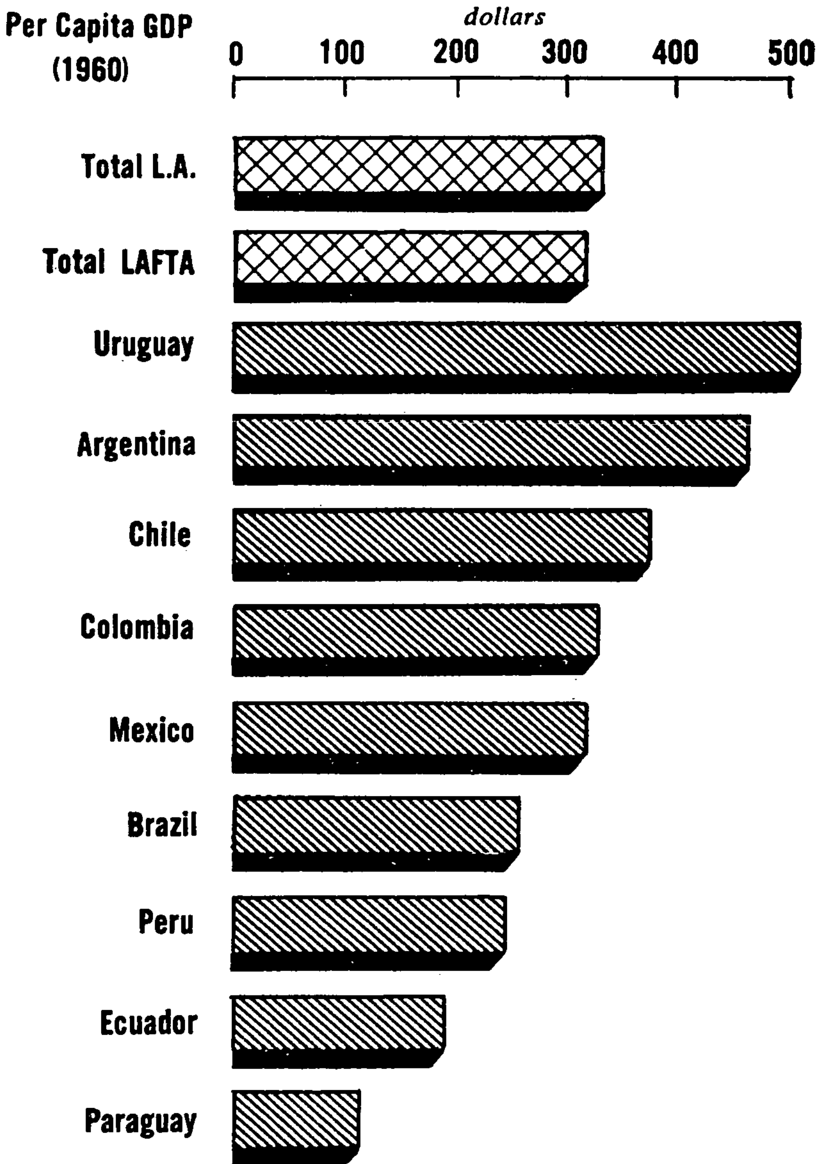
LAFTA REPRESENTS A VERY HIGH PERCENTAGE OF BOTH THE TOTAL INCOME AND THE TOTAL POPULATION OF LATIN AMERICA



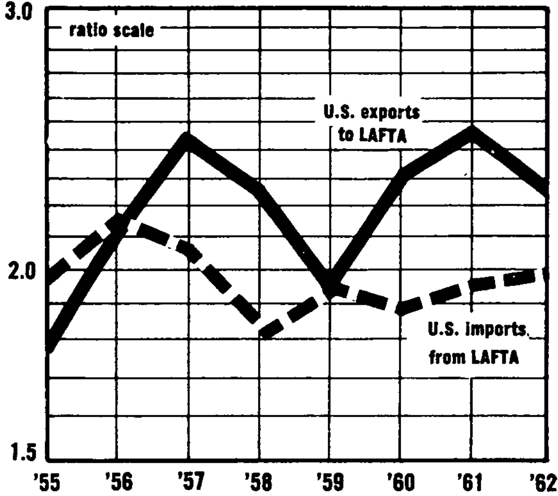
Source: The Chase Manhattan Bank
United Nations

TOTAL LAFTA PER CAPITA GDP IS SLIGHTLY LESS THAN FOR ALL LATIN AMERICA

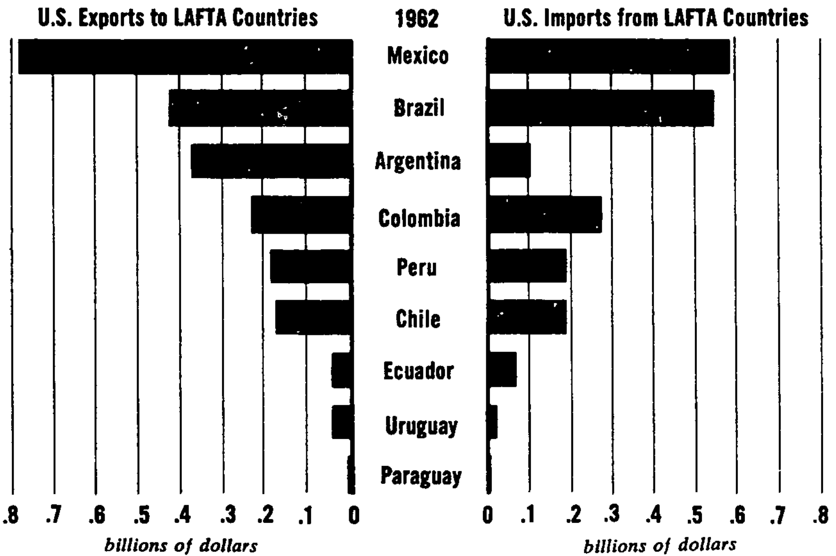


Source: The Chase Manhattan Bank

WHILE LAFTA IS A LARGE MARKET FOR U.S. EXPORTERS . . .

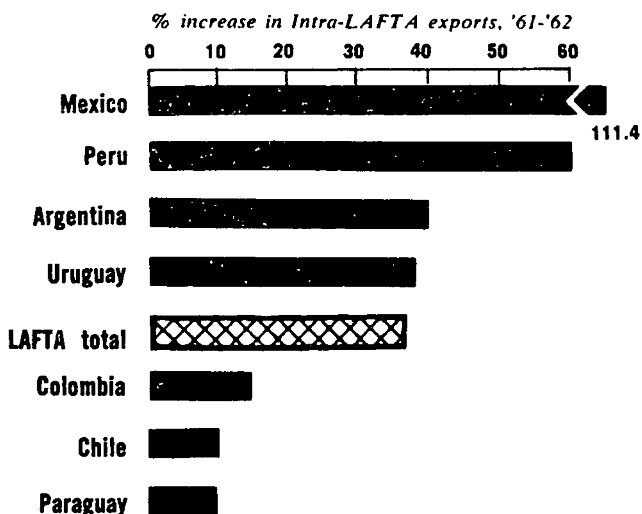


3 OR 4 COUNTRIES ACCOUNT FOR THE BULK OF THE TRADE

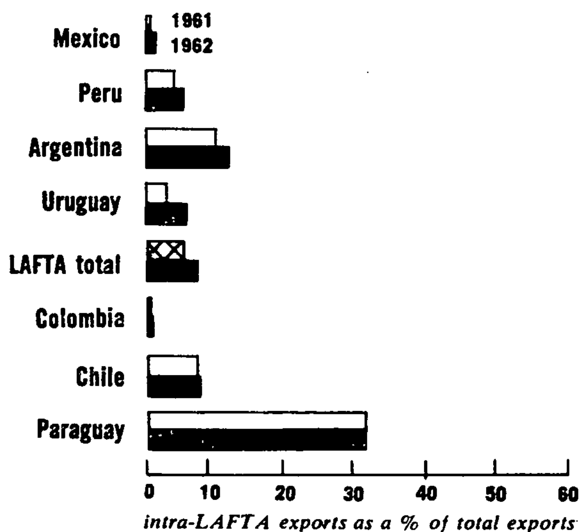


Source: U. S. Department of Commerce

ALTHOUGH INTRA-LAFTA TRADE INCREASED SHARPLY LAST YEAR . . .

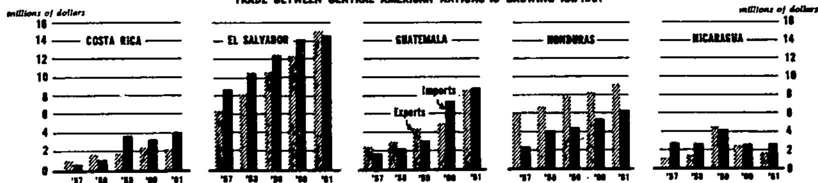


WITH THE EXCEPTION OF PARAGUAY, INTRA-TRADE IS STILL A SMALL PART OF THE TOTAL

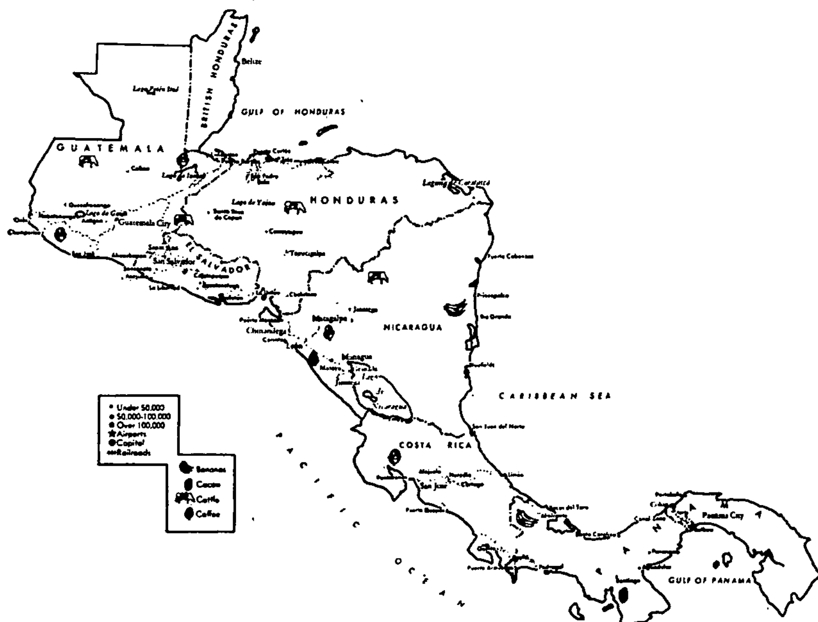


Note: Figures for Brazil and Ecuador unavailable

Source: Latin American Free Trade Association



Source: U. S. Department of Commerce

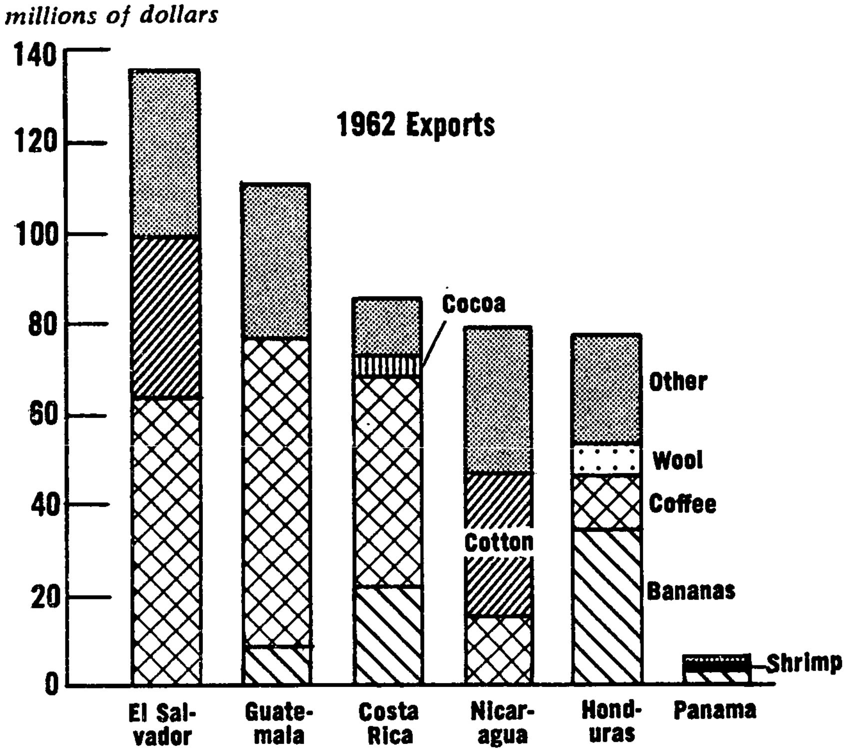


ECONOMIC MEASURES OF CENTRAL AMERICA

	Annual Rate of Population Increase	Population (thousands)	Area Sq. Miles	Persons Per Sq. Mile	1962 Estimates of GNP $ Million	1962 Per Capita GNP
Costa Rica	3.8	1,275	23,421	54	437	333
El Salvador	2.1	2,810	8,257	340	530	185
Guatemala	3.0	4,017	42,042	95	678	180
Honduras	2.5	1,950	44,482	44	335*	200*
Panama	2.8	1,139	28,576	25	500	445
Nicaragua	2.9	1,800	57,145	28	310	190

* 1960

Source: U. S. Department of Commerce, International Monetary Fund, The Chase Manhattan Bank



Source: International Monetary Fund

No decision has yet been made as to LAFTA's treatment of new products—that is, items not traded within the region at the time the treaty was signed. This subject is presently under discussion, the Mexicans having suggested the immediate elimination of all internal LAFTA tariffs on products newly produced in LAFTA. If implemented, we believe that this would represent a major step toward the integration of the area both industrially and commercially, and might spark an immediate scramble on the part of foreign investors to establish plants in LAFTA in order to take advantage of these potential markets.

Although LAFTA has been subject to some justifiable criticism for its many shortcomings, the criticisms should not be allowed to obscure two vitally important points:

(1) The treaty was apparently the best that could be worked out under admittedly difficult circumstances.

(2) The broad spirit of the treaty may ultimately overcome its excessively narrow letter.

What is more, there have already been, in spite of the shortcomings, some decided changes in trading patterns. During the first year, exports inside LAFTA rose a resounding 37 percent with every member showing an increase. True, the gain came from a very low base since intra-LAFTA trade accounts for less than 10 percent of the area's total. Still in all, the showing should not be equated to a zero—or anywhere near it.

But there are many problems ahead for LAFTA.

Among them are transportation and finance. The LAFTA Transportation Commission is preparing proposals that will promote the complementary development of the transportation industry, but it seems unlikely that the difficulties here can be overcome in the near future.

On the financial side, the Inter-American Development Bank has already offered a $30 million capital goods export financing system for intra-Latin American trade. This will make a significant contribution to the medium-term financing problems inherent in developing regional markets. We, at the Chase Manhattan Bank, through our correspondent banks and affiliated institutions in the area, offer short-term credit facilities which have significantly aided the financing of intra-LAFTA trade.

Also, a matter of major concern in the evolution of LAFTA is the attitude it will take toward the rest of the world. If it moves toward high permanent external values and discriminating trade arrangements against the European Common Market, the United States, or others, Latin America's long-term growth prospects will be sorely damaged.

But perhaps the hardest problem facing the region in the near future is simply that its major imports cannot be supplied from within the Montevideo countries. Not even the most efficient treaty conceivable can change this fact so it would be highly unrealistic to suppose that LAFTA can be transformed into another European Common Market overnight. Too much in the way of capital, skill, communications, and tradition are lacking for that.

Yet, if the enthusiasm that has sparked the progress made to date continues, and, if the climate for private capital is favorable, LAFTA

could become an increasingly attractive location for investment. This is particularly true of manufacturing industries where large markets are needed. Perhaps an attitude similar to the one that led to the surge of U.S. investments in the European Common Market could develop.

Although the Central American Common Market is much smaller both in area and in population than LAFTA, during the few years since its beginning it has several accomplishments to its credit. These include the elimination of trade barriers on about half the trade of member countries with more to be freed by 1965; the standardization of external tariff on over 80 percent of all commodities; the beginning of a regional development bank; and machinery for resolving disputes arising among members of the new union.

The backbone of the Central American Common Market is the General Treaty of Economic Integration which was initially signed by four of the five Central American countries in 1960 and now adopted by all five.

Under the General Treaty, the five signatory countries agreed to establish a common market within 5 years of ratification of the treaty. Until then, certain commodities listed in a special annex are exempted from immediate free trade. Most of the listed products are those of companies that would be harmed by elimination of duties. Products not contained in the special annex were made free of all duties and other restrictions on trade among the member countries.

Under the agreement, goods originating in any member state enjoy the same treatment in other member states as the national products of the other members. Industrial development laws and other legislation of member states related to investments and business activities are to be made as uniform as possible.

While much has been accomplished in the area, there are two major problems facing economic integration and industrialization of the Central American Common Market.

(1) The dependence on primary commodities such as cotton, coffee, and bananas for the bulk of their export earnings. During the 1950's these commodities provided over 80 percent of the areas' export earnings, but recent world oversupplies have tended to depress the export earnings of the area.

(2) The existing inequalities in the development levels of the countries have given rise to a concern that these inequalities may be augmented rather than diminished. The argument is that labor and capital might tend to migrate to the more industrialized areas making them even more efficient, raising their income even more relative to those in the currently less developed areas.

Fears of this kind have tended to retard the program of the so-called integrated industries. To qualify as an integrated industry the minimum volume of production that can be achieved at reasonable cost must be greater than the needs of any single member country's market. The company receiving the designation must make certain guarantees as to quality, price, and delivery in return for such guarantees and an "integrated industries" company is granted a 10-year exemption from import duties on raw materials, a waiver of production taxes, and tariff protection from third countries.

While the framework from the Central American Common Market has been largely put in place, much remains to be done in order to fill it out and thus achieve a fully integrated operating market in the area. But the general treaty has called attention to the areawide market potential. This has not only caused an increase in regional trade but has aroused the interest of a growing number of foreign companies many of which are now investing, or planning to invest, on a scale to supply the entire market.

With this start, and assuming that the five nations continue to work in the cooperative spirit that has animated the efforts up to now, the region may well be on the threshold of a new era of rapid economic advance.

U.S. investment in Latin America: The development of LAFTA and the Central American Common Market comes at a time when U.S. investment in Latin America has been on the decline. While the total investment figure rose from $3 billion in 1945 to $9 billion in 1961, the rate of growth relative to other areas has slowed—especially since 1958. Thus the area's share of total U.S. oversea investment has fallen—from 38 percent in 1950 to about 23 percent in 1962. There are several reasons for this, but they all boil down to the fact that the security and profitability of investments has been generally higher elsewhere than in Latin America. In some cases this can be traced to the relatively slow expansion of markets for primary commodities. This would include petroleum in recent years and most nonferrous metals. In other cases the public attitude toward foreign investment has become increasingly cool leading to uncertainty about the long-run security of the companies involved. In still other cases the relatively slow expansion of domestic markets for manufactured goods has reduced incentives to produce these goods locally. Finally, on the heels of political upheaval in the area, there have been great uncertainties about the economic future and about the stability of the institutions and laws in which private enterprise must have confidence in order to expand. These political changes led in many cases to a flight of local capital and to retrenchment by foreign business enterprises.

It is clear that the two regional markets will increasingly alter the pattern of U.S. investment and trade in the area. It is difficult at this point to say how fast or tell what the new patterns will be. But the markets are now functioning and given a higher degree of political stability, especially in some of the LAFTA countries, it would be reasonable to expect that the total amount of new U.S. investments in Latin America will increase also.

Conclusions: It is obvious that new dimensions have been added to the traditional trade and investment picture of Latin America with the advent of LAFTA and the Central American Common Market. Progress to date, while limited by most yardsticks, has been significant in view of the short time since their organization and considering the lack of background and tradition of intraregional trade. It is equally obvious that the U.S. business community in the future must take into account the existence of these two regional markets in making their decisions concerning their activities in the area.

The creation of LAFTA and Central American Common Market represent a new approach to the problem of achieving a rate of growth adequate to meet the rising aspirations of the Latin American people.

However, a number of factors could tend to slow the progress toward full realization of the potential of these regional markets. Attitudes toward investments, political instability, the lack of sound economic policies are but a few of these. But an integrated market might well help deal with these problems since it will become increasingly clear that in order to participate fully in these programs, each nation must get its own house in order.

If these market areas move toward increasingly high protective trade barriers against outside competition, their long-range growth potential will be sorely damaged. However, if they push toward eventually lowering these trade barriers and expanding multilateral trade, they can promote economic growth among themselves, and in the entire free world.

For these reasons, we believe that a positive attitude toward LAFTA and the Central American Common Market by both U.S. business and Government is warranted. Our willingness to cooperate with our Latin neighbors in their mutual attempt to combat their serious common problems should be demonstrated at every opportunity.

Thank you, Mr. Chairman.

Senator SPARKMAN. Thank you, Mr. Grimes.

Now, Mr. Lea, may we have your presentation?

STATEMENT OF SPERRY LEA, ASSOCIATE DIRECTOR OF RESEARCH, CANADIAN-AMERICAN COMMITTEE, NATIONAL PLANNING ASSOCIATION

Mr. LEA. I am very happy to respond to the invitation of this committee to summarize some of the work of the Canadian-American committee on a possible free trade arrangement between Canada and the United States. The following remarks are based on this study which our committee sponsored but they represent my own views and are not necessarily those of the Canadian-American committee as a whole, or of its 60-odd individual members on both sides of the border.

You have just heard about the two free trade arrangements which are being set up in Latin America, and in a few minutes Mr. Clayton will talk about hemispheric free trade. Between these two concepts there is one question left hanging, and that is what is Canada going to do? After all, Canada is in the hemisphere, and so it is useful to think a bit about what Canada and the United States might do together.

The possibility of some kind of a free trade arrangement has been the subject of numerous speeches and some conferences. Just this last year there were two conferences in the Pacific Northwest area, one in the United States, in Yakima, Wash., and one in Harrison Hot Springs, British Columbia, on the possibilities of Canada-United States free trade arrangements. Later in 1964 there will be some other conferences on this subject.

This Canadian-American interest in regional free trade I think, comes from several factors. First of all, everybody else seems to be doing it. Australia and New Zealand are now thinking of forming a free trade area. As we know, Latin America is following the regional path to free trade. The African countries are planning something. Europe, of course, has led the way with the EEC and EFTA.

Actually if you think of the developed countries in the world, only Canada, the United States, and Japan are now not actively engaged in creating or contemplating some kind of a free trade arrangement.

So a lot of people say, if everybody else is doing it, we should at least be thinking about it.

There is also a historical basis. Canada and the United States a century ago did have free trade and as late as 1948 had some official discussions, shrouded in secrecy, about setting up some kind of a free trade area. Those discussions broke down, however.

Also, quite apart from any historical events, Canada and the United States are remarkably integrated. We have very similar markets. We have a similar standard of living. We have a common language. We have practically a common market for capital, although the recent Canadian budget and our own interest equalization tax may move away from that slightly, and we have, of course, virtually free movement of people. So, in effect, we have almost a "common market" without the free trade aspects at its core.

But it should be also noted that there is an understandable reluctance on the part of Canadians to embark on a policy which might blur even further the cherished distinctions between their country and ours, or which would appear to further reduce their ability to make independent decisions on economic policy. And there is also some deep Canadian concern over what would happen if they did have free trade with the United States. There are tremendous opportunities and tremendous threats, and some Canadians are right now trying to balance the opportunities against the threats and see whether by and large free trade with us would be good for them or not.

And for ourselves, the United States might be reluctant to establish a special relationship with a single country which might prejudice or limit our vast network of worldwide responsibilities. Certainly before we would engage in any free trade arrangement with Canada, I think we would look very seriously at the effect on the imports of certain Latin American goods which Canada also produces, like petroleum, lead, and zinc.

So with the pulling for and against a bilateral free trade scheme, it is natural that the discussion is mostly on the questions, "Is is desirable?" "Do we want it?" Another question raised is, "What would it mean?" But the Canadian-American Committee felt that this discussion was a bit sterile because the basic question had never been asked, and that is, "Just what are we talking about?" What would this be likely to look like? And we felt that we should start by trying to identify what such a scheme would look like, and then we can figure out what the implications might be.

So our work thus far in the Canadian-American Committee is strictly limited to trying to answer the question, "What are we talking about?" and the Committee has taken no stand at all on the desirability or feasibility of such a scheme.

Before we look at the possible characteristics of a Canada-United States bilateral free trade arrangement, let us make a clear distinction between this and the multilateral approach to free trade which both of our countries have traditionally followed and which we are preparing to apply in this forthcoming "Kennedy round."

The essence of the multilateral approach is respect for the most-favored-national principle, MFN principle. According to this, any

reduction in trade barriers must be extended to all other countries which are members of the GATT or with which Canada and the United States have trade agreements containing the MFN clause.

In contrast, the bilateral arrangement we are talking about leads to a discriminatory arrangement. The abolition of trade barriers between Canada and the United States would not be automatically extended to other countries. The GATT permits such a violation of the MFN principle only when the relationship follows certain very precise standards which prevent it from becoming an inward-looking trade bloc. Just to summarize these standards, all of which are found in article 24 of GATT, the arrangement must be a free trade area or a customs union providing for complete and not partial elimination of trade restrictions. In other words, it can't set up something like the Commonwealth preference system. And the commodity coverage must account for substantially all the trade of the countries involved. And there shall be no increase in the restrictiveness of trade barriers against nonmember countries, and where it develops from an interim arrangement it must be fully formed within a reasonable period of time. It can't procrastinate.

These requirements account for very basic differences between the GATT approach to a bilateral free trade arrangement and the multilateral approach of the "Kennedy round." While the multilateral approach cannot be expected in most cases to do more than reduce trade barriers bit by bit over an indefinite period, a Canada-United States bilateral arrangement under GATT rules would require the two countires to abolish, perhaps gradually but nonetheless deliberately, all the restrictions affecting substantially all their mutual trade, an act with obviously far-reaching consequences.

Now, when we look at all the possible characteristics that a Canada-United States free trade arrangement might have, we are confronted by a problem because there are so many choices. In attempting to simplify our selection task, let us follow the practice of the smorgasbord chef who eases his guests' dilemma by grouping together the various options of meats, fish, salads, and so forth. All the meats are on one part of the table, all the fish on another part, and all the salads on another. The full number of dishes remains, but at least we make choices in logical sequence among various types of meats and various kinds of fish, and so forth. Our smorgasbord table greets the potential founding fathers of a Canada-United States free trade arrangement with six such decision areas, each one of which contains several options.

GEOGRAPHIC SCOPE

The first question is geographic scope. What is the dramatis personae of such an arrangement? This breaks down into two questions. One is whether the territories or countries related to either Canada or the United States would be included. For the United States the most important one would be Puerto Rico and for Canada there are the Commonwealth countries.

The second question, and one which is very pertinent to the interests of this committee, is whether and under what conditions a Canada-United States arrangement would permit or even encourage eventual inclusion of other independent countries, and if it is chosen to be open-ended, what is the orientation of this open end? This open end might

look southward, as Mr. Clayton does, toward the Caribbean and Latin America as potential future partners; or it might look across the Atlantic to the European free trade groups with which some kind of a link could be established; or the orientation of the open end might look not to any geographical region but to developed countries or free trade arrangements anywhere, and this, of course, would include Australia, New Zealand, and eventually Japan.

Now, in talking about such far-flung arrangements as this, we are getting a little bit off our subject of just a Canada-United States bilateral arrangement. But I think they deserve to be mentioned since they would probably figure in the long-run thinking of the founding fathers of the Canada-United States free trade scheme. Indeed, it might well be that—especially in Canada—a bilateral scheme is conceivable only as a preliminary step to a free trade arrangement of considerably wider geographic scope.

COMMODITY COVERAGE

The second decision area concerns the commodity coverage of the free trade arrangement, and here there are three possible approaches. There is all-inclusive commodity coverage, as has the EEC, where everything is included and nothing left out, not even agriculture.

Or we could aim for maximum possible coverage where we would say that we would like to include everything but we recognize that certain products have special problems, economic and political, and they would have to be left out. There are several ways we could approach maximum possible coverage. We could draw up the "free list" in the beginning and identify everything which was to go free. Or we could try to approach maximum coverage by beachheads. Here we would begin with certain sectors with the understanding that they would be expanded step by step.

A third approach to free trade might be called limited free trade, where we would start with a small sector, and have no understanding that we would go any further. We might have free trade in automobiles and parts, or something like that, with Canada.

BASIC FORM

The third set of choices on our smorgasbord table relates to the basic form of the free trade arrangements, and here we have two well-defined options. We have a free trade area or we have a customs union.

Now, a free trade area such as LAFTA and EFTA provide for free trade between the members, but they are allowed to keep their own national tariffs and their own commercial policies toward the rest of the world. A customs union provides for free trade between the countries but it also requires them to adopt a common external tariff and a common commercial policy.

ECONOMIC INTEGRATION

The next decision area we get to is economic integration. This is a lot more complex because there are many actions that might be taken up here. It is generally conceded that the removal of the trade barriers among members of either a free trade area or customs union

would not necessarily create meaningful free trade. You still have major difficulties in public and private policies and practices affecting the production or distribution of goods.

For instance, Canada has a 50-cents-a-ton duty on coal, but coal coming from the Canadian Maritimes to Ontario, a big market for coal, has a transportation subsidy of, I understand, up to $6 a ton. This is 12 times the tariff. It wouldn't mean much for Canada to eliminate the 50-cents-a-ton duty if it didn't also eliminate this special subsidy to transport the coal to Ontario.

Now, there are two general approaches to economic integration. We could take the maximum approach that the EEC does and try to harmonize all sorts of ground rules and labor costs and have an approximation of laws, so that in effect we end up with a single political economy. This is the route that the EEC has taken because it is basically a political entity.

On the other hand, there is the example of the EFTA, which shuns any step toward the economic integration that isn't absolutely necessary to make the free trade meaningful.

The route that Canada and the United States would take would, of course, fit their own special conditions, such as the substantial degree of integration already existing and the fact that we both have Federal political structures.

INSTITUTIONAL ARRANGEMENT

The next decision area concerns the institutional arrangement, and by and large the institutions follow what they need to do. In other words, the choices made in the other decision areas would determine what the institutions would look like. If we had a large program for economic integration, we would have to have a large staff to formulate and implement such a program. You can just look at the difference in figures between Brussels, where there are 2,000 so-called "Eurocrats" formulating the integration policy of the EEC, and Geneva, where there are less than 100 staff members in the EFTA. The difference comes from the fact that the EEC is engaged in a great deal of economic-political integration and the EFTA is not. There would be a choice about whether or not to have a separate headquarters distinct from Washington and Ottawa, and there would be some institutional questions on how to settle disputes. When you have only two members, you can never have a majority vote, and so disputes would have to be settled by some independent body.

TIMING ARRANGEMENTS

The final decision area has to do with the timing arrangements which bring all of the provisions into force. The most important would be those governing the freeing of trade between the two countries. It is probably unrealistic to think we could go to free trade immediately. This would probably be delayed over some period known as the transitional period, and as we will see later, it may be that the transitional trade would be a little longer for Canada on account of the differences in size of Canada and the United States.

There is also some timing, in the strategic sense of timing, in bringing into effect the nontrading aspects of a Canada-United States

arrangement. Finding the strategic moment is a very important consideration for the Founding Fathers. They should bring to their momentous project not only a full comprehension of the "whats" included in the six decision areas but also a keen sense of the most appropriate "whens."

Now we have a rather large collection of options laid out on the smorgasbord table. The question comes, can we take any of these plates off? Can we narrow these choices down? To some extent we can do that by confronting the various choices with certain facts of life existing within Canada and in the United States or between them in their joint position today.

One fact of life, not present in Europe, is the tremendous difference in size between the two countries. The United States has over 10 times the population of Canada and about 15 times the gross national product. This means that both the threats and the promises of free trade loom larger to Canadian industry than the U.S. industry.

Free access to the Canadian market would generally add about 10 percent to the U.S. industry's present domestic market. In other words, if we add 18 million Canadians to our markets, it is about 6 years of our population growth. But for Canada to add 180 million Americans to its market, that would add about 1,000 percent to the present size of its market, or the amount of population growth that they would have in about 90 years.

All of this means that the Canadian industry would probably have to be very much restructured. Its present status is that it makes a very few copies of many, many items, and it would have to be changed to make many copies of fewer items. All this would require extensive changes which are very expensive. And so we feel that the fact that there is such a big difference in size would mean that Canada would have to be given a longer time to adjust to free trade than the United States.

There is also the fact that only two members are involved. We already mentioned the implication this has for the institutions, that with only two members, you cannot have a majority vote. The institutions would have to arrange some other way of settling disputes and making decisions.

Then, when you combine the fact of the great contrast in size with the fact that there are only two members, it means that when Canada looks southward it sees just one huge partner and might understandingly feel very uneasy. I think Canada would be far less anxious if it saw 3 countries with 60 million population each rather than 1 country with 180 million, and this might have an implication on the open-endedness of the scheme. I think the Canadians would feel a lot happier if there were some other countries involved besides the United Stats.

Another fact to be considered is that both countries are loyal participants in GATT and that they would follow the rules of GATT. The choice for approach to commodity coverage would have to respect the "substantially all trade" requirement. This would rule out free trade just on a limited number of commodities and probably mean that a substantial number of commodities would be covered.

The existence in both countries of fuels and industrial raw materials raises certain problems that are not important in Europe. Europe

does not have petroleum produced in large quantities within any of its countries, or lead and zinc, and so forth. These products can have very severe free trade adjustment problems, much more than industry. In some cases no amount of investment would make them competitive with production in the partner country. This suggests that a prolonged transitional period be applied in certain raw materials cases to permit a special adjustment assistance program to have a chance to operate.

A number of facts show that the free trade area form is far more realistic than a customs union. Creating a common external tariff and common commercial policy would challenge the traditional congressional role in setting U.S. trade policy. I am sure you gentlemen appreciate the difficulties that this would present. It would also force Canada to abandon its Commonwealth ties. With a free-trade area this wouldn't occur at all. The United States and Canada would be able to adopt any policy they wished toward other countries.

The Federal nature of both countries would set limits on the degree to which economic integration could take place. Neither country has shown a great interest in homogenizing its State or Provincial tax systems or wage levels or laws and practices governing natural resources or industry. It is difficult to imagine much enthusiasm for doing everything the same way in the name of a Canada-United States arrangement when Canadians and Americans are quite happy to see, for instance, that certain States have taxes and certain States do not have taxes.

The status of Puerto Rico within the U.S. customs territory, together with the fact that its people are American citizens, would probably require the inclusion of Puerto Rico along with the 50 States.

If we summarize the impact of these facts of life on our choices then, we could say the geographic scope would include Puerto Rico but would not include the Commonwealth. Initially there would be Canada and the United States, and the United States would include Puerto Rico.

On the matter of commodity coverage, the problems that we would have with certain agricultural products would rule out the all-inclusive approach. On the other hand, the GATT rules would rule out the very limited approach to free trade. I think we would end up with the maximum possible coverage approach where we try to include everything possible but recognize that there would be certain agricultural commodities that could not be included.

The basic form of the arrangement would definitely be a free-trade area and not a customs union. The approach to economic integration would probably stick to steps related to assuring the meaningfulness of free trade and would avoid the more extensive schemes which the EEC has adopted.

Institutions would be simple, reflecting the limited approach to economic integration and the choice of the free trade area form.

Finally, the timing arrangements might be such as to allow Canada a little more time to adjust than the United States.

Now, this description can be considered only a very preliminary conclusion, really just a dry run. The final narrowing of the choices for the characteristics of a Canada-United States free-trade arrangement can only come when the authentic founding fathers appear on

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the scene, for only they can supply the most important fact of life of all—the fundamental rationale and purposes of the scheme, the "why" of it. Until that day comes, a Canada-United States free-trade arrangement may well remain the subject for occasional speeches, and animated conferences, and these may set the idea of a bilateral free-trade arrangement to resonate within important circles in both countries. But what are needed are North Americans, comparable to the European men like Schuman and Adenauer and De Gasperi and Spaak. These men not merely articulated their ideas very clearly but they could deliver their own countries to a common political commitment. Such North Americans alone could change a theme for discussion and occasional eloquence into one for action.

Thank you very much.

Senator SPARKMAN. Thank you, Mr. Lea. Your formal presentation with the charts will be placed in the record at this point.

(The statement is as follows:)

STATEMENT OF SPERRY LEA, ASSOCIATE DIRECTOR OF RESEARCH, CANADIAN-AMERICAN COMMITTEE, NATIONAL PLANNING ASSOCIATION, ON POSSIBLE CHARACTERISTICS OF A CANADA-UNITED STATES FREE-TRADE ARRANGEMENT

I am happy to respond to the invitation of your committee to summarize some of the work on the subject of a possible free-trade arrangement between the United States and Canada which has been sponsored by the Canadian-American Committee of the National Planning Association (U.S.A.) and the Private Planning Association of Canada. (A brief description of the Canadian-American Committee is appended to this statement.)

While the following remarks are based on our Committee's work, most specifically a study entitled "A Canada-United States Free Trade Arrangement: Survey of Possible Characteristics,"[1] they represent my own views and do not necessarily reflect those of the Canadian-American Committee as a whole or of its 60 individual members.

You have just heard about free-trade arrangements being set up in Latin America. And in a few minutes you will be hearing about a hemispheric approach to free trade. The latter assumes not merely that the United States would work out some arrangement with its neighbors south of the border, but that it would have established some sort of free-trade partnership with Canada to the north.

The possibly of such an arrangement is currently the subject of occasional speeches and a number of conferences in both countries.

For instance, the Pacific Northwest Trade Association sponsored two conferences in 1963 on the theme of a Canada-United States free-trade area, and I understand that other groups will discuss the subject in 1964.

This current interest in North American free trade is ascribable to a number of factors. First of all, everybody else seems to be doing it. Europe led off with the Benelux Economic Union (1948), the European Coal and Steel Community (1952), the European Economic Community—the "Common Market"—(1958), and EFTA in 1960. We then saw the launching of LAFTA (1960) and CACM (1960) in Latin America, the forming of Malaysia (1963), numerous plans for African free-trade arrangements, and just now consideration of an Australia-New Zealand free-trade area. Only the United States, Canada, and Japan among the industrialized countries are not currently creating or contemplating some kind of free-trade arrangement. Then there is an historic basis for Canada-United States free trade in the reciprocity agreement of 1854–66, the stillborn agreement of 1911, and some exploratory negotiations in 1948. Quite apart from past history, Canada and the United States now constitute the world's largest trading partnership, and the two countries are in many real ways integrated economically, with very similar market conditions and standards of living. Furthermore, we exercise between us virtually free movement of persons and of capital (although the Canadian budget of 1963 and the U.S.

[1] S. Lea, "A Canada-United States Free-Trade Arrangement: Survey of Possible Characteristics," Washington, D.C., Canadian-American Committee of the National Planning Association (U.S.A.) and the Private Planning Association of Canada, November 1963.

interest equalization tax proposals curtail the latter somewhat). This means that Canada and the United States actually have several key attributes of the "Common Market" which the EEC is striving to create; we lack only some type of free-trade arrangement at its core.

A number of considerations should also be noted which quench enthusiasm on both sides of the border to create the free-trade core. On the part of Canadians there is an understandable reluctance to embark on a policy which might blur even further the cherished distinctions between their country and ours, or which would appear to further reduce their ability to make independent decisions on economic policy. Meanwhile, Canadian industry is at the same time excited about the vast opportunities presented by our large and rich market and concerned over the threats which free trade with its mass-producing neighbor to the south would bring.

As for ourselves, the feelings of both opportunity and threat from free trade with Canada are much more faint. And we have a natural reluctance to establish a special trade relationship with a single country which might prejudice or limit our vast network of worldwide responsibilities. For instance, I think we would examine closely the effects of free trade with Canada on our imports of certain Latin American products such as lead, zinc, and crude petroleum.

With many factors thus pulling for or against a bilateral free-trade scheme—especially from the Canadian viewpoint—it is natural that discussion on the subject centers on the question of desirability ("Do we want it?") or on its economic or political feasibility ("What would it mean?"). Largely unasked was the question which, we felt, must necessarily have priority over all others: What are the possible and most probable characteristics of such a free-trade arrangement? Or more simply, "What are we talking about?" Our study seeks to clarify this single question, and takes no position one way or the other on the matter of feasibility or desirability.

THE BILATERAL APPROACH

Before examining the possible characteristics of a strictly bilateral Canada-United States free-trade arrangement, let us clearly distinguish it from the multilateral approach to freer trade which both countries have traditionally followed and which they are preparing to apply in the forthcoming "Kennedy round" of tariff negotiations.

The essence of the multilateral approach is respect for the most-favored-nation (MFN) principle. In accordance with it, any reduction in trade barriers which either Canada or the United States may negotiate with each other must be extended to all other countries which are members of the General Agreement on Tariffs and Trade (GATT) or with which the two countries have trade agreements containing MFN clauses.

In contrast, the bilateral approach to free trade leads to a discriminatory arrangement. The abolition of trade barriers between Canada and the United States would not be automatically extended to other countries. The GATT permits such a violation of the MFN principle only when the relationship follows standards designed to prevent its becoming an inward-looking protectionist "trade bloc." Article 24 of the GATT stipulates that the scheme must take the form of a free-trade area or a customs union (or an interim arrangement leading to either) with these characteristics:

Complete, not partial, elimination of trade restrictions among its members;

Commodity coverage accounting for "substantially all trade" among its participants;

No increase in the restrictiveness of trade barriers against nonmember countries except where unavoidable in the case of a customs union, and then with adequate compensation offered; and

Where it develops from an interim arrangement, it must be fully formed in a "reasonable length of time."

These requirements account for basic differences between the two approaches. While the multilateral approach could not be expected in most cases to do more than reduce trade barriers bit by bit, over an indefinite period, a Canada-United States bilateral arrangement under GATT rules would require the two countries to abolish, perhaps gradually but nonetheless deliberately, all restrictions affecting substantially all of their mutual trade—an act with obviously far-reaching consequences.

THE BASIC DECISION AREAS

In attempting to settle on the optimum characteristics for a bilateral free-trade scheme, the Founding Fathers would be confronted by a great number of choices. To simplify this task of selection, let us borrow the practice of the smorgasbord chef, who eases his guest's dilemma by grouping together the various options of meats, fish, salads, etc. Our smorgasbord table greets the potential founding father of a Canadian-United States free-trade arrangement with six such decision areas, each of which contains several options.

The first decision area, *geographic scope,* raises two questions. The first is whether a Canada-United States free-trade arrangement would extend some or all of its provisions to countries or territories having special trading relationships with either of them. These would be Canada's partners in the Commonwealth preference system and, for the United States, the Commonwealth of Puerto Rico, a number of small island dependencies, and until 1974 the Philippines.

The second question of geographic scope is whether and under what conditions the Canada-United States arrangement would permit or even encourage eventual inclusion of other independent countries. If the choice is made to be "open ended," the question arises as to the orientation of the open end. This might look southward, toward the Carribbean and Latin America. Or it might look across the Atlantic to the European free trade groups with which some link might be established. Or the orientation of the open end might be to developed countries or areas wherever they might be, which would, of course, include Australia, New Zealand, and probably Japan.

In talking about such farflung arrangements we are getting away from our subject of a Canada-United States bilateral arrangement. Nevertheless, they deserve to be mentioned here since they would probably figure in the longrun thinking of the founding fathers of a Canada-United States free trade scheme. Indeed, it might well be that—especially in Canada—a bilateral scheme is conceivable only as a preliminary step to a free trade arrangement of considerably wider geographic scope.

In the second decision area, *commodity coverage,* we may distinguish several possible approaches.

The all-inclusive approach would provide that, from the outset, all commodities traded between the two countries would be placed on the "free list." No exceptions would be permitted, although commodities with special problems might be granted a longer period to reach free trade. The EEC is, of course, the prime example of the all-inclusive approach.

The maximum possible coverage approach would exempt a few commodities or sectors for which free trade would cause unusual difficulties. Two approaches to maximum possible coverage may be distinguished:

The free list might be fully defined and committed at the outset, with all exemptions identified. This was done in the EFTA, which excluded agricultural and fishery products.

A second or "beachhead" approach to maximum possible coverage would initially commit only a limited number of specified commodities to the free list with the understanding that this beachhead would be expanded step by step. Free trade might start with an individual sector—as did the European Coal and Steel Community. Another variant might be to begin with "pioneer products," those with low levels of existing tariffs or those for which free trade could be most easily and quickly established.

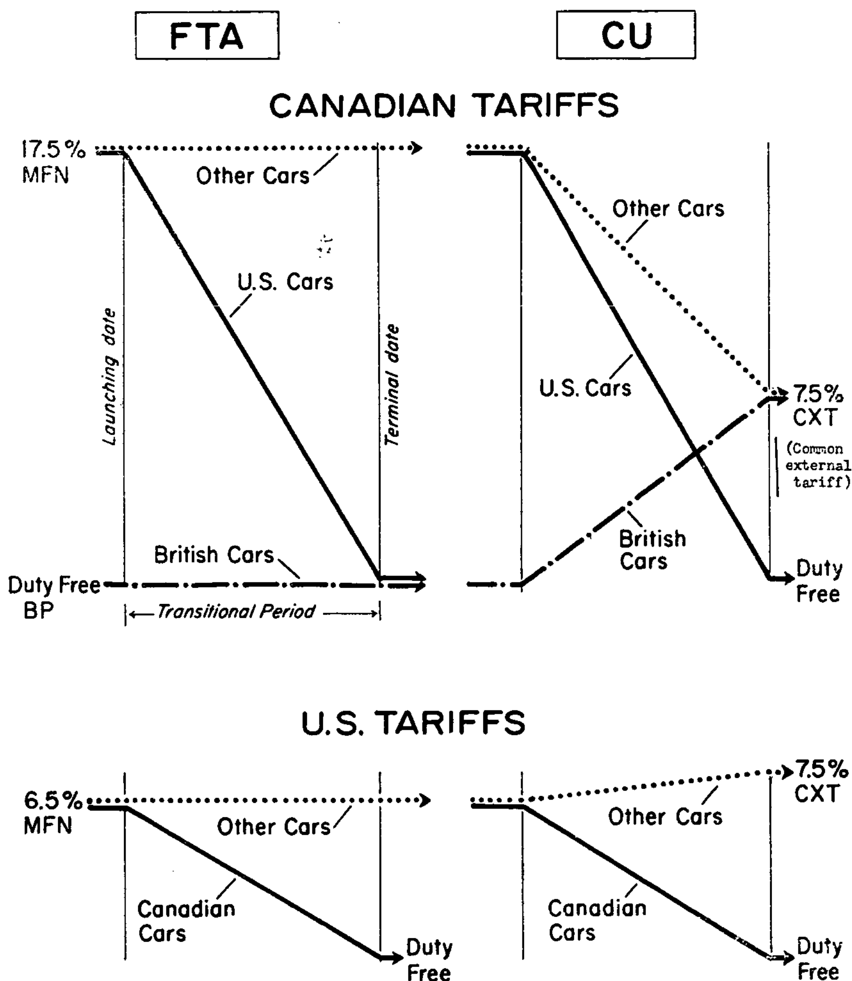
The third approach to commodity coverage, limited free trade, would put on the free list only a small number of commodities, perhaps all within a single sector. Unlike the beachhead approach, there would be no understanding to expand the commodity coverage at a later date. Limited free trade is not as realistic an option for a Canada-United States free trade arrangement as the other approaches discussed, since it clearly flouts the GATT requirement to cover "substantially all trade" and, therefore, would require a GATT waiver of a type that might be difficult to obtain.

The third set of choices relates to the *basic form* of a free trade arrangement between Canada and the United States. The options here are limited to two: the free trade area and the customs union as defined by the GATT. While both forms provide for the total abolition of trade barriers among member countries, they may be distinguished by their treatment of imports from nonmember countries. In a Canada-United States free trade area, each partner would remain free to determine its trade restrictions against the rest of the world. But in a Canada-United States customs union, both partners would adopt a common

external tariff against imports from nonmember countries and, consequently, a common trade policy and related institutional arrangements.

The comparative effects of the two forms in the case of automobiles is illustrated in the chart. The Common External Tariff (CXT) is estimated at 7.5 percent by weighting the three duty levels now in effect (the United States and Canadian MFN rates, and the Canadian British Preference (BP) rate—free entry) by the value of imports at these rates.

FIGURE 1.—*The effects of a Canada-United States Free Trade Area (FTA) and Customs Union (CU), on each country's tariffs against passenger cars, an illustrative example*



Assumptions:

The Canada-United States Common External Tariff (CU) for passenger cars is set, by weighting existing tariffs by imports, at 7.5 percent ad valorem and is developed over a transitional period identical to that governing the elimination of tariffs between the two countries.

In a Canada-United States Customs Union, the special British Preference (BP) duty applicable to British cars (free entry) will be canceled, and the CXT will apply to them.

The charts are based on present duty levels. They reflect no change in the present MFN duties of 17.5 percent for Canada and 6.5 percent for the United States, which in all likelihood would be lowered in the process of multilateral negotiations (which would also tend to lower the CXT below 7.5 percent).

Source: S. Lea, A Canada-United States Free-Trade Arrangement: Survey of Possible Characteristics. Washington, D.C., Canadian-American Committee of the National Planning Association (United States of America) and the Private Planning Association of Canada. 1963. P. 44.

The fourth decision area concerns acts of *economic integration.* The removal of trade barriers among members of either a free trade area or a customs union might not create meaningful free trade if major differences in public and private policies and practices affected unequally the costs of producing and distributing goods.

For instance, Canada's transportation subsidy for its coal from the Maritime Provinces to the Ontario market runs as high as $6 a ton. Eliminating its 50-cent-a-ton tariff on coal would not provide "free trade" unless this transport subsidy were also abolished. Meanwhile, if we are subsidizing the production of any product more than the Canadians, for instance ships, these subsidies would have to be harmonized to permit meaningful free trade. And the price of cotton would have to be equal in the two countries if free trade in textiles was to be fair.

Steps to abolish such differences involve acts of economic association more far-reaching than those implied in the terms "free trade area" or "customs union." Such steps may be considered acts of economic integration.

The options for the founding fathers on this question can best be seen as alternative approaches to economic integration. The maximum approach is illustrated by the integration program being developed by the EEC, a program which is animated by a broader movement toward political union. The principal steps include providing for the free movement of labor, services, and capital; abolishing certain Government aids and business practices which "distort" competition; approximating certain laws pertaining to business, such as taxation; developing common transportation and energy policies; harmonizing wage rates and social security benefits among countries. There are also plans for creating a monetary union. Many of these steps are still being formulated by the EEC Commission, but there is at least a formal commitment that the goal originally set for the EEC, the "progressive fusion of national economies," should be fulfilled by the end of 1966.

In contrast, owing largely to the special circumstances surrounding its creation, the EFTA has not embarked on any definite program of economic integration per se. The EFTA intends, however, to eliminate policies or practices which prove to frustrate its objective of obtaining the benefits of mutual free trade. In a few cases (e.g., drawback), the EFTA Convention provides for the termination of specific policies. But on the matter of business practices, it has adopted a "wait and see" attitude by calling attention to undesirable situations that might arise and by scheduling a review of the situation after 4 years of operation. No action has been contemplated on harmonizing taxation, transport, or wage policies, but it is understood that members will take appropriate measures when and if this proves necessary.

Other free trade arrangements have approached the question of economic integration between the extremes illustrated by the EEC and the EFTA. So, most likely, would a Canada-United States arrangement, in recognition of a number of factors unique to it, such as the substantial degree of integration already existing between the two economies, by the implications of their Federal political structures, by the disparity in their sizes, and by their traditions and the "style" of their relations with each other.

The fifth decision area concerns the *institutional arrangements.* A Canada-United States free trade arrangement would require common institutions to undertake a number of functions: concerting policies, providing technical staff services, providing adjustment assistance and insuring availability of investment capital, adjudicating complaints and appeals, and subjecting operations and the common institutions to legislative review.

The types and functions of the common institutions would be determined largely by choices made in other areas. For instance, a customs union would require a special technical group to formulate and administer common trade policy, while a free trade area would not. The approach chosen to economic integration would have an especially significant effect on the importance of the secretariat or technical staff, as illustrated by the more than 2,000 "Eurocrats" of the EEC Commission in Brussels against less than 100 in the EFTA central staff at Geneva.

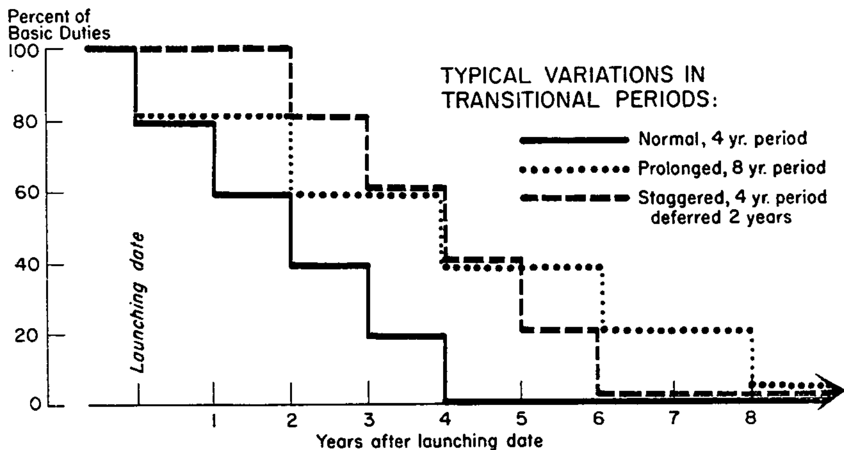
While the institutional framework would be developed largely in response to decisions made on other matters, the founding fathers of a Canada-United States arrangement would have scope for choice on two questions concerning the common institutions themselves. The first is the extent to which the various functions would be geographically centralized rather than left to the bilateral links between Washington and Ottawa. Choice must also be made as to how to

settle disputes and make common decisions, keeping in mind that with only two members majority voting is not possible.

The sixth and final decision area concerns the *timing arrangements* governing the entry into force of the various provisions. Different concepts of timing apply to trade and nontrade provisions.

Scheduling changes in trade restrictions would involve setting a timetable for eliminating trade restrictions between Canada and the United States and, only in the event of a customs union, for shifting national tariffs to the common external tariff. Probably discounting as impractical the possibility of eliminating trade restrictions between the two countries all at once, the founding fathers could choose among various forms of transitional periods, some of which are illustrated in the chart. All commodities and all member countries might move to free trade on an identical schedule; the transitional periods might be prolonged for certain commodities and/or member countries; or transitional periods could be staggered to start at different times and might or might not have the same duration. The transitional period might also be accelerated or delayed under certain specified conditions.

FIGURE 2.—*Typical variations in transitional periods*



Source: S. Lea, "A Canada-United States Free Trade Arrangement: Survey of Possible Characteristics." Washington, D.C., Canadian-American Committee of the National Planning Association (United States of America) and the Private Planning Association of Canada, 1963, p. 67.

Undertaking nontrade operations does not lend itself to precise date setting. Certain steps toward economic integration—for example, the approximation of business laws or the establishment of a common transportation policy—break new ground. We may schedule the commitment to prepare a new policy. But its gestation period is not known, and even if it were, the founding fathers might, for political reasons, wish to retain flexibility in "timing" the introduction of the new policy. There is much to be said both for and against being able to defer decisions involving crucial confrontations of existing national policies. Timing strategy in this sense is a very important consideration for the founders of any Canada-United States free trade arrangement. They should bring to their momentous project not only full comprehension of the numerous "whats" included in the six decision areas but also a keen sense of the most appropriate "whens."

CONSIDERATIONS NARROWING CHOICES

Let us now narrow down the wide range of choices by confronting the various options with certain facts of life existing within Canada, and the United States, or between them, or in their joint position in the world today.

The great difference in size between the two partners would mean that both the threats and promises of reciprocal free trade loom far larger for Canadian than for U.S. industry. Free access to the Canadian market would generally

add, in terms of population, about 10 percent (6 years of population growth) to U.S. industry's present domestic market; but for Canadian industry, free access to the U.S. market would add 1,000 percent to the size of its present domestic market (almost a century of population growth), and thus bring a totally new competitive environment requiring drastic restructuring to permit much longer production runs. This suggests that the timing arrangements might provide Canada with a longer transitional period than the United States.

The fact that there would be only two members would have implications for the institutional framework by excluding the possibility of majority voting. The great contrast in size gives added meaning to the bilateral nature of the arrangement. Looking southward, Canada would see a single giant partner of 180 million people, understandably the cause of greater anxiety than 3 partners of 60 million each. Canada might therefore be eager to expand the geographic scope to include additional members.

The fact that both countries are loyal participants in the GATT would probably mean compliance with its article 24 ground rules for free trade arrangements (mentioned above in the discussion of the bilateral approach). Trade barriers would be completely eliminated between the two members, not merely reduced to "preferential rates." And the choice for approach to commodity coverage would have to respect the "substantially all trade" requirement. This would surely challenge the "limited free trade" approach and also, perhaps, beachhead approaches which failed to fully commit from the outset the eventual range of freely traded commodities. Maximum possible coverage, if fully committed and, of course, the all-inclusive approach would avoid difficulties with the GATT. For other reasons, all-inclusive commodity coverage would probably not be a realistic choice. Certain agricultural products related to special Government programs would have to be excluded, at least at the outset.

As we noted, the process of adjusting Canadian industry to free trade would require considerable restructuring, whose scope should be as broad as possible. This consideration, quite apart from the GATT requirements, points to wide rather than narrow commodity coverage, reinforcing a preference for the maximum possible coverage approach.

The existence in both countries of fuels and industrial raw materials—a situation generally absent in Europe—raises problems, since in some cases (certain Canadian coal mines and U.S. mineral deposits), no amount of investment can make them competitive with freely entering supplies from the partner country. This suggests that a prolonged transitional period be applied in such cases, during which time a special adjustment assistance program would have a chance to operate.

A number of facts make it appear that the free-trade area form is possible for a Canada-United States arrangement, while a customs union would be virtually impossible. Creating a common external tariff and commercial policy would challenge the traditional congressional role in setting U.S. trade policy, and force Canada to abandon its Commonwealth ties, while a free-trade area would permit each country to maintain national tariffs and trade policies to all other countries. In any case, a free-trade area could rather easily be transformed into a customs union at a later date if this appeared desirable.

The federal nature of both countries would set limits on the degree to which economic integration could take place. Neither country has shown a great interest in homogenizing its State or Provincial tax systems or wage levels or laws and practices governing natural resources or industry. It is difficult to conceive of enthusiasm—or the practical political possibility—of doing in the name of a Canada-United States free-trade arrangement what Americans and Canadians have felt no compulsion to do within their own nations. This does not mean, however, that certain subsidies and other policies and practices clearly frustrating the beneficial effects of free trade could not be eliminated or harmonized between the two countries.

The status of Puerto Rico within the U.S. customs territory together with the fact that its people are American citizens, requires its inclusion within the geographic scope of a Canada-United States free-trade arrangement. A comparable relationship does not apply to Canada's Commonwealth partners, which could easily be left out and almost certainly would be.

POSSIBLE CHARACTERISTICS OF A CANADA-UNITED STATES FREE-TRADE ARRANGEMENT

On the basis of the facts of life mentioned above we can clear off a number of the options from our smorgasbord table. This leaves us with a reasonable range of possible characteristics for a Canada-United States free-trade arrangement.

The geographic scope would include Puerto Rico but not Canada's Commonwealth partners. It would probably be open-ended, looking toward the eventual inclusion of additional members, or the linking of the Canada-United States arrangement with similar groups elsewhere.

On the matter of commodity coverage, problems with certain agricultural products appear to eliminate the all-inclusive approach, while Canada's necessarily wide scope for readjustment plus the GATT requirements would rule out limited free trade. The GATT might also seriously challenge the "beachhead" approaches. This leaves as the most probable choice the maximum possible coverage approach with the eventual free list fully committed at the outset.

Moving to the basic form of the arrangement, we can definitely select the free-trade area over the customs union.

The approach to economic integration would stick to steps related to assuring the meaningfulness of free trade and avoid extensive programs which would require more harmonizing or equalizing between the two countries than now exists within either.

Institutions would be simple, reflecting the limited approach to economic integration and the choice of the free-trade area form. The mechanism for settling disputes would have to employ means other than voting by representatives of the two partners.

Finally, the timing arrangements for trade matters might allow Canada generally more time to open its frontier to American goods than vice versa. It might also be desirable to grant the longer transitional period to certain fuels or raw materials in either country which present special problems, and to provide programs for adjustment assistance.

The above description can be considered a very preliminary conclusion, the product of earnest effort, perhaps, but still only a dry run. The real narrowing of choices for the characteristics of a Canada-United States free-trade arrangement can only come when the authentic founding fathers appear on the scene. For only they can supply the most basic fact of life against which choices among possible characteristics are tested. This is the fundamental rationale of the scheme, its "why." This consideration is paramount in every decision area and may overpower choices made, as we have done above, on the basis of apparent practicability. For in a creation as important to its participants as a free-trade arrangement, what is necessary would outweigh what is most readily possible.

By way of an epilog, a few additional words might be said about what thus far remains missing ingredients in consideration of free trade between Canada and the United States, the sense of "why" and the founding fathers who would articulate it and build on it. First of all, a clear idea of purpose can probably develop only in response to common awareness of a distinct and pressing North American predicament for which a Canada-United States free-trade arrangement offers not an idealistic escape, but the most realistic down-to-earth solution. The postwar movement for European integration can be seen as a vigorous response to a European predicament, within which resolve to solve for all time the "German problem" and concern over the place of Europe among the new superpowers were central elements. We should note that economic integration was a very practical response to pressing European concerns, and not the more idealistically centered movement so eloquently advocated by prominent Europeans before World War II.

As for the Canadian-American founding fathers themselves, their abilities must extend beyond the capacity to formulate the rationale of a free-trade scheme upon understanding of the deep common needs of their countries. They must also be able to supply vigorous political leadership. These "North Americans," like such "Europeans" as Schuman, Adenauer, De Gasperi, and Spaak, would have to be able to deliver their national governments—and in their case some regional governments as well—to a common political commitment.

It is safe to say that a possible Canada-United States free-trade arrangement will remain the subject for occasional speeches and animated conferences which may well set the free-trade idea to resonate within important circles in both countries. But until the entrance of the "North Americans" with a coherent and compelling sense of "why," the characteristics of a bilateral scheme cannot be precisely known; and the theme of Canada-United States free trade will remain one for discussion and occasional eloquence, but will not become one for action.

APPENDIX

THE CANADIAN-AMERICAN COMMITTEE

The Canadian-American Committee was established in 1957 to study problems arising from growing interdependence between Canada and the United States. With approximately equal representation from coast to coast in the two countries, its 60 members are business, labor, agricultural, and professional leaders. The Committee is sponsored by two nonprofit research organizations—the National Planning Association in the United States and the Private Planning Association of Canada.

The Committee believes that good relations between Canada and the United States are essential for the future prosperity, and perhaps even the survival, of both countries. It is therefore seeking not only to encourage a better understanding of the problems which have arisen and may arise, but also to develop solutions for such problems which are in the common interest of both countries. The Committee is taking a North American approach in its search for constructive programs.

The Committee sponsors a series of objective research studies on various aspects of Canadian-American relations. These are being undertaken by qualified experts in both countries and, with the Committee's approval, are being published. On the basis of these factual studies and of discussions at its meetings, the Committee also issues policy statements signed by its members. Such statements are directed at increasing public understanding of the attitudes, policies, and actions which the Committee believes would best serve the mutual interests of the peoples of both countries.

The Canadian-American Committee meets twice a year, once in Canada and once in the United States. Its work is jointly financed by funds contributed from private sources in the United States and Canada and by foundation grants.

Offices on behalf of the Committee are maintained at 1606 New Hampshire Avenue NW., Washington 9, D.C., and at 716 Sun Life Building, Montreal, Quebec. John Miller (assistant chairman and executive secretary of NPA) serves as secretary of the Committee, and H. Edward English (secretary of PPAC) is Acting Director of Research.

Senator SPARKMAN. Now, Mr. Clayton, if we may have yours, please, sir.

STATEMENT OF W. L. CLAYTON, BOARD OF DIRECTORS, ANDERSON, CLAYTON & CO.

Mr. CLAYTON. Mr. Chairman and Mrs. Griffiths, gentlemen of the committee, if the committee has no objection I would like to read my entire statement instead of summarizing it, because is very succinct.

Senator SPARKMAN. That is all right, sir. Go right ahead. It looks like it is pretty well summarized already.

Mr. CLAYTON. It will only take about 10 or 12 minutes.

Senator SPARKMAN. All right, sir.

Mr. CLAYTON. Looking at the world political and economic situation, I am convinced that Latin America is the most pressing problem now facing the United States.

Perhaps we can live with one Cuba, if we must, but we could not live with half a dozen Cubas.

What can we do to assure the freedom and independence of all countries of Latin America and our prestige and influence in them?

I do not think the Alliance for Progress, by itself, is the answer.

I believe the answer is to be found in opening up our markets to the products of these countries and assisting them to open up the markets of the rest of the free world to their exports.

Latin American countries themselves have shown us the way.

Already a common market has been set up by five Central American countries and a free trade area has also been started by seven of the principal Latin American countries: Mexico, Brazil, Uruguay, Ar-

gentina, Chile, Peru, and Colombia. Later, Paraguay and Ecuador joined this free trade area, making a total of nine countries.

On the other hand, the United States has substantially closed its markets to Latin American sugar, petroleum, lead, and zinc, to name the principal items affected.

The quota system for sugar was first adopted by us in 1934 and was revised in 1937, 1948, and 1962.

In 1934 we consumed about 6.5 million tons of sugar. Today we consume annually about 10 million tons of sugar.

In 1934 the domestic quota for sugar was about 1.8 million tons. It has increased almost yearly until now it stands at 3.5 million tons, all figures including both beet and cane sugar. That is the domestic quota for sugar. In other words, the amount of sugar that the domestic farmers are permitted to raise and process is now 3.5 million tons out of—in other words, about 35 or 36 percent of our total consumption.

There is perhaps no lobby in Washington more active and effective than the sugar lobby.

But for the quota system, or a very high tariff on imports, we would produce little sugar in the United States. We can generally buy it from Latin American and other countries much cheaper than we can produce it. The dollars we would pay for it would be promptly returned to us in payment for goods that we can produce cheaper or better than the sugar countries.

The substantial closing of our markets to foreign sugar, petroleum, zinc, lead, and other commodities has been done in the short-term special interest of politically powerful minority groups and against the national and international interest.

Moreover, the United States has established heavy export subsidies on cotton, which is also one of the principal exports of several Latin American countries.

During the Hoover administration, when the United States had occasion to complain of a foreign country for "dumping" a commodity in the United States, we defined dumping as the sale of a commodity in the country of destination at a lower price than in the country of origin.

I think it makes no difference whether we take that definition or Webster's definition of a sale of a commodity in quantities at less than the cost of production.

The U.S. Government is selling cotton for export at 24 cents, whereas for domestic use the Government price is 32.5 cents.

Thus, we are dumping our surplus cotton in the world markets. This causes deep and bitter resentment on the part of our Latin American and other foreign cotton-growing competitors.

On December 19, 1963, Senator Javits of New York made an outstanding speech in the U.S. Senate on Latin America. Senator Humphrey of Minnesota, immediately following Senator Javits, said this of Senator Javits' speech:

> I wish to associate myself with the text and substance of the Senator's speech. I believe it is one of the truly great speeches made on this whole subject matter. The Senator is to be commended.

In the speech referred to, Senator Javits said:

> It is essential that the United States revise its trade policies toward Latin America and put its full support behind the formation of a hemispheric common market.

This is not only sound doctrine; it is imperative doctrine. It will pinch the toes of a few U.S. producers, but it is decidedly and definitely in the national interest.

This is the age of the common market or free trade area. General De Gaulle cannot change the course of history; he can delay it, and that is what he is doing.

In the 4 years that the European Common Market has been operating, intramarket trade has increased 100 percent, that is, just double—and total trade has increased more than 50 percent. The European Common Market is now the greatest trading unit in the world.

Rightly, Senator Javits strongly supports the formation of a Western Hemisphere Common Market or free trade area.

But both the United States and Canada contain highly efficient, giant industries with which the small industries of Latin America, each geared to the buying power of the country in which it is situated, could hardly compete.

I suggest that a Western Hemisphere free trade area should be established, as a beginning, on the following limited basis:

1. The United States, Canada, and Latin American countries would reduce their tariffs on imports of raw materials originating in other Western Hemisphere countries at the rate of 10 percent per annum for 10 years, until such tariffs are at zero. Where import quotas are employed on such trade, such quotas are to be modified annually, so that at the end of 10 years they will have completely disappeared.

2. Latin American countries will reduce tariffs at the rate of 10 percent per annum on all imports (both raw materials and industrial products) originating in Latin American countries so that at the end of 10 years such tariffs will be at zero. And then the same condition applies to import quotas as mentioned in 1.

This second step must be taken if the Latin American area is ever to be developed industrially. In 10 years' time, a common market or free trade area of 200 to 300 million people (larger even than the U.S. Common Market) will be created, justifying the establishment of highly efficient, giant industries in Latin America.

3. It is expected that the Western Hemisphere free trade area will further multilateralize the above plan by negotiating arrangements with other free trade areas, or common markets.

4. At the end of 10 years, the foreign ministers of Western Hemisphere countries will meet to discuss their future problems in respect of trade and to advise their respective governments on the course that should be pursued for the future.

A Western Hemisphere free trade area on the above basis would accomplish the following:

(*a*) Raw materials originating in the Western Hemisphere would circulate freely throughout the whole of the Western Hemisphere.

(*b*) All goods—raw materials and industrial products—originating in Latin America would circulate freely throughout Latin America, now with over 200 million people and growing in population faster than any other area of the world. This provision would be similar in an economic sense to the adoption of the U.S. Constitution which welded the Thirteen Colonies into one Nation, under an edict that there should never be any tariffs, quotas, or other Government-made impediments to trade between the Colonies, or States. Who is to say that the

end result of this economic policy for Latin America would not be similar to that achieved in the United States?

In the January 1961 issue of Foreign Affairs, there is an excellent article by Alfred C. Neal, president of the Committee for Economic Development, entitled "New Economic Policies for the West." I quote one paragraph from this article:

It is too little recognized, especially by the new political leaders, that modern industrial development is heavily dependent upon what economists call "economies of scale" and "external economies." The first of these pertains to the size, and therefore potential output, of a plant. Most of the commonplace goods associated with a high standard of living (and high productivity) cannot be made in small plants and workshops. The reasonably economic size of a flat-rolled steel products mill is about a million tons per year; for a bar mill, about half that. Similarly, petroleum refineries, automobile tire and synthetic rubber plants, automobile and tractor plants, all require large outputs to achieve reasonably low cost. The low income of underdeveloped countries and their low level of development make almost all of them too small a market to support such plants.

Mr. Neal shows here, for instance, that the buying power of a country like Ghana, is about the same as Rochester, N.Y., the city of Rochester, N.Y., and he further shows that in Nigeria, which is the most populous country of Africa, that Nigeria has a buying power about equal to that of West Virginia.

Without forming large customs unions among themselves, their development will be limited for a very long time to agriculture and the extractive industries, to the earlier stages of processing of their products for export markets, and to a few small-scale large industries (bricks, slaughtering) whose products enjoy the protection of high transport costs or perishability. This is precisely the kind of economy that their political leaders wish to escape from. Politically as well as economically, it is important that we help them to find avenues of escape that lead somewhere other than to the Soviet Union.

This avenue of escape is a road that leads to markets for Latin American products and, at the same time, leads to a Latin American free trade area.

There is no other way of which I am aware to lay the foundation for the industrialization of the Latin American economy.

Thank you.

Senator SPARKMAN. Thank you, Mr. Clayton, for a very interesting and thought-provoking statement.

By the way, I shall leave the questioning almost entirely up to other members, but let me ask you, Mr. Clayton, just this one question.

As I recall, you had a hand in the establishment of GATT. How does your proposal fit in with GATT?

Mr. CLAYTON. I think GATT makes an exception for regional free trade areas. Certainly what I am proposing is only similar to the European Common Market.

Senator SPARKMAN. I may be wrong on this, but I had the impression, from one of the papers, that the United States probably would not be a welcome partner in connection with the Latin American countries because it was so big and it would be regarded as overweight, so to speak. Was that your paper, Mr. Grimes?

Mr. GRIMES. I believe Mr. Lea mentioned that in regard to the Canadian situation. But the same thing does hold true with regard to Latin America. We are considered to be the colossus of the north and I think there would be quite a bit of reluctance on the part of Latin America at this particular moment of history to embrace

the United States as a trading partner in a hemisphere trade association.

I might add that I am very pleased to see that the Latin Americans have beat Mr. Clayton to the punch here by formation of their LAFTA which is aimed precisely toward the elimination of tariffs between the countries of Latin America.

Senator SPARKMAN. Wasn't that question involved also in the fact that the five smaller Central American countries did not become a part of the LAFTA free trade association?

Mr. GRIMES. I believe that the question of the preponderance in size of a particular potential member came about between the Central American Common Market countries and Mexico. There was some reluctance on the part of the smaller Central American countries to welcome Mexico because of its size and evolved industrial status.

Is that the point you were trying to make, sir?

Senator SPARKMAN. Yes, in other words, you had an overbalance there in size.

Mr. GRIMES. There is a definite reluctance at this stage of the game on the part of the Latin Americans to include the United States in the inter-LAFTA discussions and negotiations which are going on now.

Frankly, I think this is one of the things which we should try to overcome. As I said in my paper, I think that LAFTA represents a great potential for the area and a huge step which Latin America has taken toward curing some of its problems. The curing of these problems is in their own interest obviously. I feel that we in this country, both in the business community and the Government, should look for opportunities to aid and help the evolutionary processes of LAFTA and the Central American Common Market.

Senator JAVITS. Would the Chair yield at this point?

Senator SPARKMAN. Yes.

Senator JAVITS. Isn't it a fact, Mr. Grimes, that you really can't make major progress, especially as the terms of trade have turned against Latin America so markedly, within the period of time that Mr. Clayton gives you, without something bigger than what you have got?

Mr. GRIMES. I believe that is so, sir. I believe that is definitely so.

Senator SPARKMAN. Mr. Clayton, I presume your answer to this question that I have been bringing up has been that it would be a difficulty but it is not insuperable, is that right?

Mr. CLAYTON. Mr. Chairman, I don't think there would be any objection on the part of Latin American countries to form a partnership with the United States on the basis that I have proposed here which simply is that it would affect raw materials only which Latin America largely ships to the United States but we have excluded their raw materials in many particulars, lead and zinc and sugar and to some extent petroleum.

I don't think there would be any serious objection on the part of any Latin American country to come in on the basis on which I have indicated here in this paper, and I was particular to indicate that basis, that particular basis, because of my knowledge of Latin American countries and a feeling that our popularity there is deteriorating practically all the time, and that they would not welcome an opportunity to go into partnership with us on a Common Market basis except only with respect to raw materials.

Senator JAVITS. Mr. Chairman, before the Chair leaves that, Mrs. Griffiths, will you allow me to develop exactly what Mr. Clayton has suggested?

Senator SPARKMAN. Yes.

Senator JAVITS. In the first place, let us state the classic difference between the Free Trade Association and the Common Market. You would not affect the external tariffs as to the rest of the world of either the United States or Canada or any other Latin American countries, is that correct?

Mr. CLAYTON. That is right. I proposed a free trade area and not a customs union or common market.

Senator JAVITS. And second— I will get to my own questioning, but I just want to get my premise—is it fair to say what you are proposing is that in return for the United States opening its doors to the primary materials of Latin America, Latin America will open its doors mutually to its own manufacturers?

Mr. CLAYTON. To its own manufacturers, and make a free trade area of 200 million people as at present but increasing faster than any other area of the world, and in 10 or 15 years, why there may be 300 million people there.

Senator JAVITS. But it would still have tariffs against the United States and Canada?

Mr. CLAYTON. Surely.

Senator JAVITS. I just wanted to get the facts.

Mr. CLAYTON. Against the United States in industrial products.

Senator JAVITS. That is correct.

Representative GRIFFITHS. Thank you very much.

I would like particularly to thank all three of you. I was very impressed, and I would like to say I have only one real distinction in this Congress, I have read every sugar hearing, and I couldn't agree with you more, Mr. Clayton, that it is ridiculous for us to grow the amount of sugar that we do. We should be importing that sugar out of Latin America where it is cheap and good.

Mr. CLAYTON. Right.

Representative GRIFFITHS. It makes a much finer product, cane sugar makes a much finer product, than American beet sugar.

I would like to say also that one of the real practical things we could do immediately as Members of Congress would be to open up the stamp plan program to permit the users of those stamps in big cities to buy the products of Latin America, bananas and coffee and so forth. That would be of some assistance to them right now. But I would think, too, that in the primary products, they would have no real objection to them if we had free trade and I think it would be terribly helpful.

Mr. CLAYTON. I didn't quite catch the last, Mrs. Griffiths.

Representative GRIFFITHS. I would think that it would be very helpful if in primary products between Latin America and the United States we did have free trade.

Mr. CLAYTON. Yes.

Representative GRIFFITHS. Perhaps Argentina would object on wheat, would they not?

Mr. CLAYTON. I beg pardon?

Representative GRIFFITHS. Would Argentina object to wheat being a free traded item?

Mr. CLAYTON. Well, Argentina, of course, is starting to export more wheat. She didn't export wheat for a long time. In the old days, Argentina was a big exporter of wheat, and then there came a time when they didn't export any, and now they have resumed again.

I just hadn't thought about the wheat, whether most countries who are importers of wheat have very little tariff on wheat or very little impediment to the flow of wheat into their country.

Representative GRIFFITHS. However, if Argentina is in LAFTA they might be quite anxious to be the sole sellers of wheat to the rest of Latin America, so we might have some trouble but we might be able to get around it. I think also we are dumping cotton, and I think Public Law 480 is responsible for it, on the other markets of the world. We are dumping rice, too.

Mr. CLAYTON. We are dumping other commodities besides cotton.

Representative GRIFFITHS. You are right. We are dumping rice.

I would like to ask the gentleman who first spoke, do you think there is any possibility that LAFTA and the Central American market will become one market or not?

Mr. GRIMES. This has, of course, been mentioned as a possibility. I think it is fairly obvious in the evolutionary steps through which LAFTA is going at the moment that it itself is headed toward a common market approach and there will be common exterior barriers amongst themselves.

I would not be surprised personally to see eventually an amalgamation of the two systems.

Representative GRIFFITHS. What are the chief objections now?

Mr. GRIMES. Primarily the incompatibility of products now, I think that is the main thing and neither group can see itself involved enough to really get much out of dealing with the other. There is not enough intratrade.

Representative GRIFFITHS. Isn't Central America also afraid of Mexico?

Mr. GRIMES. Yes, they are.

Representative GRIFFITHS. Perhaps as much as of the United States?

Mr. GRIMES. Yes, that is one of the points I mentioned previously.

Representative GRIFFITHS. I would like to ask the gentleman who discussed Canada and the United States, what are the differences in the fringe benefits for a Canadian autoworker and one from the United States?

Mr. LEA. I am afraid I don't know that, but I can find out for you.

Representative GRIFFITHS. Could you supply the answer?

Mr. LEA. Yes.

The UAW operates in both countries, and I would imagine there isn't a great deal of difference but I will find out.

Representative GRIFFITHS. What are the social security differences between Canadian workers and those in the United States, aren't they more completely covered by social security or are they not? I don't really know.

Mr. LEA. I think there is also a provincial factor that enters in there, but I don't know.

Representative GRIFFITHS. I see.

Could you supply those, too?

Mr. LEA. Yes.

Representative GRIFFITHS. Do they have a minimum wage in Canada, does Canada have a minimum wage?

Mr. LEA. I am afraid you have got me on a subject on which I don't know, but I can supply it.

Representative GRIFFITHS. Could you supply that?

Senator SPARKMAN. Yes, that would be fine.

Representative GRIFFITHS. Thank you.

(In response to the foregoing requests for supplemental information, the following communication was received:)

U.S. DEPARTMENT OF LABOR,
BUREAU OF LABOR STATISTICS,
Washington, D.C., January 27, 1964.

MRS. MARIAN T. TRACY,
Financial Clerk, Joint Economic Committee,
Congress of the United States, Washington, D.C.

DEAR MRS. TRACY: I am pleased to furnish the Joint Economic Committee with information on differences in social security programs between the United States and Canada, minimum wages in Canda, and fringe benefits for automobile workers in the United States and Canada. This information is provided in response to questions raised by committee members during the testimony of Mr. Sperry Lea of the National Planning Association on January 16, 1964.

Enclosed is a compilation of information on the principal social security programs in the United States and Canada. This information describes the source of funds, qualifying conditions, benefits to insured, and administration of the various programs. Also enclosed is a table showing legal minimum wages by Province in Canada.

Information on fringe benefits in the automobile manufacturing industry is not separately available. The Bureau conducted a survey of average expenditures for selected supplementary payments covering the year 1959, which contains such information for the entire transportation equipment industry. It was found that supplements for this industry amounted to approximately 21.7 percent of the gross payroll. I am enclosing a table presenting details on the supplementary benefit payments in the U.S. transportation equipment industry. I am also enclosing a table showing summary results of a Canadian survey of supplementary benefits for the year 1959. No separate information was reported for the automobile industry.

I hope that the enclosed information will be helpful to the committee.

Sincerely yours,

EWAN CLAGUE, *Commissioner.*

TABLE I.—*Comparative social security programs, United States and Canada*

OLD AGE, INVALIDITY, DEATH

Canada	United States
I. Type of law and program: Universal old-age pension system.	I. Type of law and program: Various social insurance systems.
II. Coverage: All residents.	II. Coverage: Gainfully occupied, including self-employed. Voluntary coverage for employees of nonprofit institution and State and local governments, and clergymen. Special programs for railroad employees, Federal, and many other public employees.

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

OLD AGE, INVALIDITY, DEATH—continued

Canada	United States
III. Source of funds: Income taxpayers, corporations, general (manufacturers' sales) and Government.	III. Source of funds: Insured person and employer.
IV. Qualifying conditions: Old-age pension: Retirement age at 70; 10 years of residence immediately before claim (or residence prior to 10-year period double the absences during such period, and 1 year of residence immediately before claim. Retirement not necessary. Old-age assistance: Age 65 to 69; income below specified amounts; and same resi-ance: Totally and perma-dence as for old-age pension. Disability and blind assist-nently disabled or blind; income below specified amounts; and 10 years of residence.	IV. Qualifying conditions: Old-age pension: Retirement age at 65, or 62 with five-ninths of 1 percent reduction per month under 65. Coverage for one-fourth of calendar quarters since 1950, or 40 quarters. Pension reduced by earnings over $1,700 a year, and half of those $1,200 to $1,700, until age 72. Invalidity pension: Incapacity due to long or incurable impairment. Coverage for one-fourth of quarters since 1950, or 40 quarters; and in 20 of last 40 quarters; 6-month waiting period. Survivor pensions: Widowed mother and orphans, or aged widow and parent if deceased was pensioner or covered in 6 of last 13 quarters. Pensions reduced by earnings, as above.
V. Cash benefits for insured workers (except permanent disability): Old-age pension: $55 a month, flat; aged couple, $110. Old-age assistance: Up to $55 a month to needy; maximum reduced by other income over $300 per year.	V. Cash benefits for insured workers (except permanent disability): Old-age pension: 58.85 percent of first $110 of average monthly earnings since 1950; plus 21.4 percent of next $290. Minimum and maximum pension, $40 and $127 per month. Dependents' supplements: 50 percent of pension each for aged wife, or wife caring for child; aged dependent husband; and children under 18 or invalid. Maximum total pension: $254 a month or 80 percent of earnings if less. Old-age assistance payable to needy after needs test, under Federal-State program.
VI. Permanent disability and medical benefits for insured workers: Invalidity pension: None. Assistance: Up to $55 a month to needy, permanently and totally disabled persons and blind persons under National-Provincial programs: maximum reduced by other income over $300 a year for disabled or $540 for blind.	VI. Permanent disability and medical benefits for insured workers: Invalidity pension: Same as old-age pension under V. Dependents' supplements: Same as under V. Maximum total pension: Same as under V. Assistance: Payable to needy disabled after means test.

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

OLD AGE, INVALIDITY, DEATH—continued

Canada	United States
VII. Survivor **benefits and medical** benefits for dependents: Survivor pension: None. Survivor age 70 or over receives old-age pension. Assistance: All Provinces provide assistance on means-test basis to needy widowed mothers. (Orphans receive family allowances.)	VII. Survivor benefits and medical benefits for dependents: Widow's pension: 82.5 percent of basic pension of insured if age 62 or 75 percent if below and caring for child of insured. Orphans' pensions: 75 percent of basic pension of insured for each half for full orphan under 18 or invalid. Parent: 82.5 percent of pension of insured for 1 dependent aged parent, or 150 percent for 2 parents. Maximum survivor pensions: $254 a month or 80 percent of earnings if less. Funeral grant: Lump sum of 3 months' basic pension of insured; maximum, $255. Assistance: payable to needy orphans and relatives with whom living, after needs test.
VIII. Administrative organization: Department of National Health and Welfare.	VIII. Administrative organization: U.S. Department of Health, Education, and Welfare.

SICKNESS AND MATERNITY

Canada	United States
I. Type of law and program: National and Provincial laws. Hospitalization insurance.	I. Type of law and program: Four State laws only. Limited social insurance system (Cash sickness benefits mainly).
II. Coverage: All residents. Special national programs for seamen, Indians, and Eskimos.	II. Coverage: Employees in industry and commerce in California, New Jersey, New York, and Rhode Island. Exclusions: Agricultural and domestic employees; employees of nonprofit institutions. Special national systems for railroad employees and Federal employees; and Federal-State system for aged persons of limited means.
III. Source of funds: Insured person: Flat contribution. Employer: None, except in cases where labor-management agreements divide contributions. Government: National Government, grants to Provinces of	III. Source of funds: Insured person: 1 percent of earnings (California and Rhode Island) or 0.5 percent of earnings (New Jersey and New York). Employer: None (California and Rhode Island); 0.1 to 0.75 percent of payroll, ac-

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

SICKNESS AND MATERNITY—continued

Canada	United States
III. Source of funds—Continued Government—Continued 25 percent of national per capita cost plus 25 percent of Province's per capita cost times the number of persons covered. Provincial governments, all or part (where insured contribute) of remaining cost in all but 3 Provinces.	III. Source of funds—Continued Employer—Continued cording to risk (New Jersey); and any benefit costs above 0.5 percent of earnings (New York). Government: None.
IV. Qualifying conditions: Hospitalization benefits: Vary among Provinces; residence in Province main condition.	IV. Qualifying conditions: Sickness benefit: $300 of insured earnings in last year (California); 17 weeks of employment in last year (New Jersey); employment during last 4 weeks (New York); and 20 weeks of employment in last year (Rhode Island). Medical and maternity benefits: Same as above, where provided (provided only on limited scale).
V. Cash benefits for insured workers (except permanent disability): Sickness and maternity benefits: None.	V. Cash benefits for insured workers (except permanent disability): Sickness benefit: 50 percent of weekly earnings (New York and Rhode Island), or 61 to 67 percent (New Jersey); or 4 to 7 percent of quarterly earnings a week (California). Supplement of $3 a week per child payable in Rhode Island only. Payable after 7-day waiting period (none in California when hospitalized) for up to 26 weeks. Maternity benefit: In Rhode Island, 50 percent of earnings for up to 6 weeks before and 6 weeks after confinement. All other States, none.
VI. Permanent disability and medical benefits for insured workers: Medical benefits: Service benefits provided by hospitals paid directly by Provinces. Hospitalization including standard ward care, necessary nursing, inpatient diagnostic services and drugs, operating room facilities, and radiotherapy and physiotherapy where available.	VI. Permanent disability and medical benefits for insured workers: Medical benefits: In California, cash refund of $12 a day toward hospital expenses for up to 20 days. In New York, medical benefits may be provided under a private plan in lieu of cash sickness benefits up to 40 percent of the latter. Other States: No medical benefits provided.

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

SICKNESS *and* MATERNITY—continued

Canada	United States
VI. Permanent disability—Continued Hospitalization, etc.—Con. Provinces may furnish emergency or diagnostic outpatient services. Duration: No limit. Patients must pay small daily fee for hospitalization in some Provinces, as well as fees for outpatient services.	VI. Permanent disability—Continued Medical services provided to aged persons unable to pay for own care under Federal-State program.
VII. Survivor benefits and medical benefits for dependents: Medical benefits for dependents: Same as for family head.	VII. Survivor benefits and medical benefits for dependents: Medical benefits for dependents: None provided.
VIII. Administrative organization: Department of National Health and Welfare, administration of grants to Provinces and provision of consultative services. Provincial public health departments or hospital commissions, administration of program in Provinces.	VIII. Administrative organization: Departments of State governments administering unemployment insurance, administration of program in three States (California Department of Employment, New Jersey Department of Labor and Industry, and Rhode Island Department of Employment Security). Workmen's Compensation Board, administration of program in New York.

UNEMPLOYMENT

Canada	United States
I. Type of law and program: National law. Compulsory insurance system.	I. Type of law and program: Federal law (imposes tax on employers, with offset for contributions to approved State programs; grants to States for administration of programs and extended benefits; and minimum administrative standards). State laws: All 50 States, Puerto Rico, and the District of Columbia have separate laws creating own programs; State laws. Compulsory insurance system.
II. Coverage: Employees in industry and commerce. Exclusions: Salaried employees with salaries above $5,460 a year, employees in agriculture and hunting, private domestic servants, employees of nonprofit institutions, teachers, public employees, casual employees, and family labor.	II. Coverage: Federal law: Employees of firms in industry and commerce with four or more workers. State programs: Employees covered by Federal law; about one-half of States also cover employees of firms with one to three workers. Common exclusions: Agricultural employees, domestic servants, employees of nonprofit institutions, State, and local government employees

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

UNEMPLOYMENT—continued

Canada	United States
	II. Coverage—Continued Common exclusions—Con. (two-fifths of States), casual employees, and family labor. Special Federal programs for railroad employees and Federal employees.
III. Source of funds: Insured person: 10 cents a week if weekly earnings under $9 (1st wage class), up to 94 cents if earnings $69 or more (12th wage class). Employer: Same as for insured person. Government: 20 percent of combined employer-employee contributions (National and Provincial Governments also share whole cost of unemployment assistance). Maximum earnings for contribution and benefit purposes: $69 a week.	III. Source of funds: Insured person: None, except in Alabama (0.1 to 0.25 percent), Alaska (0.6 percent), and New Jersey (0.25 percent of earnings). Employer: Federal tax, 0.8 percent of payroll (3.5 percent basic rate less 2.7 percent offset for contributions to State programs). State programs, basic rate of 2.7 percent of payroll, with actual rates varying from none to 4.5 percent according to individual employer's unemployment experience; average rate, about 1.5 percent. Government: None from general revenue. Federal Government pays cost of administration of State programs and of extended duration from above Federal tax (balance of tax set aside in $550 million reserve, or returned to States). Maximum earnings for contribution and benefit purposes: $3,000 a year under Federal tax and most State programs.
IV. Qualifying conditions: Unemployment benefit: 30 weeks of contribution in last 2 years, including 8 weeks during last year (special conditions for workers seasonally unemployed in winter). Capable of work (if incapacitated after qualifying for benefit, not disqualified by such incapacity); available for work; unable to obtain suitable employment; and registered at employment office. Unemployment not due to voluntary leaving, dismissal for misconduct, work stoppage in which directly interested, refusal of suitable offer, neglect of opportunity to work, or failure to undergo direct training (disqualification for up to 6 weeks).	IV. Qualifying conditions: Unemployment benefit: Most State programs require minimum earnings in preceding base year equal to specified total amount (e.g., $300). A few States require 14–20 weeks of employment in last year. Ability to work, availability and readiness for work, and registration. Unemployment not due to voluntary leaving, misconduct, labor dispute or refusal of suitable offer (length of disqualification varies among States).

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

UNEMPLOYMENT—continued

Canada	United States
V. Cash benefits for insured workers: Unemployment benefit: $6 a week if earnings under $9 (1st wage class), up to $27 if earnings $69 or more (12th wage class). Supplement for one dependent: $2 a week (1st wage class), up to $9 (12th wage class). Payable after 1-week waiting period, for up to 52 weeks, or for one-half of number of weeks of contribution during last 2 years if fewer than 104. (Unemployment assistance under National-Provincial program available to needy persons exhausting benefit rights or for whom benefits inadequate.)	V. Cash benefits for insured workers: Unemployment benefit: 3.8 to 5 percent of highest quarterly earnings a week, in about one-half of States. Weighted percentages of weekly, quarterly, or annual earnings equal to 50–75 percent of earnings in remainder. Dependents' supplements: About one-fourth of States provide $1 to $5 a week per child and sometimes for other dependents. Maximum benefits: $26 to $70 a week according to State. Payable after 1-week waiting period in most States, for up to 18 to 39 weeks according to State (duration extended 50 percent beyond normal limit, with overall maximum of 39 weeks, under temporary Federal law of 1961). (Assistance available to some needy unemployed exhausting benefit rights).
VI. Administrative organization: Ministry of Labor, general supervision. Unemployment Insurance Commission, administers program along with employment service through its regional and local employment offices; tripartite membership.	VI. Administrative organization: Department of Labor administers program nationally through its Bureau of Employment Security. State employment security agencies administer State programs through their local employment offices; agencies are either a department of State government, or a board or commission.

WORK INJURY

Canada	United States
I. Type of law and program: Provincial laws. Compulsory insurance with public carrier (Provincial programs).	I. Type of law and program: Fifty State laws. One territorial law (Puerto Rico). Three Federal laws (Federal employees, longshoreman and harbor workers, and private employees in the District of Columbia). Compulsory or voluntary insurance with public or private carrier (according to State).

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

WORK INJURY—continued

Canada	United States
II. Coverage: Employees in industry and commerce, in general (with some differences among Provinces). (Common exclusions: Agricultural, domestic, and casual employees; employees of small firms.). Special systems for seamen and employees of National Government.	II. Coverage: Employees in industry and commerce generally, and most public employees. (Common exclusions: Agricultural employees (two-thirds of States), domestic servants (five-sixths of States), casual employees (four-fifths of States), employees of firms with 2 to 14 employees (three-fifths of States), and employees in nonhazardous occupations (one-fourth of States). Coverage compulsory in about one-half of States and voluntary in others.
III. Source of funds: Insured person: None. Employer: Whole cost, through contributions varying by industry according to risk (large firms in Ontario and Quebec may self-insure). Government: None. Maximum earnings for benefit purposes: $3,000 to $6,000 a year, according to Province.	III. Source of funds: Insured person: Minor contributions in a few States. Employer: Whole cost in most States, and most of cost in others, through insurance premiums varying with risk or self-insurance. Government: None.
IV. Qualifying conditions: Work-injury benefits: No minimum qualifying period.	IV. Qualifying conditions: Work-injury benefits: No minimum qualifying period.
V. Cash benefits for insured workers (except permanent disability): Temporary disability benefit (work injury): 75 percent of earnings in all Provinces. Minimum benefit: $15 to $30 a week, according to Province. Payable after 1 to 5 days' waiting period, for duration of disability.	V. Cash benefits for insured workers (except permanent disability): Temporary disability benefit (work injury): 60 to 66⅔ percent of earnings in most States. About one-third of States provide supplements for dependents. Maximum benefit: $30 to $150 a week, according to State; about one-half of States have maximums of $50 a week or more. Payable after 7-day waiting period in majority of States, and after 2 to 5 days in others.

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

WORK INJURY—continued

	Canada		United States
VI.	Permanent disability and medical benefits for insured workers: Permanent disability pension (work injury): 75 percent of earnings, if totally disabled. Minimum pension: $15 to $30 a week, according to Province. Proportion of full pension corresponding to impairment of earning capacity, if partially disabled (converted to lump sum if impairment 10 percent or less). Medical benefits (work injury): Medical, surgical, nursing, and hospital services, medicines, and appliances, in all Provinces (may be furnished under approved private employer plans).	VI.	Permanent disability and medical benefits for insured workers: Peramnent disability pension (work injury): 60 to 66⅔ percent of earnings in most States, if totally disabled. Constant-attendance and dependents' supplements provided in some States. Maximum pension: $30 to $150 a week, according to State. Payable for life or throughout disability in about three-fifths of States, but only for 330 to 550 weeks or up to $7,500 to $30,000 in remainder. Partial disability: Proportionate to wage loss or full rate for fewer weeks in case of scheduled injuries. Medical benefits (work injury): Medical services provided for as long as required in three-fourths of States, and for a specified period or up to a maximum total cost in others.
VII.	Survivor benefits for dependents and medical benefits for dependents: Widow's or invalid widower's pension (work injury): Flat pension of $50 to $100 a month, plus lump sum of $100 to $300, according to Province. Orphans' pension (work injury): $20 to $35 a month for each orphan, or $30 to $50 if full orphan, according to Province. Other dependents (if no spouse or orphan): Reasonable sum proportionate to pecuniary loss. Maximum survivor pensions: 75 percent of earnings. Funeral grant (work injury): $200 to $400, according to Province.	VII.	Survivor benefits and medical benefits for dependents: Survivor pensions (work injury): 35 to 66⅔ percent of earnings of insured for widow, in most States; 60 to 80 percent for widow plus children. Maximum pension: $30 to $50 a week under most laws (payable for only 300 to 600 weeks or up to specified aggregate amount under about four-fifths or laws). Other eligible survivors (some laws only): Dependent parents, brothers, and sisters. Funeral grant (work injury): Lump sum of $100 to $1,000 according to State.

TABLE I.—*Comparative social security programs, United States and Canada*—Con.

WORK INJURY—continued

Canada	United States
VIII. Administrative organization: Workmen's compensation board (in Quebec, commission) in each Province, fixing and collection of contributions, management of accident fund, and award and payment of benefits.	VIII. Administrative organization: State workmen's compensation agencies, administration of program in about one-half of States, State departments of labor in about one-third of them, and courts in most of remainder. Government workmen's compensation funds exist in about one-third of States. Employers must insure with State fund in 8 States; may insure with State fund or private carrier, or self-insure, in 11 States; and may insure with private carrier or self-insure in remainder.

FAMILY ALLOWANCES

Canada	United States
I. Type of law and program: Universal public system.	I. Type of law and program: None.
II. Coverage: All residents, with one or more children.	
III. Source of funds: Insured person: None. Employer: None. Government: Whole cost.	
IV. Qualifying conditions: Family allowances: Child must be under 16, and in school. Child must have been born in country or resident there 1 year (unless parent was resident 3 years before birth.)	
V. Cash benefits for insured workers: Family allowance: $6 a month for each child under age 10; $8 for each child age 10 or over.	
VI. Administrative organization: Department of National Health and Welfare, general supervision. Family Allowance and Old-Age Security Division in Department administers allowances through 10 regional offices (in conjunction with Department of Finance).	

Source: "Social Security Programs Throughout the World, 1961," Social Security Administration, Division of Program Research, U.S. Department of Health, Education, and Welfare, Washington, D.C., 1961.

Prepared by Division of Foreign Labor Conditions (BIC), Bureau of Labor Statistics, U.S. Department of Labor, January 1964.

TABLE II.—*Canada: Legal minimum wages by Province*

Province	*Minimum wage* [1]
Newfoundland	$0.50
Prince Edward Island	----
Nova Scotia	[2].45
New Brunswick	[3].65
Quebec	.70
Ontario	[2].625
Manitoba	.66
Saskatchewan	.73
Alberta	.68
British Columbia	.75

[1] Highest rates provided by general orders; applicable to factories in major industrial centers.

[2] Rates for female workers; no male minimum rates in effect.

[3] Applicable only to canning industry.

Source: "Man-hours and Hourly Earnings," November 1961, and "Provincial Labour Standards," December 1962, Department of Labour of Canada.

Prepared by Division of Foreign Labor Conditions (BIC), Bureau of Labor Statistics, U.S. Department of Labor, January 1964.

TABLE III.—*Supplementary ("fringe") remuneration practices, United States and Canada (United States: Average expenditures for selected supplementary employee remuneration practices in the manufacture of transportation equipment, 1959)*

Item	Paid leave	Premium pay	Legally required payments	Private welfare plans
Percent of gross payroll	6.9	4.5	4.3	6.0
Percent of straight-time payment	7.2	4.7	4.5	6.3
Cents per hour paid for	18.2	11.8	11.4	16.0
Cents per plant man-hour	19.5	12.7	12.3	17.2

Source: "Employer Expenditures for Selected Supplementary Remuneration Practices for Production Workers in Manufacturing Industries, 1959," Bulletin No. 1308, Bureau of Labor Statistics, U.S. Department of Labor, January 1962.

Fringe benefits in Canada

Item	*Percentage of payroll*
Paid time off	10.6
Vacation	4.1
Holidays	2.6
Rest, coffee break	3.3
Bereavement, jury duty, militia	.1
Other time-off pay	.5
Legally required outlay	2.7
Unemployment insurance	.6
Women's compensation	.6
Old-age security	1.5
Pension-welfare plans	6.4
Pension contributions	3.6
Welfare	2.1
Other benefits	.7
Special bonuses	1.5
Noncash benefits	1.0
Total	22.2

Fringe benefits in Canada—Continued

Industry	*Total fringe benefits as percentage of payroll*
All companies	22.2
Manufacturing	22.8
Food, beverages, and tobacco	26.6
Textile mill products	16.5
Paper	17.6
Chemicals	23.0
Petroleum	24.9
Iron and steel	20.2
Miscellaneous	22.1
Nonmanufacturing	20.5
Public utilities	23.6
Transportation	18.0
Trade	17.2
Finance, insurance	20.6
Miscellaneous	17.4

NOTE.—Data refer to 100 companies covered in a survey.

Source: Industrial Relations Counselors Service, Inc., "Fringe Benefits Costs in Canada, 1959."

Senator SPARKMAN. Mr. Curtis?

Representative CURTIS. One of the witnesses a couple of days ago pointed out that at the Alliance for Progress meetings there were not any Latin American businessmen present. Was this true in the LAFTA and the CACM meetings? Were these done through the political sector without the Latin American businessmen of the various countries being part of the movement? What is the situation?

Mr. GRIMES. Sir, I believe that the thing referred to at Punta del Este was certainly correct. However, since then each one of the missions or groups that represented the various participating countries in LAFTA have included businessmen from those areas.

Representative CURTIS. But in the inception?

Mr. GRIMES. At the inception, no. As you can well recognize, it was primarily a government-sponsored movement to begin with. Since then, however, it has encompassed the business group.

Representative CURTIS. I don't know that I do agree with your premise that it would have to be that way, but that is what I was trying to find out.

One of the points in dealing with Latin America that I think needs to be stressed is that a lot of this relates to the private sector versus the political sector. The Latin American countries have not developed a civil service system; so when we rely on the political sector there we are usually not relying on a trained corps of civil servants. It may be equally true, I don't know, that in the private sector there is also a lack of training. But I was interested in knowing what the setup was. You say that at least in the beginning it was political, but that now it has been moved over to where it is heavily oriented toward the private sector. Or how would you describe it?

Mr. GRIMES. I would not say heavily oriented. I would say it has become conscious of the great help and assistance which the free enterprise section can give the movement.

Also, there is a recognition of the fact that basically the work will be done by private investment in these areas.

There was a recent meeting of the Business International to look into the LAFTA held in Montevideo and the report of the Business International meeting went out of its way to highlight the fact that each one of the missions from the various countries did encompass businessmen, and they commented this was a very salutary development and they thought LAFTA was headed in the right direction because of that.

I might add that the Central American Common Market in its initial stages was primarily played or instrumented or orchestrated by the business community there. The business leaders there were really the ones who gave the impetus to the movement to begin with. I believe this is a very proper development.

Representative CURTIS. Thank you.

Mr. CLAYTON. I share with Mrs. Griffiths the belief in the importance of sugar. I have been urging this committee, the Joint Economic Committee, in writing for some time, to make a study into the economics of sugar. This is a committee that does not deal with legislation and, therefore, in some ways is better able to make objective studies. Perhaps I can encourage her to support me and persuade the chairman to do this.

I have felt for some time it was very important, whether we did it with sugar or whether we did it with coffee, copper, lead, zinc, or any raw material that becomes a base of the economy of other nations. This is very true in Latin America. It deserves this kind of study, and I would think we would make the study before we reach conclusions, but we haven't begun studying.

When you make these proposals, which I am very interested in, and I think I share the motivation, I can't help but remark about what this Congress did without much comment on the part of people like yourselves and others. Congress passed the International Coffee Agreement. We had it in the Ways and Means Committee. I wrote minority views, and I felt very deeply this was going in exactly the opposite direction from which you point out in your paper we should be moving.

So, I really worry a great deal about the difference between talk and proposals and the way in which we are actually moving.

A very similar thing happened in the field of textiles with the Geneva agreement moving further to licenses and quotas. These are the most regressive of all restrictions. I find when it comes to the specifics of fighting through some of these battles it is almost a lonely fight. It certainly was in the International Coffee Agreement. This, in my judgment, will do great damage in the long run in developing the economies of the nations that are involved in coffee. But that is a prejudgment, and I would like this committee to do a study of coffee, as well as sugar, to see what we can find out about the economics of it.

I have followed things in some degree through taxes and tax systems. There are essentially five basic taxes that could be paid by our businesses in Latin America and the Latin American businesses.

These are the income tax; the excise tax, whether it is at the manufacturer's level or not; the tariff; the property tax, which I think is by far the most valuable tax, the most economic and basic, and the one

that is practically nonexistent in Latin America as far as I can figure; and the payroll tax.

I wonder what the ratios were as far as a business in Latin America is concerned. This would vary with the countries. How much do they pay percentagewise in income taxes, excise, tariffs, property, and payroll? I think probably the bulk is through the income and a form of tariff.

Collateral with that, I have noticed that the incomes of the governments down there are heavily based on export taxes. We, of course, in our Constitution forbid, in effect, an export tax. A tax on exports is going to deter those very exports.

Our country, from its inception until the Civil War, relied heavily on tariffs as our source of income, and we shifted, and I think wisely so.

But certainly when we talk about the field of trade and how to encourage it, we ought to be thinking in terms of what sort of charges we are levying against it to support the Government, or whatever charges are being imposed. That is the reason I raise that question.

So the question would be, do you have information whether there are studies made along this line and could you supply what data there are for the record?

Mr. GRIMES. Sir, I don't know of any particular study that has been directed toward this thing but I would like to look into it in my bank to see what we have prepared and see what we may have available for you. If available, might we supply it for you?

Representative CURTIS. Yes. I would hope at some time to get around to looking into that.

The other thing that I find we haven't developed very much in these hearings to date is that this question of mobility of labor within these areas, and also that very important corollary question of immigration.

As I pointed out yesterday, we are dealing with areas that are underpopulated, not overpopulated. I think the figures you provided here show a market of 180 million people with twice the land area of the United States. The United States in relationship to other nations in the world is certainly not overpopulated.

The other item I have marked down was mobility of capital, and I would like to get into that aspect. The third thing that I would like to know a little more about is the antitrust laws, such as they may be. I mean by that, going into the full aspect of state trading, cartels, and so on—the relationship of the private sector to Government and subsidies. I don't believe there has been any real development along this line in the Latin American countries, am I correct?

Mr. GRIMES. I believe that is right, sir.

I don't think the question of mobility of labor is a really pertinent problem in Latin America today because there is obviously an oversupply of available labor, hand labor.

Representative CURTIS. Yes, but not an oversupply of skilled labor.

Mr. GRIMES. That is correct. This is one of the potential problems. The development down there has been at a pace where the shortage of skilled labor has not been a problem, I would submit.

Do you agree with that, Mr. Clayton?

Mr. CLAYTON. Yes.

Mr. GRIMES. However, I can see as these markets develop, under LAFTA and the Central American Common Market, if this industrialization takes place at the desired rate, the mobility of skilled labor might become a serious problem.

Representative CURTIS. I think it is a problem and I am just basing this on one or two specifics. But in Venezuela they had to import some thousands of skilled laborers from Italy in order to move forward with some of the plans that were necessary to develop their oil resources.

Mr. GRIMES. That is true.

Representative CURTIS. And certainly in referring to a country that is undeveloped, both undeveloped and underpopulated, the immigration policies, if any, of these countries become important. I am a little bit aware of the fact that through the United Nations, where we have a problem of locating displaced people, there was practically no cooperation. I think this is probably true today, from these areas that we are now talking about.

The United States, of course, was one that had most of the pressure put on it to accept these displaced people. We took the big load, and yet we were the ones who needed the skilled labor the least. I think this all becomes a very important picture in trying to understand how this might go.

Along with this, and this I haven't verified, I have heard recent reports that Japanese immigrated into Brazil in rather large, noticeable numbers. Again it was the skilled person coming in. I don't know how significant that is, but I think we are talking about the economies of these countries, and this becomes one of the very, very important things to know about.

Mr. GRIMES. I believe that the population of the Japanese colony in Brazil is between 200,000 and 300,000 people, mostly, as I understand it, in the truck farming industry, supplying commodities for the local market there.

Representative CURTIS. Yes.

Mr. GRIMES. It is certain that from time to time there have been great immigrations from Europe toward Latin America. I can give you the example of Chile and Argentina which are populated primarily by people of European backgrounds based on immigrations there.

Representative CURTIS. Right.

Mr. GRIMES. I was rather surprised to hear you say there was resistance in Latin America to the location there of displaced persons.

Representative CURTIS. Maybe apathy would be a better word than resistance.

Mr. GRIMES. I was wondering, sir, if it might not have been a case where the immigrants recognized that greater opportunity for immediate advancements or immediate betterment lay in this country rather than in Latin America and was not a matter of the skills that they may or may not have had.

Representative CURTIS. In my views to this subcommittee's report I called attention to what seemed to be a complete lack of homesteading laws which would tend to encourage their own people, as our people moved west into these areas that are underpopulated.

Senator SPARKMAN. Will the gentleman yield?

Representative CURTIS. Yes.

Senator SPARKMAN. I will have to leave now but Senator Pell is going to take the Chair. There is a bill coming up on the floor of the Senate with which I am expected to help. I want, however, to express my personal appreciation, and that of the committee to you gentlemen for coming here and giving these very able, clear, and interesting presentations. I apologize to you for having to leave, but I must.

Thank you.

Representative CURTIS. I just have a few more questions I wanted to direct attention to.

One, in regard to Canada: What are the ratios or the percentages of trade that now exist between Canada and the United States, which are completely free of restrictions? It is a very sizable amount, isn't it?

Mr. LEA. Of Canadian exports to the United States about 60 percent are duty free, and the largest items, if I recall, are pulp and newsprint and farm machinery. We have published a chart showing this and I would be glad to furnish it for the record.

Representative CURTIS. Yes, if you would.

Representative CURTIS. I have always been surprised every time I look at the figure to find how much of our exports and imports in this country are completely devoid of restrictions. When we direct our attention to the areas where there are tariffs or controls, we tend to lose perspective, and that is why I wanted to get this in context. Although I don't know the exact percentage, I think a very high percentage of Canadian-United States trade is free.

Mr. LEA. Of course, the fact that there is such a large concentration of some of these products is precisely because they are duty free.

Representative CURTIS. Well, it could be, but I don't know that it is. That is a fair observation that would bear on it. I wonder whether that is so. This isn't to argue a point, but it is simply to get that in context because I think my observation is correct. We already have developed a tremendous trade area, that is between Canada and the United States, that is quite integrated and could aptly be described as a common or free market.

In mobility of labor, which is one of your criteria, certainly it is very gratifying.

Mr. LEA. Well, we have between Canada and the United States at this moment probably more mobility of labor and mobility of capital than exists in Europe.

Representative CURTIS. Yes.

Mr. LEA. But we do not have a program to provide free trade at this time.

Representative CURTIS. I have a feeling that without anybody in the government watching it, this has happened. I sometimes worry that when the government starts looking at things, they start going in the other direction. I think the recent trend is that when government has intervened we find more restrictions rather than less. The areas where we are freeing up is where the private enterprise system has just been going along and following out its pursuits.

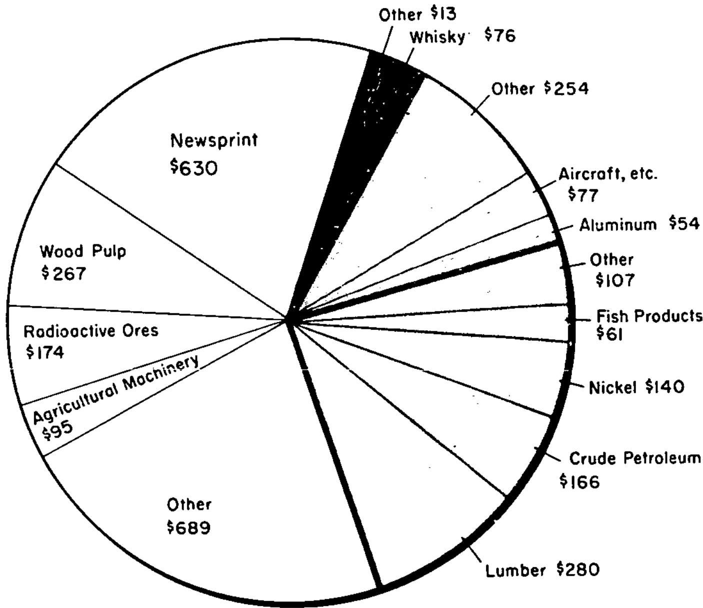
You list the principal steps providing for these various things.

I just wanted to add two other points just for your comment. I think they are so vital today. One relates to patents or laws on how you recoup the money you are willing to risk in research and develop-

(The chart referred to follows:)

FIGURE 3.—*U.S. imports from Canada: distribution by tariff levels*

(Values in Millions of Dollars)



U. S. Tariff Level

DUTY FREE $1,855 (61 percent of total)

DUTIABLE AT
5% or less $754 (24 percent of total)
6% to 19% $385 (12 percent of total)
20% and over $89 (3 percent of total)

Source: 1960 and 1961 figures from H. S. Piquet. "The U.S. Trade Expansion Act of 1962: How Will It Affect Canadian-American Trade?" Washington, D.C., Canadian-American Committee of the National Planning Association (United States of America) and the Priavte Planning Association of Canada, March 1963.

ment. I call it patents, but isn't this coming to be greatly significant in these areas where we are trying to develop free trade and common markets?

Mr. LEA. Yes, it is; and the Commission of the EEC in Brussels is working to formulate a common patent law for Europe. In the case of Canada and the United States this is something where if any harmonizing needs to be done, it could be done easily because we do not have a New York State patent system and a New Jersey patent

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system, and 48 others. I believe that we have a single national system here, and Canada has one up there. It should be easy to put these two national patent systems together into a common system.

Representative CURTIS. I think there is considerable cooperation in that area now, if I am not mistaken.

Mr. LEA. Well, the Canadian-American Committee was formed to look into the squeaky wheels and we haven't heard any squeaks from the patents area so presumably there are no difficulties now and I don't think that free trade would make any appreciable difference.

Representative CURTIS. I think it would help. But to me there is a criterion of whether you have and are establishing a free trade area. The very fact that we have problems in the European Common Market in this area demonstrates how vital and how important it is. I have felt, incidentally, that some of the problems in our chemical industries, and what they think are tariffs, are really the inadequacies of our patent laws in international trade. Here we don't have sufficient protection for the economic process of investing money at risk and innovation, in research and development, because people take the results of all of this investment and money in various European countries and then take over the market without permitting those who spent the money to have some opportunity of recouping this investment.

The second point is the antitrust legislation where Canada and the United States are pretty much in accord. It indicates that we have a pretty good common market going. This they really haven't implemented in the Rome Treaty yet as near as I can figure. Is that correct?

Mr. LEA. Yes, the EEC is having a considerable amount of difficulty in implementing their program of economic integration; there is a series of articles on this now, five articles in the Journal of Commerce.

Representative CURTIS. If we ever start on that in Latin America, where the cartels seem almost a way of life, I think we are going to run into similar troubles.

But at least these are our criteria.

You raised a question in your statement I worried about, and that is the fact that between Canada and the United States we have our State systems and they have their Provinces. You raise this as a real problem involved in working out arrangements with Canada, and I frankly don't see where that is a problem.

Mr. LEA. It would be a problem only if we wanted to embark on a program that would provide, for instance, identical State and Provincial taxation for industry throughout Canada and the United States.

Representative CURTIS. Why would we want to? We work all right in the United States——

Mr. LEA. That is precisely the point I am making here.

Representative CURTIS. You don't think it is necessary?

Mr. LEA. Americans and Canadians are quite happy to have their different States and Provinces do things in different ways, and so it would be very difficult to imagine how we would want to give up that diversity.

Representative CURTIS. The point I am making is we certainly wouldn't have to, though, would we?

Mr. LEA. No.

Representative CURTIS. In other words, it isn't a barrier. I thought you had posed it as being a possible reason that would deter us from getting together. I think we both agree this is a fine thing to have this kind of diversity.

Mr. LEA. It would deter us only if we picked up the blueprint for the EEC and tried to follow it.

Representative CURTIS. I couldn't agree more, and I think that is one of the places where they are making a mistake.

Senator JAVITS. I have to get to the floor by noon so I would like to ask two questions.

First, I want to thank Mr. Clayton for mentioning me so favorably. It is an unexpected pleasure and I am very grateful. I shall pursue the subject. I am grateful for your implementation of it.

I ask this question of the whole panel.

Congressman Curtis spoke about the International Coffee Agreement and he thought it went the other way from this general idea. Of course, in the first place we have nothing now. We don't have a hemispheric free trade area so we have to do something about it.

To me what Mr. Clayton has testified to is the fact that the bell is tolling on us in Latin America. We are racing against time, and time is very short. We will have more Cubas than we already have, in my judgment.

So, I would like to ask you all this question: What do you think about this commodity stabilization measure like the International Coffee Agreement? Is it in accord with, contrary to the thesis that you respectfully espoused here, and what do you think about its desirability? If we can start with Mr. Clayton.

Mr. CLAYTON. Senator Javits, I am not a believer in international commodity agreements. Usually they are entered into to advance prices of commodities. I don't think that they achieve that purpose in the long run, and I think they have many objectionable aspects to that type of international agreement.

Senator JAVITS. Mr. Lea?

Mr. LEA. The product which is under scrutiny for a possible commodity agreement between Canada and the United States is, of course, wheat, and it is a little too early to say what the feelings are in Canada about this. They are doing very fine under their present system now but we may well have to consider with them some further kind of an arrangement on wheat.

But as soon as you take a product like that you realize there are other countries involved. There is Australia involved, there is Europe involved, and I would say that within the next year or so there will be some very serious discussions between the Canadians and the Americans on wheat.

Now, the Canadians and the Americans would not discuss coffee in the sense that this is a bone of contention between us. It is not the type of major Latin American commodity which is produced in any quantity within Canada or the United States.

Senator JAVITS. Mr. Grimes, will you give us your judgment on this International Coffee Agreement specifically?

Mr. GRIMES. Well, I certainly echo Mr. Clayton's reaction to commodity agreements in general.

However, in justification for the coffee agreement I believe we have to bear in mind the importance to Latin America of coffee as a product. Throughout Central America, as we know, this is the prime source of income to them, Brazil also, and Colombia.

I believe in the context of what we were trying to do in Latin America, a way to demonstrate our community of interest with their problems, there was a place in the scheme of things for the coffee agreement as such.

Senator JAVITS. And in the absence of other things which you have testified to?

Mr. GRIMES. Yes.

Senator JAVITS. Just one other question if I may, Mr. Grimes. I noticed in your statement you made quite a point about U.S. investment, the fact that it is drying up, the reasons for it, and so on. I would like to ask you what about European investments?

Mr. GRIMES. European investment in Latin America?

Senator JAVITS. Right.

Mr. GRIMES. The trend is up, of course, as you know. And I hope that your ADELA thing is going to tee off a flow of European investments and I certainly think there is a place for it in the scheme of things in Latin America. The European trade to Latin America as you know—buying and selling—has increased perceptibly since World War II. I don't think it has gotten back yet to where it was before the beginning of World War II so we are still ahead of the game. To repeat, I think there is a definite place in the scheme of things in Latin America for a very substantial increase in European investment in the area.

Senator JAVITS. Now, is it a fact that we can hardly expect to obtain the cooperation of Latin American countries with regard to mobility of labor problems, immigration problems, all the problems which we lay at their door, including a restrictive trade policy unless we give them some better economic outlook according to their terms of trade than they have today?

Isn't it a fact as it is in any business, and certainly Mr. Clayton is an outstanding businessman, that lots of things lean on each other? Unless you go in for something like the creation of common markets, or free trade areas, I feel as does Mr. Clayton, you are not going to get anything except the danger of more Castroism and more Cubas because we are giving them no way out. The noose is just tightening about their necks economically. They are all governments which are elected. If we don't give them a way out they are going to find one that may be more extreme and distasteful to us.

Now, the Chase Manhattan Bank has so many branches down there that you are really an expert witness on that.

Mr. GRIMES. I certainly concur with you, Senator Javits. It is definitely up to us to make every effort to see that these regional markets prosper and are a success because of the potential impact they will have on the growth potential of the area.

Senator JAVITS. Well, I am very grateful to the witnesses and again to Mr. Clayton, and I think the hearings conducted here by Senator Sparkman are tremendously important to the whole Nation.

Thank you, Mr. Chairman.

Senator PELL. Senator Jordan?

Senator JORDAN. Just briefly, gentlemen, I wanted to express my appreciation to the panel for the very fine papers you have presented, and the great avenue of questions it opens up. Because of the shortage of time, I am going to confine my remarks rather specifically to the effect which a free trade throughout the Western Hemisphere in raw materials might have on the raw materials producing areas of the United States.

I raise this question because I come from the West, and when you get west of the Mississippi River the dominant part of the income of the Western States comes from the extractive industries, the production in my State of Idaho of lead and zinc, of meat and wool products, of wheat, of sugar, of dairy products, of lumber and down in the Southwest, of cotton.

Now, these basic and primary commodities are very important to our economy there. The principal component costs of the production of any of these commodities are labor, taxes, and interest.

Now, if we are to compete on a Western Hemisphere free-trade basis without tariffs and without quotas, what dislocations are likely? Have any studies been made in this regard?

Mr. CLAYTON. Senator Jordan, I don't know that any studies have been made of that subject, but I do know that in the Trade Expansion Act of 1962, that provision is made for relieving the most pressing of problems of that kind that result from import competition, and a commission is set up to administer that aspect of the Trade Expansion Act, to retrain labor and to help out capital that might be involved, and I think that also is the same with the European Common Market situation.

They have a provision in the treaty of Rome whereby a bank can help out in situations of that kind where import competition will upset industries and labor.

Senator JORDAN. Yes, I am well aware of the provisions of the Trade Expansion Act of 1962. I was one of eight Senators who voted against it, and yet I do know that its objectives are laudable. But because I come from a State whose economy is wholly dependent on extractive industry, we are finding it very difficult to live with the kind of program that would prevail under the Trade Expansion Act.

It is quite well to say that we can take the people who were employed in industries such as lumber, beef, and livestock, and retrain them to make television sets or shoes or something like that, but what of the great resources, the forests in the timbergrowing areas, the grass on the grazing lands, the lead and zinc and the minerals in the ground? Perhaps we could take care of the people who are displaced by this kind of free and open competition, but what of the resources?

Are they to stay there until such time as the standard of living of the competing countries rises to the level where we can go back in and take out our lead and zinc and saw our trees into lumber and so on? That is my basic problem.

Mr. CLAYTON. Senator Jordan, it certainly—the proposal that I make with reference to a hemisphere, Western Hemisphere, free-trade area, certainly proposes problems such as you have well stated, and they will have to be dealt with.

Senator JORDAN. I agree that the objectives are laudable, but there will be dislocations. Either our costs must be reduced so that we are

competitive, or the costs of our competitors, by the raising of their own standards of living, will have to come up. I don't know where the balance is going to be struck. But I do see a very real and protracted period of dislocation if anything like this takes place.

Mr. CLAYTON. I think there is no question but what the standard of living of the peoples who would be favorably affected by such a program as I have outlined would certainly rise.

Senator JORDAN. Yes.

Well now, getting over to Mr. Lea, and his discussion of our dealings with Canada. We have had the Canadian representative with us for the past 2 days; we have enjoyed a very fine exchange of ideas with them, but here is a situation that develops with respect to lumber. Canada at one time enjoyed a very fine outlet for their sawed lumber in England. Because England can buy lumber cheaper in Russia, the Scandinavian countries, they are buying lumber in Russia and in the Scandinavian countries. Imports from those areas are thus replacing in an English market lumber that formerly came from Canada.

Canada, and the Canadian mills seeking an outlet for their sawed lumber, turn naturally to the United States, and we do enjoy a very favorable balance of trade with Canada, $1 billion a year in our favor. Yet the very fact that this English market was taken away from them by imports from Russian and Scandinavian countries, directed their attention to our markets. They can produce lumber and ship it into our markets much cheaper than we can from our Western mills by reason of several natural advantages: Cheaper stumpage rates, lower labor costs, a favorable balance of exchange, the fact they can ship in tramp steamers and we are required under the Jones Act to ship in American bottoms, the fact they can move into a market that is developed by American lumber people, and advertising and promotion. All of these advantages inure to their benefit so that the end result is that Canadian lumber can be placed on the Atlantic seaboard of the United States at $10, $15 a thousand cheaper than our Western mills.

These conditions are having an almost disastrous effect on Western sawmills. These are some of the problems I would hope that before we close these discussions some attention can be paid to, the dislocations that will prevail under a free and open exchange and trade between the countries.

Mr. LEA. If a free trade arrangement was made between Canada and the United States, the present U.S. tariffs on sawn lumber would be gradually eliminated but those tariffs don't amount to much now anyway. They are about 1 or 2 percent.

Senator JORDAN. Right.

Mr. LEA. So the effect of that would be negligible on increasing imports from Canada.

On the other hand, you would reduce the present tariffs on plywood from what they are in both countries—about 20 percent ad valorem—down to zero. So the thing to watch would be what would happen in plywood.

Would the United States prove to be the more efficient producer of the two in plywood, and perhaps Canada, because of the situation of its forests and so forth, might be the more efficient producer in lumber.

The other thing that would have to happen with free trade would be that we have to do something about the Jones Act. The Jones Act is an amazing piece of legislation; it is, in effect, an import restriction which the United States imposes on its own producers. Presumably if there was a free-trade arrangement between Canada and the United States this is one of the kind of laws that would have to be dealt with. Either you would have to extend the Jones Act to all of North America or you would have to do away with it.

Now, doing away with it or harmonizing the Jones Act would be of great help to those U.S. producers who ship by water.

Senator JORDAN. Yes.

Mr. LEA. It wouldn't help the inland producers, it might actually hurt them somewhat. This is another kind of effect that would take place.

Now, when we look at developing free trade between Canada and the United States, we recognize that the greatest problems of adjustment would not occur in industry, because you can always "buy" a more efficient industry, or you usually can, if you put up enough capital anyhere to modernize an inefficient industry. But where we consider raw materials which are second rate or more expensive to extract from field or forest or ground, then no amount of capital may ever make you competitive. So we foresee the biggest adjustment problems would come on both sides of the border with these raw materials and many of them would occur in Canada.

For instance, in the Maritime Provinces they mine coal under the sea 7 miles out, and as I mentioned before this coal gets a sizable transportation subsidy to the market. If that were done away with it probably would mean closing down those mines and they would have to accept that. They would have to provide something else for the people in the area to do. In our country, meanwhile, on other raw materials there would undoubtedly be the same kind of adjustment, and that is why we feel if there was free trade between Canada and the United States there would have to be a prolonged transitional period for certain raw materials to cover these kinds of problems, so there would be a lot of time for adjustment assistance programs to actually work.

Senator JORDAN. Where the costs would be equated more or less by common agreement, though, or common laws or rules or something that would give reasonable parity between competitors in different geographic areas.

Mr. LEA. I think what we would do is to give each producer equal opportunity, but on the other hand, we wouldn't want to disturb the fact that the whole idea of a common market is to let the law of comparative advantage operate. So if our coalfields are much more efficient than the Canadian coalfields, I don't think we would want the Canadians to do anything to try to subsidize their production or transport of coal. And by the same token, if what happens in the forest is that our public saw timber is bid up by the people who want to make plywood and pulp and lumber to a greater extent than theirs is so that our stumpage rate is bid up much higher than theirs, I don't think Canadians would want to see us in some way subsidize stumpage rate for lumber.

I think what would be equitable is to have absolutely the same rules in the forests on both sides of the border and then let the chips fall where they may.

Senator JORDAN. Thank you.

Thank you, Mr. Chairman.

Senator PELL. Mr. Curtis?

Representative CURTIS. Mr. Clayton, would a Western Hemisphere free-trade area for only raw materials circulated freely in the whole area be compatible with the GATT?

Mr. CLAYTON. I didn't quite understand that question, Mr. Curtis.

Representative CURTIS. In this Western Hemisphere free-trade area that you projected, if we were just allowing our raw materials to move freely, would that be compatible with GATT? I want to direct your attention to the section in GATT, article 24, which requires elimination of duties, et cetera, with respect to substantially all the trade between the constituent territories. I think your proposal more or less was limited to raw materials, and I understand the practical reasons, but I am just posing the question, would this be compatible with GATT?

Mr. CLAYTON. I took it when I wrote the statement that it would not be incompatible with GATT, but I might be wrong about that. I can't be positive about it until it is put up to GATT to decide.

Representative CURTIS. Even if it were, of course, there could be a waiver. They do this on some of these things for the special reasons that exist. I did not raise the question as adverse criticism, but really for speculation to see where we would be going.

Mr. CLAYTON. Well, it is a question well raised, and I am not sure that I am right about it, but I think that it could be shown to GATT that it was the right way and that any objection would be overcome.

Representative CURTIS. Thank you.

Now, just a little bit on the colloquy Senator Javits had with respect to the International Coffee Agreement. There is no question, of course, of the importance of coffee to a number of these Latin American countries, particularly the Central American countries mentioned, where it is almost the base of their economy. That was not the point.

The point I was raising was in respect to the very fine statements, I felt, that Mr. Clayton made with regard to what happened with sugar when we started the cartel setup in 1934. I question whether this kind of operation now going into coffee is the real way to help these countries in the long run. Sure, we have problems here. But do you solve them through improvising or do you do it by getting down to the base of it?

I wanted us to study sugar because Cuba had become almost a one-crop economy. The little studying I was able to do indicated, and this is quite interesting, that up until 1890 or thereabouts Cuba had a pretty well diversified economy. This shift to a single crop economy occurred almost within the 20th century. I certainly think that in the long run it has hurt Cuba. To encourage these countries to remain single crop economies, I think, would be a basic mistake.

Furthermore, in these types of agreements, and this is what I tried to spell out in my minority views, you don't allow the advances in productivity in the growing of a commodity and possibly in the distribution to enter into the picture. You throttle competition. You freeze it.

My suggestion is that because we do need stabilization of prices we should look into the development of futures markets, if they are properly regulated. But it seems that futures markets are the favorite whipping boys of some of our economists.

But I don't think we have analyzed what a futures market, if properly regulated, can be. It is the price for stability. Those who are in our futures markets in the United States are often very wise and intelligent men who perform a great economic service. What is the weather? Who has planted what? What are the demands this year? They take up the risk from the standpoint of the farmer, the producer, and those, like the Purina Co. in my own community of St. Louis, who have to buy in vast quantities but don't want to take the risk. They want to stabilize their price, and so this mechanism provides this service for both the producer and the consumer. The people who are in the futures markets become great experts, men of deep knowledge in the field of production. I don't know why we can't start going along those lines in some of these areas.

Mr. CLAYTON. Mr. Curtis, I agree with everything you have said about the futures market, and I think that one of the tragedies of a Government control of cotton production and cotton market has been that it has practically destroyed the futures market in this country.

Representative CURTIS. I didn't know you and I were in such accord on so many things, but it is very obvious that we are.

Mr. CLAYTON. I have had many years' experience in this, in using futures markets for hedging purposes, and I agree with everything you say.

Representative CURTIS. Thank you, sir.

Mr. GRIMES. I presume neither of you refer to the present day thing in New York with futures in vegetable oil.

Representative CURTIS. Well, it is very proper to make those remarks. Any mechanism can be abused. Sometimes the abuses reveal that the mechanism itself is fundamentally unsound, but it behooves us to look to see when there are abuses. Is it something that is fundamental to the mechanism that makes it bad or is it something that needs correction?

I know they did the same thing with onion futures, a tragic thing, before this very committee. They denigrated it, and of course, some of the people involved in it deserved some of the epithets. But the mechanism itself in my judgment was sound economically. In our concentration on the abuse, we threw out the baby with the bath water. It is right to call attention to such situations, just as we did in the stock market which produced the SEC, which I think was a very fine development. But we didn't eliminate the stock market, which is so basic in the private enterprise system, in the market economy.

Would you comment on that?

Mr. GRIMES. I certainly agree with both of you that basically the futures market represents a great potential toward the stability of commodity prices.

However, getting back to your coffee agreement, given the facts as they existed at the time the agreement was perfected, it seemed to me that there was an area in which, even sacrificing the long-range points that we all have for commodity agreements—that there was an area here where a definitely specific dramatic step could be made to-

ward helping Latin America cure a real, basic today's problem and I think for that reason I said while I did not——

Representative CURTIS. I might be willing to buy that kind of argument if there had been emphasis on the fact that this was purely temporary to solve a problem and that it was going against our long-range objectives. But I regret to say it was not presented that way. It was presented as if this was going to help the consumer. It was said that it was not going to hurt the consumer in the United States, which was nonsense, of course. It was going to raise prices. And I was willing to take the political heat which some others were not. If I thought it was necessary, I might have been in favor of the coffee agreement. If it had been approached on that basis, if I saw that the guidelines were being put in that were to make this only temporary, and if it was going to meet the basic problems, I would have supported it.

But that isn't so. The sugar cartel setup, going back to 1934, gives us the picture. I mentioned the textile agreement in Geneva to Secretary Hodges and asked how he was going to determine how much textiles were going to come in from a particular country and at which port of the United States. His answer was, "Well, we would use the pattern of 1960." To that I said, "Boy, that demonstrates exactly what you are getting into. You are freezing the structure as of that date. How can you move forward in that kind of approach?" And yet our country, our administrations—it isn't only this administration, it existed in the same approach of the previous one—toward more and more of these techniques.

Sure it is easy. It is dramatic. You are going to do something, but in the long run I think it is damaging.

One other question of fact. The Canadian paper mentioned the fine development of the telephonic communication with respect to, or was it in your paper?

Mr. GRIMES. I think it was in mine, sir.

Representative CURTIS. Was it? I wanted to ask how much of that really did exist between the countries involved. Is there this kind of communication between São Paulo, Buenos Aires, and Rio?

Mr. GRIMES. I think in general you can say that the telephone communications in Latin America are very, very outdated, very primitive, to say the least.

Representative CURTIS. Yes.

Mr. GRIMES. Very frequently I have heard it said it is quicker to catch a plane in Rio and go down to São Paulo, conduct your conversation and fly back, than it is to have a telephone conversation. The distance is the same as between here and New York. The question in reference is made about the Central American common market and the need for this communication system in those countries.

Representative CURTIS. You are developing the need. I guess I got it wrong, I forgot to note which paper it was in.

What you are now saying is what my understanding was. Another major study nearing completion is a draft project for a Central American telecommunications network. That is a draft for the future and you point out the importance of it.

Mr. GRIMES. Yes; it is one of the big stumbling blocks to an integrated system there.

Representative CURTIS. Yes.

In Venezuela I remember talking to one business group where they actually set up their own infrastructure in this respect because they wanted to have their own communications system. But again I want to point out that one of the things I wanted to contrast was the Canadian-United States setup. I think a great deal of the criteria that I would apply to defining a common market is already in existence between Canada and the United States. In so many ways this is a common market now if we use these criteria to relate to our definition. By saying that, I do not mean that we shouldn't continue to move. The Canadian-United States situation is way ahead of what I would judge the European Common Market is at this stage, and certainly way ahead of the two Latin American common markets.

Did you want to comment on that?

Mr. LEA. Yes; I agree with you. We can just dial an area code and get Montreal or Quebec or for that matter anywhere in Canada.

Representative CURTIS. Yes; and yet aren't these part of the criteria that need to be developed and related to observations and as checkpoint to determine how far along we are in developing a common market?

Mr. LEA. They certainly are a criterion of a de facto common market, but for a de jure common market, as it is generally considered, you have to have a free trade agreement at the core.

Representative CURTIS. Well, thank you for using——

Mr. LEA. Between Canada and ourselves we don't have the free-trade core, that is all.

Representative CURTIS. Thank you for using those two words because the de facto is what I am primarily concerned about. What bothers me is that the de jure is interfering with the further development of the de facto.

In other words, government seems to be following up that which is normally coming about. The Government didn't know it was happening and it just normally developed between Canada and the United States.

Mr. LEA. Well, I would say as that what prevents the normal development which you mention is not actions by our Government but a very natural reluctance on the part of the Canadians to get any closer to us. In fact, they feel they have too much de facto integration now.

Representative CURTIS. I know.

A lot of the complaints you are making about how New York seems to be running things in Canada is the same thing I hear from businessmen in St. Louis. We sometimes think we are an economic province of New York.

Well, thank you all for what I regard as very splendid and stimulating papers.

Mr. Chairman, I would like to ask unanimous consent to put in at the conclusion of today's record an article that appeared in the Bank of London and South American Limited Quarterly Review, volume III, July 1963, No. 3. The article discusses "Foreign Investments in Latin America, the Role of Private Capital."

Senator PELL. Without objection the article will be included in the record at the end of today's proceedings. (See p. 442.)

I regret that I was not here for the reading of your papers but I have had the opportunity to read them and congratulate you on them.

I have just two questions: (1) Have you found that the creation of LAFTA, the Latin American Free Trade Association, has slowed down in any way the flight of private capital out of Latin America? This leads into another factual question: Is the flow of private capital out of Latin America for investment in Europe or the United States larger, about the same, or less than the flow of American private capital into Latin America?

Mr. GRIMES. I think I see what you are driving at.

The flow of capital is a very hard thing to trace to begin with, as I am sure you know. There are some certain guidelines that we try to go by in the banking industry in New York. I would say that the development of LAFTA as of now has not had a significant impact on the stability or the mobility of capital.

I think that the potential of LAFTA is such as to have a very significant impact on the possible inflow of capital into the area.

The biggest single factor, I would think, that controls the flow of capital is this very elusive thing called atmosphere, investment atmosphere. There is a very tarnished picture at this moment in this respect in the LAFTA countries because of political upheavals or internal economic policies which are not conducive to sound investments.

At the moment there is a lack of the proper atmosphere for investment in some of the LAFTA countries. I think that when this atmosphere starts improving that you will see an inflow of investment from the United States and from Europe and the other normal sources of investment.

I would guess that at the moment the inflow of investment to the area from the United States is less than the outflow of money out of the area to the United States and Europe. This is just a guess; I have no statistics, nothing specific to refer to.

Senator PELL. This is what I suspect, too, without knowing the facts, but it does make our whole private investment program seem a little bit like the boy putting his finger in the dike. If, even as we increase the amount of private capital invested in Latin American development, more capital is going out than is coming in, what steps can we take to prevent this situation?

Mr. GRIMES. Well, the same elements that make for a hesitancy for investments in Latin America are the same elements which cause the outflow of local money to the United States, again, the lack of political stability.

It gets back to that, and it opens up the broad definition of this area of atmosphere. It is practically impossible to define as such. Certainly, from the negative approach you can name a lot of things which shouldn't exist in these countries if the atmosphere is going to be proper. But the investment program, the guarantee program to which you refer, given a normal type atmosphere, would certainly add a great deal toward encouraging the inflow of investments into Latin America.

There is no question, I believe, on that point. Again, it gets back to the point I think, though, of the existence of proper investments atmosphere.

Do you agree with that, Mr. Clayton?

Mr. Clayton. Yes, I do. But I would like to make the point, Mr. Chairman, that in the initial stages of LAFTA, that you can't expect a great deal from it because the LAFTA countries all produce pretty much the same materials for export, that is, raw materials.

Later on when you get the duties down to close to zero, if they ever get them that far, then I think foreign capital will come in to establish manufacturing industries based on the whole LAFTA population and area instead of geared to some little country in which the factory might be located.

Senator Pell. One further question. Do you gentlemen feel that it might be preferable to continue with the most-favored-nation arrangement on an individual basis, rather than encourage the creation of these various regional groups which could complicate the MFN concept that we have developed in the past?

Mr. Grimes. Personally, I would think that the regional market concept is the indicated step for Latin America at this time. At the moment there is no integration at all. It is quite impossible to conceive of some of these markets growing to be large enough to where they attract investments because the markets themselves are individually—the country markets—just not big enough to investors to establish a plant.

These plants do seek areas where there is a wide market possibility. To do this thing on a most-favored-nation basis, as I visualize the thing, would not be as effective by way of developing these regional markets and making these markets big enough to be attractive to investment.

Senator Pell. Thank you very much.

Mr. Curtis?

Representative Curtis. I forgot to mention it. I am not going to develop it at this point, but it is a big subject. This is the problem created by the African countries who are producers of profitable agricultural products which are in competition. Their markets seem to be tied up in European countries, while we in turn are developing the markets for South America. It creates some very serious problems, and possibly will be involved to some degree in our discussions in this Kennedy round going on right now.

It is a big subject, but if any of you would comment on that problem. Would you, Mr. Grimes? Is it a serious one, as you see it?

Mr. Grimes. The tendency toward our concentrating on hemisphere trade as compared to others?

Representative Curtis. Here is the picture as I see it. Here we are trying to help the Latin American countries in their developing these common markets, and Europe seems to be working out a tendency quite similar with the African countries which are likewise underdeveloped and dependent on some of these same agricultural products. I worry about where this is all leading us, if we start working it in too much of a straight line, where we are taking South American tropical agricultural produce instead of encouraging Western Europe to take some of them or at least to get competition, if we can, between these two very important undeveloped areas.

Mr. GRIMES. Well, I don't really see a conflict there, Mr. Curtis. After all, you already have the European Common Market. It is an integrated area. They have had traditional ties with Africa which we have not had. The same thing we can say about ourselves in Latin America. The significant thing is, we are destined to share this hemisphere with Latin America for a lot of years yet, and I think it behooves us to see to it that our own traditional trade channels are kept open and allowed to expand.

Representative CURTIS. Well, I just wanted to have it on the record here because there is a big area, I think, and one that we should develop on its own bottom.

Mr. GRIMES. Thank you.

Senator PELL. Thank you, gentlemen, very much indeed.

I think this winds up this series of hearings before the subcommittee.

The hearing is adjourned.

(Whereupon, at 12:45 p.m., the subcommittee adjourned subject to call of the Chair.)

(The following exhibit was ordered placed in the record of the hearing during testimony:)

FOREIGN INVESTMENT IN LATIN AMERICA: THE ROLE OF PRIVATE CAPITAL [1]

At a time when so much emphasis is being placed on the expansion of official aid programmes to meet the capital needs of Latin America and developing countries elsewhere, it is perhaps worth recalling that until the second world war almost all the capital that entered Latin America was provided by private investors. In a period of little more than half a century, from about 1860 to the outbreak of the first world war, the inflow of foreign capital, which brought about a revolution in the economies of many of the republics, proceeded almost without restriction on the part of either the supplying or the receiving countries, and such measures as host governments took to influence the movement were generally to encourage the inflow by means of concession contracts. Bonds issued abroad by Latin American governments and subscribed by private investors provided many of the funds to finance public works and urban improvement; direct investments were channelled into export industries, and they also created much of the economic infrastructure—railways, port works, and utilities—besides contributing largely to the development of trading and financial services.

Although the Latin American republics are now inclined to resent the outward-looking orientation which such investments gave to their economies, it is difficult to see how their evolution in that era could have proceeded on other lines. Among the direct investments that played a decisive part in economic development may be mentioned the mining industries in Chile, Peru, and Mexico; petroleum in Mexico and later in Venezuela, and the railways and the meat-packing industry in Argentina. In Argentina, indeed, the inflow of foreign capital—and of immigrants—helped to transform the country in two generations from a region on the very fringe of the world economy into the most prosperous and, culturally and politically, one of the most advanced nations of Latin America.

In the second half of the nineteenth century, when the inflow of private investment into Latin America first began to assume significance, and until the first world war, British capital provided by far the most important contribution. United Kingdom investments in Latin America are estimated to have reached £757m. by 1914; the inflow of British capital into Argentina and Brazil alone probably exceeded £200m. between 1907 and 1914. By this time investments in all Latin America, of which nearly half was in railways and about one-third in government bonds, accounted for about 20 percent of British investments abroad.

At the turn of the century, after the Spanish-American war, United States investors became increasingly active in Latin America, especially in the neigh-

[1] Reprinted from the "Quarterly Review," July 1963, Bank of London and South America, Limited, whose Chairman is Sir George L. F. Bolton, K.C.M.G.

bouring countries, developing sugar production in Cuba and the banana trade in the Caribbean, mining in Mexico and also in Chile, petroleum in Mexico and elsewhere, railways and public utilities in Cuba, Mexico, and Central America. United States investments in Latin America are estimated to have risen from U.S.$308m. in 1897 to U.S.$1,649m. in 1914 (nearly half of total U.S. overseas investment at that time) of which U.S.$1,281m. were in direct investments. Among the European countries, France began investing in Latin America on a substantial scale in the 1880s, and investments are estimated to have been trebled between 1900 and 1914, to reach about 6,000m. francs (U.S.$1,200m.), when they represented 13 percent of total French investments overseas—chiefly, like those of Britain, in government bonds and railways. German investments, small in scale before 1900, increased considerably in the years up to the first world war when they were estimated at 3,800m. marks (about U.S.$900m.). Significant amounts of capital were also received by Latin America from Belgium, the Netherlands, and Portugal. The total nominal value of foreign investments in Latin America on the eve of the first world war has been placed at U.S.$8,500m.; of this total one-third was invested in Argentina, almost a quarter in Brazil, a similar amount in Mexico, and the remainder largely in Cuba, Chile, Uruguay, and Peru.[2]

THE YEARS BETWEEN THE WARS

After the first world war the U.S.A. became firmly established as the principal source of capital for Latin America. Investment conditions remained on the whole unchanged, both in the capital-exporting countries, where freedom of capital exports remained the rule, and in Latin America, where governments generally continued to allow the unrestricted entry of foreign capital, maintained full convertibility of their currencies, and kept taxes low. But the international position of the United Kingdom had changed and the outflow of British capital to Latin America was very much smaller than before 1914; new Latin American issues on the London market and new direct investment, including petroleum development in Venezuela, were offset by amortizations and other withdrawals of capital. France ceased to be an important source of new funds, and there was little change in French business investments in Latin America. German investments, though remaining important in some fields of manufacturing, notably chemicals, and in trade and aviation, were affected by war-time and post-war changes of status through transfers from nonresident to resident ownership. Substantial investments made by Italians in Argentina, Brazil, Chile, Peru, and Uruguay may also have acquired resident status. There appears to have been little net change in the investment holdings of other European countries in Latin America.

United States investments, on the other hand, increased rapidly in this period. There was a substantial inflow of capital from the U.S.A. during the first world war, when the value of United States investments in Latin America increased by about a half to U.S.$2,406m., and in the decade after 1919 when it was more than doubled to U.S.$5,244m. The Latin American countries were eager to borrow abroad, and conditions in the U.S.A. were favourable to an increased outflow of capital which, during the brief period 1925–29, may well have exceeded that from the United Kingdom during the peak period of 1904 to 1914, even allowing for the rise in prices. Especially noteworthy was the number of Latin American bond issues floated on the United States market, many of them under conditions that later gave rise to widespread criticism. The net nominal value of issues publicly offered in the U.S.A. between 1920 and 1929 amounted to U.S.$2.176m. (of which U.S.$1.504m. were government or government-guaranteed, and U.S.$672m. were private). Direct investments also expanded during the war years and the 1920's, and United States investments in Latin America, hitherto concentrated in the nearer countries, spread throughout South America. At first, the emphasis was principally on agriculture—especially sugar production—minerals, and petroleum, where the focus shifted from Mexico to Venezuela. In the later 1920's there was a significant expansion of investment in public utilities—especially electric power—and in manufacturing industry, chiefly in Argentina, Brazil, Cuba, and Uruguay. The total value of United States direct investments in Latin America increased from U.S.$1,281m. in 1914 to U.S.$1,988m. in 1919, U.S.$2,819m. in 1924, and U.S.$3,634m. in 1930, when,

[2] These estimates, which vary considerably in definition, may be regarded only as approximations. They are reproduced from *Foreign Capital in Latin America,* U.N. 1955.

with the addition of U.S.$1,610m. of portfolio investments, the total for United States private long-term investments in Latin America reached US.$5,244m. (more than one-third of all United States investments abroad, and a total not to be regained until as late as 1950).

The depression of the 1930's brought foreign investment in Latin America abruptly to a halt. The cessation of the inflow of capital, together with the fall in commodity prices and in the volume of exports, made it quite impossible for the Latin American republics to service their foreign debts. It is estimated that, for the Latin Americans to have met their external obligations during the years 1934 to 1938, they would have had to reduce their 1925–1929 volume of imports by as much as 60 percent. In the specific case of Chile, one of the worst hit by the depression, the Government was quite unable to raise the local currency equivalent of debt services due, which in 1932 exceeded the value of exports. Every Latin American central government except Argentina defaulted, and even in Argentina payment was suspended on provincial and municipal bond issues. It was not until twenty years later, in some cases, after lengthy negotiations on refunding arrangements and the scaling down of both principal and interest—which involved investors in heavy losses—that the position of the bonded debt of the Latin American republics was finally regularized.

AFTER THE SECOND WORLD WAR

Since the second world war there have been further important changes in both the capital-exporting and the capital-importing countries, which have affected the flow of private capital to Latin America; though much has been done to reconstruct a world economic order that was shattered by depression and war, there has been no possibility of a return to a pre-1914 situation in which private capital, moving unhindered, could meet the needs of the developing countries. The European countries, which had suffered economically far more from the second world war than from the first, had perforce to restrict the export of capital for some years until the late 1950's, and significant controls still remain, especially in the United Kingdom for transactions with nonsterling countries. On the Latin American side, the 1930's brought exchange controls and some increase in other forms of official regulation of private economic activity, though there were great differences among the republics in the extent to which such controls were imposed.

These policies were partly a response to the technical problems facing Latin American governments in their attempts to maintain economic growth in periods of declining export earnings, and were partly symptomatic of an economic nationalism in reaction to their experiences in the depression years; the Latin Americans felt themselves to be the victims of a system over which they had no control and which, as they saw it, had been devised principally to suit the needs of the great industrial powers. In the conditions then prevailing they tended to see foreign capital as a burden rather than as an aid to development. Popular resentment was especially focused on foreign-owned enterprises engaged in public services, many of which, because of restrictions on their right to fix their charges, became unprofitable and ultimately incapable of providing adequate services. In Mexico the wave of economic nationalism, which was to a large extent political in its origin, led to the expropriation of foreign-owned petroleum companies, and foreign as well as domestically owned estates were affected by land reform.

In the early postwar years the Latin Americans were in general little interested in encouraging new foreign investments, and in some cases pursued an active policy of repatriating existing capital. With substantial accumulations of exchange through unrequited wartime exports, and with the terms of trade moving in their favour under the pressure of demand for their commodities in the reconstruction period, they were able briefly to forget their basic need to augment local resources with capital from abroad. By the end of the war a large part of the external bonded debt of Latin American countries had been repatriated through open market purchases and normal amortization, as well as by the scaling-down of the nominal value of external government bonds, notably in Brazil and Mexico. Although the terms of many of these war time and postwar debt settlements involved investors in heavy losses, they have, with few if any exceptions, been faithfully carried out; the balance of the old funded debt of the Latin American republics has now been either extinguished or reduced to a very small part of total external obligations. In addition to the redemption of public debt bonds, the postwar years also saw a considerable re-

patriation of investment in public services, of which the most important were the British- and French-owned railways and United States telephone and telegraph companies in Argentina, the British railways in Brazil, and railways, tramways, and waterworks, in Uruguay. These repatriations involved payments of about £227m. to the United Kingdom between 1946 and 1951 and of U.S.$361m. to the U.S.A.

LATIN AMERICAN ATTITUDES

The change in the world economic climate that became apparent in the mid-1950's induced many Latin American governments to take a more positive attitude towards foreign capital. The terms of trade moved sharply against Latin America as commodity prices fell and the prices of imported manufactures continued to edge upwards. As this movement in the terms of trade reacted on domestic incomes, savings, and investment, there was a perceptible slackening of the rate of economic growth, which for the first 10 years after the war had, in general, kept ahead of the rise in population. From the mid-1950's, therefore, there was a fairly general change in Latin American policies towards providing more favourable conditions for the investment of foreign funds, ranging from the removal of obstacles to the inflow and outflow of capital to the enactment of legislation specifically designed to attract foreign investment.

Of the general measures, one of the most important was the relaxation, and eventual abolition, of exchange controls on financial operations; this was especially important in Brazil (1953) and Argentina (1955), where outward remittances had previously been subject to restriction. The decision to permit the operation of free exchange markets was also prompted by other considerations besides the attraction of foreign capital—notably the requirements of the IMF and the manifest inefficiency of the complex systems of control that had been tried but it did have a significant influence in improving the investment climate.

Specific legislation to attract foreign direct investment was very varied, including laws that offered certain guarantees on the remittance of profits and the repatriation of capital for investments in approved activities; laws relating to specific activities, such as Chilean legislation designed to induce greater investment by the major foreign copper mining companies; general industrial development laws offering tax concessions and other incentives; and laws governing the establishment of individual industries as, for example, the motor vehicle industries in Brazil, Argentina, and elsewhere. There were, of course, countries, such as those of Central America, which had never imposed significant restrictions on foreign exchange and investment. Peru, one of the most consistently liberal in its policy towards foreign capital, and with only a brief postwar period of exchange controls, has actively encouraged investment with legislation enacted at various times since 1950.

On the whole such legislation in Latin America did not give special privileges to foreign as distinct from domestic capital, though in Brazil the facilities given for imports of capital goods as foreign investments were criticized by domestic industrialists who had to purchase exchange at high auction rates to buy similar goods as ordinary imports. These arrangements were introduced in 1955; during the succeeding eight years foreign investors were authorized to import capital goods amounting in value to some U.S.$500m., nearly half of which was destined for the motor vehicle and allied industries. The distribution of these investments in the form of capital goods by class of industry and country of origin is shown in the accompanying tables.

Brazil: Imports of capital goods as investment[1]

[Million U.S. dollars or equivalent]

Year	Value	Year	Value
1955	31.3	1960	106.8
1956	55.7	1961	38.4
1957	108.2	1962	20.3
1958	82.5		
1959	66.1	Total	509.3

[1] Licenses issued by the Cacex under Decree 42,820 and earlier legislation.

Source: Sumoc, Boletim, December 1962.

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Brazil: Imports of capital goods as investment—Registration up to Dec. 31, 1961 [1]

[Million U.S. dollars or equivalent]

	Basic industries		Light industries, total	All industries, total
	Motor vehicles and parts	Total		
United States of America	122.6	160.9	58.7	219.6
Germany	69.3	92.3	10.3	102.6
Switzerland	7.9	20.1	17.4	37.6
France	13.5	21.9	2.4	24.2
Canada	------	21.9	0.5	22.4
United Kingdom	4.9	9.7	10.6	20.3
Japan	1.8	13.7	4.7	18.4
Italy	3.7	7.0	7.1	14.1
Netherlands	------	6.9	3.7	10.6
Belgium	0.3	9.3	0.8	10.1
Sweden	5.7	5.9	2.6	8.5
Others	5.4	9.8	13.0	22.8
Total	235.2	379.4	131.7	511.2

[1] Registration under Decree 42.820 and earlier legislation. These figures differ slightly from the totals of licenses issued by the Cacex.

Source: Brazilian Business, Rio de Janeiro, March 1962.

The case of Argentina is particularly instructive: the Perón régime, which was strongly nationalist in character, expended a considerable part of the country's exchange reserves in repatriating foreign capital established in Argentina and declared that it would never accept a foreign loan. By 1953 this same régime had passed a foreign capital law designed to attract investment, though it evoked little response abroad. Only after the succession in 1955 of a government with liberal economic principles, the establishment of a free exchange market, and the enactment in 1958 of new legislation encouraging foreign investment, was there any notable inflow of investment funds into Argentina. The inflow of new direct investments, which had averaged less than U.S.$4m. a year from 1951 to 1955, increased to U.S.$66m. a year in 1956–57, and to an annual average of U.S.$232m. in the years 1958–60. The Banco Central has shown that authorizations for investments under the legislation of December 1958 amounted to the equivalent of U.S.$195m. in 1959, to U.S.$117m. in 1960 and to U.S.$147m. in 1961; authorizations in 1962 are estimated at U.S.$84m.

THE VARIOUS FORMS OF CAPITAL

The investment climates in Latin America and the attitudes of Latin American governments towards foreign capital have undergone important changes since the war; conditions have also changed in the capital-exporting countries. The memory of earlier defaults on government debts and the effect on potential investors of political and economic instability in many of the republics made it virtually impossible for Latin American governments to raise funds abroad from private investors on the open market, and the narrowness of the capital markets in most Latin American countries also limited the scope for investment in locally quoted securities; the decline in foreign portfolio investment in Latin America probably continued throughout the 1950s. The floating of an Argentine bond issue in Europe in 1961, and the placing of Mexican bonds with foreign institutions, stand out as exceptions to what is still the general rule.[3]

In these circumstances, which were foreseen at the end of the war, the role formerly played in Latin American development finance by bond issues has been to some extent taken over by the international lending agencies, notably the International Bank for Reconstruction and Development (IBRD) and its affiliates the International Finance Corporation (IFC) and the International Development Association (IDA), and more recently by the Inter-American Development Bank (IADB). In addition, the U.S. Government has made substantial amounts

[3] Participations by foreign commercial banks in loans to Latin America by the IBRD and the IADB should be mentioned as an example of indirect investment that appears to be of growing importance.

available to importers in Latin America through loans by the Export-Import Bank of Washington for purchases of U.S. goods, and from other government funds under the Alliance for Progress.

Latin American countries have also sought extended commercial credits from European and other suppliers anxious to retain or expand their markets. These medium-term export credits have grown substantially and have become increasingly important in sustaining Latin American imports from Europe. But they are, for the Latin American countries, an expensive form of borrowing and, since they require repayment in a relatively short period, they constitute a heavy burden on the borrowing countries' balances of payments. The President of the Inter-American Development Bank, Sr. Felipe Herrera, noted recently that export credits and debts to commercial banks amounted in 1962 to U.S.$3,400m. out of a total Latin American external public debt of U.S.$9,000m. in that year, and that during 1961–62 payments were approximately U.S.$1,200m. a year, representing about 15 percent of the value of the region's exports.

The effect of this increasing volume of loans and credits to Latin America has been to diminish the relative importance of direct investments as a source of development capital. This is a comparatively recent phenomenon, however, and throughout the 1950's direct investments exceeded the inflow of other long-term development capital—as distinct from loans and credits granted specifically to finance balance-of-payments deficits, and other "compensatory" financing. In 1961, however, long-term loans and official donations represented 78 percent of the inflow of long-term capital (excluding "compensatory" financing) and this trend seems, on present evidence, likely to continue.

Statistics are not complete enough for a quantitative assessment of the inflow of direct investment capital since the war, nor the relative importance of foreign enterprises in the individual Latin American countries. A few of the republics publish details of authorized investments broken down by country of origin and by industrial sectors, though these are not always complete and there are inevitable discrepancies, between investments authorized and those actually carried out. A general picture may be obtained from published balance-of-payments data, but private capital movements are the point where balance-of-payments statistics are generally at their weakest. Among the capital-exporting countries, only the U.S.A. produces an annual estimate, analysed by country and by industry, of the book value of direct investments overseas, together with data on the outflow and inflow of capital and earnings. Some European countries also measure outflows of direct investment capital, though in much less detail.

Despite these deficiencies in the available statistics, they are nevertheless of interest as giving some indication of the magnitude of the sums involved. According to one source,[4] the book value of direct foreign investments in Latin America increased from about U.S.$6,000m. in 1946 to U.S.$13,000m. in 1958. Of the latter figure, a litle under 70 percent was United States capital, but if petroleum were excluded the proportion would fall to below 60 percent, and to approximately 50 percent if mining and smelting activities were also excluded. A little over two-thirds of this total, it was estimated, was concentrated in five countries: Brazil, Chile, Cuba, Mexico, and Venezuela. More recent estimates,[5] based on I.M.F. balance-of-payments statistics, suggest that the total of new direct investments in the period 1951–61 was also nearly U.S.$7,000m. As the total inflow of long-term capital over these eleven years was estimated at less than U.S.$10,000m. (excluding balance-of-payments loans) direct investment was by far the most important means of financing development—even if Venezuela is excluded the proportion is over 50 percent—though the relative importance of long-term loans began to outweigh that of direct investment after 1960.

These second estimates show very large short-term fluctuations in direct investment: A steep increase from 1951 to 1952, when the total reached U.S.$509m., was followed by a decline to well under U.S.$300m. in 1954–55 and a further rise to over U.S.$1,100m. in 1956 and nearly U.S.$1,600m. in 1957, declining thereafter to probably less than U.S.$300m. in 1961. The average annual inflow of direct investment, including reinvested earnings, was U.S.$343m. in the years 1951–55 and U.S.$906m. in 1956–60. Such figures are somewhat misleading as a

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[4] *Foreign Private Investment in the Latin American Free Trade Area,* Report of the Consultant Group jointly appointed by the ECLA and the OAS, U.N., 1961.
[5] *El Financiamiento Externo en el Desarrollo Económico de América Latina,* U.N., ECLA 1963.

presentation of long-term trends, however, because of the distortions caused by the inclusion of Venezuela, where there was an exceptionally large inflow of investment capital in 1956–57 when new petroleum concessions were auctioned, and also an apparent outflow of investment capital, presumably also from the petroleum industry in 1960–61. If Venezuela and Cuba are excluded, the fluctuations are much less marked, and there is a steady increase in direct investment (including reinvested earnings) from a low point of U.S.$173m. in 1954 to U.S.$657m. in 1959 and a fall to U.S.$574m. in 1960 and U.S.$352m. in 1961, though the latter figure is not completely comparable with those for earlier periods. Even with the most obvious distortions removed, there remain others, such as the fluctuations in investment in mining and the change in the position of Argentina from one of the smallest to one of the largest recipients of capital. For the period 1951–60 as a whole, four countries, Argentina, Brazil, Mexico, and Venezuela, received 75.5 percent of new direct investments in Latin America; Cuba, Chile, and Peru together 16 percent, and the other 13 republics together 8.5 percent.

The reasons for the sharp fluctuations in the inflow of direct investment capital into Venezuela have already been mentioned. In Brazil, though annual variations have not been inconsiderable, there was a definite rising tendency over the decade, the average inflow in 1951–55 being U.S.$70m. and in 1956–60 U.S.$149m.; this high level, though apparently sustained in 1961, can hardly have been maintained in 1962. The trend was even more marked in Argentina where, for political as much as for economic reasons, the annual average of new investments was negligible in 1951–55, rising to U.S.$166m. in 1956–60. The more regular trend in Argentina and Brazil is largely explained by the fact that most new investment in these countries went into manufacturing industry, though in Argentina there was a considerable flow of capital into the petroleum industry as a result of the contracts signed by YPF. In Mexico, where most foreign investment was also in manufacturing, there were some surprisingly large fluctuations—notably a decline in 1952–53 and an increase beginning in 1954, perhaps related to the exchange rate adjustment, and a net outflow in 1960—but the averages for the two periods 1951–55 and 1956–60 were fairly close at U.S.$88m. and U.S.$85m. Variations in foreign direct investments in Chile and Peru seem principally related to the trend in world commodity markets, since the large foreign mining companies accounted for over 40 percent of all new foreign investment in Chile in 1951–60, and in Peru mining and smelting absorbed 75 percent of all new U.S. direct investment in the same period.

POSTWAR UNITED STATES INVESTMENTS

During the war and for some ten years after, the U.S.A. was virtually the only source of direct investment capital for Latin America; Europe had been crippled by the war and there was very little European investment in Latin America except in petroleum; since the mid-1950's, however, European investment—direct as well as export credits—has become increasingly important, and German investment has been especially significant. The President of the Inter-American Development Bank recently quoted a figure of U.S.$400m. for suppliers' loans and private investments in Latin America by the European Economic Community alone in 1960. According to estimates in the ECLA study already quoted, the inflow of direct investment capital other than from the U.S.A. in the decade ended 1960 was about U.S.$1,400m., 23 percent of the total, or—since it was concentrated in the period 1956–60—nearly a third of the total in those years, a percentage that rises to 47 if Venezuela is excluded. This non-U.S. capital was principally European, since Canadian and Japanese investments were relatively small. These estimates contain a large margin of possible error, since they are based on a subtraction of the published data on United States investments from the totals shown in the republics' balances of payments; the differences in definitions and the scope for inaccuracy are wide, but the figures do indicate that there has been a sizable inflow of European capital since 1955, which, without regaining the position it occupied before the crisis of 1929, let alone before the first world war, is again making a large contribution to financing Latin American development.

Postwar direct investments have been chiefly concentrated in petroleum, mining and, to an increasing extent—especially European capital—in manufacturing. Agriculture has not attracted much foreign capital, nor have transport and public utilities, in contrast to the period up to 1930 when railways and public utilities absorbed more than one-fifth of U.S. direct investment in Latin America and probably more than half of British investments. Statistics on direct investments in Latin America by the three main capital-exporting countries are shown in the accompanying tables. These differ considerably in scope and are not strictly comparable.

The value of United States direct investments in Latin America was practically unchanged from 1936 to 1943, but thereafter grew rapidly to reach U.S.$4,445m. in 1950 and U.S.$8,387m. in 1960.[6] Provisional figures for 1961, showing a value of U.S.$8,166m., are distorted by the exclusion of investments in Cuba (valued at U.S.$956m. in 1960) in view of their confiscation by the Castro government, and by the revaluation of plant and equipment of a major oil company in Venezuela by U.S.$406m. Although the total of United States investments in Latin America has increased by a substantial amount and is about one-quarter of all United States capital overseas, investments in other regions have shown a more spectacular growth; between 1950 and 1961 United States investments in Latin America rose by 84 percent, while those in the other two main targets for United States investment, Canada and Europe, increased by 230 percent and 341 percent, those in the other two main underdeveloped areas, Africa and Asia, by 273 percent and 148 percent—though in these two areas the absolute amounts are much smaller—and investments in Oceania by 330 percent. The picture of United States investments presented by general statistics is greatly distorted by petroleum investments, especially in Venezuela, by mining investments in Chile and Peru and by shipping investments in Panama. Investments in manufacturing industry in Latin America showed more general increases: in Argentina from U.S.$161m. in 1950 and U.S.$158m. in 1959 to U.S.$283m. in 1961; in Brazil from U.S.$248m. in 1950 to U.S.$543m. in 1961; in Mexico from U.S.$133m. to U.S.$414m. over the same period, and in Venezuela from U.S.$24m. to U.S.$196m.

United States: Distribution of direct investments abroad, 1950–61

[Million U.S. dollars]

	1950	1957	1959	1960	1961 [1]
Latin America	4,445	7,434	8,120	8,387	[2] 8,166
Canada	3,579	8,769	10,310	11,198	11,804
Europe	1,733	4,151	5,323	6,681	7,655
Africa	287	664	833	925	1,070
Asia	1,001	2,019	2,237	2,291	2,482
Oceania	256	698	879	994	1,101
Total (including others)	11,788	25,394	29,827	32,778	34,684

[1] Provisional.
[2] Excluding Cuba.

Source: U.S. Department of Commerce.

[6] In assessing the significance of these figures the considerable rise in prices over this period must be taken into account; on the other hand, book values of investment (usually depreciated original cost) do not reflect current replacement values.

United States: Distribution of direct investments in Latin America, 1950–61

[Million U.S. dollars]

	1950	1957	1959	1960	1961 [1]
Argentina	356	333	366	472	635
Brazil	644	835	828	953	1,000
Chile	540	666	729	738	725
Colombia	193	396	401	424	425
Cuba	642	849	956	956	----------
Dominican Republic	106	88	104	105	105
Guatemala	106	106	132	131	126
Honduras	62	108	110	100	95
Mexico	415	739	758	795	822
Panama	58	201	327	405	468
Peru	145	383	428	446	437
Uruguay	55	57	45	47	49
Venezuela	993	2,465	2,690	2,569	3,017
Others	131	207	247	247	262
Total	4,445	7,434	8,120	8,387	[2] 8,166

[1] Provisional.
[2] Excluding Cuba.

Source: U.S. Department of Commerce.

The inflow of direct investment capital from the U.S.A. has declined markedly in recent years, and reinvested earnings have assumed a greater proportionate significance.

U.S. investment in Latin America

[Million U.S. dollars]

	1956	1957	1958	1959	1960	1961 [1]
Net capital outflow	592	1,163	299	218	95	141
Reinvested earnings	241	239	143	202	215	221
Total	833	1,402	442	420	310	362

[1] Provisional.

More recent data are not available but, according to U.S. balance of payments figures, the net capital outflow to Latin America on account of direct investments fell from U.S.$141m. in 1961 to a net inflow of U.S.$18m. in 1962. Mr. Teodoro Moscoso, Coordinator of the Alliance for Progress, has estimated that this is due primarily to large remittances from Venezuela; if these are excluded the net flow from the U.S.A. to Latin America of new direct investments in 1962 is estimated at U.S.$150m. to U.S.$200m., of which between U.S.$120m. and U.S.$150m. were probably in the key area of manufacturing. This estimate, which does not include reinvested earnings, shows, however, a more optimistic view than that taken by some other observers.

United States: Direct investments in Latin America, 1961 [1]

[Million U.S. dollars]

	Total	Mining and smelting	Petroleum	Manufacturing	Public utilities	Trade	Others
Argentina	635	(2)	(2)	283	(2)	28	324
Brazil	1,000	14	92	543	198	127	26
Chile	725	503	(2)	27	(2)	13	183
Colombia	425	(2)	229	94	28	50	24
Guatemala	126	(2)	28	(2)	66	6	26
Mexico	822	130	48	414	29	97	104
Panama	468	17	64	12	21	189	165
Peru	437	242	71	37	20	43	25
Uruguay	49	(2)	(2)	22	(2)	5	23
Venezuela	3,017	(2)	2,371	196	33	186	231
Total [3]	8,166	1,105	3,247	1,655	664	763	732

[1] Provisional.
[2] Included in "Others."
[3] Excluding Cuba, but including other countries.

Source: U.S. Department of Commerce.

POSTWAR BRITISH INVESTMENT

In contrast with the U.S.A., the United Kingdom has made only a modest contribution to post-war direct investment in Latin America. The large-scale liquidation of British investments in the years just after the war, the scaling down of Latin American government debts, and the persistence of certain long-standing disputes, especially over old investments in Argentina, undoubtedly had an adverse effect on British investors and contributed to a neglect of Latin America unparalleled in Britain's relations with any other major region of the world. The Commonwealth provided a powerful counter-attraction for British trade and investment, especially as it belonged to the same currency area with complete freedom of capital movements. In contrast, Latin America had a reputation for much political and economic instability, exchange controls were in force in several of the republics and, since Latin America is outside the sterling area, it was not so easily accessible to British investors; on all these counts Latin America appeared unattractive. The relatively low level of British investment helps in turn to account for the slower progress made by the United Kingdom than by most other European countries towards improving its position in Latin America's import trade.

United Kingdom: Private direct investment overseas [1]

[Millions of pounds]

	1958	1959	1960	1961
Latin America	5.2	11.7	14.6	20.2
Of which—				
Argentina	.8	3.1	4.0	8.6
Brazil	4.3	5.3	4.0	4.3
Chile		.6	.6	1.7
United States and Canada	38.1	51.4	42.8	35.5
Western Europe	13.8	19.9	24.8	37.7
Other nonsterling countries	7.8	5.6	5.1	1.8
Rest of sterling area	78.8	100.0	152.0	112.6
Total	143.7	188.5	239.4	207.6
Adjusted total [2]	144.0	196.0	247.0	226.0
Of which unremitted profits of subsidiaries	74.0	93.0	85.0	74.0

[1] Annual figures, excluding petroleum and insurance.
[2] Adjusted for incomplete reportage.

Source: Board of Trade.

Bank of England figures published annually up to 1957 show that the nominal value of all Latin American securities (including government bonds) owned by United Kingdom residents and quoted on the Stock Exchange fell from £774m. in 1938 to £314m. in 1948 and to £140m. in 1957, at which date the greater part was in direct investment. Against a repatriation of investments with a nominal value of £353m. between 1946 and 1951, payments of £227m. were received, the greater part of the discrepancy being accounted for by the difference between the purchase price agreed for the Argentine railways (£150m.) and their nominal capital of about £250m. This statistical series, admittedly incomplete in its coverage, has been discontinued with the publication by the Board of Trade of figures showing the annual movement of capital and profits into and out of the United Kingdom; no new measurement of the total value of British investments abroad has been attempted. The figures of new investment, covering the years 1958 to 1961, are summarized in the accompanying table. They show that investment in Latin America, though only a relatively small part of United Kingdom overseas investment, increased fourfold between 1958 and 1961 to reach about 10 percent of the total. When it is remembered that these figures exclude insurance and petroleum—in which the United Kingdom has important investments in Latin America, especially in Venezuela—the total of £20m. for 1961 is not so small as is commonly supposed.

OTHER EUROPEAN COUNTRIES

In contrast with Great Britain, Western Germany has made Latin America the principal destination of its capital exports to developing countries. The total flow of funds from West Germany to Latin America (official and private, multilateral and bilateral) between 1950 and mid-1962 is quoted as DM.4,521m. (approximately U.S.$1,100m.),[7] of which the bilateral component was DM.3,962m., and which is rather more than a quarter of the total outflow from Western Germany to all developing countries. The effective outlay of private capital—including the net increase in guaranteed export credits, direct investment and other bilateral assistance—to development areas was DM.8,179m., of which DM.3,385m. went to Latin America, DM.1,415m. to developing countries in Europe, DM.1,623m. to Asia, and DM.777m. to Africa.

Western Germany: Private direct investments abroad[1]

[Millions of deutsche marks]

	End 1961	End 1962
Latin America	1,098.9	1,356.9
United States and Canada	792.1	1,007.7
Europe	1,747.7	1,979.0
Africa	221.9	316.9
Asia	150.4	186.5
Australia and Oceania	98.5	108.7
Total	4,109.5	4,955.7

[1] Cumulative figures. Latin America includes West Indies and dependent territories.

Source: Bundesministerium für Wirtschaft, Bonn.

West German private direct investments abroad were resumed after the war in 1952, the annual outflow rising from DM.421.1m. in 1952/53 to DM.947.7m. in 1961 and DM.846.2m. in 1962. The regional distribution of these investments, given in the accompanying table, shows that investments in Latin America far outstripped those in any other developing area. Brazil alone has received more West German investment than any other country in the world, not even excepting those of North America and Europe. Brazilian figures indicate that about two-thirds of this investment have been concentrated in the motor-vehicle industry and most of the remainder in steel, chemicals, and heavy engineering. Argentina is the second main focus for German investment in Latin America, investments in other countries, even Mexico, being relatively small.

[7] Deutsch-Südamerikanische Bank. *Deutsche Entwicklungshilfe und Lateinamerika.*

Western Germany: Private direct investments in Latin America[1]

[Millions of deutsche marks]

	End 1961	End 1962
Argentina	159.7	231.2
Brazil	639.7	772.6
Chile	21.2	23.2
Colombia	38.0	63.3
Ecuador	4.4	4.7
Peru	10.1	21.2
Uruguay	13.3	13.3
Venezuela	23.4	27.8
Mexico	37.4	52.8
Panama	33.4	32.9
Central America	6.3	8.3
Cuba	5.2	5.2
Netherlands Antilles	87.0	87.9
Others [1]	19.8	12.5
Total	1,098.9	1,356.9

[1] Cumulative investment from 1952, including West Indies and dependent territories.

Source: Bundesministerium für Wirtschaft, Bonn.

Among other European countries, net foreign investments (not more specifically defined) by Italian residents in six main Latin American countries—Argentina, Brazil, Chile, Colombia, Mexico, and Venezuela—rose, according to the Italian Exchange Control, from the equivalent of U.S.$7.7m. in 1958 to U.S.$22.8m. in 1959, to U.S.$20.9m. in 1960, to U.S.$23.4m. in 1961, and to a provisional figure of U.S.$59.1m. in 1962. In the last year investments in Argentina and Brazil accounted for U.S.$30.0m. and U.S.$23.3m.

Swedish direct investments in Latin America averaged about 43.4m. kronor annually between 1955 and 1962, equivalent to about U.S.$8.4m. In a period in which total Swedish foreign investments, and those in the developing countries generally, show a marked increase, the annual flow of investments to Latin America shows on balance little change.

Latin American access to the Swiss capital market has been chiefly through export credits and direct investments. Of a total of 3,718m. Swiss francs in loans floated on the Swiss market from 1947 to mid-1961, Latin American borrowers accounted for only 15.3m. francs, and for only 112.3m. francs out of 2,510m. in bank credits. However, Latin American countries received 34 percent of Swiss exports covered by Swiss export credit insurance outstanding at the end of 1962; insured exports of capital goods to Latin America in 1962 were valued at 275m. francs, out of a total of 776m. francs. Swiss private direct investments in Latin America have also accounted for a high proportion of the country's total investments in developing countries, amounting to 60 percent in 1959.

CONCLUSION

The general picture of private investment in Latin America since the war cannot reasonably be described as disappointing when it is considered that direct investment alone reached an annual average of over U.S.$600m. over the decade ended in 1960—even though trends in the past two years have been more ambiguous. The features of the Latin American scene that are often regarded as discouraging, political and economic instability, have not perhaps been as great a deterrent as might have been expected. Less satisfactory aspects of the matter have been the fluctuations in the capital inflow over quite short periods and the very uneven distribution of foreign investment among the twenty republics; those that have the greatest need of foreign capital have on the whole received the least.

The outlook for direct investment in the area is now perhaps rather more uncertain than in 1960: Brazil and Argentina seem less attractive than two years ago, one because of the worsening of the economic situation and some recrudescence of nationalism, and the other because of the persistence of political problems and the consequent delay in remedying certain basic defects in the economy. In Mexico, the most stable of the larger republics, the inflow of

foreign funds seems to have recovered from the setback that occurred in 1960, but in the other main focus for foreign direct investment, Venezuela, there seems to be little prospect of any large inflow into petroleum and mining as in former years, and new investment is likely to be directed more to the growing, but still relatively small, manufacturing industry. It does not seem reasonable to expect that the total of foreign private investments in Latin America will quickly regain the peak levels of the late 1950's; yet the capital-exporting countries were never in a better position to make investments. It has to be recognized that the U.S.A. faces balance-of-payments problems, but it does not seem likely that Washington will allow this to obstruct the flow of capital to Latin America at a time when the Alliance for Progress has still to be firmly established.

Clearly much could be done to improve the investment climate in Latin America, and the foreign investor might reasonably ask how he can be expected to have greater confidence in countries where domestic holders of capital sometimes prefer to invest in low-yielding securities abroad.[6] There are very wide differences in investment conditions in the Latin American Republics, ranging from virtually unrestricted freedom, as in Peru, to the more complex situations in Mexico and Brazil. There are still free exchange markets for the remittance of profits and the repatriation of capital in nearly all Latin American Republics, though now with the important exception of Brazil. The regulation of the movements and employment of capital is generally confined to specific activities deemed of special interest to the nation.

Economic nationalism remains a force to be reckoned with in Latin America, but in most countries it is latent rather than active. The less developed countries seem on the whole to attract official loans rather than private direct investments, and multilateral rather than bilateral aid. This does not in general lead responsible governments to restrict the flow of private capital, though in Brazil the Government's relatively mild profits remittance Bill was modified by Congress and made much more restrictive. Nationalism in Brazil is also apparent in the Government's plan to acquire the remaining U.S.-owned public service undertakings.

The move to restrict profit remittances in Brazil was probably influenced by exaggerated estimates of their incidence on the balance of payments. Yet figures compiled by *Conjuntura Econômica* show that the inflow of risk capital into Brazil (excluding reinvestments) in the seven years up to 1953, when the free exchange market was established, amounted to U.S.$105m., whereas in the following seven years they reached U.S.$608m.; on the other hand, the effective remittance of profits and dividends averaged U.S.$47m. a year from 1947 to 1953, but an average of only U.S.$34m. annually in the period 1954 to 1960. This was a very small proportion of the debit items in the balance of payments, and it was, moreover, in service of foreign capital that did not expect to be repatriated within a definite period. Certainly the effect of the Brazilian profit remittance legislation can only be to deter new foreign direct investment, which had in any case shown signs of falling off; even if the permitted level of profit remittances were higher than the percentage that is in practice normally remitted, the very existence of restrictions is seen as evidence of hostility to foreign capital and provokes fears of further restriction.

Nevertheless, if economic nationalism still remains a force in Latin America, it has revealed itself on a fairly well-defined pattern; it has been directed primarily at public services—which no longer attract foreign investors as in the past—and the extractive industries that have a dominant position in the economy. Outside these spheres the Latin American republics remain largely private-enterprise economies; even in Mexico, where State economic activity has developed more than in most republics, and where the "Mexicanization" of utilities and mines has been carried out by agreement with the owners, the State has been careful to delineate the areas of industry that the private sector is being encouraged to develop. In broad terms, it is estimated that about 30 percent of economic activity in Latin America is government-controlled, with the private sector accounting for 70 percent; of the latter, 90 percent is in turn estimated to be owned domestically and only 10 percent by foreigners. With few excep-

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[6] There have been many references, particularly in the U.S.A., to the flight of domestic capital from Latin America to havens abroad, and several estimates of the total volume of capital so lodged. Adequate data on this subject are hard to obtain, but it is proper to note a Latin American view that holds the largest estimates to be misleading; since a strict definition of "flight capital" involves motives and intentions, movements of funds responding to this concept are virtually unidentifiable and it is possible that some of the estimates are inflated by the inclusion of capital movements of a different nature that cannot be legitimately classified as speculative.

tions, mostly in heavy industry such as steel and petroleum products, manufacturing industry is left to the private sector. It is worth noting that there have been virtually no expropriations of a manufacturing industry for economic reasons; the few known cases have been motivated by political considerations.

Relatively little has been achieved under the Alliance for Progress to encourage a greater contribution by foreign private capital to Latin America's development, and the impression persists that the Alliance is essentially a government-to-government aid programme. The Inter-American Development Bank has, however, made loans amounting to U.S.$59m. (up to April 1963) to private industrial companies, and has made 24 loans to development banks, *financieras*, and groups of domestic banks, for relénding to small or medium-sized enterprises.

The foreign investor has an important contribution to make—qualitatively even more than quantitatively, particularly in helping to raise technological standards. The problem of stimulating the flow of private investment capital to Latin America was considered in a report submitted to the U.S. Secretary of Commerce in January 1963 by the Commerce Committee of the Alliance for Progress (COMAP) under the chairmanship of Mr. Peter J. Grace. The Committee reached the somewhat discouraging conclusion that there was "little hope for creating the kind of climate that U.S. investors want in Latin America without increasing substantially the assistance that is being extended, and even then it is unlikely that normal conditions attractive to foreign capital can be created for a number of years." The Committee recommended various changes in U.S. tax legislation to favour investors in Latin America. Other recommendations included the establishment of a substantial pool of local currencies, to be fed from counterpart funds of surplus food shipments and other sources, for lending to both United States and locally owned enterprises, and the extension of the U.S. Investment Guarantee Programme.

This programme, which offers investors protection against the specific risks of inconvertibility, expropriation or confiscation, and war, as well as "extended-risk" insurance in certain cases, has evoked a very rapid rise in applications for cover by United States investors. At the end of September last, U.S.$1,000m. of specific risk guarantees had been issued, with U.S.$771m. currently outstanding, and applications for approximately U.S.$2,600m. were pending, of which about 42 percent related to Latin America. These investment guarantee agreements do not cover all Latin American countries; the nonparticipating republics include Brazil and Mexico. Relatively few countries participate in all three specific risk coverages: they are Colombia, the Dominican Republic, Nicaragua, Panama, and Venezuela; and Argentina has now been added by an agreement reached in June 1963. One of the difficulties in extending the programme has apparently been the reluctance of many governments to enter into bilateral agreements with the U.S.A. which provide for the U.S. Government's succession to the investor's property rights or foreign currency assets, for most-favoured-nation treatment for losses due to war, and for arbitration following payment of a claim under an investment guarantee. The Agency for International Development has, however, devised a formula "which is expected to eliminate the most serious objections to acceptance by foreign governments".

Recent months have also seen the formation of several private or semiofficial groups whose purpose it is to stimulate European interest in Latin America and a greater flow of private capital to that area. The activities of these groups should eventually bring a greater awareness of Europe's obligations to Latin America as an integral part of the Western world and, within the private sector, of the opportunities for profitable investment in Latin America. Fundamentally, however, a greater flow of private capital to Latin America must depend on conditions in the republics themselves. Until there is a general improvement in the investment climate, the inflow of investment funds will continue to be selective and liable to sharp fluctuations. The size of the inflow since the war, despite adverse circumstances, and the enthusiasm of many who have made a success of investment ventures in Latin America in recent years, give an indication of what could be expected if greater political and economic stability were assured.

Assistance in obtaining statistical information is gratefully acknowledged to the following:

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Union de Banques Suisses, Zürich, Switzerland.
The Italian Economic Corporation (U.K. Representatives and affiliate of Banca Nazionale del Lavoro), London.

(Subsequently the following communication from David E. Bell, Administrator, Agency for International Development, and a paper by Harvey S. Perloff and Romulo Almeida were received:)

DEPARTMENT OF STATE,
AGENCY FOR INTERNATIONAL DEVELOPMENT,
Washington, D.C.

Hon. JOHN SPARKMAN,
Subcommittee on Inter-American Economic Relationships,
Joint Economic Committee, U.S. Senate,
Washington, D.C.

DEAR SENATOR SPARKMAN: To supplement the information provided the subcommittee in testimony and supporting documents, I am enclosing a paper on private enterprise under the Alliance for Progress.

If we can provide any other data for the committee's use, please let me know.

Sincerely,

DAVID E. BELL, *Administrator.*

Enclosure.

PRIVATE ENTERPRISE UNDER THE ALLIANCE FOR PROGRESS

A number of the major objectives of the Alliance for Progress concern themselves directly with raising per capita income, diversifying national economic structures, accelerating industrialization, and increasing productivity. To accomplish these and the other Alliance goals, both public and private resources must be mobilized effectively. U.S. private investment is playing a significant role in Latin American development, and is being backed up by further U.S. Government activity.

The problems which have plagued the Latin American economies are not new, nor will they be solved quickly. One-commodity countries remain at the mercy of fluctuations in the world market. Low export prices have plagued the trade position of many. Inflation has weakened currencies. Capital has fled where political and economic climates have been unstable. Internal credit is not easily available. Institutions for development financing—savings and loan associations, development banks, and so forth—often are just coming into existence. At the same time, the demands of the Latin Americans are increasing as population grows at the fastest rate in the world.

Nevertheless, encouraging trends are developing which indicate how private enterprise—by its own initiative and aided by favorable Government action—can effectively contribute to the amelioration of some of the region's most basic economic problems.

The growth of manufacturing—the backbone of a developed economy—is continuing at an accelerated pace. U.S. firms have contributed to this growth substantially. Now, Japanese, German, and other European investments also are coming in.

Economic integration, through the Central American Common Market and the Latin American Free Trade Association, is shifting traditional trade patterns. More than just eliminating barriers and reducing tariffs, integration stimulates production and reduces dependence on imports. In some cases, improved terms of trade combined with the growth of manufacturing and diversification of exports are beginning to show results in improved balance-of-payments situations. New credit and other private financial institutions are being created and are flourishing, making available money for the development of the private sector.

MANUFACTURING GROWS

Of all the growth in the private sector, the most notable has been in the manufacturing sector—both in the more stable countries and in those where considerable risk is involved. Manufacturing output has increased significantly in the mechanical industries, such as transportation equipment, appliances, spare parts, cars, and electrical equipment. The economic integration movements in the hemisphere can help to provide the large markets needed for these industries.

New U.S. investments are being made more in the manufacturing industries, and less in the more traditional mining and utilities investments. Many U.S. firms have expanded their Latin American operations. U.S. industry has made

significant new investments in, for example, automobile production (in Brazil and Argentina), petrochemicals (a group project in Argentina), tractors and similar equipment production. U.S. enterpreneurs are going into more joint ventures, allowing greater Latin American participation in the new industries. Since the inception of the Alliance, U.S. banks have expanded considerably their Latin American operations. A U.S. tire company's investment in a plant in Ecuador helped revitalize a depressed area and spurred the expansion of small local industries. This pattern is repeated again and again.

Considerable publicity has been given to the fact that in 1962 there was a net outflow of U.S. direct new investment in Latin America. The great weight of remittances of oil earnings from Venezuela has distorted the entire picture, however. Excluding Venezuela, the net inflow of new U.S. investment was $158 million in 1962. U.S. investment activity in Latin America is reflected even more accurately by adding new investment plus reinvested earnings and depreciation. The total U.S. private investment in Latin America in 1962 then comes close to $1 billion.

AID'S EFFORTS

All of AID's efforts are directed at stabilizing and strengthening Latin American economies so that they can increase their output. These increases can be generated only by a vigorous private sector. AID encourages the Latin American governments to involve the Latin American private sector in development efforts, and to support stabilization programs which will insure that both foreign and domestic private resources are directed into development efforts. Similarly, AID strives to involve the U.S. private sector even more in the Alliance, to complement the public U.S. support given through AID's programs, food for peace, the Peace Corps, and others.

Direct capital participation in Latin America's development by the U.S. private sector is encouraged by AID's incentive programs. Private contractors are frequently enlisted to provide essential training for manpower development and to carry out construction or other services in loan projects.

AID's loans—the U.S. public effort—are used to strengthen these incentives. They provide direct help to industries. Indirectly, they can provide credit for the banking system, supply vital imports, or improve the investment climate by alleviating underlying structural problems.

AID INCENTIVES

AID programs for encouraging U.S. investors to go into Latin America include investment survey grants and guarantees for both business and housing investments.

Entrepreneurs surveying investment possibilities in Latin America can be reimbursed for half the cost of the survey if they do not proceed with their investments. Surveys approved to date could result in a total private invest- of over $80 million, without cost to the U.S. Government.

Investors in 18 of the Latin American countries (including Jamaica and Trinidad) can be insured by AID against losses due to inconvertibility of currency, expropriation, or war risks, as well as against certain other losses. Four hundred and thirty-eight million dollars in specific risk guarantees had been issued for U.S. investments in virtually every phase of private sector activity, as of December 31, 1963. Eighty-six percent of these guarantees have been issued under the Alliance for Progress. Activity in the last quarter of 1963 alone almost doubled the activity of the previous 15 months for Latin America.

Still other investors can receive the so-called all-risk insurance for business undertakings. To provide the much-needed capital for mortgage lending in Latin America, and to provide guidance in the methods of large-scale housing development, the housing investment guaranty program provides U.S. investors with insurance on the return of their investment. The operation of the housing guaranty program has speeded up considerably in the past few months. Sixty-one million dollars in housing guarantees is already authorized, AID is now utilizing the experience and talent of the Federal Housing Administration to process other applications expeditiously.

SPECIFIC LOAN ACTIVITIES

AID's funds are used to support private enterprise in many ways. Program loans have helped bolster the general economic development situation in Colombia and Chile, particularly by providing development imports for the private sector. They help to provide the basic stability essential for a good investment climate.

In Colombia, furthermore, a large portion of the local currency proceeds of such a loan are being used for the private investment fund—a new investment agency in Colombia which is channeling domestic and foreign investment into top priority areas of the private sector. Assistance from the fund will be available for industries which promote diversification and growth of Colombian exports; eliminate domestic shortage of goods and services considered essential to promote exports and domestic industry; or make available goods successfully substituting for imported products and thus strengthening Colombia's balance of payments. The equivalent of over $18 million has been lent so far by the private investment fund to Colombian businessmen.

Under the Alliance for Progress, great emphasis has been placed on directing resources into institutions which will provide the credit usually unavailable for small businessmen, farmers, and homeowners. AID has made 30 loans to help establish and support development banks, agricultural banks, and savings and loan institutions. These banks also are receiving substantial support from the Latin Americans, who are beginning to realize the importance of channeling their private resources into the development process.

Extensive work is being done under AID auspices to establish a cooperative movement in Latin America. Credit unions and housing, labor, agricultural and rural electric cooperatives are being supported with AID loans and with training and administrative assistance under contract with the counterpart U.S. groups.

AID loans have been made directly to private industry in Latin America. Technical assistance is being provided to help the growing industrial sector train the manpower it needs.

AID is helping to finance numerous infrastructure projects—essential undertakings by the Latin American governments, directly affecting the growth of private enterprise. By the improvement of road, airport, port, and power facilities, new areas are being opened up for development, entire regions are being brought into the national economy, expanded industry and agriculture have access to markets they need. Immediate benefits are felt in the economy of the Latin American country, where these projects stimulate employment. U.S. private enterprise benefits also from these loan projects. Private U.S. contractors—engineers, consultants, and construction firms, for example—are being used to carry out a major portion of the work required, especially for planning and implementing projects in transportation in virtually all of the Latin American countries.

Private enterprise also benefits from AID loans in other areas. Education loans help provide skilled manpower and increase the capabilities of unskilled labor. The provision of housing will provide a more stable labor force.

The Alliance for Progress and Latin American development have benefited indeed from the expanded and energetic activity of U.S. private enterprise. U.S. firms have gone into Latin America often against considerable odds; and without seeking assistance, they have fought until success was achieved. Similarly, U.S. private enterprise has benefited from its participation in the Alliance as financier, teacher, builder, manufacturer. New mechanisms are constantly being sought to encourage U.S. private enterprise to assume an even greater role in Latin American development. U.S. business will be tied in more closely in the future with European, Japanese, and Latin American ventures, carried out on a joint basis. One encouraging venture of this type—the Atlantic Community Development Group for Latin America (ADELA) has already begun its investment programing.

AID will continue to utilize every available resource of the private sector in its own programs.

Harvey S. Perloff

Romulo Almeida

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REGIONAL ECONOMIC INTEGRATION IN THE DEVELOPMENT OF LATIN AMERICA

THE RAPID economic development of the Latin American countries—a substantial industrial expansion, the growth of highly productive commercial agriculture, and an increase in high-income service activities—appears to be feasible only through regional economic integration. This is so because of the limitations in national markets and resources, as well as in the prospects of traditional international trade.

FROM FREE TRADE AREA TO COMMON MARKET

The effort to encourage intra-regional exports through free trade area negotiations has made only limited progress to date.

DR. HARVEY S. PERLOFF (UNITED STATES) *is presently a member of the Panel of Experts (OAS), on leave from his position as Director of the Program of Regional Studies, Resources for the Future. A graduate of the London School of Economics and Harvard University, he was formerly Professor of Social Sciences, University of Chicago.*

DR. ROMULO ALMEIDA (BRAZIL) *is presently a member of the Panel of Experts (OAS). He has for several years been very active in the development of his home state, Bahia, where he helped organize and was president of the Banco do Nordeste do Brasil. He has also served as Representative in the Federal Chamber and as Economic Adviser to the President of the Republic. Immediately prior to joining the OAS, he held the post of Executive Secretary of the Latin American Free Trade Association.*

[We wish to record our indebtedness to the authors of the reports and papers on regional economic integration in Latin America (listed in the footnotes that follow), as well as to those who gave valuable suggestions on earlier drafts of this paper, including our colleagues on the Panel of Experts, Felipe Herrera, Pedro Irañeta, John W. Delaplaine, Walter J. Sedwitz, Joseph Grunwald and Alberto Fraguio.]

Clearly, the full potential value of the Latin American Free Trade Association (LAFTA) has not been exploited as yet. It is useful to consider the conditions under which the most serious limitations could be overcome within the terms of the Treaty of Montevideo. Thus, under the Treaty there could be a substantial expansion of negotiations under the general "program of liberalization" as well as in the special industrial complementarity agreements, if the following conditions could be created:

(a) The establishment of confidence in the future developmental opportunities, particularly for the medium sized and smaller and less developed countries. While these countries are given privileged status involving unilateral tariff concessions, under existing arrangements they do not see this as resulting automatically in actual production and trade opportunities.

(b) Tariff concessions on items not now traded in Latin America, rather than concentrating mainly on traded items, as well as the working out of some fundamental agreements on industrial complementarity. In looking ahead, it is essential to accept the necessity for a *quid pro quo* in abstaining from certain lines of production while increasing output in others, largely following the dictates of natural advantage where it genuinely exists.

(c) Effective promotion of industrial and trade opportunities on the technical, entrepreneurial and financial levels. In developing countries, trade liberalization must be accompanied by industrial and trade promotion.

(d) More extensive harmonization of legislation on trade, foreign exchange and related economic matters, and the creation of financial mechanisms on a regional basis.

Through the extension of the various arrangements provided by the Treaty and, in general, through a more dynamic approach to achieve the basic objectives set forth in the Treaty, which would

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follow from stronger political backing,[1] LAFTA could actually become, with certain modifications, a common market arrangement, since automatic across-the-board tariff cuts and progressive implementation of a common-standard tariff are institutionally possible.[2] The necessary modifications could be expected to come as a consequence of new expectations and firmer political support.

Without the existence of such positive conditions, negotiation of tariff reductions, product by product, within a free trade area is inevitably a slow and painful process. Existing industries, no

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[1] Raúl Prebisch, in a valuable statement to a LAFTA conference, underlined the importance of certain "great political decisions" for progress in regional economic integration. These, he suggests, should cover four principal points: (a) establishment of quantitative goals for reduction and elimination of tariffs; (b) laying the foundations for industrial complementarity agreements; (c) defining the means for putting into practice the principle which establishes reciprocal advantage for all the contracting parties; and (d) creating the technical and financial agencies for the promotion of the common market. *Exposición del Dr. Raúl Prebisch, Subsecretario de las Naciones Unidas a cargo de la Secretaría Ejecutiva de la Comisión Económica para América Latina (CEPAL) en la Segunda Sesión Plenaria del Segundo Período de Sesiones de la Conferencia de las Partes Contratantes de la Asociación Latinoamericana de Libre Comercio, México, D.F., 28 de agosto de 1962* (mimeographed).

[2] Basic documents on economic integration and discussion of the free trade area and a common market are presented in studies by ECLA, IDB, OAS, and others, including: ECLA, *Multilateral Economic Co-operation in Latin America, Vol. 1 Text and Documents,* E/CN.12/621, 1962 (contains, in addition to the treaties and other basic documents, studies on payments and credit, on customs policy, and nomenclature and procedures); ECLA, *The Latin American Common Market,* E/CN. 12/531, 1939; *Inter Latin American Trade: Current Problems,* E/CN.12/423, January 1957; *Towards a Dynamic Development Policy for Latin America,* E/CN.12/680, 14 April 1963; ECLA and OAS, *Foreign Private Investments in the Latin American Free Trade Area,* E/CN.12/550, 1961; OAS/ECLA, *Economic and Social Survey of Latin America,* Vol. 1, 1961, Chapters 1 and 2 (Pan American Union, Washington, D.C.); IDB, *Economic Integration: Financial Aspects,* Report on Roundtable Discussion, Fourth Annual Meeting of the Board of Governors of IDB, April 1963; IDB, *Toward a More Effective LAFTA,* John W. Delaplaine, January 1963; ECLA, *Realizaciones y Perspectivas en el Proceso del Mercado Regional,* E/CN. 12/668, 1963; OAS, *Latin American Economic Integration,* OAS/Series H/X.1, June, 1961; CEMLA, *Problemas de Un Mercado Común en América Latina,* Sidney Dell, 1959; CEMLA, *La Contribución de los Sistemas Financieros a la Integración Económica de América Latina,* "Relatorías de la VII Reunión Operativa," 1962.

Other useful studies are those of Victor L. Urquidi, *Free Trade and Economic Integration in Latin America* (Berkeley and Los Angeles: University of California Press, 1962), and Sidney Dell, *Trade Blocs and Common Markets* (New York: Knopf, 1963).

matter how small and insignificant they may be, will want to protect themselves against outside competition and bring pressure to bear on their governments to this end. Thus, free trade area negotiations, lacking demonstrative, positive attractions—gains apparent to the key groups in each country—tend to be carried out in a cautious and protective atmosphere, rather than in an atmosphere dominated by expansionism and the possibilities for the future.

The great need is to achieve a true common market conceived basically as a customs union, as well as the direct and positive promotion of large-scale industrial and agricultural expansion on a regional, continent-wide basis. It may well be that both of these—i.e., both the common market and the direct promotion—must be achieved together if they are to be achieved at all. The individual countries may have to have a view of the positive productive gains to be made before they will back enthusiastically a true common market arrangement which removes internal tariffs across the board by specific percentages, and sets up a common external tariff. In this regard, it may be that the lesser developed regions cannot follow the same path to a common market as the European countries. The latter did not require any new regional industrial and agricultural promotion to appreciate the value to themselves of being able to sell their goods and services in a vastly expanded market.

Given the apparent limitations of the current approach to regional integration, consideration should be given to a new and broader approach. This would involve the promotion of specific arrangements for regional industrial expansion on an industry basis (as well as agricultural, mining, and service expansion where appropriate), with accompanying tariff reductions and the removal of other restrictions.

This might evolve as follows (using a specific example):

One can imagine a Latin American *fomento* agency as a dynamic organization with broad objectives and a variety of means at its disposal, which, as part of its promotional activities, brings together consortia: first, of private firms from Latin America, and, second, from Europe, the United States and other countries, with Latin American associates, willing to establish in Latin America

a series of new industrially-linked highly advanced chemical, electrical and machinery firms to sell to the whole Latin American market.[3] The removal of tariff and other restrictions for the products of these linked industries could then be negotiated through LAFTA and the Central American Common Market. The location of the specific new plants, it is to be assumed, would be based essentially on productivity considerations, but without neglecting the proper balancing of industrial growing points in the various sections of the region. Even if the location of the first new plants was not fully satisfactory in terms of present national aspirations for industrial production and prestige, the certainty that fast-growing and diversified industries would establish other new plants in additional countries over time would provide the atmosphere for an expansionary approach to negotiations.

Once several such specific industrial arrangements were evolved, the need for a customs union would become overwhelmingly clear and the basis for true regional economic integration established.

There is, in addition, another side to this proposal. Even if a true common market were set up in Latin America tomorrow, there would still be need for an organized powerful effort to promote transnational industrial, agricultural and service development. In an underdeveloped region, the freeing of trade alone is not likely to be sufficient to spark a great economic expansion, as was the case in industrially-advanced Europe. The newly created opportunities and potentialities have to be exploited directly through a coordinated effort and new mechanisms because the existing financial and organizational resources within the individual countries tend to be inadequate to take maximum advantage of such new opportunities. As a matter of fact, even a concerted effort in industrial and agricultural promotion, as the only companion to tariff negotiations, would not be adequate. Many additional measures of a region-wide nature would be called for to bring about rapid and broad-based economic development in Latin America. Such region-wide measures, when related to

[3] The industries mentioned are those in which some firms are already operating in various Latin American countries, but in which promotion falls far short of present use, not to mention projected demand.

investment programs or projects, would also have to be the concern of a *fomento* organization of the type proposed.

THREE PROPOSITIONS

The reasoning that lies behind this conclusion concerning the need for a full spectrum of regional measures is as follows:

(a) Regional economic integration can contribute enormously to the successful development of the countries of Latin America and therefore should be pursued vigorously;

(b) The present operational and institutional approaches to regional integration are inadequate and too timid to be successful; [4]

(c) The economic integration of an underdeveloped region is an extremely difficult task because of the lack of intra-regional trading traditions and lack of knowledge concerning specific possibilities.[5] Thus, the means employed must be appropriate in breadth, scale and boldness. The necessary breadth and scale can be achieved only if integration is supported by a multi-faceted regional development program, backed by broad knowledge of Latin American industry and industrial potential.

Let us examine these propositions.

THE REASONS FOR REGIONAL ECONOMIC INTEGRATION

In shorthand terms, regional economic integration can be defined as bringing together into a common market a number of countries, all aspiring toward a proportionately large and easy movement of goods and services across national boundaries. In the case of Latin America, economic integration can provide a

[4] This is not to depreciate in any way the accomplishments to date. A good many positive achievements have been scored, including trade classification, sectoral conferences, trade analyses, as well as the negotiation of some meaningful tariff reductions.

[5] There are also some great advantages: new patterns can be evolved and trade effects are less rapid in their impact on vested interests.

number of important advantages. These can best be seen against the background of recent developments.

Powerful international forces and trends within individual Latin American countries necessitate new approaches to economic development within the region. These forces have been analyzed in some depth in the studies referred to earlier and need only be outlined here.

It has become increasingly difficult to accelerate, and in some cases even to maintain, the previous growth rate of traditional exports. In the face of expanding import needs, there have been serious efforts to speed the process of import substitution. However, in the countries of Latin America where industrialization is most advanced, the possibilities of development based on import substitution for consumer and simpler producer goods are rapidly being exhausted. Imports of intermediate and capital goods from outside the region are substantial. Joined with other needed imports, and bumping up against a relatively low export-earnings ceiling, most of the countries have experienced severe balance of payments difficulties.

The efforts to encourage import substitution have, in most cases, resulted in the establishment of extremely high protective tariffs and other trade barriers. The proliferation of industries of every kind which have thus developed in essentially closed markets has deprived Latin America of the advantages of specialization and economies of scale and of a sound form of internal development.

The industrially more advanced countries face a situation in which the most hopeful areas of expansion are in the substitution of intermediate and capital goods. However, these generally require markets much larger than the domestic markets. Their establishment is also complex and costly, so that additional savings and investment, as well as an advanced type of know-how, must be attracted.

The enlargement of the market for Latin American production could greatly enhance the opportunities for the expansion of industry (as well as agriculture and services), bring gradually into being a healthy type of competition which can encourage a sturdier kind of internal development, and at the same time

significantly improve the balance of payments situation. The specific advantages that can be anticipated include the following:

New industries

Regional economic integration can provide a foundation for economic growth through the establishment of new industries and the expansion of existing industries which are characterized, for technological and economic reasons, by substantial economies of scale. Such economies may be internal or external to the firm. The former normally arise from technological production characteristics of the industry. External scale economies arise from sources external to the firm such as the increasing efficiency of an industry as a whole when its growth attracts specialized suppliers or permits the organization of specialized services or better organized marketing arrangements.[6]

A number of studies by the United Nations Economic Commission for Latin America have highlighted the many possibilities for the expansion of manufacturing in Latin America through an enlargement of the market. These include a variety of chemical industries, iron and steel, automotive products, pulp and paper, the production of railway equipment, naval equipment, heavy electric equipment, and a host of other products.[7]

It is well to note that the size of the market is not a simple matter of counting heads. Sales are dependent on "effective" demand, people who not only want a product or service but are able to pay for it. Thus, the market for most consumer products in

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[6] In the United States, for example, due to the variation of scale economies, a plant of minimal efficient scale producing typewriters can produce up to 30 percent of the nation's capacity output, while, by contrast, a cement mill of minimal efficient scale produces less than one percent of the national total. Industries with characteristics like that of typewriter production—including many machinery industries—and a whole host of specialized industries, can be established only in areas with a large market, Cf. Joe S. Bain, "Economies of Scale, Concentration, and the Condition of Entry in Twenty Manufacturing Industries," *American Economic Review*, Vol. 44 (March, 1954), pp. 15–39.

[7] For example, ECLA, *La Industria Quimica en América Latina*, Vol. II, E/CN. 12/628 (Nov. 1962); *El Mercado Latinoamericano de Productos Quimicos*, E/CN. 12/591 (1961); *The Manufacture of Industrial Machinery and Equipment in Latin America; 1. Basic Equipment in Brazil*, E/CN.12/619 Rev. 1.

Brazil, for example, is not a simple proportion of the 75 million persons who may need or want the product but a small fraction of that number (and very often a very small fraction indeed) due to the poverty of the majority, as well as other factors. For industries that supply producers, rather than consumers directly, the industrial underdevelopment of the Latin American countries means that such producer markets can be quite small even in a relatively large country. A supplier of specialized steel-making machinery may well need a market as large as all the present steel producers in Latin America, rather than in only one country, to produce efficiently and competitively.

But this point need not be elaborated too much since the stimulus to industry of increased size of market has been so dramatically demonstrated in Europe with the development of the European Common Market.

An effective *fomento* effort should not only serve to increase significantly total investment in Latin America, but also to improve the investment "mix." At the present time, because of the lag in industrial programming in most of the countries and in the availability of industrial projects, investment in infrastructure projects and other government programs tends to dominate the investment picture. The *fomento* effort can be expected to increase the proportion of investment channeled into directly productive activities and thereby achieve a more favorable investment "mix."

The stimulus of competition

Regional economic integration can provide a great stimulus to economic growth through the strengthening of competition—competition of goods, entrepreneurs, ideas, methods, style. Possibly the most important aspect is the potential influence that integration can be expected to have to reduce the tendency of producers to sell at a high price in a limited, rather than a mass, market, with high over-all production costs because of the small scale.

Professor Howard S. Ellis points out that "for the larger part of the economically less developed world—but particularly for

most of Latin America—conservatism of producers is a formidable barrier to progress."[8] Possibly much more important than conservatism per se is the effect of monopolies arising from the minimum scale of production in the face of the limitations of the markets, growing out of the efforts with regard to import substitution.[9] The invasion of previously monopolized territory by foreign (extra-national) wares, Ellis suggests, can serve to reduce price and profit margins, so that "many consumer goods now regarded as luxuries or semi-luxuries become articles of mass consumption." The process tends to be self-reinforcing; that is, markets continue to expand as costs of products drop and as incomes are boosted.[10]

In the case of Latin America, a distinction can justifiably be made between the competition of imported goods from countries of more or less the same degree of economic development and committed to the integration of their markets on a mutually advantageous and reciprocal basis and those from much more highly industrialized countries having advantages of already established economies of scale and distribution organizations. The initial disadvantages of the lesser developed countries need to be recognized. However, it should be accepted, at the same time, that such a distinction cannot be made over too long a period of time, since regional monopolies should no more be tolerated for longer than an incubating period than national monopolies. If regional monopolies were to keep the prices of key products, such as machine tools, far above the world price for long periods of time, the whole process of industrial development in Latin America would be damaged. The proper method would be to agree that, first, competition should be fostered inside the common market

[8] Howard S. Ellis, "National Development Planning and Regional Economic Integration," *Organization, Planning, and Programming for Economic Development*, Vol. VIII of U.S. papers prepared for the U.N. Conference on the Application of Science and Technology for the Benefit of the Less Developed Areas (Washington, D.C., U.S. Printing Office, 1962), p. 44.

[9] The unfavorable economic effects associated with such monopolies are spelled out in the recent ECLA study: *Towards a Dynamic Policy for Latin America.*

[10] Tibor Scitovsky has attributed to the factor of increased competition the greatest advantage of Western European integration. *Economic Theory and Western European Integration* (London: George Allen and Unwin, Ltd., 1958).

and, second, that the common tariff on protected products should, after a certain specific initial period, be progressively diminished.

Spirit of progress

A closely associated benefit of integration that can be anticipated is its stimulus to a spirit of progress with possibilities for realizing the full fruits of progress. It can be expected to bring with it a strong sense of growth and change, of modern management, modern technology and modern methods of selling, of research and development (an integral feature of many of the larger manufacturing firms)—in general, a faster diffusion of technological progress. It can also be expected to help foster more advanced approaches to management-labor relations, the social responsibilities of business, and a more fruitful relationship between private enterprise and government.

An increase in external trade

An important element in regional economic integration is an expansion of the possibilities for import substitution. Domestic production within the region will inevitably displace many items previously imported from outside the area. Yet, to the extent that integration achieves its major purpose—a rapid over-all increase in production and income throughout the region—historical experience suggests that the result will be an increase in external trade. As income rises, the Latin American countries will increase both their desire and ability to buy more from outside the region than they do now.

The potential is very great indeed. By 1975 the population of Latin America is expected to exceed 300 000 000. ECLA has prepared some rough projections to suggest the general order of magnitude of production and investment under a successful economic move forward. Assuming the stimulus of a regional program could enable Latin America to resume the per capita income growth rate that had been recorded from 1945 to 1955 (2.7 percent per annum, only slightly higher than the minimum set by the Charter of Punta del Este), in order to achieve the projected income expansion, gross investment would be in the

vicinity of $30 billion in 1975, compared to $9 billion in 1955. One quarter or more of this total would be comprised of machinery and equipment (some $8-10 billion, compared to $2.2 billion in 1955). Projections of gross expenditures suggest impressive increases all along the line; for example, the purchase of chemicals might be expected to reach over $8 billion compared to $2.3 billion in 1955. Many of these requirements of an industrializing economy will have to come from outside. Obviously the composition of imports will change, away from those goods that can be locally produced (most foodstuffs, many consumer manufactures, and some capital goods) and toward others that cannot be domestically substituted because of insufficient natural resources, technological skills, or financial capacity (some durable consumer goods, many heavy and complex capital goods).

The economic implications of a substantial increase in incomes and exports are very great indeed. For instance, U.S.-Canadian trade and investment totals are very close to those involved between the U.S. and Latin America, even though Canada's population is less than 10 percent of Latin America's. This is due largely to Canada's higher income and export levels. If the Latin American economy grows by anywhere near the projections recorded above, it will offer greatly expanded market opportunities to foreign traders and investors.[11]

Economic and political leverage

Regional economic integration can be expected to enhance the economic and political importance of Latin America in international affairs, with an accompanying greater capacity for promoting its own interests. An increase in bargaining power can be expected to make a substantial difference in negotiations centering on the export of basic commodities and trade relations in general.

It is to be hoped that Latin America's economic development can take place in a world increasingly geared to extensive and

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[11] David H. Pollock, "LAFTA: A Description and Evaluation," paper presented at the Waterloo University College Seminar on International Business Management, 2 April 1962.

relatively free international trade. While the economic integration of Latin America can certainly contribute to an increase in world trade, it can also serve to further Latin America's development goals under today's more restrictive trade conditions. In a longer-run dynamic sense, the ability of a lesser developed region to obtain a liberalization of tariffs on its exports to the highly industrialized countries, and therefore to improve its terms of trade and increase export earnings, is itself a key element in strengthening its economic structure and in enabling the region to reduce its barriers to imports from outside the region.

The other side of the coin of using greater trade leverage is, of course, the possibility of retaliation. Here again the advantages of an integated regional *fomento* approach to economic expansion come to the forefront. Relatively favorable trade arrangements would undoubtedly be easier to work out if attractive investment possibilities and suppliers' and other credit provisions were under consideration by the trading partners at the same time.

In general . . .

What is suggested, in the final analysis, is that regional economic integration can be expected to change the terms of reference within which economic development in Latin America will take place. In essence it would amount to shifting the balance in favor of more efficient production for mass consumption, in a spirit of expansionism and progress. Also, as Pierre Uri has pointed out, integration provides a greater capacity to resist outside shocks, helps overcome balance of payments difficulties and monetary instability,[12] and avoid cumulative restrictions. "This decrease in vulnerability and instability, as well as the freer circulation of skills and the revival of entrepreneurial spirit, is a decisive contribution to development itself."[13]

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[12] Monetary instability is particularly pernicious because it forces producers to keep boosting the prices of their goods and services so as not to be caught at any time in a price squeeze. The capacity to expand the consumer market is severely limited under such circumstances.

[13] Pierre Uri, *Suggestions on the Problem of a Regional Market for Latin America,* ECLA Doc. N° 2083/59 e (mimeographed), p. 5.

LAFTA: A first practical step

Against this background there are two things that can be said about the present free trade area approach. First, joined with the rapid progress being made in the establishment of a common market for Central America, LAFTA is a clear indication that the advantages of regional economic integration, at least in the broadest sense, are generally appreciated by the leaders of Latin America. And, secondly, it can be said that LAFTA represents a first practical step in the integration direction. It is not unexpected that caution should rule when the gains to be had are still rather vague and in the distant future, while the threatened losses through new competition seem both real and immediate.[14] The problem, then, is to make the potential gains understandably concrete so that the countries can countenance some small immediate losses. And it is here that the *fomento* approach, as suggested earlier—jointly with other program elements—can serve to establish an expansionary atmosphere, within which a genuine common market can emerge.

A FULL PROGRAM FOR INTEGRATION AND DEVELOPMENT

The third of our three propositions is that regional economic integration, to serve fully as a powerful lever for economic growth (in an underdeveloped region, as contrasted to Europe), must be supported by an extensive regional planning and development program. Such a program would have to include a number of interrelated activities, in addition to the movement toward a common market: (a) regional planning, (b) infrastructure projects on a regional basis and cooperative service arrangements, (c) industrial promotion, (d) the promotion of primary commodities, (e) the promotion of cooperative regional financing and international financing, and (f) the provision of detailed knowledge about indus-

[14] Actually the assumptions made about the extent of immediate losses that would be suffered from the competition which would follow upon the lowering of tariffs often tend to be unrealistic. The advantages of local production in most cases would be retained for some time, given the relatively high transportation costs in shipment of goods among Latin American countries (even assuming significant improvements in transportation)—certainly enough time to permit an improvement in local productivity adequate for survival.

tries, industrial expansion potentialities, credit sources and other subjects of importance to private and governmental decision-makers.

Region-wide planning

Region-wide planning is a foundation for all the other regional activities.[15] Such planning need not be very elaborate to be useful and effective. In fact, it should be quite practical and geared closely with the regional integration effort. It should provide a "framework" for regional activities by revealing the basic problems and the developmental potentialities for the future. Such framework planning should include the preparation of analyses of economic and social trends on a region-wide basis together with the projection of key series to reveal the regional implications of the evolving situation. Particularly important would be analyses and projections of regional markets within and outside Latin America for major services and products. Such planning would also focus on the detailing of the developmental potentialities of the region, seen as a single cooperating unit, in terms of complementary industries, increased trade, and development of region-wide infrastructure facilities, such as transportation and communication.

This type of multinational planning would furnish extremely useful specific terms of reference for the preparation of country plans and of expansion plans by private firms. It would, at the same time, provide a key element in the strengthening of Latin American economic integration. The major objective of such integration is the speeding of *new* economic development, particularly in manufacture, rather than merely the freeing of current trade. The basic need is to attract investment from within the region in productive enterprises as well as to encourage investment

[15] Cf. Harvey S. Perloff and Raúl Saez, "National Planning and Multi-National Planning, under the Alliance for Progress," *Organization, Planning, and Programming for Economic Development*, Vol. VIII, of papers prepared for the U.N. Conference on the Application of Science and Technology for the Benefit of the Less Developed Areas (Washington, D.C.; U.S. Government Printing Office, 1962), pp. 47-54.

from outside. Broad practical planning can help reduce certain kinds of risks and encourage productive expansion.

Multinational planning is also required to arrive at some basic decisions as to the degree of autonomy and types of external trade that the region should seek. It would not be wise to develop product surpluses which were not exportable to other markets; nor to encourage dependence on external sources of capital goods and raw materials without seeing to it that the corresponding means of finance were available.

Finally, such planning should concern itself with the questions of the appropriate scope for a common market. It is to be assumed that the *fomento* operation would extend to all countries of Latin America so that regional planning, as its counterpart, should also cover the entire region. The problems of relationships among the present two groupings and those not now members of either group should be of high-priority concern. It seems likely that the advantages of an all-inclusive common market will increasingly come to the forefront. However, whether or not such a market comes into being, the economic welfare of each country should be the concern of regional planning as well as of industrial promotion.

Regional infrastructure projects and cooperative arrangements

There is no mechanism at the present time for the preparation of multinational development projects, and yet it is evident that the success of regional integration will depend in no small part on such projects. Increased intra-Latin American trade calls for much better transnational transportation and communication facilities.

Due to the nature of Latin America's development in the past, the transportation and communication systems within each country tend to be turned toward the outside. In many instances transportation and communication between two Latin American countries is done through foreign centers. The circle of no-transportation-without-trade and no-trade-without-transportation must be broken. A deliberate policy of planning for transport and communication integration needs to be adopted, even though

subsidies may be necessary initially until the intra-regional trade develops.

Other types of multinational projects should also be evolved. For example, there are important gains to be had through the joint development of the international rivers for navigation, irrigation, electric power, and other purposes. Such multinational projects might well encompass the full development of international river basins looking toward the most productive uses of the land, water, forest, wildlife, recreation, and other resources. In general, the relationship of the directly productive activities—agriculture, mining, forestry, fishing and manufacturing—to the expansion of the infrastructure facilities is a logical concern of regional planning and development efforts.

Alliance for Progress, as well as World Bank, financial support for infrastructure investments of regional scope could contribute importantly to encouraging regional economic integration.

Aside from new construction and developmental projects, there are significant improvements in transportation and communications that can be achieved through cooperative regional arrangements. These can be employed to get better geographic and time distribution of services and facilities and also to strengthen the services administratively and financially. Such arrangements might well be useful in commercial aviation, coastal and inland-water shipping, transnational trucking and railroads, telecommunications, postal communications, and related activities.

Industrial promotion

As already suggested, the rapid economic expansion of Latin America can be greatly advanced by the direct promotion of industry, services, and commercial agriculture on a regional basis. Such direct promotion will undoubtedly require the establishment of a dynamic *fomento* corporation with a broad range of activities. These might well include the following:

(a) bringing to the attention first of Latin American, and afterwards to outside capital, opportunities for the establishment of industries on a regional basis;

(b) providing various types of financial aids to proposed

region-wide industries when their feasibility, as well as their need for financial assistance, has been established. The *fomento* organization should not only be in a position to make loans, but also to acquire equity holdings in new firms. Such equity holdings could be sold over time to Latin American investors, thus not only encouraging a greater amount of savings and investment in the region, but also more diffused ownership of business enterprises;

(c) providing technical assistance to regional firms, ranging from help in organizing firms (including help in design of plant and product and in management arrangements) to assistance in marketing and transportation of products;

(d) promoting uniform, high-level industrial and agricultural standards for export products;

(e) studying the reconversion and expansion of national industries and the readaptation of areas and retraining of working groups in order to facilitate specialization in regional markets;

(f) studying infrastructure needs of regional industries and seeking means of fulfilling these needs;

(g) studying the natural resources of Latin America with a view to evolving a firmer base for industrial and agricultural development;

(h) encouraging national industrial programming on an increasingly uniform basis so that region-wide industrial programming becomes possible;

(i) promoting trade among the Latin American countries;

(j) promoting Latin American tourism, through such means as the development of low-cost systems of travel to and from Latin America and within the region, including the development of "packaged" multi-nation trips, encouragement of hotel and related construction, encouragement of high standards in the maintenance of significant features of the national heritage which have cultural, historical, artistic or natural value.

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The important need is to have a focal point where effective action is sparked by bringing together people with ideas, knowledge of opportunities, risk-taking capital, and technical expertise.

Primary commodities

Both region-wide planning and a common market can contribute importantly to finding solutions for the various problems associated with primary commodity exports. Regional planning can help evolve a better relationship between supply and demand in such commodities, as can the common market. The expected advantages of increasing specialized, and often large-scale production, provided by a common market, apply to primary commodities as to other kinds of goods. Thus, there is mutual gain when the various countries give up the production of products for which they are not particularly suited, whether it be wheat or rice or sugar or wool, and can instead increase the production of their specialized commodities for sale in nearby markets.[16]

In addition, as suggested earlier, the establishment of an effective mechanism for consultation will lead to a stronger capability for common negotiation with the outside world. The strengthening of international bargaining power will come about, moreover, through the ability to negotiate a common external tariff or margins of preference by a customs union. This can help obtain more favorable international trade conditions as regards Latin American commodity exports as well as the newer possibilities for the export of manufactured goods—a negotiation more or less among equals rather than the strong and the weak. Also, the establishment of an integrated regional unit greatly facilitates the working out of arrangements with other economically integrated regions for trade and economic cooperation, both developed and developing. Regional arrangements are, of course, no substitute for world-wide trade arrangements, but they can provide valuable complementary tools.

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[16] Shifts in production must be properly phased so as to avoid too great an adverse impact on employment.

International financing and cooperative regional financing

Finally, there is need for a direct approach to the promotion of new and improved sources and kinds of international financing in order to permit the growth of industries and the improvement of agriculture, given the current limitation of internal capital for the financing of new enterprises and the expansion of existing ones. Here, as in other items mentioned, a joint regional approach can be expected to be more effective than a purely national approach.

It is important to conceive of international financing in the broadest possible terms. Every kind of inward financial flow has an economic impact on the receiving nation—on the total burden of interest and repayment, on the kinds of projects and activities that can be undertaken, on the kinds of external controls imposed, and so on. Therefore, the full financial spectrum is a matter of concern for the individual countries and Latin America as a whole—from short-term supplier of commercial bank credit given to a single firm all the way to long-term credit from a consortium of international banks and governments given to a government. Substantial improvements are conceivable through a concerted effort to improve terms of financing all along the spectrum. A 10-percent lengthening of supplier credits can be economically significant, as can somewhat better terms for short-range commercial bank credit provided to Latin American governments.

The situation here is basically similar to that characterizing the other program elements discussed above, i.e., improved international financing and regional economic integration are intertwined, the one supports the other. Certainly the expansion of the Latin American market will be a great attraction for international financing, while the greater supply of external capital and technology is an important ingredient to make Latin American economic integration flourish.

Special types of financial arrangements will be required if the full potentialities of a customs union are to be realized. This grows out of a series of fears in Latin America. Thus, for example, the prevalent fear that under a common market arrangement,

branch plants of firms from highly industrialized countries might put new and weak Latin American firms under a competition disadvantage must be squarely faced.[17] A similar fear of not being able to compete without national tariff and other protection is common among the smaller and lesser developed countries vis-à-vis the larger and more developed countries within Latin America itself. Furthermore, complementarity agreements tend to be hindered by the fear that the different lines of production may not offer the same expanding market or the same stability of outlets. To overcome that particular risk, cross-participation in the capital offers an attractive solution. The same can be said of the other two cases. Broad scale Latin American investment

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17 Two Latin American comments on this key point are worth noting:

"There is general concern that foreign enterprise, because of its very superiority and knowledge of the different markets, will make better use of the vast opportunities for trade that are emerging in the member countries and assume a leading role in the complementarity agreements and in the area in general. Unless the danger is averted, this great undertaking will not be able to advance very far because of the heavy opposition it is liable to provoke. The fundamental solution is to support Latin American enterprise so that it can achieve its full vigour in the formation of the common market, and stand up to foreign enterprise, either by making common cause with it or by competing on an equal footing, since competition on an unequal basis usually boils down to the alternative of liquidation of the weaker party or subordination to the stronger." ECLA, *Towards a Dynamic Development Policy for Latin America*, op. cit., p. 121.

". . . Another important political difficulty for integration lies in the fear that because of the smaller capacity of national entrepreneurs in terms of capital, access to new technology and international connections, the integrated market will be a more favorable field of operations for large foreign enterprises than for them. This leads to a sceptical attitude among the leftists and also among businessmen with regard to the favorable effects that integration might have. . . . This attitude is inspired by what happened in Europe and deserves attention and study. It would seem that the evolution of the Alliance towards a multilateral operation, where the development program of Latin America would constitute part of its economic integration or vice-versa, and would receive the formal support of the United States and of the industrial countries of Europe, would facilitate the rejection of this doubt and, even more, would provide new conditions for attracting and fixing external capital that would come to develop new sectors, introduce new techniques and complement the effort of national enterprises." Romulo Almeida, *The Latin American Free Trade Area*, address delivered at the Second Florida World Trade Conference, March 7-8, 1963 (mimeographed), pp. 17-18.

A realistic approach to this issue would serve over time to strengthen the role of foreign capital in Latin America, to the point where it is fully welcomed and protected.

in the new industries selling in the regional market can help to overcome much of the fear of foreign capital. But given the shortages of capital in Latin America as a whole, a variety of schemes to permit such Latin American participation in joint enterprises will have to be worked out. These might include the gradual sale of equity holdings to Latin American investors by the *fomento* corporation (as suggested earlier), expanded development bank facilities to aid Latin American investment in new regional industries, and the creation of mutual funds for small investors. Valuable experiments along some of these lines have been carried out in India and Italy, among other countries, and the techniques evolved deserve careful attention.

The Inter-American Development Bank has taken an important initial step in providing a special fund, in addition to funds provided for this purpose in its normal operations, to assist in the financing of intraregional exports, particularly of capital goods.[18] Other features of regional integration as well will require special types of financing, such as assistance for reconversion and readaptation of industries when imposed by new competitive conditions. The availability of such financing can facilitate negotiation among countries, within either a free trade area or common market arrangement. In the same light, financial assistance might be provided, through a regional adjustment fund, for the purpose of assisting industries and workers adversely affected by integration, as was done under the Schuman Plan.

More broadly conceived, the question of financing involves the problems of foreign exchange policy, convertibility, monetary and stabilization policy, and a host of related questions.[19] It is evident that regional economic integration could be advanced through

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18 While the emphasis here is on special forms of financing, it is evident that export financing and other financing associated with regional trade are basically complementary to general production credit. Since most internationally traded products are sold within the country as well as outside, the availability of production credit is normally the most important part of the picture.

19 A suggestive treatment of these and related issues is provided by Felipe Herrera in his address, *The Financing of Latin American Integration,* delivered at the University of Chile, May 22, 1963 (Inter-American Development Bank, mimeographed). The financial problems of economic integration are discussed in Inter-American Development Bank, *Economic Integration: Financial Aspects,* op. cit.

the harmonization of exchange and monetary policies and that Latin American cooperative efforts, by way of a Latin American clearinghouse or payments union, would enhance multilateral convertibility. However, perhaps these are matters that cannot be carried out as first steps; rather, such harmonization is likely to be a consequence of a successful launching of the other aspects of the integration program, as covered above.

REGIONAL INTEGRATION AND THE ALLIANCE FOR PROGRESS

Taken together, the program items outlined add up to a substantial series of tasks, and yet they are all necessary and, as a matter of fact, are very closely interrelated. The central point is that the economic development of the Latin American countries can be speeded up by many years, and even decades, by focusing attention, and resources, on the active promotion of regional economic integration. This would, as we have suggested, change the *terms of reference* within which economic development would take place.

The Charter of Punta del Este treats regional economic integration—along with national planning, reform measures, primary commodity arrangements, and international financial assistance—as one of the five focal points of the Alliance for Progress. However, the Charter does not set down any specific criteria or organizational techniques in order to link integration with the other features of the Alliance. To date, the Alliance operation, functioning as it does essentially in a bilateral framework, has not actively promoted the integration objective—with the noteworthy exception of Central American integration. In fact, in spite of an intellectual attachment to the broad integration objective, there have been some unintentional consequences flowing from the actual operation which tend to pose barriers to rapid Latin American economic integration.

Effort and interest are focused on financial assistance for specific projects and sector programs geared entirely to within-nation development, thus putting into the background the more systematic effort needed to speed the integration process. The Panel of

Experts has spelled out in detail, in its first report to the Inter-American Economic and Social Council, the problem of coordination among the national plans and has emphasized the importance of giving priority to the national and regional programs and efforts leading to integration. The isolated preparation of national plans, without any regional framework of information and projections, puts economic integration very much in the background. An important exception is the stimulus that has been given to regional programming in the case of Central America through the formal organization of the *Misión Conjunta de Programación para Centroamérica.* While the Ad Hoc evaluating committees have attempted to evaluate plans in terms of their implications for regional integration, most of the plans do not contain sufficient elements to make any meaningful judgments possible.

It is well to note also that discussions in meetings of LAFTA suggest strongly that certain political misgivings as to the position of the United States with regard to an over-all Latin American integration program, and, specifically in reference to LAFTA, have yet to be dispelled through U.S. policy declarations and action. While the core measures of regional integration must obviously come from the Latin American countries themselves, clear-cut United States backing would help to create an environment within which more rapid progress toward integration might be made.

Should a new multilateral approach to the Alliance for Progress be evolved—and that seems to be a critical requirement for the success of the effort—it should be characterized by a fundamental concern for regional economic integration. External financing and other forms of international cooperation should, it seems to us, take the economic integration of Latin America as a point of departure and assist in realizing the various integration elements discussed above. The multilateralization of the Alliance for Progress, to be truly meaningful, would need a powerful focal objective which can provide a framework for the diverse programs and activities and a basis for judgments on priorities. Regional economic integration can provide just such a focus.

ORGANIZATIONAL ARRANGEMENTS

Because of their close interrelationships, the various elements involved in a full-fledged regional economic integration, as described in this paper, might well be made the responsibility of a single agency, such as the Inter-American Development Bank, which would of course work in the closest possible coordination with LAFTA.

If this were done, the Bank would need to set up a regional *fomento* corporation as one of its activities, as well as sections to handle activities related to stimulating and financing trade among the Latin American countries.

An alternative arrangement might be the establishment of a purely Latin American organization combining LAFTA activities with the activities suggested above—including the *fomento* activities. Or these functions might be carried out through a cooperative arrangement among IDB, LAFTA, ECLA and the OAS.

Another possibility would be to establish these functions among the responsibilities of a new multilateral organizational arrangement of the Alliance for Progress (such as the Inter-American Development Committee proposed by former Presidents Kubitschek and Lleras Camargo), if any arrangement of this type were to come into being. In this case, it would necessarily include LAFTA and the Central American Integration Secretariat, as well as the Bank, in its decision framework.

The *fomento* organization, whatever its form, would need a strong staff, combining competence in industrial promotion, in industrial project evaluation, including the design of new plants and organization of new firms, in economic and industrial analysis, and in financial matters. At the same time, the LAFTA Secretariat would need to be strengthened since it would have many additional tasks beyond those assigned to it now, as a result of greater political backing for the integration objective.

The main point we would like to stress here is the importance of putting the question of organization of the integration effort on the agenda when discussions of possible changes in the Alliance and inter-American organization take place. It seems to us that the time has come when a full-fledged strategy for integration needs to be worked out, including a specific program of action, the

designation of agency responsibility for every step in the program, and a realistic arrangement for financing the effort. Under present circumstances, while substantial funds might ultimately be forthcoming from the international banks, the European and other nations, and from contributions of the Latin American countries, it is likely that the most rapid progress could be made if Alliance for Progress funds could be channeled for the *fomento* operation initially. This would mean, in the case of the whole of Latin America, following the significant precedent set in the case of financing of the Central American integration program.

NEEDED STUDIES

Since there are many serious problems that would have to be overcome in successfully launching a regional *fomento* effort, and even more in undertaking a full regional integration program, both the potentialities and obstacles need to be studied in some depth. Such studies would be a logical next step in encouraging the process of integration. They are particularly important since it seems evident that one of the major obstacles to progress in economic integration has been a lack of adequate knowledge of what integration entails for specific industries and what its implications are for government policy. Businessmen and governments, while intuitively recognizing the desirability of common market arrangements, have been wary of accelerating integration for fear of unknown repercussions.

Four kinds of studies are needed:

One might be of a more general economic, institutional, and policy nature, probing in an across-the-board fashion the problems, as well as potentialities, of regional economic integration. Thus, attention needs to be given to each of the program elements discussed above: (a) the steps in evolution into a broader and more effective free trade area and then the steps from free trade area to common market; (b) the form that region-wide planning should take so as to help achieve the objectives of integration in a practical way; (c) the types of regional infrastructure projects and cooperative arrangements that could advance integration; (d) how the development and use of natural resources on a regional basis

might best be promoted; (e) the types of policies that would be needed to make a success of a regional *fomento* effort; and (f) the various possible approaches to attracting Latin American investment funds and international financing for new and expanding regional industries.

Under this general heading would also come studies of governmental policies vis-à-vis regional integration, including questions of monetary, fiscal, foreign exchange, treatment of foreign capital, and other key policies. Techniques for achieving the necessary harmonization among the individual countries would have to be carefully examined. Such an examination should extend to harmonization in other areas as well, such as uniformity in port, customs, and consulate procedures, harmonization of statistics, and the like.

Alternative institutional forms to meet the various integration requirements also need to be probed. An examination of the questions involved in the relationships among trading groups is also needed, including not only the relationships with the United States and the European Common Market, but other areas of the world as well.

A second category is country studies, involving the investigation of industrial opportunities as they are interrelated and linked within a given country. These are particularly meaningful for the medium-sized and smaller countries looking toward active programs to help reduce the inevitable inequality that, in the short run, would arise from a reciprocity that tends to favor the larger, better endowed countries. In this category would also fall studies concerning the implications for each individual country of existing trade arrangements and of possible new arrangements, such as an all-inclusive Latin American Common Market.

A third major category is that of broad-scope industry studies. Here it would be useful to examine the general types of industries that might be attracted to the region, covering, where appropriate, their prospects and requirements for a "planned-complementarity" expansion within an enlarged regional market, including questions of vertical and/or horizontal integration. A joint Latin American-U.S. study group has indicated that the following are among the issues that need to be explored with relation to various key indus-

tries (particularly those industries—like steel, automotive products, paper, pulp and other wood products, chemicals and textiles—concerning which businessmen and government agencies are already considering possible "complementarity agreements" between two or more nations): What, over time, and with different scale-of-market assumptions, are the cost prospects for a given industry and/or its several component processes in different Latin American countries? Where does comparative advantage seem to lie? What are the long-term prospects for such expanded intra-regional production to become, without protection, competitive with imports from outside the region? Is there a chance that the industry, by achieving economies of scale within the region, might become a competitive exporter outside the region, thereby earning foreign exchange for the region as a whole?

The fourth group of investigations that needs to be undertaken is of so-called "feasibility studies." This is the practical and detailed follow-up of the general industry studies discussed as the third category. Industry feasibility studies are specific in nature, examining concrete investment opportunities, with detailed assumptions on scale, location, financing, techniques to be employed, and the like. Quite specific examinations of markets, availability and quality of resources, availability of overhead facilities and of labor are a feature of such studies. Different types of feasibility studies are also required. These are detailed examinations of multi-regional projects—in transportation, communication, etc.—needed to reduce the costs of transnational movement of goods and in general to establish the infrastructure necessary for regional economic integration. In some cases a regional infrastructure project will be a key requirement in making feasible the establishment of a regionally integrated industry.

Certain of these matters have already been studied to some extent by ECLA, OAS, the Inter-American Development Bank and other organizations. In such cases it is mainly a question of extending and deepening the investigations. Others of the subjects mentioned, however, have not yet been given serious attention and here new ground will have to be broken.

The Central American experience has shown the value of this type of approach. In that case, the beginning toward a common

market, and perhaps its greatest boost, was made through the study of 10 broad basic industries that seemed to offer opportunities for the region, later advancing toward feasibility studies and finally arriving at the specific projects that are now being carried out. A similar procedure seems called for in looking forward to the promotion of regional economic integration for all of Latin America.

Because of the wide variety of studies required, and because of the shortage of personnel available for research at the present time, it would be logical to encourage the organizations already involved in such research to deepen and extend their work, as well as to encourage universities and research institutions, particularly in Latin America, to undertake the necessary new kinds of studies. It would be extremely helpful if one organization, such as the Inter-American Development Bank, could accept the responsibility for coordinating the study effort and for channeling the funds necessary to carry it out.

CONCLUSION

To bring the previous points to a focus . . .

A dynamic regional *fomento* organization (or, more broadly conceived, a regional integration organization)—having available detailed information on industry prospects, armed with the capacity to channel bank funds and to attract capital from both Latin America and overseas, backed by the possibility of applying Alliance funds to overcome bottlenecks and to help finance regional infrastructure projects—could set the stage for a rapid increase in investment in existing and new industries and linked industrial complexes, together with associated tariff cuts on the products of such industries. This, in turn, would hopefully provide the platform for agreements on scheduled across-the-board tariff cuts and removal of other restrictions on trade, as well as the harmonization of economic and financial policy. It should also make evident that a region-wide planning framework was needed to help the individual countries to program their development in keeping with the requirements of an evolving regional economic integration. Interest in improved payments arrange-

ments can also be expected to reach a point in this process where new cooperative arrangements can be worked out.

At every stage new difficulties and problems are certain to arise but once the reality that genuine regional economic integration is under way becomes apparent, practical solutions will surely be forthcoming. The problem now is to demonstrate the reality of the potential advantages.

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