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# The World Bank and the Origins of the Washington Consensus: Negotiating the Imperatives of American Finance

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**The World Bank and the Origins of the Washington Consensus: Negotiating the**  
**Imperatives of American Finance.**

The literature on the World Bank in neoliberal governance tends to assume that its strategies are largely shaped by the objectives of the US. The hegemony of neoliberalism as a political paradigm in the US is conventionally considered to be expressed in the Bank as the 'Washington Consensus'. The structural adjustment loan is the medium through which the Washington Consensus is extended to the realm of 'development'. Yet structural adjustment lending was developed before the neoliberal paradigm became hegemonic in the US, in the service of Bank policy objectives which did not express the tenets of the Washington Consensus. The tendency of critical accounts to ignore this disjuncture and adopt the Washington Consensus narrative suggests that they take the Bank's capacity to enact US objectives for granted. My central claim in response to this is that the Bank has never been a passive recipient of the American hegemonic agenda.

I articulate this argument at two levels of analysis. Firstly, I draw upon Constructivist accounts in arguing that the agency of management was crucial in creating an organisational structure which allowed the Bank to meet the imperatives associated with the development of its operations. The process of developing a viable organisational structure allowed management to carve out a proprietary terrain in which their agency is decisive in constructing the tools and strategies of governance. However, I move beyond the Constructivist tendency to de-contextualise managerial agency, by arguing that management's strategic choices are socially anchored in the infrastructure of American financial capital.

Secondly, I argue that the social basis of the Bank in private American finance means its relationship with the US is defined by its imperative as an institution: is to secure access to the uniquely deeply capitalised US financial system. In pursuing this institutional imperative, the Bank's agenda has become increasingly intertwined with US objectives. However, the parameters of its capacity to act are set by the basis of its operations in private US finance.

On this basis, I offer a revisionist history of development of Bank's structure and lending practices at four critical moments from the 1930s to 1980s, which leads me to cast the turn to neoliberal governance in a new light. Firstly, I explore the enlistment of US financiers in support of the Bank at Bretton Woods. Secondly I illustrate how the Bank's imperative of capitalisation crystallised as it began lending. Thirdly, I demonstrate how management's pragmatic negotiation of the Bank's institutional imperative shaped the technology of governance during the Bretton Woods era. Finally, I present the origins of structural adjustment lending in McNamara's strategic renovation of the Bank's institutional structure and lending practices in order to render pro-poor lending strategy legible to US financiers. Structural adjustment was not an artefact of American power, but was rooted in management's pragmatic negotiation of the imperatives which followed from the social anchoring of the Bretton Woods order in the unique infrastructure of American finance.

Ultimately I will show that American hegemony cannot be understood without the agency of the Bank.

I hereby declare that this thesis has not been submitted,  
either in the same or different form to this or any other  
University for a degree.

**Signature:**

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30<sup>th</sup> September 2014

Brighton.

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## Introduction

More than three decades on from the 1982 debt crisis, scholarship on the role of the World Bank in global governance still frames the institution in terms of its relationship to the Washington Consensus. As a set of policies, the term is seen to reflect the extension of neoliberalism into the realm of development. The neoliberal agenda was to roll back the state – de-regulating financial services and promoting the free international movement of capital, liberalising the international trade regime, and controlling inflation. Debtor states were to undertake massive retrenchment, privatising state-owned enterprises, reducing public-sector pay and making civil service bureaucracies smaller and cheaper. Social spending was to be limited and cost recovery in health and education was to be deployed to keep expenditures down. These were the type of conditions attached to structural adjustment loans – which have become synonymous with the term ‘Washington Consensus’, and by extension, with ‘neoliberalism’.

This is seen as a major shift away from the Bank’s policy in the 1970s. According to conventional wisdom, Robert McNamara oversaw the Bank’s most progressive moment – the orientation of the lending programme towards rural farmers and ‘basic needs’ investment in education and social spending.<sup>1</sup> This is often seen as the culmination of the era of Bretton Woods’ association of Keynesian macro-management and state intervention with ‘development’.<sup>2</sup> Yet by 1981, the Bank had made a significant change away from these sophisticated applications of modernisation theory. The Bank’s 1981 report, *Accelerated Development in Sub-Saharan Africa* (often known as ‘the Berg Report’), in considering the ‘tragedy of low growth’ in African economies in 1981, argued that post-independence trade and exchange rate policies had over-protected industry, and overextended the public sector<sup>3</sup>. As a remedy, state involvement should be rolled back, and the private sector should be incentivised to take on the task of creating growth.<sup>4</sup> Further, with the appointment of Anne Krueger to the position of Chief Economist, the Bank had taken on a leading intellectual light of neoliberal New Political Economy who had published treatises on the perverse incentives and

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<sup>1</sup> Morawetz, D., *Twenty-Five Years of Economic Development*, Johns Hopkins University Press, Baltimore, 1977.

<sup>2</sup> Leys, C., *The Rise and Fall of Development Theory*, James Currey, London. 1996

<sup>3</sup> World Bank, *Accelerated Development in Sub-Saharan Africa: an Agenda for Action*, World Bank, Washington D.C. Pg.4-5

<sup>4</sup> Ibid. Pg.37-42



wastefulness flowing from government economic controls,<sup>5</sup> and considered development economics to be a betrayal of the basic tenets of economics as a positive science.<sup>6</sup>

The shift from the ideas of 'basic needs' to the Berg Report seemed to many to go against the Bank's inclinations. In considering this issue, scholarship on the Bank turns to the power of the US state in search of an explanation. The shift was the outcome of the US' response to a dual crisis of the Bretton Woods order and the Keynesian economic paradigm which underpinned it. The neoclassical economic paradigm was waiting 'in the wings' and attained hegemony as an intellectual and political paradigm simultaneously. The US transmitted the monetarist agenda to the international order through interventions to attack inflation and remove barriers to international capital movements and trade. Three examples are often cited to support this thesis. Firstly, in 1981 under President Reagan, Federal Reserve Chairman Paul Volcker raised interest rates significantly driving up the cost of debt held by less developed countries. The impact of this was to bring numerous borrowers to the point of default and to worsen terms of trade. Secondly, Alden W. Clausen was appointed to replace McNamara as president of the Bank. Clausen brought Anne Krueger in as his chief economist in 1982, bringing monetarism to the Bank. Thirdly, three years after the debt crisis, in 1985, the 'Baker Plan' was introduced. Proposed by US Treasury Secretary Baker, any transfers of new monies from the international financial institutions to defaulted debtors were made conditional upon entry into a standby agreement with the Fund, before the Bank's structural adjustment loans could be accessed. This did not only provide new liquidity. By insisting that lending was conditional upon agreement with private creditors, the Bank and Fund maintained financial discipline, and by appending further conditions to the loans, they promoted the US agenda of removing public bodies from their involvement in the business of development.

The shift from the paradigm underpinning Bretton Woods to that which underpinned the Washington Consensus is predominantly explained as a response to a crisis. In this radical epochal break, the strategies and tools of governance were made as new as the neoliberal vision of the good society was old – to fit the US' hegemonic strategy.

However, it is clear that the practices which came to be known as 'structural adjustment' were discussed, experimented with, and deployed for some time before they were enshrined in the Washington Consensus through the Baker Plan in 1985. In their path-breaking 1991 study *Aid and Power*, John Toye, Paul Mosley, and Jane Harrigan emphasise that conditional programme lending was deployed between 1973 and 1975 in Kenya, Zambia, and

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<sup>5</sup> Krueger, A., 'The Political Economy of the Rent Seeking Society', *American Economic Review*, 64, 1974. Pg.302

<sup>6</sup> Krueger, A., 'Trade Policy and Economic Development: How We Learn', NBER Working Paper No.5896, January 1997.

Tanzania. Most importantly although they acknowledge that “...it quickly began to be seen as the instrument which could exert pressure on developing countries to follow orthodox liberal economic prescriptions of price reform and privatisation”<sup>7</sup>, they make the crucial observation that ‘structural adjustment’ was not an invention made in response to the second OPEC price hike of 1979, or the election of conservative governments with neoliberal policy programmes in the OECD. Likewise, Patrick Sharma has illustrated that the Bank’s traditional mode of lending was ill-suited to the political economic context of the 1970s – and that discussions internal to the Bank were conducted around new techniques for speeding up lending before the crisis of 1979-82.<sup>8</sup>

The fact that the practice of structural adjustment preceded the Baker Plan is not a controversial observation in itself. But it is an essential starting point in illustrating the importance of the agency of the Bank. It follows that the political paradigm of the US and the strategy and practice of the Bank are not only linked through the exercise of direct political power. As I will show, the key mechanism by which the lending programme which revitalised the Bank as an institution of governance in the later 1970s was translated to financiers was a specifically American management technique, and the epistemological underpinning of the lending programme was provided by a positivist economics rooted in American academe. Yet neither bespeaks a specifically neoliberal intellectual programme. The Bank developed the capacities upon which the shift to neoliberal governance would be predicated in response to an earlier impasse. The neoliberal turn was built upon foundations which were laid during the McNamara era.

Further, traditional accounts of the Washington Consensus underestimate the agency of management in the creation of the tools of neoliberal governance which Sharma and Tøye et al point towards. The Bank does not figure in these accounts as an agent in its own right, but as an enforcer of the power of the US state: it is unequivocally a tool of US strategy in response to the crisis, with the objective of defending the US financial system and the dollar itself. In Williamson’s article coining the term, he argues that through ‘conditionality’ on their structural adjustment loans policies of privatisation and trade-liberalisation have ‘duly’ been enforced among applicants by the IMF and the World Bank<sup>9</sup>, following Baker’s statement that “Adjustment programs must be agreed before additional funds are made available, and should

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<sup>7</sup> Mosley, P., Harrigan, J., and Tøye, J., *Aid and Power: The World Bank and Policy-Based Lending – Volume 1, Analysis and Policy Proposals*, Routledge, London, 1991. Pg. 38

<sup>8</sup> Sharma, P., ‘Bureaucratic Imperatives and Policy Outcomes: the Origins of World Bank Structural Adjustment Lending’, *Review of International Political Economy*, Vol.20, No. 4, 2013. Pg.670

<sup>9</sup> Williamson, J., *What Washington Means by Policy Reform*, in Williamson, J. (ed), *Latin American Adjustment: How Much has Happened?*, Institute for International Economics, U.S., 1990.

*be implemented as those funds are disbursed.*<sup>10</sup> Reproducing this analysis depicts structural adjustment as a simple tool of neoliberal power, an off-the-shelf technical fix for market failures caused by the bad policy of ignorant Southern bureaucrats and corrupt politicians.

In sum, by beginning their account of the role of the Bank in neoliberal governance with the Washington Consensus, critical accounts make significant assumptions about the capacity of the Bank to straightforwardly enact US strategies. This naturalises the conflation of the practice of structural adjustment and neoliberal governance, denying their distinctiveness and erasing the historicity of the processes through which they became intertwined.

My central claim in response to this is that the Bank has never been a passive recipient of American hegemonic agendas. I articulate this argument at two levels of analysis. Firstly, I draw upon Constructivist accounts in arguing that the agency of management was crucial in creating an organisational structure which allowed the Bank to meet the imperatives associated with the development of its operations. The process of developing a viable organisational structure allowed management to carve out a proprietary terrain in which their agency is decisive in constructing the tools and strategies of governance. However, I move beyond the Constructivist tendency to de-contextualise managerial agency, by arguing that the strategic choices management make are socially anchored in the imperatives of American financial capital.

Secondly, I argue that the social basis of the Bank in private American finance means its imperatives as an institution are to secure and promote its access to the uniquely deeply capitalised American financial system. The relationship between the Bank and the US is defined by its continuing reliance on American capital markets. In pursuing this institutional imperative, the Bank's agenda has become increasingly closely intertwined with that of the US. However, the basis of its operations in private financial capital sets the parameters of its capacity to act. Financial imperatives mediate the Bank's relationship to American agendas.

By focusing on the specifically American financial imperatives which set the parameters of management's capacity to act in pursuit of American agendas, we are able to locate the Bank in its specific social context. This is important in that it helps us to decentre the US state from the historical narrative by emphasising how the agency of the Bank emerges through the pragmatic negotiation of institutional imperatives arising from its social anchoring in American private finance. This helps to break the causal linkage between US power and Bank practices. It is perhaps counter-intuitive that the imperatives shaping the development of structural adjustment should be, in broad terms, the same as those which demanded that

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<sup>10</sup> Address of James A. Baker, III, US Governor of the Bank and Fund, in IBRD, IFC, IDA, *1985 Annual Meetings of the Boards of Governors Summary Proceedings*, Washington, January 1986. Pg.208

the Bank adopt an approach of lending for specific productive projects in the course of the 1950s. However, this is an extremely important observation for our understanding of the origins of structural adjustment as it helps us to take an important step in disaggregating it from the Washington Consensus as an artefact of US power.

I will open my exploration of these themes with a review of contemporary literature on the role of the World Bank in global governance in Chapter 1. The most important currents in writing on the Bank appear to offer dramatically different readings of the nature of the Bank. For authors in what I term the 'Wall Street – Treasury Nexus' approach, a material assessment of the political and economic field of social forces in which the Bank operates offers the conclusion that the Bank should be considered no less than a part of the infrastructure of the American state. Counterposed to this, writers in the 'Relative Autonomy' tradition consider that while the location of the Bank in this field of social forces must be acknowledged, the agenda of the institution is defined by the intellectual and professional norms into which its management is socialised to a greater extent than external factors. However, paradigm change within the Bank relies upon political-economic paradigm change in the US, and American dominance of recruitment into key managerial positions. Both these approaches tend to rely upon the coercive power of the US in explaining the change in the Bank across the post-war era, and retain the tendency of the Washington Consensus narrative to locate the origins of structural adjustment in the neoliberal politics of the US.

To begin to uncover the agency of the Bank I will take a longer historical view. By exploring four critical moments from the 1920s to the 1980s, I will trace the impact of American financial imperatives on the Bank's structure, practices of management, and processes of lending. I begin, in Chapter 2, with an exploration of the way in which the Bank has been located in a Polanyian narrative of 'disembedding' and 'embedding' the power of finance in the real economy, after J.G. Ruggie and Eric Helleiner. This is founded on a reading of the era of the Bretton Woods conference as one in which the Bank was a force for the 'embedding' of financial power in social purpose: the internationalisation of America's New Deal. Yet, as I will show, finance played a much greater role in the pre-history of the Bank: important aspects of the Bank as conceived at Bretton Woods were inherited from the private financial planners of the international conferences of the 1920s. More importantly, the anti-financier rhetoric of the New Deal was highly specific. Finance was uniquely socially important in the US, and financiers were an extremely important part of the coalition upon which New Deal social policies and multilateral internationalism were founded. As a result, financiers were supportive of the Bank and were able to extract important changes to the Bretton Woods Act. On the basis of these necessary changes, the Bank as it was eventually founded was the central

agent of international liquidity provision prior to the Marshall Plan – and was intended to function to restore the international capital market as a profitable arena for investment. This suggests that the transition to neoliberal governance in the 1980s was not a new departure for the Bank, in terms of its organic relation to private American finance.

The importance of the social anchoring of the Bank in the infrastructure of American private finance would, as I show in Chapter 3, rapidly become apparent as the institution attempted to begin lending operations. During its first eighteen months, it faced a series of challenges which confirmed the central importance of financial considerations. By 1948 it was managed differently, capitalised differently, and lent differently than had been imagined. Accounts of the period speak of a financiers' 'coup', or argue that the most important feature of the changes to the institution are derived from an internal 'battle of ideas', on the basis of the autonomy from member states afforded by its basis in private capital. However, I will show that the imperatives of the financial community in which the Bank's agency was situated framed the parameters of management action in crucial ways. The inconvertibility of European currencies meant that the Bank had very limited funds to operate with: it would have to borrow. If it were to borrow, it would have to issue bonds. For Bank bonds to be attractive to investors, they would have to be backing loans made by the Bank itself – not the guarantees of private financial operations which had originally been planned. Finally, it would have to convince investors that it would lend for economic, rather than 'political' reasons. This entailed transforming the way the Bank was run – ousting the Executive Directors from the quotidian operation of the institution and asserting management control. In order to facilitate this and expand operations in support of Truman's 'Point Four' agenda, the US accepted the appointment of a management team of Wall Street lawyers and bankers. To illustrate the struggles over these issues between management and Executive Directors, I will provide a case study of the Chilean loan application over which these battles were fought. The transformations wrought by management in the period 1946-8 reflect the limitations placed on the Bank's capacity to act in support of the US agenda. They were the consequence of rooting the Bank in the infrastructure of American finance.

In Chapter 4, I will explore what this means for our understanding of the longer Bretton Woods period from 1948-68 – a period conventionally understood as the 'turn to development'. The Bank was further transformed through the reorganisation of 1952, the diversification of the Bank's investor base, and the foundation of the IFC and IDA. Writing on this period tends to argue that in spite of the Wall Street 'coup' under McCloy, management adopted project-oriented lending model in order to pursue US 'Point Four' objectives. In response, Jeffrey Chwieroth has argued this change was not directed by the US or external

financial interests, but emerged internally. It was, he argues, driven by the recruitment of elite individuals socialised into commercial managerial practices which they lobbied to reproduce in the Bank. Yet I will show that the specific transformations made by management were not, as Chwieroth argues, only one possible choice. They reflect the Bank's perennial imperative of securing and increasing access to investment in private international capital markets. Stretched by the Point Four programme, and pressure for more concessional lending through the UN from the South, the Bank had to find ways to meet these demands without damaging its creditworthiness. I will show that the 'turn to development' was not a voluntarist move – as a phenomenon, it was contingent upon the achievement of the Bank's institutional objectives. The technology of governance of this era – the project model – was shaped by management's pragmatic engagement with the imperatives of financiers in solving the Bank's on-going crisis of capitalisation. This is important for our understanding of the Washington Consensus, as it shows that there was no easy consonance between 'embedded liberalism' and 'development'.

In Chapter 5, I will explore the origins of structural adjustment in Bank management's response to a new contradiction emerging from the rapid expansion of the Eurocurrency market. By 1968, the Bank was faced with a new crisis: its clients were able to access the Eurodollar markets, and bypass the conditions attached to project loans. It was more liquid than ever, but struggling to lend. This period is often considered the Bank's most progressive moment, as it engaged with international organisations such as the ILO and reconceptualised its interventions to target the rural poor through a massive new lending programme. The new agenda is associated with McNamara's dynamic – if flawed – personality, and deep moral engagement with development. The shift from these practices to structural adjustment is portrayed as the outcome of larger external forces acting on the Bank in ways beyond its control, and the imposition of a neoliberal agenda on the Bank by the US. In response to these currents, Sharma has argued that the shift was driven by internal bureaucratic processes. As the debt profile of low-income borrowers worsened across the 1970s, it became more difficult to find projects which could be considered viable investments – and the Bank's ability to lend was again restricted. Structural adjustment was a solution to this disbursement problem, driven by the imperative to maintain the organisation's position in the governance of the international political economy. However, I argue that the specific nature of the changes was shaped more profoundly by the necessity to re-enlist financiers in expanding the lending programme than internal bureaucratic imperatives. As I will show, convincing financiers of the soundness of pro-poor lending saw Bank management take two major steps in the direction of structural adjustment lending in the 1970s. Firstly, the Bank was reorganised on the basis of cutting-edge American managerial techniques of systems analysis which McNamara had

encountered at the Pentagon and facilitated the generation of quantitative data. This was allied to the basis of the new approach to development in positive mathematical modelling, in order to illustrate that it was based upon sound economic principles. The second was the rehabilitation of programme lending, in order to provide the Bank with greater leverage over the broad macroeconomic policy environment in which its interventions would take place.

By taking this longer view, I show that the Bank was an important agent in the construction of the international regime of governance in the post-war period, in its own right. Because the Bank was socially anchored in the infrastructure of American finance, the agency of both management in the pursuit of the Bank's institutional imperatives and the objectives of the US, was mediated by the imperatives of US finance. Accordingly, American managerial techniques were of particular importance to the Bank, in translating the US agenda to financiers and making the Bank's activities legible in commercial terms. It is from the agency of Bank management that the specific form of the tools and practices of governance emerge, not the ideology or power of its most important donor.

## Chapter 1: It's the Washington Consensus, Stupid.

As I have suggested in the introduction, more than three decades on from the 1982 debt crisis, writing on the role of the World Bank in global governance still frames the institution in terms of its relationship to the Washington Consensus. From the Baker Plan onwards, the nature of the Bank is seen to have been transformed from a relatively benign 'development'-oriented institution lending for 'basic needs' under McNamara; to a dogmatic adjunct of the US Treasury policing the extension of free-market capitalism for the benefit of American finance and business. As in the Bank, so in the South: since they were formulated in 1990, Williamson's ten policy guidelines have been reified to the extent that political transitions in the global south are frequently depicted as the 'adoption' of the Washington Consensus, as an externally imposed off-the-shelf package in which neither the agency of international financial institutions nor subaltern groups have any meaning.

In this review I will explore how the continuing deployment of this analytical frame for understanding the Bank's role in global governance casts the contemporary nature of the institution – and the nature of the contemporary neoliberal order more broadly – in the mould of the political struggles of the 1980s. The notion of the Washington Consensus as the origin of the neoliberal era of governance has functioned as an analytically obstructive cipher for the nature of the role played by the Bank (and Fund) in the process of the construction of this international order. As I shall show, even the most sober reviews largely concur: the policy of the Bank largely reflects the strategy of the US. The Bank is persistently constructed as the passive object of US state strategy, of the historic Bretton Woods-era objective of 'embedding' finance in national economies and the contemporary objective of 'disembedding' it again. The power of the US state and private finance is coercively extended through the Bank. Accordingly, the 'post-Washington Consensus' is depicted as a rhetorical shell for American power, in pursuit of the same objectives, acting on the Bank in the same direct way. It's still the Washington Consensus, stupid.

One of the most important features of this account is the conception that the US oversaw the institutional capture of the Bank by neoliberal economists, drawn from an elite pool of Ivy League scholars or Wall Street financiers. The Reagan administration is credited with having initiated and successfully overseen a transition which has been global in scope, and a runaway strategic success. The outcomes of the crisis are equated with the success of an ideological project, and the adoption of the 'Washington Consensus' in the Bank under Clausen



and Ann Krueger entailed a radical US-enforced change from the McNamara and Chenery regime.

Defining the nature of the neoliberal international order by juxtaposing it with the Bretton Woods regime directs the critical gaze away from important continuities, particularly in the policy and practices of the Bank. The basis of structural adjustment in crisis and the convenient bundling of the actors involved in its development in a notional 'Washington' has obviated the need to scrutinise the specific processes which have led it to become a central feature of neoliberal governance beyond the observation of more-or-less contingent material events. Following from this, the endurance of the hegemony of neoliberal interests is frequently explained simply by reference to the power of 'Washington', with varying emphasis on its ideational or real components.

I hope, by reassessing this narrative, to contribute to an understanding of the historical development of the agency of the Bank in neoliberal governance which is capable of moving beyond the obstructive reification of the Washington Consensus as a diktat from the imperial heartland imposed upon passive recipients, and its origins in the crisis of the Bretton Woods regime. Rather, the roots of neoliberal governance are to be found in the mediation of the US' hegemonic agenda by financial imperatives throughout the Bretton Woods era and its successor.

I will begin this review by illustrating the way in which the persistence of the Washington Consensus as a frame for the analysis of the neoliberal regime of governance cuts across contemporary Liberal, Neo-Gramscian, and Constructivist political economy. The continued deployment of this signifier for the nature of the contemporary regime is the consequence of the enduring tendency of these traditions to depict the institutions of global economic governance as the passive objects of US state strategy, and to neglect the way in which the Bank is anchored in specifically American financial relations. More generally, neoliberalism is often conceived of as a disempowering technology of governance which swept away the practices of the Bretton Woods era.

The broad thrust of this narrative can be captured by considering its two most salient features. Firstly, the advent of neoliberalism in the Bank is consistently represented as the result of the power of the American state following from a sudden epochal political change occasioned by international crisis. By exaggerating the break between the two eras, critical accounts tend to turn to the external power of the US to explain the turn to neoliberal governance in the Bank. As an extension of their accession to state power in the US and UK, neoliberal economists effected institutional capture of the Bank. Secondly, the Bank's policies of conditionality in offering balance of payments financing in exchange for 'structural

adjustment’ are the specific signifier of governance in the neoliberal age; as the primary tool through which the objectives of the US state and financial capital are pursued. These policies, which temporally correspond to the Kuhnian paradigmatic shift in political economy and the attainment of political power by the Right in the US and UK as described in this literature; are considered to be the direct outcome of the neoliberal capture of the state and the international financial institutions.

Underpinning this common functionalist narrative, as I shall show in the second and third sections of this review, are two apparently divergent conceptions of the Bank. I turn first to what I term the ‘Wall Street – Treasury nexus’, in which the Bank is an essentially passive recipient of American objectives. The most prominent exponents of this tradition of writing about the Bank are Robert Wade and Richard Peet. The analytical centre of their interventions is the intellectual hegemony of the US. Here, the Bank’s strategy is a reflection of the dominant political paradigm at a particular juncture – or, where necessary, the hard power of the US Treasury. This is the objective of these accounts, to illustrate that the hegemony of the US remains the determinant of the nature and practices of global neoliberal governance.

In the third section, I explore the ‘relative autonomy’ tradition, which proffers a narrative of change which is rooted in the agency of the management and staff of the institution mediated by epistemic change in the elite academic community. The most important interventions in this tradition have been made by Constructivist authors Jeffrey Chwieroth and Patrick Sharma. Their writings focus upon the internal culture and bureaucratic imperatives of the Bank as an institution possessed of autonomy from the direct domination of its largest donors by virtue of its basis in private finance. These works make important contributions in decentring the US state from the analysis, and illustrating the historicity of the agency of Bank management. Ultimately, I will show that they rely upon the same narrow social anchoring of the Bank in elite scholarly and commercial networks as the ‘Wall Street Treasury nexus’ accounts, and provide an account of change on a largely voluntarist basis.

Yet in both traditions, the transition to neoliberalism is the result of the power of the American state, expressed in the ideational consonance of Bank management and state managers, or in the domination of the Bank by neoliberals opportunistically manipulating the crisis of the Bretton Woods system. In this respect, they adopt the central failing of the Washington Consensus narrative – beginning with the hegemonic ideology of the US. The outcome of this is that for all that they emphasise the processes of socialisation and change internal to the institution, they erase the agency of the Bank from their account of the historical development of practices of global governance.

In the fourth section, I will argue that in order to provide a satisfactory account of the origins of structural adjustment, it is essential to recognise the agency of Bank management. I show that in order to make space for this in our account, we must locate the material basis of the imperatives which shape the parameters within which their actions take place. To do this, I take a longer historical account, drawing on the work of Martijn Konings, Hannes Lacher, and Leo Panitch.

By showing that the institutional imperatives of the Bank and the complex of social power relations in which it is situated are mutually constitutive of the changing regimes of global governance, I hope to contribute to an understanding of the political economy of the Bretton Woods order and its successor which is capable of demonstrating how the agency of the Bank is anchored in the everyday life of the societies it aims to support, create, and police.

## 1: A Paradigm with Nine Lives?

The most striking feature of writing about the Bank's role in neoliberal governance is the tendency to view it through the prism of the Washington Consensus. As far as the international financial institutions are concerned, the use of the term denotes the practice of structural adjustment which officially commenced in 1980. As I shall show, understanding the relationship between structural adjustment lending and the Washington Consensus in this way is actually quite problematic. Two distinct phenomena - an *ex-post* attempt during the 1990s to encapsulate the zeitgeist of 1980s neoliberal political economy, and Republican foreign economic policy responses to the crisis of the Bretton Woods system – have been uncomfortably conflated. The tendency to bundle structural adjustment along with the 'Washington Consensus' and deploy these terms as interchangeable synonyms for 'neoliberalism' is problematic for two reasons.

Firstly, it privileges the imperatives which mobilised the Washington Consensus – those of the US state – and obscures those which gave rise to the development of the practice of conditional programme lending in the 1970s, by assuming they are the same. The tendency to deploy the terms interchangeably as a cipher for neoliberalism more broadly means that Williamson's mis-appropriation of the practice of structural adjustment in the name of neoliberal Republican foreign economic policy is reproduced in critical accounts.

Secondly, this implies a neat elision of neoliberal political economy and the agenda of the US state in spite of the tenuous basis of the policies the 'Washington Consensus' describes in neoliberal economic theory. This has been acknowledged as a political rather than academic

paradigm shift (as I shall discuss below), yet this insight is not followed through: structural adjustment lending is depicted as the *sine qua non* of neoliberalism.

In sum, this account's mis-appropriation of structural adjustment as the heart of the 'Washington Consensus' lends currency to an understanding of the Bank agenda which suggests that it is dictated by the hard power of the US state, and reflects the epochal breakdown of the Bretton Woods era. Structural adjustment is seen to reflect a new paradigm expressing the exercise of US power over the international financial institutions following the last convulsion of the old order in the debt crisis of 1982. As the neoliberal paradigm has not been dislodged by the financial crisis of 2008, critical accounts of the Bank's role in the governance of the contemporary order persistently return to the Washington Consensus as the frame in which the Bank is situated.

In this section I will illustrate how these accounts depict structural adjustment as a feature of the US response to the crisis of Bretton Woods, and persistently frame the Bank's role in the governance of the contemporary order in terms of the Washington Consensus. I argue that in so doing, they fail to account for the agency of the Bank in the construction and governance of the contemporary international order.

In her 2013 article in the *Review of International Political Economy*, Sarah Babb observes both of these problems. Firstly, she points out that "*None of the theories in vogue at the time – the rational expectations theory, public choice theory and so on – had anything to say about mobilizing international organizations to promote policy reforms*"<sup>11</sup>, and that Republicans were fond of citing *laissez faire* principles to argue that the Bank and the Fund ought to be scrapped. Secondly, she observes the central tension in the deployment of the term 'Washington Consensus' as a cipher for structural adjustment as a neoliberal reform: "*...the term 'Washington Consensus' was originally coined to help make sense of the IFIs practice of conditionality...*"<sup>12</sup>

Perhaps the most important contribution Babb offers is to shift the focus of our understanding of the development of the Washington Consensus to the Bank as the most salient agency in the operationalisation of the paradigm. Although the Bank's practice of structural adjustment is familiar, the deployment of this practice as a core disciplinary element of the Washington Consensus is more usually associated with the IMF. This, however, is problematic, she argues. While the IMF lent for policy reform, it did so only in the fields of fiscal and monetary policy. The Bank, as she points out, had experience of the application of

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<sup>11</sup> Babb, S., 'The Washington Consensus as Transnational Policy Paradigm: its Origins, Trajectory and Likely Successor', *Review of International Political Economy*, 20:2, 2013. Pg.276-277

<sup>12</sup>Ibid. Pg. 274

much wider conditionality – which made it the perfect vehicle for Baker’s objective in enforcing financial discipline to safeguard the international banking system.<sup>13</sup>

Babb makes an important contribution in observing both the problem of the conflation of structural adjustment lending with the Washington Consensus, and the proper locus of the practice of structural adjustment in the Bank, rather than the Fund. Yet by focusing solely on the Baker plan’s intention to manage the crisis by using conditional loans she does not move beyond the tropes of the contemporary critical literature on the Bank.

Firstly, having acknowledged that the Washington Consensus was an appropriation of existing practices of structural adjustment, Babb nonetheless reproduces it. Secondly, structural adjustment appears as a novel invention of the US strategic ‘neoliberal’ response to the epochal crisis of the post-war order of embedded liberalism. This aspect of Babb’s account echoes the contributions of political economists from across the spectrum of epistemology and political commitment – notably in the work of neo-Listian political economists Chang and Grabel<sup>14</sup>; neo-Keynesian ex-Bank chief economist Joseph Stiglitz,<sup>15</sup> and orthodox Marxist Paul Cammack.<sup>16</sup>

For Babb, the Bank is still the vehicle for the US government’s hegemonic project – the transformation of neoliberal political economy into a functional transnational policy paradigm through structural adjustment. The policy response of conservative political forces in the US and UK to the inflationary crisis of the 1970s and the Latin American debt crisis of the 1980s was to facilitate the institutional capture of the Bank by market-oriented neoliberal political economy.<sup>17</sup> “...as a vehicle to promote ‘growth enhancing’ policy reforms, including ‘the privatisation of burdensome and inefficient public enterprises, the liberalisation of domestic capital markets, tax reform, the creation of more favourable environments for foreign investment, and trade liberalisation’”.<sup>18</sup>

This is a position Babb holds in common with a number of critical authors – for example, Mark Beeson and Iyanatul Islam; for whom the outcome of the crisis was the constitution of the Bank, through structural adjustment, as the “...principal conduit for the

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<sup>13</sup>Ibid. Pg. 275

<sup>14</sup> Chang, H., and Grabel, I., ‘Reclaiming Development from the Washington Consensus’, in *Journal of Post Keynesian Economics*, vol.27, no. 2 (Winter 2004-2005). Pg.287

<sup>15</sup>Stiglitz, J., E., ‘Is there a Post-Washington Consensus Consensus?’ in Serra, N., and Stiglitz, J.E., *The Washington Consensus Reconsidered: Towards a New Global Governance*, Oxford University Press, Oxford, 2008. Pg.43

<sup>16</sup> Cammack, P., 2002. Pg. 126

<sup>17</sup> Babb, S., 2013. Pg. 276

<sup>18</sup> Baker’s testimony in US House, 1986, pg.595-6, cited in Babb, S., 2013. Pg.275

*transmission of neo-liberal ideas to developing countries*".<sup>19</sup> Likewise for Fine, Bayliss and van Waeyenberge; the debt crisis was the terminal convulsion of the Bretton Woods order, and the point at which neoliberal perspectives:

*"...replaced a short-lived focus on poverty reduction that had emerged during the 1970s and had been combined with a generally favourable appraisal of the need for the state to intervene to promote development."*<sup>20</sup>

In these accounts, exemplified by van Waeyenberge in the same volume, US power is the determining factor in the shift from poverty reduction to structural adjustment. The transition followed from the political hostility to aid spending among neoliberal administrations elected in OECD countries in the context of the crisis of the Bretton Woods regime. The dominance of this ideology is epitomised by the appointment of Anne Krueger as chief economist, and the publication of the Berg Report as a pointed critique of the 'over-extension' of the state, reflecting US distaste for the 'welfare spending' of the McNamara years. The oil price and interest rate rises increased the need for aid, while the latter increased donor hostility to aid. During this period the Bank adopted a 'monoeconomics' which reasserted the economic rationality of all agents and advocated structural adjustment in order to allow the primacy of the price system and the incentives of private ownership to overcome the distortions created by governmental interventions. The neoliberal discourse of the Bank in the 1980s *"...easily lent itself to ideological affiliation with the right wing leadership of core shareholders in the Bank..."*<sup>21</sup>

The radical transformation of the Bank from the McNamara regime to the Clausen era is a theme which is also expressed by Ben Fine and Jomo Kwame Sundaram, who, like van Waeyenberge, cast the neoliberal era as a major intellectual and ideological break with its roots in the crisis precipitated by the oil price and interest rate increase: *"The McNamara-Chenery era of the World Bank – of 'growth with redistribution', meeting 'basic needs' and development finance – was set aside by Anne Krueger's efforts to roll back the state...such policy perspectives had their intellectual counterpart in seeking to 'rubbish' a caricatured*

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<sup>19</sup> Beeson, M., and Islam, I., 'Neo-liberalism and East Asia: Resisting the Washington Consensus', in *Journal of Development Studies*, 41:2, 2005. Pg.198-201

<sup>20</sup> Van Waeyenberge, E., Fine, B., and Bayliss, K., 'The World Bank, Neoliberalism, and Development Research', in Bayliss, K., Fine, B., and van Waeyenberge, E., *The Political Economy of Development: the World Bank, Neoliberalism, and Development Research*, Pluto Press, London, 2011.

<sup>21</sup> Van Waeyenberge, E., 'From Washington to Post-Washington Consensus: Illusions of Development', in Fine, B., and Jomo, K.S., *The New Development Economics: After the Washington Consensus*, Zed Books, London, 2006. Pg.24

*development economics, not least by appointing ideologue Deepak Lal as head of research at the World Bank.*"<sup>22</sup>

Fine and Jomo argue that appointments such as these were not, however, only the reflection of a Kuhnian paradigm-change in economics. They were active political efforts by the Reagan and Thatcher administrations to undermine the UN system by focusing on the Bank, and implant academically respected ideologues to offer intellectual currency to the structural adjustment concept. They conclude that dominating the Bank in this way is a recurring feature of the hard-power dynamics of the institution's relationship with the US, a position they support by pointing to the way Treasury Secretary Lawrence Summers 'forced' Stiglitz to resign following his 'modest retreat' from the Washington Consensus.

By continually emphasising the persistence of the hard power of the US in dictating the agenda of the Bank, these accounts foster the persistence of the Washington Consensus as a frame for understanding the Bank's role in contemporary governance.

Colin Crouch has been the latest to note that the return to growth and stability appears not to have disturbed the socio-economic compact by reformulating the regime of accumulation in a meaningful way.<sup>23</sup> Governmental responses to the most recent crisis of global capitalism have not displaced the neoliberal paradigm. Crouch's conclusion chimes with Babb's observation that the objectives and the instruments of both national governments and the international financial institutions have not changed to an extent that would suggest the development of a new paradigm, and that therefore *"...the Washington Consensus lives on."*<sup>24</sup>

Ben Fine has argued that the McNamara-era emphasis on modernisation and industrialisation has not been restored, in spite of the intense criticism the extreme nature of the neoliberal project expressed by the Washington Consensus. In fact,

*"...the newer development economics, in the form of the post-Washington Consensus, looks much more like the Washington Consensus than the old development economics that [it] sought to displace. This is especially so within the World Bank..."*<sup>25</sup>

Likewise Ha-Joon Chang and Irene Grabel :

*"...this updated Washington Consensus...seeks to save the core tenets of the original program from embarrassment and refutation by modifying a few of its*

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<sup>22</sup> Fine, B., and Jomo, K.S., 'Preface' in Jomo, K.S., and Fine, B., (eds) *The New Development Economics: After the Washington Consensus*, Zed Books, London 2006. Pg.viii

<sup>23</sup> Crouch, C., *The Strange Non-Death of Neoliberalism*, Polity, Malden MA, 2011.

<sup>24</sup> Babb, S., 2013. Pg.285

<sup>25</sup> Fine, B., 'The New Development Economics', in Jomo, K.S., and Fine, B., (eds) *The New Development Economics: After the Washington Consensus*, Zed Books, London 2006. Pg.2

*less central policy prescriptions...Indeed, the new thinking reaffirms and even extends the neoliberal character of the original...*"<sup>26</sup>

The contemporary consensus embodies the core of the old. Therefore, the political economy of the Bank is thus seen to be rooted in the politics of the collapse of the Bretton Woods system. This period is widely seen to have been one in which a radical break took place from Keynesianism to neoliberalism – the crisis of the Keynesian economic paradigm being reflected in a political realignment across the OECD and by extension, in the Bank.

This view relies on an historical perspective which considers the transition to structural adjustment not only to be a radical break from the Bank's previous agenda, but which depends on the presentation of the McNamara era as the most progressive in the history of the Bank.

Yet there is little reference in Fine, Jomo, and van Waeyenberge's work to the nature of the Bank's role in governance and its relation to the US during this or any earlier period. Instead, there is an assumed consonance between the intellectual paradigm of development economics and the political paradigm of corporatism – though the mechanism for the transmission and maintenance of this consonance is only expressed in terms of the fact that McNamara was an American, appointed by President Johnson after his chastening experience at the Pentagon. The basis for this is John Toye's observation that the 'old development economics' consisted in modernisation theory's roots in Keynesianism, which provided the intellectual underpinning for the Bank's support for state intervention in the transition from peasant agricultural to industrial capitalist society, in the footsteps – according to Rostow – of the West. As Toye has it the prevailing academic paradigm was one in which 'development' was constituted by *"...moving from traditional society...the polar opposite of the modern type, through a series of stages of development – derived essentially from the history of Europe, North America and Japan – to modernity, that is, approximately the United States of the 1950s."*<sup>27</sup> McNamara's pursuit of public intervention to this end followed this idea. It is implied that he was given the freedom to pursue this end because it happened to express US interests.

Understanding the transition to neoliberalism as the expression of American political domination of the Bank with the goal of intellectually underpinning strategic interests served by the policy of structural adjustment; is a consequence of understanding the preceding era as an era of 'embedded liberalism', and theorising the transition as the outcome of a coherent project of global scope. As Harrison has suggested, such accounts evidence a tendency to take

<sup>26</sup> Chang, H., and Grabel, I., 2004. Pg.275

<sup>27</sup> Toye, J., *Dilemmas of Development*, ( 2<sup>nd</sup> edition), Blackwell, Oxford, 1993. Pg.30-31, cited in Fine, B., 'The New Development Economics' in Fine, B., and Jomo, K.S., (eds) *The New Development Economics: After the Washington Consensus*, Zed Books, London 2006. Pg. 5



a deterministic view of the transition to neoliberal governance – and in so doing, obscure the crucial agency of the management of the Bank. Further, in using the Washington Consensus as an explainer of change in its own right, these accounts display a tendency to “...make an agent out of a concept.”<sup>28</sup>

I will argue that the Bank’s capacity to support the US hegemonic agenda was mediated from the very outset by financial imperatives. Negotiating a way in which these could be met shaped the strategies of successive Bank management teams, and defined the way in which they related to the objectives of US hegemony. By de-centring the power of the US state from analysis of the Bank’s role in governance and taking a longer historical view of the roots of the specific practices of neoliberal governance, I will illustrate the importance of the pragmatic engagement of Bank management with often complementary, sometimes contradictory imperatives of American finance and the US state in shaping the tools and practices through which the international order is governed. The agency of the Bank, and the character of the international order is deeply rooted in specifically American financial infrastructure and managerial practices and not defined solely by the imperatives of the state or the ideological character of incumbent administrations.

In the following two sections I will illustrate the problems which follow from the way in which US power is approached in contemporary writing about the Bank in neoliberal governance. These approaches can be situated along a continuum between two poles: the ‘Wall Street-Treasury Nexus’, and ‘relative autonomy’. In emphasising the importance of the crisis, institutional capture, and US power; and perhaps most importantly in conceptualising the neoliberal alliance of state and financial power as a novel political constellation which the Bank couldn’t resist – the transition is not theorised in a way that reveals the agency of the Bank, nor the way in which it is rooted in specifically American social relations of financial power and managerial practices.

## 2: The Wall Street – Treasury Nexus

As the insider critique of the Washington Consensus built to a crescendo in the later 1990s against the backdrop of the Asian and Russian financial crises, one of the most insightful responses to the calls made by Stiglitz and Rodrik *et al* for the articulation of a ‘post-Washington Consensus’ came from another Bank insider. Former staff member Robert Wade published a series of articles which argued that whatever the nature of the development

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<sup>28</sup> Harrison, G., *Neoliberal Africa: the Impact of Global Social Engineering*, Zed Books, London, 2010. Pg.27-8

economics which animated the analyses informing Bank project and programme interventions, the future of the Bank and its role in global governance would likely display a remarkable continuity. The institution would continue to function as an instrument of American hegemony, promoting free trade and capital movement in the face of evidence of the positive role of states in development, on the basis of US interests.<sup>29</sup>

Wade's earliest intervention was animated by the limitations of both neorealist and institutionalist theorising of the endurance of a liberal international trading and financial order centred on the Bretton Woods institutions beyond the collapse of the Bretton Woods system. The state had declined in relation to 'the market', and the international order was no longer seen to be predicated on the stability of US hegemony. These debates, largely in the pages of *International Organization*, tended to emphasise the autonomy conferred upon international organisations due to the power of rules in bureaucratic structures, and the way in which this gave the regime a life of its own beyond the causal factors of its foundation.

Wade's objective in relation to these contributions from Keohane and Nye, Krasner, and Ruggie; was to offer an assessment of the "...political and economic substance of the field of forces in which the Bank operates"<sup>30</sup> as the basis of a reconsideration of their claims for the autonomy of international organisations. Not only did the US directly intervene, but its capability to dominate the Bank's authorising environment enabled the American state to treat the Bank as part of its external infrastructural power in the post-cold war context. This was manifest in the Bank's ability to absorb a Japanese challenge to core ideas about the role of the state in development and shift the institution out of directly productive activities - away from developmental strategies likely to promote potential competitors to US capital or goods<sup>31</sup>. Claims to autonomy, Wade finds, are questionable at best.

From 1998, Wade took the insight from his Japanese case study a step further, and drew on free-trade advocate Jagdish Bhagwati's conceptualisation of the international financial institutions as components of a 'power elite': "...a definite networking of like-minded luminaries among the powerful institutions – Wall Street, the Treasury Department, the State Department, the IMF and the World Bank most prominent among them."<sup>32</sup> For Bhagwati, this

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<sup>29</sup> A perspective expressed with particular clarity in 'Wade, R., 'Japan, the World Bank, and the Art of Paradigm Maintenance: *The East Asian Miracle* in Political Perspective', in *New Left Review*, 1/217, May-June 1996; and Wade, R. H., 'US Hegemony and the World Bank: the Fight over People and Ideas', in *Review of International Political Economy*, 9:2, Summer 2002.

<sup>30</sup> Wade, R., 1996. Pg.3-4

<sup>31</sup> Wade, R 'The US Role in the Malaise at the World Bank: Get Up Gulliver', paper presented at the meetings of the American Political Science Association, San Francisco, August 2001. Pg. 16

<sup>32</sup> Bhagwati, J., 'The Capital Myth: The Difference Between Trade in Widgets and Dollars', in *Foreign Affairs*, Vol.77, No.3. 1998. Pg.11

powerful network was composed of ideologues who equated global interests with their own, and deployed their power of office to force the international institutions and their members to endorse the goal of free global capital mobility.

Although Bhagwati's formula is slightly extended to a 'Wall Street – Treasury – IMF' complex, the Bank is included in this network. Its elite-educated Wall Street-oriented agents are depicted as seeking to promote free mobility of capital and goods in the global economy to the detriment of alternative forms of capitalism and alternative approaches to development beyond that currently hegemonic in the US<sup>33</sup>. For Wade, the US faces a dilemma: on one hand, it needs the international institutions to push its Washington Consensus agenda – while on the other it needs the appearance of multilateralism.<sup>34</sup> Drawing on the Gramscian concept of hegemony, Wade argues that the US exercises intellectual and moral leadership through the Bank by promoting the belief that free market capitalism is beneficial to all, and that the procedures and processes of governance are applied to it too. Perhaps more significantly, US ideology in respect of the role of governments and markets constitutes the *"conceptual centre of gravity of Bank thinking"*<sup>35</sup>. Since a majority of Bank economists hold post-graduate qualifications from US universities, the Bank is located in Washington in close proximity to the organs of the US government and US think-tanks, and staff consume American print or TV media: *"American premises structure the very mindset with which most Bank staff approach development"*.<sup>36</sup>

The great strength of this approach is its ability to incorporate multiple factors in and features of US power: the hard power to withhold funding, covert power to dismiss prominent dissenters, and the soft power in the discourse of free-market capitalism. Wade's experiences as a Bank staffer have given him special insight into its processes of management and the nature of international relationships, and he is at pains to explore the extent of independence of the Bank in the context of the Stiglitz/Summers/Wolfensohn drama. For example, he argues that *"the US Treasury does not always get the Bank to do what it wants [...] the Bank may do and say what the Treasury wants for reasons beyond the fact that the Treasury wants it."* However, at the same time he concedes that *"you do not get to be a Bank economist without having demonstrated your commitment to the presumptions of neoliberalism and to the analytical techniques of Anglo-American economics"*, and that staff can expect a negative

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<sup>33</sup> Veneroso, F, and Wade, R, 'The Asian Crisis: The High Debt Model Versus the Wall Street – Treasury – IMF Complex' in *New Left Review* 1/228, March-April 1998. Pg.20

<sup>34</sup> Wade, R.H., 'Showdown at the World Bank', in *New Left Review*, Vol. 7, Jan-Feb 2001. Pg.127

<sup>35</sup> Wade, R.H., 2002. Pg.218

<sup>36</sup> Ibid.

response to any anti-free market research findings<sup>37</sup>. Wade aims to demonstrate the socially constructed nature of Bank and IMF policy in this way, and his most significant contribution is arguably in his exploration of the ideational consensus-building role of the institutions through the strategic practice of 'paradigm maintenance'. However, there are some important problems in Wade's location of the Bank in this elite political economic relationship nexus.

Firstly, the observations that Wade marshals to support the argument that the Bank is a more-or-less passive tool of American foreign economic policy relies upon a highly familiar roll-call of institutional features and constitutional relationships. Having included the US citizenship of the president, Congressional oversight of IDA replenishments, the strategic limitation of American intervention to 'negative' power to prevent the Bank acting or speaking against US objectives, the foremost among these remains the stocking of the institution's policy formulating organs with neoliberal intellectuals as a part of the broader US response to the contingencies of the crisis of Bretton Woods. Secondly, the broader implications of the Gramscian conception of hegemony which he draws upon to illustrate the limitations of the Realist variant are only hinted at. While Wade's reading of the concept allows him to emphasise the soft power of the US, exercised through ideational colonisation of the institution and the production of a commonsense, it means there is only very limited sociological substance to the elite nexus of policymakers of which the Bank is a pillar. This is a feature which Richard Peet seeks to improve upon in his 2009 survey of the institutions of global economic governance, *Unholy Trinity*.

Wade's works, and the extension of Bhagwati's 'Wall Street-Treasury' network to the 'Wall Street-Treasury-IMF' network by Wade and Veneroso, are important points of origin for Peet. As for Wade, the Bank is a recipient and a transmitter of American economic commonsense through its staff. Presenting policy to borrowers as a response to practicalities is the persuasive element of its role in the support of neoliberal hegemony, while the US' coercive capacity to discipline by withholding support for loans lurks in the background.

The globalisation of neoliberalism is, after Harvey, a 'spatial fix' to a crisis of accumulation manifest in the stagflation of the late corporatist era. Neoliberals, as agents of the global super-rich and the transnational bourgeoisie, have exploited the hard power of the advanced capitalist countries through the international financial institutions through the leverage provided by the structural indebtedness of the poor, to implement the Washington Consensus and restore profitability to the enterprises owned by the rich, and the dividends on

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<sup>37</sup> Ibid. Pg. 233

investments to the super-rich.<sup>38</sup> It is above all a class project. However: *“the trick lies in converting a politics, which represents a distinct class interest...into a practicality that appears to come from theory”*.<sup>39</sup>

Similarly to Wade, Peet observes that US soft power is visible beyond the IFIs in the central banks and treasuries of the developing world. From this basis, Peet notes that while there is a strong connection between finance and the World Bank, there is a *“far broader circle of consent than that formed in Washington, DC.”*<sup>40</sup> Capturing the nature of this circle, centred on Wall Street, entails the further expansion of the nexus to a ‘Washington – Wall Street Alliance’ of the US Treasury, the IFIs, and elite institutions such as Harvard, MIT, and investment banks. Including the educational institutions in Peet’s framework is the key step in augmenting the structuralism of Marxist accounts of class power, and the Gramscian concept of the social construction of hegemonic rationality.

Peet’s major contribution to the literature on the Bank lies in his effort to root changes in Bank policy in American social relations. The transition to neoliberalism is best understood as a response to the fractional conflicts within the hegemonic bloc – between the common-senses of Keynesian and neo-Classical liberalism. Drawing on Foucault, Peet argues that the discursive formations of elite economists are expressive of social conventions with a distinct class base.<sup>41</sup> These originate with the organic intellectuals of financial capitalism, in their seats at elite universities, and filter via academic literature into technocratic practices. These practices are further influenced by phenomena arising from the contradictions in hegemonic ideology in material practice. This leads to transitions in executives and civil service cadres and ultimately results in new marching orders for the international financial institutions from the imperial master.

However, very similar problems follow from this analysis. The weight of causation placed on relatively opportunistic implantation of neoliberal intellectuals in key positions, on the basis of the hard power of the American state echoes Wade very closely. Like Wade, Peet emphasises the Wall Street background of the Bank’s presidents – and stresses the commonality of their outlook with financiers.

Limiting the social linkages of the presidency and key management intellectuals to small elite networks leads to a difficulty over precisely how much agency the management has. In a perhaps unwelcome echo of the liberal Brookings Institution histories of the Bank, Peet

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<sup>38</sup> Peet, R., *Unholy Trinity: the IMF, World Bank, and WTO*, Zed Books, London, 2009. Pg.1; 244; & 250-252

<sup>39</sup> Ibid. Pg. 26

<sup>40</sup> Ibid. Pg. 17

<sup>41</sup> Ibid. Pg.24

takes successive presidencies as turning points in the narrative of 'development' theory, leading up to the debt crisis when the Bank caved to US pressure. Woods initiated a 'frustrated move away from economic growth' into pro-poor lending; while McNamara brought a 'crusading energy' to a return to a New Deal liberalism on the basis of genuine motivation to deal with poverty. As this initiative was also frustrated, McNamara drew on neoliberal intellectual currents to launch structural adjustment – and the change was sealed by US treasury pressure to appoint Clausen and Krueger.<sup>42</sup> The answer, then, would appear to be 'very little'.

These examples demonstrate that by limiting the social anchoring of the Bank to elite networks, the Bank's strategy is framed in terms of its congruence with these narrow epistemic communities. Behind this, at moments of crisis, the hard power of the stands ready US to implement its strategic objectives through the Bank by promoting institutional capture, as in the cases of Clausen and Krueger. Augmenting this slender sociology by emphasising the political nature of 'science' and the class power which confers legitimacy on discursive formations mobilised as hegemonic common-sense does not move substantially beyond this. Institutional capture can only be achieved by coercive means.

In the historical chapters I reconceptualise the social anchoring of the Bank to show that the turn to neoliberalism was not effected in this way, with the Bank forced by bitter circumstance to bargain with the financial fraction of the American bourgeoisie and accept the leadership of its organic intellectuals in return. Instead, I show that this relationship is deeply rooted in the financial infrastructure and managerial practices of American society than Wade and Peet's conception of the Wall Street – Treasury nexus will allow. Most importantly, the role of the Bank as an agent can be seen in that it has not only drawn upon, but through its pursuit of specifically institutional imperatives, has enhanced this infrastructural power and played a key role in its global extension. By focusing more sharply upon the exact institutional mechanisms through which the Bank was able to make 'pro-poor' lending legible to bankers I will show that, rather than deriving from institutional capture and US-led re-orientation during the 1980s, the roots of structural adjustment lie in precisely the Bank's most progressive moment.

Exploring these specific mechanisms invites an engagement with the body of recent Constructivist literature which has sought to emphasise the importance of social processes within the institution, and thereby to overcome the recourse to US power as an explainer of change in the Bank.

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<sup>42</sup> Ibid. Pg.134-8

### 3: 'Relative Autonomy'

In recent years, some of the most insightful and challenging literature on the Bank has come from within the Constructivist paradigm. Jeffrey Chwieroth has shown that the Bank was the foremost of the two Bretton Woods institutions in the management of the new international monetary and financial settlement prior to the return to widespread multilateral convertibility. More recently still, Patrick Sharma has offered a re-appraisal of the roots of the structural adjustment phenomenon on the basis of its endogenous origins. In so doing, they have forced a re-assessment of the coercive state-power centric analysis of the relationships which succour and limit the Bank.

These contributions have been developed in relation to the broad rationalist tradition exemplified by the Brookings Institution histories of the Bank. Commissioned by the Bank itself at the twenty-fifth and fiftieth anniversaries of its foundation respectively, the tomes laboriously compiled by Edward Mason and Richard Asher; Kapur, Lewis, and Webb; and Jochen Kraske and his team develop a narrative of change which is shaped predominantly by two factors. Firstly, the power of dominant states and financial markets; and secondly, the personality and national background of the Bank's president and senior management. The imperative to secure financial sector backing for the Bank's operations has meant that, since the McCloy presidency, these key personnel have been drawn from elite financial circles. To a limited extent, this 'constituency' has mediated the influence of the US government and during the golden years of the Bretton Woods order, this gave the institution relative autonomy from its principals. Kraske et al argue that this has meant that presidents drawn from the financial elite have had very significant personal, impact on policy, strategy, and organisational character<sup>43</sup> – a distinctly Whiggish historiography.

In this vein, Mason and Asher depict the institution as 'management dominated' due to donor disinterest at the turn of its first quarter-century, and contend that this situation would continue as long as it remained a project-lending institution.<sup>44</sup> Kapur, Lewis, and Webb offer a similar analysis in the Bank's 50<sup>th</sup> year – arguing that the new conservatism of the later 1970s meant that it had to follow 'global fashions'.<sup>45</sup> The limits to the Bretton Woods autonomy were revealed in the dominance of the US and historically 'over-weighted'

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<sup>43</sup> Kraske, J., with Becker, W.H., Diamond, W., & Galambos, L., *Bankers with a Mission: the Presidents of the World Bank 1946-91*, Oxford University Press, N.Y., 1996. pg.4-5.

<sup>44</sup> Mason, E.S., & Asher, R.E., *The World Bank Since Bretton Woods*, Brookings Institution, Washington, 1973. Pg. 725;736-8

<sup>45</sup> Kapur, D., Lewis, J.P., & Webb, R., *The World Bank: its First Half Century. Vol.1: History*, Brookings Institution, Washington, 1997. pg.21

European members in formal decisionmaking in this era.<sup>46</sup> Ultimately, while change is presented as ‘internal’ to the institution,<sup>47</sup> the fundamentals of the origin of the Bank as an ‘intergovernmental co-operative’ whose governance was rooted in political realism would continue to determine its role in global governance.<sup>48</sup> The transformation of the Bank is framed in the context of the erosion of the bilateral aid constituency in the US congress as the Republican Party embraced neoliberalism.

The objective of constructivist authors such as Chwioroth, Sharma, Babb, Park, and Vetterlein; is to move the Bank out from the long shadows of state-centrism, in which the Brookings histories stand alongside the Wall Street-Treasury nexus accounts. These authors follow in the path broken by Barnett and Finnemore’s observation that although the power of international organisations must be derived from the authority which constituted them; these institutions exercise a bureaucratic form of power in their own right, based upon the ability to manipulate knowledge in such a way as to shape the behaviour of other actors by articulating and diffusing new norms and rules.<sup>49</sup> Emphasis on formal and informal material mechanisms of control cannot provide a full account of change, and an exploration of organisational culture offers an alternative understanding of the processes through which institutions such as the Bank are able to successfully gain authority and act autonomously.

Approaching international institutions with an emphasis on the processes of change and strategic staff agency marks the distinction between Chwioroth and Sharma and their antecedents. While authors such as Barnett and Finnemore argue that the nature of IOs as bureaucracies drives them to maintain their power to constitute and regulate defined policy fields – embodying and disseminating norms by maximising their budgets, for Chwioroth, this gives rise to a perception of staff as hide-bound and underplays their role in change. Formal rules and informal staff behaviour do not always align, and norms, once adopted, can be subject to struggle over interpretation and application. This is Chwioroth’s major contribution to the constructivist canon on the Bank – which is a label he modifies, depicting his focus on change and staff agency as ‘strategic constructivism’.<sup>50</sup>

In the Bank’s case, Jeffrey Chwioroth observes two crucial moments in which the Bank was able to gain sufficient autonomy to become an agent in its own right. The first is the

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<sup>46</sup> Ibid. Pg.46

<sup>47</sup> Ibid. Pg.503

<sup>48</sup> Ibid. Pg.2

<sup>49</sup> Barnett, M., and Finnemore, M., *Rules for the World: International Organizations in Global Politics*, Cornell University Press, New York, 2004. Pg.27-9

<sup>50</sup> Chwioroth, J., *Capital Ideas: the IMF and the Rise of Financial Liberalization*, Princeton University Press, Princeton, 2010.



delegation by principals which was essential in the construction of 'interpretative authority', and the second is the reconfiguration of internal processes and procedures.

Firstly, then, the authority bestowed by states in the constitution of institutions of global governance such as the Bank is depicted as an 'interpretative authority'. Chwioroth points out that this was latent from the outset, in the ambiguity which arose from the wording of the Articles of Agreement concerning the Bank's mandate to offer general-purpose financing under 'special' circumstances. Chwioroth illustrates how this authority to interpret the constitutional document of the institution and set policy accordingly allowed the Bank to make loans to European members to support their balance of payments. Prior to the Marshall Plan, this was a significant stop-gap allowing them to meet commitments already made to largely American suppliers without which the tentative steps toward reconstruction could not have been made. Yet the most significant aspect, as Chwioroth describes, is that it moved the IBRD to the heart of the international system of liquidity provision at the expense of the IMF.<sup>51</sup> Secondly, an internal shift in the formal balance of power in favour of the management was effected in the course of the appointment of President McCloy which allowed sufficient autonomy from its principals for the agency of management to become decisive.<sup>52</sup>

This is extremely important, Chwioroth shows, for two reasons. This suggests, firstly, that as the Bank was simultaneously able to draw heavily upon the American capital market for its funding, state support was not the defining material prop for Bank action. Secondly, financial opposition to the second New Deal and its international components is often overstated; and the Bank was the central pillar of the new international monetary order.

This strategy had helped it stake a claim to the centre of the new order. Yet the Bank did not retain this position. Nor, importantly, did it continue to pursue the strategy of balance of payments lending which had been so popular with members. However, the long history of conditionality shows that the Bank has lent, in the main, for specific productive projects – not for balance of payments support. Where did this new norm come from? How did this change from balance of payments lending to US allies to wider project lending come about?

There are clear material considerations which Chwioroth acknowledges, but these relate to the position of the bank in the international order: Marshall Aid dwarfed Bank capabilities. Although it made the Bank's processes and structures more akin to those of its

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<sup>51</sup> Chwioroth, J., 'The World Bank, Stabilisation Loans, and Balance of Payments Financing: Lost Pieces of the Bretton Woods Liquidity Architecture' *Working papers*, 06-3, Scripps College, Claremont, California, 2006. (<http://eprints.lse.ac.uk/41824/>).

<sup>52</sup> Chwioroth, J., 'Organisational Change from Within: Exploring the World Bank's Early Lending Practices.' *Review of International Political Economy*, 15:4, October 2008. Pg.483.

most important financial backers, unlike DiMaggio and Powell,<sup>53</sup> Chwiero does not depict this as a case of ‘institutional isomorphism’. Rather, in terms of its role and strategy in this order, the most significant factors in the transition to the project model were internal processes and collectively shared beliefs.<sup>54</sup>

These features of the strategic and intellectual life of the organisation are mediated by rounds of recruitment. Staff who are aligned to specific practices and beliefs derived from their professional and educational background may be replaced or ‘supplanted’ by new staff with different ideas. These appointments and dismissals may lead to the development of ‘subcultures’, within which ‘norm entrepreneurs’ may emerge.<sup>55</sup> The ability to institutionalise the values and strategies espoused by these individuals and groups is dependent on their ability to win what Chwiero describes as a ‘battle of ideas’ (which he derives explicitly from Mason & Asher’s 1975 history<sup>56</sup>). Success in this regard is dependent on location within the organisation, and the possession of the discursive influence to outperform advocates of competing ideas.

The most important contribution which this approach offers in exploring the transition from the early program loans to the project lending model in the 1950s, and from ‘basic needs’ to structural adjustment, lies in demonstrating the way in which strategy and policy is socially constructed within the Bank. While such processes are constant, these transitions occurred at instances when it was undergoing crises – first of capitalisation, then potentially of solvency. These moments, in which the Bank acted to reconfigure procedures and processes in order to re-frame its relationship with the ‘authorising environment’, represent the turning points in what was an on-going strategic imperative, in which for the Bank as for the IMF: *“Power politics and Wall Street financial interests were not irrelevant, but they also were not the sole or even the decisive factor in shaping organizational behaviour.”*<sup>57</sup>

The importance of member states and financiers lies, for Chwiero as for Sharma, in providing an authorising environment which is flexible enough for the agency of the Bank as an institution to be shaped and directed by its staff and management.<sup>58</sup> While Chwiero concedes that the material factors emphasised by the various functionalist approaches to the Bank do matter – in the sense that they shape the Bank’s ‘authorizing environment’, it appears in this framework as though the relationship with financiers, in mediating the hard power of

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<sup>53</sup> DiMaggio, P.J., and Powell, W.W., ‘The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields’, in *American Sociological Review*, Vol.48, No.2, April 1983.

<sup>54</sup> Ibid. Pg. 482.

<sup>55</sup> Ibid. Pg. 492.

<sup>56</sup> Mason, E.S and Asher, R.E. 1973. Pg.74

<sup>57</sup> Chwiero J., 2010. Pg.29

<sup>58</sup> Sharma, P., 2013. Pg.671

the state, has solved a problem for the Bank. It is clear that the transition to the project approach and the transition to structural adjustment were critical junctures in the development of the Bank's agency in global governance. Further, the success of both Chwioroth and Sharma in illustrating the agency of management in dynamic internal social processes leading to normative and material change is a significant step in improving upon the understanding of the Bank as an institution characterised by 'mission creep' or an imperative to maximise its budget. But success in this regard is simultaneously the most problematic aspect of their analysis of the development of the Bank's agency in global governance.

There are difficult questions which may be asked regarding the specific processes at work in the transition away from a dominant established norm. Firstly, what compels line managers – as arbiters of strategy – to adopt the premises advocated by newly-hired 'norm entrepreneurs'? Chwioroth's account of these processes is ultimately dependent upon the relative power of rhetoric in conjunction with personal 'belief'. Yet because the mutability of common belief is not sufficient, recruitment rounds are deployed to bolster this factor as the determinant of such transitions. What is the difference between this thesis and the 'institutional capture' thesis of the Wall Street – Treasury Complex approach? It appears therefore that these transitions are a 'numbers game'. The more like-minded new-hires, socialised into specific beliefs through professionalisation or education, the more likely it is that their new norm could displace the old. This feature of the analysis therefore suffers from the same problems as the 'institutional capture' thesis of the Wall Street – Treasury complex approach: by over-determining the internal processes of change, it can only conceptualise the institution as socially anchored in the same narrow elite as Wade and Peet.

Secondly, relying on these narrow social linkages suggests that normative change in the Bank is the reflection of Kuhnian paradigmatic changes in the elite epistemic communities into whose practices new recruits have been socialised. Therefore, a further problem familiar to the Wall Street – Treasury approach is retained: the conceptualisation of crisis as an external trigger of the processes leading to paradigmatic change within the Bank. Further, the nature of the shift in paradigm is broadly the same: the transitions from the inter-war liberal international order to the Bretton Woods order and again to the neoliberal era are read as major historical ruptures. Similarly to the 'Wall Street-Treasury nexus' accounts, the outcome of characterisation of the Bretton Woods order as 'embedded liberalism' mistakes the convergence of the interests of the US state and financiers in the 1982 debt crisis and the broader neoliberal context for a novel political constellation, the power of which the Bank was simply unable to resist.

The inability of this approach to grasp the broad social anchoring of the Bank in specifically American financial relationships which have come in which every stratum of society is involved, is at the root of this failure to offer a satisfying account of the logic of these transformations. Only by addressing this issue directly will it be possible to offer an understanding of the development of the 'Washington Consensus' as a system of governance which does not underplay the Bank's decisive agency in this process.

#### 4: Anchoring the Bank

As we have seen, the origins of structural adjustment have been subsumed within the rubric of the Washington Consensus. The tendency to associate it, as the most significant tool of governance in the neoliberal era, with deregulation, liberalisation, and a turn to 'market' solutions in general, arises from the faulty identification of structural adjustment as rooted in a neoliberal politics enforced by American power. Common use of the term interchangeably with the 'Washington Consensus' as a synecdoche for neoliberalism has rendered the former a truly rascal term. Its continuing currency in contemporary accounts of the Bank's strategy and role in global governance reinforces these problems, obscuring the basis on which the endurance of neoliberal governance is rooted in the infrastructural power of finance and the mediation of the US hegemonic agenda by financial imperatives. The 'Wall Street – Treasury Nexus' and 'relative autonomy' approaches which underpin this narrative share three broad tendencies that perpetuate these problems.

Firstly, they continue to frame their analyses in the Polanyian narrative of a historical trajectory of 'dis-embedding' and 're-embedding' finance in the economy. By placing the contemporary Bank in this trajectory, they support the equation of the neoliberal intellectual and political paradigms with the narrower precepts of the Washington Consensus. By taking the nature of both the Bretton Woods era and the era of neoliberal governance as axiomatic in this way, as Broome and Seabrooke suggest, they create an analytical blind spot which prevents them from examining features of these eras which do not slot into the rubric of 'embedded liberalism' or the 'Washington Consensus'<sup>59</sup>. Through eliding these distinct phenomena in an artefact of US foreign economic policy these accounts continue to cast the Bank as an object of the US' hegemonic agenda.

A second point of contact is the conception that the transition from Bretton Woods to the neoliberal international order was a major historical rupture. The novel political

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<sup>59</sup> Broome, A., & Seabrooke, L., 'Seeing Like an International Organisation', *New Political Economy*, 17:1, 2012. Pg.8

constellation which seized upon this crisis, through which the state actively fostered a zero-sum transfer to the market, was simply too powerful for the Bank to resist.

Thirdly, they represent each transition - Bretton Woods to the Washington Consensus or Keynesianism to neoliberalism - as a set of outcomes which was clearly conceptualised and coherently executed. As far as the Bank is concerned, hegemonic and counter-hegemonic ideas are transmitted via institutional capture – either through the hard power of the US to hire and fire, or recruitment rounds through which the latest economic doctrine could be transplanted. Thus, the change in norms within the institution reflects Kuhnian paradigmatic shifts in the elite epistemic or professional communities into which management have been socialised, or whose interests they nakedly represent. The agency of the Bank is therefore socially rooted in narrow elites, and reflective of ideational change in elite epistemic communities. This gives rise to a tendency to over-emphasise the moral character of key figures such as presidents in pursuit of ‘development’. By exaggerating the ability of these individuals – of whom Robert McNamara is exemplary – to transform the institution, these accounts privilege the power of free-floating ideas above material imperatives arising from the social relationships of the institution other than that of the hard power of the US.

As a consequence these approaches erase the agency of the Bank in the construction of the Washington Consensus framework of governance, even as they insist on its centrality to it. By drawing on Williamson’s narrative of the tools of the Washington Consensus as expressed in the Baker Plan, they likewise struggle to grasp the importance of financial imperatives in mediating US hegemonic strategy – even though the Plan was itself a response to a financial crisis by which American banks were the most affected. This surprising lacuna is a consequence of the de-historicisation of the tools of neoliberal governance, and the tendency to root the paradigm of the Bank in the hard power of the US or narrow intellectual or business elites. It’s still the Washington Consensus, stupid.

Therefore, disentangling the history of structural adjustment from the Washington Consensus entails addressing the historiography of the foundation, consolidation, and decline of the Bretton Woods order which has placed it there as an expression of a neoliberal US agenda. To this end, I will undertake a revisionist history of the Bretton Woods era in order to offer an alternative account of the development of the Bank’s role in the ‘Washington Consensus’.

To begin to re-frame the familiar historiography of ‘embedding’ and ‘disembedding’ it is necessary to address the core conception: that the Bank’s strategy is a reflection of the hegemonic ideology of the US in each successive epoch. In as far as they both rest upon this assumption, the ‘Wall Street – Treasury nexus’ and ‘relative autonomy’ approaches are

reminiscent of another of Polanyi's aphorisms, that: *"Interests...like intents, remain platonic unless they are translated into politics by the means of some social instrumentality."*<sup>60</sup> By conceptualising the Bretton Woods and Washington Consensus eras as diametrically opposed to one-another, these accounts appear to suggest that particular social interests can be rendered suddenly inert or platonic; repressed by political design or invoked by crisis. While I concede that it is intuitive that specific social interests may require institutionalisation via 'some social instrumentality' (such as the Bank), in order to take on the character of a coherent and legible politics, it is clear that financial interests were not shut out of the political picture in the New Deal, and suddenly reactivated with the crisis of Keynesianism and the advent of neoliberalism.

In fact, as Martijn Konings has shown, this was an impossibility: American financial markets penetrated American society in a uniquely deep way. In considering the significance of the New Deal, Konings argues that *"Policy makers recognised that the growing connectivity of socioeconomic life was not just responsible for intense contradictions but also opened up new possibilities for public policy."*<sup>61</sup> Public authority was to be put to new uses: finance was not to be repressed, but to be harnessed. This meant that while the New Deal should manage finance actively, Roosevelt's administrations aimed to prescribe limitations to short-term speculation and curb volatility in financial markets. Yet as Panitch and Konings argue, this was aimed at *"precisely the fortification of key financial institutions and so an enhanced capacity to regulate the dynamics of expansion."*<sup>62</sup> The observation of changes to the modality of the power relations between particular social groups or sets of institutional actors need not be followed with the assertion that their interests have been suddenly neutered.

Such observations problematise the narrative of the 'embedding' and 'dis-embedding' of financial power. Hannes Lacher has argued that the New Deal should be seen as the foundation of a post-war order that promoted a universalising capitalism. In the longer run, he argues, it did not express the re-embedding of the market in social purpose but *"the dominance of a protectionist form of regulation of the market economy..."*<sup>63</sup> Further, in spite of the protection of national economies, the truly novel element of the post-war order was the extent to which society was *"...geared more directly to the exigencies of the economy; never was humanity defined more clearly by an attempt to render individuals into masses of*

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<sup>60</sup> Polanyi, K., *The Great Transformation: the Political and Economic Origins of Our Time*, Beacon Press, Boston, 2001. Pg.8

<sup>61</sup> Konings, M., *The Development of American Finance*, Cambridge University Press, Cambridge, 2011. Pg.80.

<sup>62</sup> Konings, M., Panitch, L., 'US Financial Power in Crisis', *Historical Materialism*, 16, 2008. Pg.13.

<sup>63</sup> Lacher, H., 'Embedded Liberalism, Disembedded Markets: Reconceptualising Pax Americana', in *New Political Economy*, 4:3, 1999. Pg.348

*'economic' men and women.*"<sup>64</sup> For Panitch and Konings, the specific feature of the New Deal was the correspondence of this endeavour with the integration of the working classes into the financial system. The Polanyian narrative which underpins the Washington Consensus story does not capture the social importance of finance in the US during the 1930s and the war years, and worse, "*...has served as the foundation of an overly-stylised periodisation of the half century after World War Two into two highly distinct orders...*"<sup>65</sup>

It is clear that financial interests were in no way rendered platonic; and they were not ideologically opposed to the Bretton Woods institutions. As Chwierothe points out, prior to the Marshall Plan, the Bank was the most important of the Bretton Woods institutions for the provision of liquidity internationally.<sup>66</sup> The Fund would not take on its proper role until multilateral convertibility was achieved in 1958, having been marginalised by the opposition of American financiers in the course of the ratification of the Bretton Woods Act. The Bank, on the other hand, Chwierothe points out, was welcomed. As it was then envisaged, by offering guarantees to private lenders, it would have functioned to re-introduce private American finance to the international capital markets.

Of the writing on this crucial agency in the creation and governance of the post-war order, Chwierothe provides one of two important contributions from the Constructivist paradigm. The Bank was, he shows, the central agency in the international liquidity architecture before multilateral convertibility. Further, its internal processes were key in shaping the tools which were deployed to create, support, and police the order. By focussing on the internal culture and institutional structure, and centring his analysis on the agency of management, he is able to highlight the way in which major changes in the Bank's lending approach took place at junctures and under conditions which do not correspond to the neat schema of paradigmatic shifts between 'embedded liberalism' in the Bretton Woods era, and neoliberalism in the Washington Consensus period.

The second comes from Patrick Sharma. Writing on the transition to structural adjustment, Sharma builds on Chwierothe's intervention by emphasising the bureaucratic imperatives which shaped management agency. The major contribution which Sharma is able to offer is his observation that the flaws in the Bank's operational procedures were a major catalyst in the change. To remain relevant, he argues, the Bank had to alter its procedures in order that it could disburse funds more rapidly. This suggests, as Chwierothe has shown

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<sup>64</sup> Ibid. Pg. 352

<sup>65</sup> Konings, M., Panitch, L., 2008. Pg.15

<sup>66</sup> Chwierothe, J., 2006.

regarding the project approach, that the shift to structural adjustment should likewise not be framed in the narrative and trajectory of the Washington Consensus.

However, the greatest problem facing Constructivist accounts is the issue of the specific form taken by the structural adjustment loan, or, for that matter, the project loan. Were these simply one choice, from a range of possibilities? Sharma offers the stipulation that the new lending model had to be quick-disbursing, and, by emphasising the bureaucratic imperative of the institution to survive, moves to head off the charge of voluntarism. Yet while he observes the importance of these internal processes, he does not explore their precise nature or origin and cannot fully explain why structural adjustment lending took the precise form it did. The charge of voluntarism must then stick.

In building on these accounts, I will focus my analysis on two features of the Bank. Firstly, I show that the nature and origins of the specific processes of institutional governance are of central importance for our understanding of the agency of the Bank. The techniques which McNamara used to control the institution were highly specific. They were not developed organically, within the institution, by norm entrepreneurs in a process of contestation. They were uniquely suited to the Bank's imperative as an institution: to continue to expand its drawings on private capital, in order to pursue the US' hegemonic agenda. These processes were at the cutting edge of American management techniques, and their extensive use of quantitative data modelling was familiar to US financiers. Their deployment made the Bank's programme workable. The specificity of the processes through which the Bank was managed is, I argue, crucial for our understanding of why structural adjustment loans were the vehicle for the lending expansion demanded by the combination of the dollar glut and the advent of monetarist inflation targeting in the US Federal Reserve system.

Secondly, I will show that the tools which the Bank deploys are shaped by its imperatives as an institution anchored in the social infrastructure of American finance. Crucially, although I argue that the Bank was a key institution in the evolution of what Konings and Panitch describe as the American 'informal empire', its methods have not been derived in a straightforward fashion from the hard power of the US, or through the transmitting of hegemonic American ideologies. They have been developed pragmatically, as the Bank's management sought to marry political pressures to act as an agent of US imperial governance and a development institution, with the particular requirements of American investors.



## Conclusion

By emphasising the way in which the institution is socially anchored within a specific framework of imperatives which form the parameters of management agency in pursuit of the US' hegemonic agenda, I will show that during the Bretton Woods era the Bank's strategies were shaped most profoundly by specifically American financial imperatives and technologies of management. Most importantly for our understanding of structural adjustment, I will show that it has its origins in the pragmatic engagement of management with the Bank's ongoing problem of capitalisation during the course of the 1970s – not in the selective 'neoliberalism' of the Washington Consensus.

Throughout the Bank's history, the agency of management in determining lending strategy and institutional structure has been located in these parameters. By placing the Bank in this framework, I will show that we can make space in our understanding of the material basis of imperial governance for the agency of Bank management, in a way which allows us to make sense of its contradictions and its continuities.

## Chapter 2: Neither *laissez faire* nor ‘Embedded Liberalism’: Re-enlisting Private Finance in Support of Bretton Woods.

In Chapter 1 we have seen that both currents in the specialised literature on the Bank are underpinned by an essentially functionalist understanding of its relationship with the US. In this literature, the Washington Consensus is a reflection of the US agenda of liberating the financial economy from regulations aimed at subordinating it to the directly productive economy of international trade.

In this chapter, I will show that this understanding of the contemporary order is dependent upon an understanding of the Bretton Woods order as the antithesis of the Washington Consensus. The Bretton Woods order is depicted as an expression of the US’ previous epochal objective of ‘embedding’ financial agents in a liberal international trade regime – subordinating the financial economy to the real economy of production.

The conceptualisation of the Bretton Woods era as an expression of the wholesale repudiation of the liberal *laissez-faire* tradition follows from the work of John Ruggie. In his *International Regimes, Transactions and Change: Embedded Liberalism in the Postwar Economic Order*, Ruggie follows Polanyi in arguing that the Bretton Woods order represented an iteration of liberalism which expressed a radical break with the inter-war order. The pre-1914 order had been based upon British power, and a liberal international trade regime on the basis of the gold standard as an external mechanism of economic adjustment. The Bretton Woods order on the other hand reflected two major shifts. Firstly, the transition to American dominance following the decline of British power in the inter-war period and the economic crises of the 1930s. Secondly, it expressed a change in the relationship between states and societies in European and Anglo-Saxon countries that demanded the insulation of domestic economies from the consequences of monetary adjustment. The marriage of US power to this common social purpose at the Bretton Woods conference constituted the hegemony of an ‘embedded liberal’ international regime.<sup>67</sup>

The most powerful articulation of this understanding of the Bretton Woods order has been offered by Eric Helleiner. In his classic account of the role of states in shaping institutional arrangements of the Bretton Woods system and its successor, Helleiner draws upon Ruggie’s concept of ‘embedded liberalism’ as a descriptor of the changed relationship between state and society after the New Deal. For Helleiner, the subordination of the financial economy to

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<sup>67</sup> Ruggie, J. G., ‘International Regimes, Transactions and Change: Embedded Liberalism in the Postwar Economic Order’, *International Organization*, 36, 2, Spring 1982. Pg.388.

the real economy of production and trade is most clearly visible in the adoption of controls on international financial transfers, designed to eliminate disequilibrating speculative flows.<sup>68</sup>

Helleiner's argument that the New Deal constituted a break with the 'liberal tradition' in international finance has had major consequences in terms of the way in which the role of the Bank in the post-war order is understood. The relationship which is conventionally taken to define the character and strategy of the Bank in the governance of the Bretton Woods order is that between its management, directors, and the formal states of its largest subscribers – with particular emphasis on the US Congress. The hegemonic agenda of the US is the agenda of the Bank

By rooting their understanding of the creation of these respective orders in the agency of the US as hegemon, these accounts promote a tendency to conceptualise the engineering of successive international orders as radical breaks with the practices of the old. The new political paradigms which constitute each respective hegemonic order are derived from the precepts of new intellectual paradigms in economics which reject and sweep away all traces of previous practice. The inter-war period was the era of *laissez-faire* liberalism, Bretton Woods was the era of Keynesian macroeconomic management, and the Washington Consensus is the era of neoliberal New Political Economy.

I will argue that while the Bretton Woods conference was a major moment of change in the international political economy, it did not represent the radical break depicted by Ruggie and Helleiner. I will show that the most immediate intellectual heritage of Bretton Woods lay in the efforts of financiers to overcome the liquidity problem of the Versailles settlement in the international monetary and financial conferences of the 1920s.

In making this argument, I will draw upon the re-conceptualisation of the power of the US offered by Leo Panitch and Sam Gindin, which suggests that the efforts to create a liberal trading order strongly reflected the interests and influence of American financial capital and contributed to the enhancement in the longer term of its global power;<sup>69</sup> and Martijn Konings' account of the roots of the financial relations of the Bretton Woods era in specifically American institutional forms emerging in the late 19<sup>th</sup> century.<sup>70</sup> These accounts suggest that the New Deal era reforms enhanced financial power in two significant ways. Firstly, they facilitated a profound expansion and deepening of social engagement in financial relationships – enhancing financial power at the infrastructural level. Secondly, they enhanced the power of

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<sup>68</sup> Helleiner, E., *States and the Reemergence of Global Finance: From Bretton Woods to the 1990s*, Cornell University Press, New York, 1994.

<sup>69</sup> Panitch, L, and Gindin, S., 'Finance and American Empire', *Socialist Register*, 2005. Pg.46.

<sup>70</sup> Konings, M., 2011. Pg. 8-9.

American financiers to exercise direct leverage in domestic politics and the governance of the international order.

The significance of these accounts for our understanding of the Bank lies in the way in which they invite a re-framing of the famously anti-financier rhetoric of the New Deal era, and the capital controls of the post-war period. These were primarily a European feature of the post-war international political economy: as these flows were mostly in the direction of New York and the safety of the dollar, they did not pose as much of a problem to the US. Therefore, in the US context, anti-financier rhetoric may be seen to reflect the social importance of finance.

As I will show, enlisting the support of American financiers was essential to the passage of the Bretton Woods accords through Congress. Coping with the problem of illiquidity which paralysed the international system in the 1940s required buttressing the foundations of the new institutions against the uniquely socially deep-rooted infrastructure of American finance.

Firstly, I will explore Helleiner's argument that the New Deal constituted a break with the 'liberal tradition' in international finance. Helleiner roots his narrative of this transition in observation of the political currents of the 1930s, such as the increasing regulation of international capital flows, assertion of Treasury control over monetary policy, and decisive moves away from the gold standard. I argue that while these are highly salient political features of the era, they are only proximate factors in the character of the Bretton Woods era and do not necessarily offer a full account of the importance of financial relations in American society which may be captured by a longer view. Therefore they do not imply, as Helleiner suggests, that the balance was tipped decisively away from the financiers of New York and toward the state in international economic affairs.

To begin to support this claim, in the second part of the section I will explore the longer and less familiar history of the antecedents of the Bretton Woods institutions in the international financial and monetary conferences of the 1920s. These efforts to solve the problem of international illiquidity in the context of the pre-Depression drive to return to a gold standard form the direct intellectual ancestry of the Bretton Woods institutions. The ideas which were debated at the Bretton Woods conference had their origins in the proposals for international banking institutions put forward at conferences in Brussels and Genoa, and in the Dawes plan, by private financiers acting as quasi-state agents to prop up the gold standard and maintain war debt payments.

In the second section of the chapter, I will explore how the ability of American financiers to find a solution – albeit temporary – to the problem of liquidity in the 1920s

reflected the infrastructural power of finance in American society indicated by Martijn Konings. While the era was replete with anti-financier rhetoric, as Konings and Leo Panitch argue, this reflected the increasing importance of finance in American society. The New Dealers' desire to break the Morgan monopoly and gain control of powerful tools of national monetary policy need not be understood as a vendetta against finance per se. I will show that those measures and institutions which are taken to have done the most to begin the process of 're-embedding' financial power functioned to increase the structural power of finance. As the first New Deal programme of financial regulation aimed to break up veteran financiers' cosy relations with the Federal Reserve, financiers increasingly lined up behind the Roosevelt administration.

In the final section, I will illustrate how crucial this support would be in gaining the passage of the Bretton Woods Act through Congress, and launching the new international monetary and financial order. It is striking that of the two institutions which were founded at Bretton Woods, the one which emerged from the ratification process the strongest was the IBRD. Financiers' opposition centred instead on the IMF – which had, it was feared, the capacity to supplant private international finance and help irresponsible governments to avoid adjustment. As it was conceived at this stage, the IBRD on the other hand took the re-establishment of international capital markets as its primary objective. Financiers' acceptance of the Bank and rejection of the Fund may have been predicated upon the assumption that the Bank would anyway be a temporary measure, but their direct influence constituted the IBRD as the central pillar of the international liquidity architecture. As in the 1920s, private finance was to be the means to overcome the dearth of liquidity in the international system.

In sum, finance should be positioned centrally in the story of Bretton Woods – and the anti-financier rhetoric which is given such prominence in the 'embedded liberalism' thesis should be located in the politics of American financial reform in the 1920s and 1930s. Making the new institutional framework viable was dependent on the enlistment of American financiers. Crucially, for our understanding of the development of the practices of the Washington Consensus, Bretton Woods was not a radical break with the practices of the *laissez-faire* era. As I will show, the deep infrastructure of American finance and the endorsement of American financiers was as essential to the new order as it had been to the Dawes plan two decades previously.

## 1: A Break with Liberal Tradition in International Finance?

According to Helleiner, the negotiations between the allied and associated powers at Bretton Woods represented the “*culmination of a long Polanyian ‘countermovement’ against the liberal financial practices of the nineteenth century.*”<sup>71</sup> This analysis builds upon John Ruggie’s account of Polanyi – which argues that while *The Great Transformation* may not stand the test of time given the internationalisation of production and finance from the 1950s onwards, it made the significant observation that in the 1930s a “*new threshold had been crossed in the balance between ‘markets’ and ‘authority’*”<sup>72</sup>. The reorganisation of the international economic order was an imperative, in order to ensure that it reflected the change in the relationship between the state and society that had undermined the political authority of the inter-war regime.

In this reading of the period, there are two key identifiers of the social ‘embeddedness’ of the post-war order. Firstly: the restriction on movements of capital, the better to protect the societies of national capitalist states from the previously superordinate imperatives of the global marketplace. Secondly: although the powerful banking houses of New York opposed moves to control capital movements and the foundation of the new institutions, they failed to halt the passage of the Bretton Woods Act through Congress and the Senate. This is the basis on which Ruggie and Helleiner argue that the inability of Wall Street to modify the plans of the Department of the Treasury tilted the balance of power decisively in favour of the state in international finance.

Helleiner argues that the transition away from the liberal international system began after the Federal Reserve, Bank of England, and the J.P. Morgan-dominated US financial community of New York ceased their efforts to resuscitate and prop up the gold-exchange standard after failing to halt a speculative run on sterling in 1931. Their efforts to support sterling represented the highest point on liberalism’s pendular arc, although a reaction against the social outcomes of external monetary constraints on national fiscal policy had been in gestation since the 19<sup>th</sup> century.<sup>73</sup> It is not difficult to see why this argument is so compelling.

From 1931, Helleiner points out, capital controls were more comprehensive and permanent. Most importantly, they were also situated in more broadly interventionist strategies of economic nationalism in those economies which had previously been constructed as bastions of the liberal international regime. The broad trend, particularly in the US and

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<sup>71</sup>Helleiner, E ‘Great Transformations: a Polanyian Perspective on the Contemporary Global Financial Order’, *Studies in Political Economy*, 48, Autumn 1995. Pg. 151

<sup>72</sup> Ruggie, J. G., 1982. Pg.388.

<sup>73</sup> Helleiner, E., 1994. Pg.28

Britain, was that national Treasuries assumed greater control over monetary affairs, at the expense of national reserve banks and financial communities.<sup>74</sup>

For example, in Britain after the break with gold, the Bank of England ceded control over monetary policy to the Treasury, which committed to balanced budgets until the outbreak of the Second World War. Japan and Germany introduced controls to maintain their balance of payments in the course of the 1931 crisis, and retained them in order to prevent capital flight and the pressures of speculation during subsequent experiments with active monetary policy and deficit financing. In the rest of the Gold Bloc, the Swiss, French, Belgians, and Dutch attempted to remain relatively liberal - but by 1939 full financial planning and capital controls became the norm<sup>75</sup>.

In the US, the Morgenthau's Department of the Treasury gained control over monetary policy once the gold standard was abandoned. Devaluation was undertaken in 1933, and the Treasury began operations to sterilise the inflationary impact of capital flight from Europe from 1936. Although the US did not itself deploy capital controls, it accepted and supported them elsewhere. Perhaps most importantly, Helleiner notes that the financiers of New York were popularly held responsible for the crisis, and that the Roosevelt administration sought to break the Morgan empire and reverse financial consolidation through government regulation<sup>76</sup>.

It is clear that bankers fervently hoped that the levels of international investment characterising the pre-Crash era could be returned to as soon as possible. It is also clear, as Carosso points out, that the events of the 1930s identified by Helleiner - the abandonment of the gold standard combined with the transfer of power from central banks to national treasuries which subsequently undertook experiments with capital controls and planning – constituted a series of major blows to bankers' direct political influence.<sup>77</sup>

Yet these seismic changes to the shape of the international system did not fundamentally alter the central contradiction of American foreign economic policy: as in the 1920s, maintaining the stability of the currencies at the core of the global economy still required the US to either increase the volume of goods imported from Europe and South America and sacrifice its own export surplus, or continue liquidity injections to Britain and Europe. As this balance of payments adjustment would have borne too high a political price, the latter strategy persisted. However, whereas these flows had been provided by American

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<sup>74</sup> Ibid. Pg.32.

<sup>75</sup> Ibid. Pg.29-33.

<sup>76</sup> Helleiner, E., 1994. Pg.30.

<sup>77</sup> Carosso, V., 'Washington and Wall Street: The New Deal and Investment Bankers 1933-1940', *Business History Review*, Vol.44, No.4, Winter 1970. Pg.445.

bankers across the period 1910-1931, in the medium to long term these flows could not be sustained without the state intervention which followed the cessation of hostilities in 1945.

During the 1930s, as the Roosevelt administration took the US off the gold standard, abandoned the London conference, and initiated the New Deal, restrictive tariff practices and exchange controls became the new international norm, while the Treasuries of the US and Britain remained largely committed to balanced budgets and orthodox economic principles. It was only following the onset of the war that Keynesian economics attained mainstream status. Helleiner points out that in their early drafts of the proposals which would eventually become the basis for the Bretton Woods negotiations, they both argued for capital controls to prevent speculative movements of currency from undermining national macroeconomic planning and the fledgling welfare state.<sup>78</sup>

The development of Keynesian economics, the ceding of monetary control to national treasuries, and the development of social democratic political currents in national politics are the proximate sources of the currents which would constitute the post-war international order. But there is a longer history to the practical and intellectual ancestry of the Bretton Woods organisations. For the origins of many of the ideas upon which Keynes and White would eventually draw in their plans for international agencies of monetary and financial governance in the 1940s may be seen in the 1920s. Thanks to the difficulties states found in negotiating the minefield of sovereignty and debt in the aftermath of the Versailles treaty, private financial actors took on quasi-official roles in achieving the only lasting multilateral settlement of the period. It was an era which Helleiner depicts as the antithesis of Bretton Woods due to the extent to which it was “...dominated by an initiative by private and central bankers throughout the advanced industrial world to restore the pre-1914 liberal international monetary and financial order in which they had been so prominent.”<sup>79</sup> This was the decade of the Genoa Conference, and the Dawes Plan: precisely the zenith of private financial planning.

### **Financiers & Solutions to the Problem of Liquidity: Historical Precedents for International Financial Organisation.**

The history of the drafting of the Bretton Woods Accord itself has been extensively covered elsewhere – not least by Eric Helleiner.<sup>80</sup> The history of the precedents which Bretton

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<sup>78</sup> Helleiner, E., 1994. Pg. 33-4

<sup>79</sup> Ibid. Pg.26

<sup>80</sup> Notably in Gardner’s *Sterling Dollar Diplomacy*, Block’s *Origins of International Economic Disorder*, and Oliver’s *International Economic Cooperation and the World Bank*, alongside the two Brookings Institution histories of the IBRD by Mason and Asher; and Kapur, Lewis, and Webb, respectively.



Woods planners drew upon in search of solutions to the problems of liquidity which could be operationalised in the post-war period is less familiar.

Proposals for a supra-national IBRD-like organisation which would variously lend for specific productive projects, limited balance-of-payments support, or simply guarantee private investment – were made throughout the 1920s. In the drafting of these proposals, financiers acted as quasi-state agents and would ultimately come to create the only lasting multilateral agreement on monetary and financial matters of the inter-war period, in the form of the Dawes plan. For Helleiner, financiers' success in reconstructing the international capital market after 1918 through lending to governments willing to return to balanced budgets, free capital movement, the independence of central banks, and a form of gold standard – as well as their activities at the major international conferences of the era – constituted nothing less than a 'bankers' victory'.<sup>81</sup> In the third part of this chapter, I will argue that the deployment of financiers as quasi-state agents in creating the conditions under which new lending to Germany could facilitate the repayment of Allied war-debts to US bankers and re-create the international capital market was an expression of the particular financial relations of US society in the Progressive era. Firstly, I will turn to the Bretton Woods institutions' antecedents as proposed at the Brussels and Genoa conferences of the 1920s.

From 1918 to 1929, American state objectives and those of private finance were closely interrelated. The shared objective was to stabilise European currencies in relation to gold in order to return to the automaticity in international monetary relations of the classical gold standard; and maintain repayment on war debts owed to private financiers. This was to be achieved through inter-governmental agreements regarding currency reform and austerity, intended to reverse the inflationary trends in prices and wages seen during the war years. Maintaining private capital flows to overcome the shortage of international liquidity was an essential corollary of this objective.<sup>82</sup>

US foreign economic policy expressed a contradiction which was widely discussed in the popular press throughout the 1920s and which remained a constant for the Progressive-era Republican administrations and Roosevelt's first New Deal administration.<sup>83</sup> The central problem remained that while "...for the United States to receive payment it was necessary that America should import additional goods from the outside world or else reduce her exports by a corresponding amount" there was "virtually no presumption at all that the United States

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<sup>81</sup> Helleiner, E., 1994. Pg.27

<sup>82</sup> Oliver, R., *International Economic Co-Operation and the World Bank*, MacMillan Press, London, 1977. Pg.12-13.

<sup>83</sup> Frieden, J., 'Sectoral Conflict and Foreign Economic Policy, 1914, 1940', *International Organization*, Vol.42, Issue 1, December 1988. Pg.82.

*herself would be willing to increase her imports in proportion to the growth of her interest claims.*"<sup>84</sup>

At this juncture the understanding of the means by which any defaulting debtor would gain the means to repay tended to emphasise the provision of liquidity. Therefore, from 1919, American embassies and private economic 'missions' sponsored by the State Department supported bankers' foreign activities. Most importantly, the majority of attendees of the major international economic conferences of the 1920s were bankers and economists. They were not official representatives of their governments: very few were diplomats or politicians, and only a small number were civil servants. Their orthodoxy in economic matters was informed by an anti-governmental and anti-nationalist discourse which reflected the tenor of post-Versailles sentiment<sup>85</sup>.

Although ultimately unsuccessful, these plans are the immediate intellectual heritage of the IBRD and prefigure some of the controversies it would face in its early years. Due to the intended function of proposals made at the international conferences of the era as temporary measures supporting a return to a gold standard regime, and their deployment in the 'embedded liberalism' narrative as contributing to the perpetuation of the 'dis-embedding' of finance during this era the Genoa-Dawes era and the Bretton Woods institutions are conventionally discussed in opposition to one another. Nevertheless, the Bretton Woods planners would draw upon the proposals put forward by financiers to overcome the problem of liquidity in Europe at international conferences during this period.

In the general approach to the problematic of reconstruction, it was recognised that private financial assistance from 'abroad' - i.e. the United States – was a pre-requisite<sup>86</sup>. Further, the desire among politicians, financiers, and central bankers to return to a stable and automatic liberal international regime during the interwar period was clear. Recommendations made by delegates at a conference organised by the League of Nations in Brussels in October 1920 exemplified this, stressing sound public finance, balanced budgets, halting inflation, returning to the pre-war gold standard, and creating the conditions for free trade. Representing the orthodoxy of the era, these proposals were enthusiastically endorsed by delegates – although they were not binding on the states participating in the conference.

Two proposals for international banking and monetary cooperation discussed at Brussels bore striking resemblance in certain of their features to the eventual operations of

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<sup>84</sup> RIIA, *The Problem of International Investment. A Report by a Study Group of Members of the Royal Institute of International Affairs*, Frank Cass & Co. Ltd., London, 1937. Pg 13.

<sup>85</sup> Haines, W. W., 'Keynes, White, and History', *Quarterly Journal of Economics*, Vol. 58, No.1, November 1943. Pg.105-6.

<sup>86</sup> Oliver, R., 1977. Pg.7.

the Bank, particularly in terms of the importance of the mechanisms for the supervision of the deployment of funds and materials.

The first came from Leon Delacroix, simultaneously finance, foreign, and first prime minister of Belgium, also advocated the foundation of an international institution. Members of an 'International Bank of Issue' would subscribe to shares by paying in gold - however, in a major point of difference to the IBRD, the amount of shares purchased would not determine the amount of capital members were authorised to access. However, the similarities to the eventual institutional structure of the IBRD are marked.

First, each member government would be represented at an annual meeting, and the voting power of each delegate would be determined by the number of shares held by the government. Second, the 'IBI' would be governed by a board of between five and nine members, who would be elected at an annual meeting for terms of five years. Third, authority to carry on the everyday operations of the IBI would be delegated to a managerial staff under a General Manager hired for that specific purpose. Fourth, the IBI would have the capacity to issue bonds, to grant advances, loans and credits to members, to negotiate, take legal action, and regulate the use of its own capital. Fifth, members would apply to the management for loans (although these would take the form of interest-bearing gold bonds), and the operating costs of the bank would be covered by that interest. Sixth, general assessments of creditworthiness would govern the volumes lent and the securities sought in terms of specific revenues. At bottom, it was expected that private banks in exporting countries would have to provide the credit for reconstruction: the bonds could be discounted with private banks by exporters who were in receipt of payment in bonds, as the bonds were intended to be equal in value to gold<sup>87</sup>.

This proposition was not a success: while the political discourse of European elites might have been anti-nationalist, the creation of another body which could infringe upon the sovereignty of the national state in this manner was beyond countenance. The capitalisation proposed was minute proposed to the needs of European reconstruction, and the expansion of the money supply through the issuing of bonds in this way threatened to undermine progress in the reduction of inflation. While the revenues of the borrower would have functioned as the real guarantee, the bankers upon whose involvement the scheme ultimately depended were unlikely to consider the paper of such an institution to be 'as good as gold'.<sup>88</sup>

The second proposal came from Dutch banker C.E. Ter Meulen, and was met with considerably greater enthusiasm. It was adopted by the Brussels delegates, and once taken up

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<sup>87</sup> Oliver, R., 1977. Pg.28-32.

<sup>88</sup> Ibid. Pg.31.

by the League of Nations, staff were appointed to the proposed bodies and for a very short period it became the basis upon which private capital was harnessed for Austrian reconstruction strategy from March 1921 onwards – until superseded by the negotiations at Genoa in 1922.

According to the Ter Meulen plan, the League of Nations would appoint a central international commission of financial experts. The borrowing government would notify this Commission of assets preferred as securities against which it would issue five or ten year interest-bearing bonds, which would in turn be lent to importers who would offer them to private financiers of exporting countries as security for commercial credits granted with which to purchase their goods. At the close of each transaction, the supplier of the goods would return the bonds to the importer, who would return them to the government.<sup>89</sup> As in the early operations of the IBRD the Ter Meulen financing arrangements concluded with Austria required austere fiscal policy<sup>90</sup>. Essentially, the basis was (as in the Delacroix plan) the use of the revenues of governments as security against credit, to be organised through the existing mechanisms of international organisation, and predicated upon the participation of private finance. The security of the private creditor was paramount.

Brussels had laid the foundation for the 1922 Genoa conference, called by Britain's Lloyd George. Seeking to promote international cooperation to restore the international economy, it was attended by thirty-four nations although the US was notable by its absence, exemplifying the hard-line attitude to war debts later expressed by President Coolidge: *"They hired the money, didn't they?"*<sup>91</sup> American truculence notwithstanding, Genoa represented the sole occasion on which intergovernmental negotiations addressed the problems of the European condition in the post-Versailles era in a comprehensive manner.

The proposals of the conference further pre-figured the practices and concerns of the Bank. A Central International Corporation would authorise and finance specific reconstruction projects, under the auspices of nationally-based private financing corporations, to be guaranteed by national governments. The Corporation was intended to operate under its own name in the countries where specific projects had been agreed, or, lend funds to national governments for specific projects subject to assurances on the rights of private property and 'justice' against the security of specified assets.<sup>92</sup>

These plans foundered against Soviet refusal to assume the obligations of the Tsarists, the French refusal to subscribe in Sterling, Britain's refusal to subscribe in Dollars, and

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<sup>89</sup> Orde, A., 1990. Pg.118.

<sup>90</sup> Oliver, R., 1977. Pg.34.

<sup>91</sup> Cited in Oliver, R. 1977. Pg.7.

<sup>92</sup> Oliver, R., 1977. Pg.10.

American refusal to subscribe at all, instead raising tariffs on total imports to almost 16%<sup>93</sup> to protect labour intensive industries. The most significant outcome of the conference was the commitment to the restoration of the gold standard, towards which 'order' in public finances and currencies was to be pursued. Expressed as an official resolution of the Genoa Conference, the reconstruction of Europe depended on "*...the restoration of conditions under which private credits, and in particular investible capital, will flow freely from countries where there is a surplus lending capacity to countries which are in need of external assistance.*"<sup>94</sup>

Efforts to legitimise the building of the new regime of monetary orthodoxy centred upon a new supra-national institution appear in this context as idealistic pipe-dreams, given the United States refusal to participate in the Genoa conference or to recognise publicly any linkage between the issues of reparations and war debts.

The only alternative available to American and European statesmen was to turn again to private financiers, whose objective remained to re-create an international gold-exchange standard regime. In a post-war environment in which the old ways of formal diplomacy were seen to have failed to keep the peace amongst the empires and contenders of the European continent,<sup>95</sup> financiers were well placed to insist that satisfying the private creditors of the USA, Britain, and France was an essential pre-requisite of the achievement of pragmatic solutions to the debt problem which could be presented to the Allied debtors.<sup>96</sup>

Faced with this imperative, in 1922 US Secretary of State Hughes publicly invited men of 'prestige, honor, and experience' to replace statesmen in consideration of the German economic situation with a view to working out how to finance reparation payments in the wake of their default in that year.<sup>97</sup> The outcome of these decisions was the Dawes Plan.

Signed in 1924, the plan drew upon new lending arranged by J. P. Morgan to prop up Germany's ability to meet reparation payments by reducing interest rates and agreeing new financing. The Dawes Commission's committee of financial 'experts' was convened by Leon Fraser, agent of the Reparation Commission, and subsequent President (from 1937) of the First National Bank of New York. The financiers' proposals were adopted by Allied and German governments at the London Conference of August 1924. The plan outlined a total amount that

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<sup>93</sup> Hayford, M., Pasurka Jr., C.A., 'The Political Economy of the Fordney-McCumber and Smoot-Hawley Tariff Acts', *Explorations in Economic History*, 29 (1), 1992. Pg.30 & 45.

<sup>94</sup> Resolution 16, 'Report of the Financial Commission' in Mills, J.S., *The Genoa Conference*, E.P. Dutton & Company, New York, 1922. Appendix V, cited in Oliver, R., 1977. Pg.10-11.

<sup>95</sup> Hughes, C.E., 'Some Observations on the Conduct of our Foreign Relations', *The American Journal of International Law*, Vol.16, No.3 (July), 1922. Pg.365.

<sup>96</sup> Feldman, G., D., 'Political Disputes about the Role of Banks' in James, H., Lindgren, H., Teichova, A., *The Role of Banks in the Interwar Economy*, Cambridge University Press, Cambridge, 1991. Pg.14.

<sup>97</sup> Parker-Gilbert, S., 'The Meaning of the 'Dawes Plan'', *Foreign Affairs* Vol.4, No.3, April 1926. Pg.iii.

Germany would repay annually – and excluded the threat of any new demands or sanctions. In sum, in 1924 Germany would receive an external loan, issued to the public as bonds at 92 basis points, paying 7% interest in New York, London, Paris, the Swiss exchanges, Brussels, Amsterdam, Stockholm, Milan, and Berlin, to the value of \$230m. The US bloc alone amounted to £110m underwritten by J.P. Morgan and company - in Europe by Morgan Harjes of Paris.<sup>98</sup>

On the Committee, as representatives of the European nations, were Sir Robert M. Kindersley and Sir Josiah Stamp (Britain - respectively a banker with Lazard Brothers and an academic economist); M. Parmentier and M. Allix (France - both bankers); Baron Houtart and M. Emile Francqui (Belgium – a civil servant and financier); and Dr. Alberto Pirelli and Professor Federico Flora (Italy – respectively a financier and businessman, and an academic economist). The American contingent was considerably larger, comprising: Charles G. Dawes, businessman, lawyer, and banker with the Central Trust Company of Illinois; Owen D. Young, a lawyer and subsequent chairman of the Board of General Electric and the Radio Corporation of America; Henry M. Robinson, philanthropist and banker with the First National Bank of Los Angeles; John E. Barber, a colleague of Robinson at First National Bank of Los Angeles; and Colonel Leonard P. Ayers of the Cleveland Trust Company, along with several academic economists from Stanford and Princeton including the globe-trotting apostle of the gold standard Professor Edwin Kemmerer<sup>99</sup>.

These financiers, businessmen, industrialists, and academic economists were valuable in this context precisely because, while they represented the major debtors and creditors of the 1914-18 period, they were not formally state agents. Their proposals would not be binding, and were a politically accessible combination of vagueness and concrete recommendations. Participants characterised the experts' report as an expression of a simple business transaction. According to George P. Auld, then Accountant General of the Inter-Allied Reparations Commission and assistant to Owen D. Young, the Dawes Loan was "*a basic contract between a willing group of purchasers of a promise to pay and a willing seller of his own credit*" which released 'dammed-up' forces of production and trade<sup>100</sup>. A prominent American Quaker businessman in France, J. Henry Scattergood wrote in 1924 that "*It needed the businessmen of the Dawes Commission to bring the world to the realities the politicians had so long hesitated to reveal.*"<sup>101</sup>

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<sup>98</sup> Auld, G.P., 1934-1935. Pg.11-12.

<sup>99</sup> Dawes, R. C., *The Dawes Plan in the Making*, the Bobbs-Merrill Company, New York, 1925. Pg.18.

<sup>100</sup> Auld, G.P., 'The Dawes and Young Loans: Then and Now', *Foreign Affairs*, Vol.13, No.8, 1934-1935. Pg.14.

<sup>101</sup> Scattergood, J.H., 'The Dawes Report – A Business Man's View', *Annals of the American Academy of Political and Social Science*, Vol.114, July 1924. Pg. 24.

In the 1920s the Delacroix and Ter Meulen plans failed to achieve the creation of a set of formal institutions which would manage international liquidity. Doing so was a political impossibility, on the grounds either that it infringed upon national sovereignty to too great a degree, or that it was likely to have problems of creditworthiness and create inflation. Conversely, by the 1940s, it was a political necessity to found the IBRD as part of a process of accomplishing the same goal. In each case, there was no other source of liquidity than that which could be made available through private capital markets. The first sets of institutions were abandoned in favour of direct popular participation in private financing, while the second set of institutions was adopted precisely on the basis of the imbrication of private finance in their very fabric. At this juncture, the structural imbalance of the international order was exacerbated by the illiquidity which was the legacy of the collapse of the NYSE bubble and the foreign bond market in the 1930s – to which direct private participation had been a major contributor. However, the solution was the same at each juncture – although the institutional technology which was deployed to achieve it was different.

Private finance was no less central to the new regime than its predecessor, and the methods and principles which the Bank and Fund would come to operate were developed with explicit reference to the plans put forward at Brussels and Genoa by private financiers.

The Dawes Plan itself prefigured certain of the practices for which the Bretton Woods institutions would become notorious: conditions upon lending were specified, supervisory capacities were institutionalised, funds were drawn from globally significant private capital markets, and governments guaranteed repayments. In the early years of the Bank's operation it was a commonplace among management that similarly to the Dawes Plan, the Bank would function as a temporary fix to a liquidity problem. The era of the Bretton Woods institutions was to be an interregnum, during which, while the problems of illiquidity and inconvertibility were resolved, private financiers could not retain their delegated roles in international negotiations. It was hoped that subsequently, normal service could be resumed rapidly.

## **2: From Progressive Reform to the New Deal: the Infrastructural Power of Finance and Shifting Political Alliances.**

So far we have seen how the 'embedded liberalism' thesis tends to counterpose the 1920s with the New Deal era, both internationally and domestically. For example, in considering the origins of the Bretton Woods institutions, the negotiations of the 1920s and the proposals of private financiers are not usually discussed. As they did not result in a lasting institution such as the Bank, or a glorious failure like the League of Nations – they are

considered to have been damp squibs, which were anyway aimed at restoring a set of practices antithetical to the ideas of Keynes and White. Yet as I will show in this section, their relevance for the political economy of the New Deal and the post-war era can hardly be overstated – and not only for the purposes of contrast.

It is for the purpose of contrast that the pronouncements of Treasury Secretary Henry Morgenthau concerning the role of private financiers in American society – and particularly in international finance – are conventionally deployed. His closing address to the final plenary session of the Bretton Woods conference has passed into the lore of the New Dealers' supposedly idealistic approach to the post-war order. The purpose of the Bank was to *"...to provide capital for those who need it at lower interest rates than in the past and to drive the usurious money lenders from the temple of international finance."*<sup>102</sup> Extensive use of this pronouncement is a recurring feature of the mythology of Bretton Woods as the foundation of the regime of 'embedded liberalism'.

Morgenthau's famous hostility to the usurious money lenders is often cited as the exemplar of the Roosevelt administration's hostility to finance. This enmity is largely considered to have been general, and reactive to the crisis of the 1930s. However, once located in the historical context of the Progressive reforms of the 1920s as a precursor to the New Deal, and the successive Pujo and Pecora hearings into corruption and monopoly in private banking by the agents of the House of Morgan, the real target of Democratic ire can be clarified. As Martijn Konings has shown, extending the participation of wider strata of American society in financial relations was one of the key objectives of the Progressive Republican administrations of the era. The preservation of this feature of US political economy became an objective of the reforms of Roosevelt's New Deal.

Not only did the quasi-official activity of financiers at international monetary conferences result in a directly useful legacy concerning the eventual institutional structure, scope, and practice of the IBRD, but the Dawes Plan in particular had a seismic impact in American society. Its short-lived success was due in large part to the unique infrastructural power of American finance.

The most salient feature of 1924 was the boom in foreign bond issues which followed the ratification of the Dawes Plan. On the basis of the supposition that European economies were now less unstable, private American investors purchased almost \$12bn of new foreign capital issues between 1920 and 1931. Whereas in 1923 the volume of US private investment

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<sup>102</sup> Kapur, D, Lewis, J.P, & Webb, R, 1997.Pg. 912.



in foreign markets was below \$400m, it had reached \$1.2bn by the end of 1924<sup>103</sup>. The Dawes loans themselves, taken together with the Young Plan and League loans to Austria, Bulgaria, Danzig, Estonia, Greece, and Hungary, reached a total in the region of \$1bn – less than 10% of total foreign capital issues between 1920 and 1931.<sup>104</sup>

The boom in investment in foreign issues which this triggered reflects a wider implication of Helleiner's 'bankers' victory'. Ordinary citizens became financially linked in large numbers with foreign governments and firms for the first time. From this we can infer that the centring of the international order of the 1920s upon the problematique of German reparations and the delegation of governmental functions in international economic diplomacy to private financial agents expressed the increasing infrastructural power of finance in American society – even while financiers and governments sought to re-create the external monetary restraint of the gold standard.

These efforts, on the part of Republican administrations of the Progressive era to perpetuate the centrality of private finance to the international system and return the monetary order to a 'sound' basis in gold, were a counterpart to their attempts to address the political problems which had followed from the industrialisation and modernisation of the US economy in the aftermath of the Civil War. A major aspect of their objectives – to correct modernity's social pathologies through rational bureaucratic interventions - rested on the conception of the necessity to manage the processes of industrial and financial concentration which had begun to emerge through the later 19<sup>th</sup> century. In practical terms, this had two major features.

One of the first items on the Progressive political agenda was to break the hold of the so-called 'money trust' on the boardrooms of the country's most valuable companies. Allegations of anti-competitive collusion by hundreds of major businesses and financial institutions centred upon J.P Morgan were corroborated by the Congressional hearings of the Pujo Committee, and saw the era become imbued with lasting anti-banker sentiment. This was exacerbated by the perception that bankers were able to manipulate the government to ensure that World War I debts would be repaid by any means.<sup>105</sup>

The Pujo hearings formed the backdrop to some of the most important Progressive legislation, including the Federal Reserve Act of 1913. In the context of public fears concerning elite cooperation and anti-competitive practices, the Federal Reserve System was founded as a decentralised network of Reserve Banks – rather than a centralised authority in the manner of

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<sup>103</sup> Rosenberg E. S., 1999. Pg.149.

<sup>104</sup> Fishlow, A., 1985. Pg. 418

<sup>105</sup> Carosso, V., 'The Wall Street Money Trust from Pujo through Medina', *Business History Review*, Vol.47, No.4, winter 1973. Pg.422.

the Bank of England. It was mandated to formalise the rules of credit extension – constituting the dollar as an asset-based currency in the context of the formal gold standard. In order to avoid the concentration of financial power so abhorrent to the public, a network of Federal Reserve Banks would therefore take responsibility for credit policy, which was understood as creating a market for banks' assets – bills of exchange, and commercial and agricultural paper – to ensure that the banking system remained liquid.<sup>106</sup>

As Konings observes, for all that Progressive rhetoric excoriated financial elites, this was not a significant challenge to the concentration of business ownership and financial power in the hands of the Money Trust. It was intended to restore 'sound financial conditions' i.e. to meet demand for credit, and although its institutional structure was decentralised, this had no bearing on the highly concentrated existing structures of financial intermediation which 'pyramided' the entire US financial structure on the Wall Street 'money centre' banks. As the Fed's mandate for credit-creation in response to demand for bank reserves saw it expand credit during upturns, and tighten it during downturns, this institutional feature would have major significance in the context of the Dawes plan and the boom in foreign lending – as I will explore below.

This relates closely to the second – and most essential – feature of the Progressive agenda: a process of detailed public and civic regulation with the objectives of promoting self-improvement, entrepreneurialism and competition in the domestic economy.

One of the key features of reform to working and middle-class people was the extension of formal credit. Following the First World War, instalment credit products other than mortgage lending were popularised, seeing borrowing and lending enter the social mainstream as a means to accommodate enhanced productivity by promoting consumption. As Martijn Konings has shown, during the 1920s, stock market speculation and new forms of lending and borrowing entered the middle and working-class milieu. The entrance of large numbers of small investors into the domestic and international capital markets through Progressive reforms effectively served the interests of the financial and corporate elites.<sup>107</sup>

The new features of the Progressive landscape of the US did not cause the bubble of the 1920s on their own: this was intimately related to the particular institutional nature of the American banking system, which was centred on the New York Stock Exchange, and the role it played in the international economy.

In this era the general character of international investment was already determined to a greater degree by the practices of New York than by the City of London. Following the First

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<sup>106</sup> Konings, M., 2011. Pg.56-8.

<sup>107</sup> Konings, M., 2011. Pg. 55-65.

World War, American financial methods and practices were highly influential. The entry of new groups into the capital markets combined with the newly-founded Federal Reserve's mandate to generate credit pro-cyclically led to increased volumes of funds being channelled into the stock market. Commercial banks promoted the holding of securities, and began to take on functions of investment banks such as underwriting, in their efforts to challenge the House of Morgan-oriented institutions of the so-called 'Money Trust' targeted by the Republicans.

Securities – commercial stock or government bills – were used by commercial banks to replace their cash reserves. A proportion of these reserves would be held on deposit at larger banks, which would in turn keep accounts with New York's largest financial institutions. The 'money centre banks' then used these assets as the basis for short term overnight deposits in the accounts of stockbrokers. These short-term loans were known as 'call loans', the profitability of which was predicated upon capital appreciation via the 'call rate', a feature of the volume of business done on the exchange. Short-term money was available at rates which were determined only by activity on the exchange - unlike in London, where short-term obligations were highly sensitive to international conditions, as they were only settled every two weeks. Call rates rose to fantastic levels during periods of expansion, and would suck funds in from rival exchanges.<sup>108</sup> The reforms of the Progressive era, combined with the centrality of the Wall Street to international capital markets led to the 'pyramiding' of almost the entire system's stock of rapidly realisable assets on the NYSE.

The potential returns on international investment through this pyramid were a major driver of the growth of the domestic US financial market. The attraction of foreign bonds to private American investors was rivalled only by the attraction of foreign bonds to New York's major issue houses. From 1918 until 1927, a larger proportion of US capital invested in new issues was employed abroad than at home. New issues on foreign account increased both in absolute terms, and relative to domestic investment, and the profits available attracted large numbers of foreign countries, municipalities, and corporations.

It was not just the prospect of the returns which could be gained from international investment undertaken by private individuals which made it such a central aspect of the extension of the infrastructural power of finance in American society. Again, this was related to the specific practices of US intermediaries: the profits to the issuing house consisted of the spread between what the ultimate borrower received, and the ultimate purchaser paid, with floatation expenses deducted. Foreign issues were passed through long chains of syndicates of banks and houses, selling onwards at ever increasing margins – investors enjoyed a positive

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<sup>108</sup> RIIA, 1937. Pg.167-8.

interest rate differential of between 1.7 and 1.9 points over domestic issues, and an average return of 6.4%. Bond salesmen were dispatched to new metropolitan bank branches across the US, which were not bound by the laws preventing branch banking – entailing higher costs and pushing the spreads up – in the pursuit of new investors. Eventually, the popularity of this market drew in sufficient new participants to force issue houses to drop their margins, making it cheaper for borrowers while continuing to yield above domestic investments<sup>109</sup>.

The way in which international investments were undertaken was therefore of huge importance to the international system. Large numbers of investment houses would compete over the same loan, incurring huge expenses while entertaining clients and bribing officials. The loans and their contracts provided a considerable market for US materials and services and employed engineers in large numbers abroad, and projects enhanced demand for the products of US industry. All manner of loans – for stabilisation, for productive purposes, residential developments, to church organisations and schools – were made as American promoters travelled widely in search of borrowers.

In a contemporary account, Cleona Lewis observed that:

*“Some of the more conservative bankers attempted to protect the public from the losses likely to follow unrestrained foreign lending, but there were many others who were urging loans upon foreign borrowers in excess of their requirements, and sometimes in opposition to the advice of responsible officials in the borrowing countries.”*<sup>110</sup>

The weaker the issue, the larger the spread – seeking out poor risks and selling them to gullible private buyers was strongly incentivised, to the extent that the Senate Committee on Banking and Currency would later comment that:

*“The record of the activities of investment bankers in the floatation of foreign securities is one of the most scandalous chapters in the history of American investment banking. The sale of these foreign issues was characterised by practices and abuses which were violative of the most elementary principles of business ethics.”*<sup>111</sup>

In 1927 the Peruvian president made a personal visit to New York to request that the size of the loan they were negotiating be halved: his request was refused, and several further loans followed. Lewis comments that a great many applicants demonstrated extravagance,

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<sup>109</sup> Ibid. Pg. 169-173.

<sup>110</sup> Lewis, C., *America's Stake in International Investments*, the Brookings Institution, Washington D.C., 1938. Pg.376.

<sup>111</sup> Cited in Fishlow, A., 'Lessons from the Past: Capital Markets During the 19<sup>th</sup> Century and the Interwar Period', *International Organization*, 39,3, Summer 1985. Pg.423.

wastefulness, and borrowed far more than they needed. However, warnings from both sides including from representatives of J.P. Morgan, and the Agent General for Reparation Payments in respect of new lending to Germany, went unheeded by the banking community and largely escaped the notice of the investing public.

After the crash of 1929, falling commodity prices and the decline in world trade and productive activity were structural conditions of the global political economy of the inter-war era. These obstacles to repayment were in fact consequences of American policy: imports were restricted, which was highly problematic for those debtors who were dependent on single product exports which were already impacted by falling prices.

Around 75% of total foreign bonds held in the US in 1929 were the obligations of municipal or local governments. By 1937 35-40% of foreign bonds issued were in default – nearly half were European borrowers with Germany alone counting for almost 32% of the total. 39% were South American countries, of which Brazil and Chile accounted for 22%. As local currencies sank against the dollar, the terms of repayment became even less favourable than they already were. Loans had been agreed at onerous terms of between 6 and 8%, in some cases reaching levels of 10.2% by maturity. If amortization charges were included, this often rose to 12-15% of the amount originally borrowed<sup>112</sup>. In terms of foreign private lending, the ultimate impact of the 1929 crash and ensuing Depression was that the US itself became a distressed creditor, with an aggregated sum outstanding of \$6.3bn at the end of 1935.

The salient feature of the era then, was the way in which mass participation in financial relations and the specific practices of intermediaries interacted with Progressive reforms in the context of the NYSE's centrality to international liquidity provision. This represented the deepening of the infrastructural power of finance, and it was this power which was reflected in the delegation of financiers to negotiate at the conferences which would shape the international monetary order prior to the Depression. Although Roosevelt appeared to follow in the ostensibly anti-financial traces of Progressive reformers, legislating more directly against the institutional concentration of the US banking system upon the 'money centre' banks of New York, these conditions would not be threatened by the New Deal. As I will show in greater detail in the following section, the 'anti-finance' rhetoric which emerged as a key feature of political discourse in this era was in fact designed to locate the Democratic project in the legacy of Progressivism and safeguard the involvement of anti-Morgan financiers in the historic New Deal coalition.

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<sup>112</sup> Lewis, C. 1938. Pg. 392-417.

### *Shifting Political Alliances and the Political Economy of the New Deal.*

The narrative of ‘financial repression’ which is developed at the centre of the ‘embedded liberalism’ thesis on the Bretton Woods era draws considerable credibility from the popular discourse of the Progressive era. It is clear enough that the zeitgeist remained significantly anti-financier or perhaps more accurately, anti- J.P. Morgan during the New Deal era. The public were again scandalised by the monopolistic practices and corruption revealed in the course of the Republican-initiated Pecora investigation into the Wall Street Crash. The level of public interest in the hearings as Jack Morgan testified during reached ‘hysterical’ levels<sup>113</sup>. Hysteria was also a driver in a run on commercial banks beginning in February 1933, which prompted US citizens to hoard cash – increasing private holdings by \$1.78bn between the 8<sup>th</sup> of February and the 8<sup>th</sup> of March. This led Roosevelt to call a bank holiday universalising the ad-hoc moratoria called independently across the country, during which Congress passed the Emergency Banking Act as a predecessor to the Banking Act of 1933 – which would become famous as the ‘Glass – Steagall Act’<sup>114</sup>. However, the resolution of the crisis of the 1930s which is emphasised in the ‘embedded liberalism’ thesis was contingent upon the enlistment of financiers in the cause of the New Deal.

The Roosevelt administration was determined to be seen to break up the close relationships between the Federal Reserve System and Wall Street by enacting legislation reigning in the FRBNY and bringing its powerful Open Market Committee under the control of the Reserve Board in Washington. Roosevelt also sought to protect investors through the foundation of the Securities and Exchange Commission with the remit to enhance oversight, improve competition, and undermine the House of Morgan’s hold on the financial system at large by enforcing the separation of deposit-taking commercial banking operations from investment banking under the terms of the Glass-Steagall act.

It is interesting to note the extent to which this objective has been mythologised in order to make it fit the narrative of the New Deal as a radical break with the practices of the 1920s which underpins the concept of ‘embedded liberalism. As I noted above, the quotation from Morgenthau’s closing address to the final plenary session of the Bretton Woods conference is frequently deployed as *prima facie* evidence of the New Dealers’ commitment to this end. Yet it is extremely surprising to note that it is conventionally distorted through

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<sup>113</sup> Pecora, F., *Wall Street Under Oath: the Story of Our Modern Money Changers*, Simon and Schuster, New York, 1939., Pg.4.

<sup>114</sup> Silber, W.R., ‘Why Did FDR’s Bank Holiday Succeed?’, *FRBNY Economic Policy Review*, July 2009. Pg.19-25.

paraphrase, or slightly but crucially misquoted, divorced from its context in the remainder of his speech.<sup>115</sup>

As Brett Christophers has pointed out, the word ‘only’ is omitted from its position in the famous quotation.<sup>116</sup> It is worth quoting this passage at length, as it appears in the minutes of the final plenary session of the UN monetary and financial conference at Bretton Woods on the 22<sup>nd</sup> of July 1944:

*“Objections to this Bank have been raised by some bankers and a few economists. The institutions proposed by the Bretton Woods Conference would indeed limit the control which certain private bankers have in the past exercises [sic] over international finance. It would by no means restrict the investment sphere in which bankers could engage. On the contrary, it would greatly expand this sphere by enlarging the volume of international investment and would act as an enormously effective stabilizer and guarantor of loans which they might make. The chief purpose of the Bank for International Reconstruction and Development is to guarantee private loans made through the usual investment channels. It would make loans only when these could not be floated through the normal channels at reasonable rates. The effect would be to provide capital for those who need it at lower interest rates than in the past and to drive only the usurious money lenders from the temple of international finance. For my own part I cannot look upon this outcome with any sense of dismay.”<sup>117</sup> (My emphasis).*

Wall Street may not have been invited to Bretton Woods, as Kapur *et al* have it, but Morgenthau was speaking in praise of the Bank’s role in support of finance – the IBRD would, by offering guarantees, complement private capital and facilitate the expansion of investment beyond its contemporary limits on a sounder basis than during the inter-war boom. This should be seen in the context of the effort to break the Morgan monopoly in the form of the ‘money trust’, as he alluded to only very slightly later in the same speech: “*Capital, like any*

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<sup>115</sup> Kapur, D, Lewis, J.P, & Webb, R, 1997. Pg. 912. See also Panitch, L., and Gindin, S., ‘Finance and American Empire’, *Socialist Register*, 2005. Pg.50.

<sup>116</sup> Christophers, B., *Banking Across Boundaries: Placing Finance in Capitalism*, Wiley-Blackwell, New York, 2013. Pg.154-5.

<sup>117</sup> Cited in *Verbatim Minutes of the Closing Plenary Session* (July 22, 1944, 9.45PM), Document 547 in *Proceedings and Documents of the United Nations Monetary and Financial Conference, Bretton Woods, New Hampshire, July 1-22, 1944 Vol 1*, United States Government Printing Office, Washington, 1948. Pg.1118-9.

*other commodity, should be free from monopoly control, and available upon reasonable terms to those who will put it to use for the general welfare.*"<sup>118</sup>

The 'usurious money lenders' had developed an extremely close relationship with the Federal Reserve system during its efforts to resuscitate and prop up the gold exchange standard from 1925-1931. The J. P. Morgan-dominated New York financial community and Federal Reserve Bank of New York governor Benjamin Strong continued to espouse the core ideal of the classical gold standard era: that monetary policy should be insulated from politicians' interference, while seeking to extend their own influence over it. Strong successfully lobbied for the central administration of open market operations in support of European currencies, which had been controversial among the member banks of the federal system<sup>119</sup>. Policy would be formulated by the Governors' Conference (the Federal Open Market Committee from 1930) and executed by the FRBNY, transforming it into a de-facto American central bank for international transactions – to which Washington remained 'indifferent'<sup>120</sup>. This coup meant that the established financial elites of Wall Street had been able to gain significant institutional influence over the main tool of US monetary policy.

It had been clear since the later 1920s that the adjustment mechanism of the international regime was not working to eliminate surpluses and deficits as it should, and that the capital flows which had previously financed current account deficits were too volatile to be relied upon.<sup>121</sup> Arguments for the gold standard had been forcefully made, and the House of Morgan and the Federal Reserve had undertaken major efforts to support established parities – of Sterling in particular. Yet austerity, strictly balanced budgets, and greater adherence to the rules of the system - which had been habitually broken in the US and Britain<sup>122</sup> - had failed to achieve stability. The rigor of such a position had already become politically unsustainable, and the scale of the problem posed an existential crisis for the financial systems of Europe and the US. Following the Wall Street Crash, as conditions deteriorated everywhere, so did prospects for successful management of the international monetary system through informal cooperation among central bankers and private financiers.

That the international monetary system of the 1920s was supported by financial practices which while stabilising in the short term in the longer term would confound hopes of

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<sup>118</sup>Ibid. Pg.1119.

<sup>119</sup> Konings, M., 2011. Pg.65

<sup>120</sup> Kunz, D. B., 'American Bankers and Britain's Fall from Gold' in James, H., Lindgren, H., Teichova, A., *The Role of Banks in the Interwar Economy*, Cambridge University Press, Cambridge, 1991. Pg.35-6.

<sup>121</sup> Eichengreen, B., *Globalizing Capital: A History of the International Monetary System*, Princeton University Press, Oxford, 2008. Pg. 61-66.

<sup>122</sup> Ibid. Pg.87



a return to stability and growth, became an article of common sense in the 1930s<sup>123</sup>. These features were stressed in the RIIA report of 1937 which cited Keynes' 1922 *A Revision of the Treaty* to the effect that the European dependence on American financial flows as seen in the 1920s was not analogous to America's heavy borrowing in European capital markets during the 19<sup>th</sup> century. By the time of the Hoover Moratorium and the abandonment of the gold standard in 1931, the connection between war debts and reparations was finally made explicit - after the US had received over \$2.6bn in war debt payments, the majority of which had been interest<sup>124</sup>. There was little likelihood that American investment would re-develop Europe because there was "...no natural increase, no real sinking fund, out of which they will be repaid."<sup>125</sup>

Although the political discourse of the age was replete with anti-financier rhetoric, it does not necessarily follow that finance was actually 'repressed'. The desire to break the Morgan monopoly and gain control of powerful tools of national monetary policy need not be equated with abandonment of the close relationship between the financial community and previous Republican administrations.

Fred Block expressed the currents in American political economy of the 1930s and 1940s concerning the role of the US in the international economy as a conflict between 'business internationalists' and 'idealistic internationalists'. Business internationalists, on the one hand, feared links between 'planners' and labour – high taxes and the attenuation of capital's power would cause US goods and finance to be priced out of global markets. This group sought a multilateral and open global system, in contrast to the 'idealists' who hoped to extend the New Deal internationally and create international institutions which would funnel capital into under-developed areas without the participation of private capital. According to Block, this division was reflected in governmental bureaucratic conflicts, between the idealistic anti-Wall Street planners of the Treasury and the Wilsonian free-traders among the business internationalists of the State Department<sup>126</sup>. The central issue for both was how to prevent a return to socially unacceptable levels of unemployment and simultaneously overcome the illiquidity of the international system of the inter-war era, exacerbated by the capital flight into the US in the late 1930s.

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<sup>123</sup> Fishlow, A., 1985. Pg.424.

<sup>124</sup> Oliver, R. W., 1977. Pg.8

<sup>125</sup> Keynes, J. M., *A Revision of the Treaty: Being a Sequel to The Economic Consequences of The Peace*, MacMillan and Co. Ltd., London, 1922. Pg.162

<sup>126</sup> Block, F.L., *The Origins of International Economic Disorder: A Study of United State International Monetary Policy from World War II to the Present*, University of California Press, London, 1977. Pg. 33-41.

The evolving foreign economic policy debate of the era did hinge on the export surplus, but perspectives on solutions and the constituencies taking positions in relation to this matter were not as monolithic or inflexible, or easily comparable to partisan politics between departments as Block suggests. The positioning of finance was relatively fluid in terms of its political support and while international transactions cleared 'automatically' in gold might well have been considered an ideal in some quarters, financiers engaged pragmatically with the new managed political economy in seeking to achieve *new* conditions for profitable investment.

The Treasury's moves to stabilise the dollar against the Sterling and Gold blocs, engineered by Harry White and Roosevelt's economic adviser-at-large in European relations Jacob Viner, were popular among the banking fraternity. The pronouncements of Leon Fraser of the First National Bank of New York are exemplary of this political flexibility, revealed in the transition between the first and second New Deal administrations. Fraser deplored the policies of the Roosevelt administration of 1933, while eulogising the policies of the Roosevelt administration of 1937 as a move toward an international policy which would incorporate the best of the old gold standard, corrected on the basis of contemporary experiences of currency management<sup>127</sup>

Finance houses such as J.P. Morgan and Company; Kuhn, Loeb and Company; or Dillon, Read and Company had historically been the most internationally oriented fraction of the business community, along with those industries which had grown profitable during the First World War. Their political interests were potentially as bipartisan as their business interests were diverse: it was revealed during the Pecora investigation that J.P. Morgan representatives had made attempts to influence prominent figures in business, finance, and both Republican and Democratic parties including Roosevelt's first Secretary of the Treasury William Woodin by privately offering discounted shares.<sup>128</sup> It was understood that the future of the international monetary system would not look the same as the past.

Industrialists related to the question of planning and protectionism, labour rights and taxation depending upon their relation with European competitors. Ferguson's study of the socio-political transitions of the New Deal era explores this fluid set of relations between political representatives, industrialists, and financiers. Older industrial concerns in steel, textiles, and coal, faced competitive pressures from European and Latin American firms and sought the protection of tariffs or specific bilateral trade treaties. These labour-intensive

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<sup>127</sup> Fraser, L., 'Economic Recovery and Monetary Stabilization', *Proceedings of the Academy of Political Science*, Vol. 17, No. 1, Economic Recovery and Monetary Stabilization, May 1936. Pg.113.

<sup>128</sup> Pecora, F., 1939. Pg. 31-33.

industries were characterised by bitter antagonism with unions, in contrast to a smaller group of newer capital-intensive industrial firms which had profited enormously from the First World War and within which labour relations were broadly more conciliatory. Organised according to modern Taylorist production models; these latter firms had less stake in Republican '*laissez faire*' social policies. World leaders such as General Electric found that rather than threatening competitors, European markets represented potentially lucrative zones of expansion. As the war had transformed the US into a net creditor, investment and commercial bankers, who had previously supported the Republican party's combination of aggressive nationalism and *laissez faire* international monetary and financial practices, found that their greatest interest lay in a multilateral trading system and advocated lower tariffs with a view to rendering their investments in capital intensive industry more productive<sup>129</sup>.

The withdrawal of governmental support to international investors during the Coolidge and Hoover administrations drove greater numbers of financiers and industrialists into this nascent internationalist bloc<sup>130</sup>. Within the financial community a further split developed in the previously Republican-oriented compact of banking and industry, as outrage among smaller and newer investment houses grew at the cosy relationship between the house of Morgan, fellow veteran institutions such as Kuhn, Loeb, and newer public organisations, particularly the FRBNY. The ability of these established firms to manipulate interest rates in order to support the viability of their own international commercial and financial interests drove newer and smaller firms such as Brown Brothers Harriman, Goldman Sachs, Lehman Brothers, the First National Bank of Chicago and Dillon Read into the arms of the Democratic party in the election of 1928. This was compounded by Hoover's international debt moratorium, and industrial and agricultural interests were further alienated by Republican attitudes against deficit financing, tariff rises beyond Smoot-Hawley, cartelisation, and 'easy' monetary policy. The shared interest of industry and finance in traditional liberal international political economy was disappearing.

Behind the first New Deal programme of financial regulation, expansionary domestic monetary policy, devaluation, and the protectionism of the National Recovery Administration, stood a coalition of industrialists, farmers, major anti-Morgan financial interests and oil companies. Recovery destabilised this coalition, as internationally-oriented industrialists and financiers sought to resume business overseas. However, the success of Roosevelt's banking reforms, moves toward freer multilateral trade, and stabilisation of the dollar combined with

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<sup>129</sup> Ferguson, T., 'From Normalcy to New Deal: Industrial Structure, Party Competition, and American Public Policy in the Great Depression', *International Organization*, Vol.38, Issue 1, December 1984. Pg.63-5.

<sup>130</sup> Frieden, J., 1988. Pg.82.

social welfare programs such as the 1935 National Labour Relations Act saw a reconfiguration of the Democratic support base. Crucially, by 1938, reserves had become sufficient to allow deficit financing without devaluation or significant protectionism – partly at the expense of the absorption of European flight capital. For financiers such as Leon Fraser, the bilateral agreements, managed floating, and negotiations with Latin American governments over defaults constituted highly welcome moves in the direction of the foundation of a functioning international capital market<sup>131</sup>.

A crucial element of the solution to the crisis of the 1930s was laid as financial interests lined up for Roosevelt. These included the established houses of the Warburgs, Rockefellers, and J.P.Morgan - as the second New Deal administration formed an historic coalition of high-tech industry, finance, and labour around issues of social welfare, free trade, Keynesian counter-cyclical spending, and oil price regulation<sup>132</sup>. During the Congressional hearings on the Bretton Woods Act, their support for the new institutions over Williams' Key Currency Plan, and the spoiling tactics of Republican Senators such as Robert Taft, would be crucial in the launching of the new international monetary and financial order.

### **3: Passing the Act, Founding the Bank.**

The re-constituted gold standard did not outlast the first year of the 1930s: the continual avoidance of adjustment by the leading players in the gold exchange standard regime which the Dawes plan had aimed to support ultimately prevented the system from functioning, and had led to increasing protectionism and volatility in capital flows. The New Deal had followed the collapse of the inter-war system, and as described above, financiers had been instrumental in attempts to reconfigure the social instrumentalities through which the international regime of the future would be structured and operated.

These efforts did not mean that financiers accepted the necessity of capital controls. Indeed, the trenchant opposition of certain of the foremost members of the New York financial community to the political consensus on the necessity of capital controls expressed by the US and British proposals is a prominent theme of Helleiner's account of the Bretton Woods regime. According to Mason and Asher, US commercial banks feared the creation of any institution which would compete with them; while Eckes describes private bankers as the 'natural' enemies of the new institutions. In seeking to undermine the proposals for the post-war liquidity regime, these bankers were part of a wider conservative group including the Wall

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<sup>131</sup> Frieden, J., 1988. Pg.86.

<sup>132</sup> Ferguson, T. 1984. Pg.92-3.

Street Journal, New York Times, and Chicago Tribune; and a vocal contingent of the Republican Party<sup>133</sup>.

These observations constitute the foundation of Helleiner's argument that the Fund and the Bank were founded in opposition to the wishes and interests of New York bankers. That the Act was passed by Congress in the face of this opposition is taken to mean that the interests of financial capital were not served by the Bretton Woods regime to the same extent as the 'liberal' regime which had preceded it, and by Ruggie to mean that they were 'embedded' in the relatively more socially legitimate interests of 'states' in building a regime based upon Fordist production and free trade.

Opposition to the institutions of the post-war regime centred upon the IMF as the principal lightning-rod of the critique of the financial community. Article VI, Section 3 of the IMF Articles of Agreement concedes the right to utilise capital controls to member governments, although this is hedged elsewhere in the Articles to discourage policy tools which functioned to delay transfer of funds in settlement of 'commitments' (Article VI, Section 3), or which could obstruct payments and transfers in relation to current international transactions (Article VIII Section 2a)<sup>134</sup>. In drafting its articles, British and American officials sought to create a system where capital controls would be the norm.

In White's original conception the Bank had featured as the stronger of the two proposed institutions, with powers to act in support of global full employment<sup>135</sup>. With a gold and local currency capital stock of \$10bn, 50% of which would be paid-in capital, it would depart significantly from multilateral orthodoxy by acting against financial fluctuations to support member currencies, stabilise commodity prices, and lend over long terms at low rates<sup>136</sup>. Bankers found themselves almost superfluous in the international system envisaged in this plan, and criticised it accordingly.

Nonetheless, in comparison to the IMF, Eckes' 'natural opponents' such as prominent banker Winthrop Aldrich, treated the Bank as relatively uncontroversial in the process of Congressional ratification of the Bretton Woods Act. Mason and Asher suggest that this may have been a strategic effort on the part of the financial community to present their position in

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<sup>133</sup> Eckes, A.(Jr.), *A Search for Solvency: Bretton Woods and the International Monetary System, 1941-1971*, University of Texas Press, London, 1975. Pg.165.

<sup>134</sup> Chwioroth, J.M., 2010. Pg.107.

<sup>135</sup> Block, F., 1977. Pg.43.

<sup>136</sup> Gardner, R.N., *Sterling Dollar Diplomacy in Current Perspective: the Origins and Prospects of Our International Economic Order*, Columbia University Press, New York, 1980. Pg.77.

such a way as to demonstrate that they were not entirely negative about the post-war settlement, and thus retain the capacity to influence it<sup>137</sup>.

While fear of being squeezed out by state financial capital was clearly a significant characteristic of private financiers' attitudes to the proposed institutions, their opposition was ameliorated by the idea that the new institutions would constitute a set of temporary measures aimed at creating a sound regime for international trade. This was also a feature of the early attitudes of members of Bank management. Sections of the financial community also expressed appreciation of the Bank's potential utility in establishing the conditions under which international investment would become profitable again, following the breakdown of relations between Wall Street and Latin American investors which had remained unresolved since the onset of the Depression. Further, the efforts of the anti-Bretton Woods grouping to reduce the scope of the IMF's operations would come to enhance the significance of the Bank in the short-term, and the same contingent's intransigence on the matter of capitalisation would necessitate close engagement with the bond market in a way which would institutionalise the interests of financial capital in the Bank's practices, policies, and personnel through to the present day.

These efforts began with a series of intensive discussions of potential revisions to the proposals which took place among officials from the State, Treasury, and Commerce Departments; the Securities and Exchange Commission, the Export-Import Bank, and the Board of Governors of the Federal Reserve System between April 1942 and January 1944. It was concluded that the new institutions were to co-operate with private financial agencies with a view to facilitating flows of private portfolio investment where this would not occur under 'normal' market conditions.

This was reflected in the substantially revised position evident in a January 1944 question-and answer document shared with foreign representatives: investment capital should be provided by private investment channels supported by Bank guarantees, and private capital was to be supplemented through Bank participation in loans, or 'encouraged' through direct lending. From this point onwards, the Treasury's concept of the Bank reflected financial concerns and aimed to encourage private capital to invest overseas by offering guarantees – its' primary function should be to share private risk, with direct lending as a secondary strategy<sup>138</sup>.

These concessions began to thaw the attitudes of the financial community, eliciting a statement from the American Institute of Banking (AIB) that it would likely have a 'wholesome'

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<sup>137</sup>Mason, E.S, and Asher, R.E., 1973. Pg.34.

<sup>138</sup> Ibid. 1973. Pg. 17-18.

effect on the volume and quality of international investment. The ability to consider loans in the light of the general conditions of member economies would enable it to help investors to overcome the excessive extensions of credit which had been at the root of the defaults which remained outstanding in 1944. Further, it would be able to coordinate lending policies to offset large fluctuations in international investment and hence to facilitate counter-cyclical policies.<sup>139</sup>

None of this was considered inimical to the activities of financiers: Bank guarantees would be essential in supporting private lending – the emphasis upon which the AIB particularly welcomed *“in view of the general disrepute into which foreign loans have fallen and the fact that the public in many cases may not be familiar with the position of the borrower and thus the quality of the security”*<sup>140</sup>. The importance of creating the conditions for long-term international investment called, in the view of the AIB, for the supervision of such flows by an international organisation<sup>141</sup>. This perspective was shared by the Executive Committee of the American Bankers’ Association (ABA) and the US Chamber of Commerce’s Finance Department. Their conclusion was that the Fund should be deferred, but the Bank should play a major role in facilitating the return of private capital to the international arena. Their attitude towards the IMF was an entirely different matter.

During the 1945 Congressional hearings, a loose coalition of isolationists, Republican business-people and laissez-faire conservatives began to coalesce around figures such as Republican Senator Robert Taft of Ohio and Winthrop Aldrich, the chairman of the Chase National Bank. Alongside other prominent Rockefeller-oriented Democrats, Aldrich had supported Roosevelt’s campaign during the formation of the first New Deal coalition when tensions between rival financial groups played an important role in redefining the national political agenda. Conflict with the House of Morgan over his chairmanship of the Chase had seen him personally lobby for the Glass-Steagall bill in order to further undermine Morgan’s interests<sup>142</sup>. In spite of this bitter conflict, Aldrich now found common ground with Morgan’s Thomas W. Lamont during the Congressional hearings.

Their opposition took a familiar form – around the same arguments which had confounded the Delacroix and Ter Meulen plans: the contravention of national sovereignty, and potential to cause inflation. Speaking on behalf of the Republican National committee, Aldrich attacked the Bretton Woods accords in his September 1944 address to the Executives

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<sup>139</sup> American Institute of Banking, Foreign Research Division, *Further Details on the Bank for Reconstruction and Development*, March 31<sup>st</sup> 1944. Pg.6

<sup>140</sup> Ibid. Pg.1-2.

<sup>141</sup> Ibid. Pg.7

<sup>142</sup> Ferguson, T., 1984. Pg.

Club of Chicago. Arguing that the Fund was little more than a trick by which governments would be allowed to avoid responsibility for enacting unpopular internal adjustments, Aldrich contended that the proposed institutions should be abandoned in favour of a return to a gold anchored system which would operate automatically to enforce adjustment in response to deficits and surpluses<sup>143</sup>. Prominent figures in the American financial community who had also previously supported the Roosevelt administration, such as Leon Fraser, Eugene Stetson (chairman of the Guaranty Trust), Gordon Reutscher (City Bank), George Whitney (J.P. Morgan and Company<sup>144</sup>), and most damagingly of all, veterans of the Federal Reserve system including American Bankers' Association (ABA) chairman W. Randolph Burgess, Edward 'Eagle' Brown of the Federal Reserve Advisory council, and both the FRBNY president Allan Sproul and vice-president John H. Williams, all lined up in favour of a supplanting the Fund with a stabilisation programme akin to the 19<sup>th</sup> century form of the gold standard.

Their alternative was formulated by Williams. The 'key currency plan' he proposed entailed stabilising sterling and the US dollar as a first order priority. These were the only truly international currencies, and their determined the relations between all others. Therefore, if this were to be achieved, international trade and finance could be organised without any kind of international governing body. To this end, Britain should be offered significant dollar funds in either credits or aid grants.<sup>145</sup> If sterling resumed an international role, Britain could pursue multilateral trade policies – and the City of London could reduce the strain on the scarce US dollar by re-opening as an international capital market. This would facilitate European – US trade, and obviate the necessity to engage in bilateral financing arrangements through the IMF, and costly nationalist economic policies. Leon Fraser, in an address to the New York Herald-Tribune Forum on November 21<sup>st</sup> 1943 suggested a loan of \$5,000m; while Aldrich, speaking before the International Business Conference at Rye, New York, a year later suggested a grant-in-aid of \$3,000m; and Williams suggested the continuation of Lend-Lease in May of 1945<sup>146</sup>. The ABA argued instead for the Williams plan and for the merging of the IMF with the IBRD<sup>147</sup>, and was supported in this by the Association of Reserve City Bankers, and the Bankers Association for Foreign Trade.<sup>148</sup> The system simply needed enough capital.<sup>149</sup>

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<sup>143</sup> Eckes, A.E., 1975. Pg.174.

<sup>144</sup> Woods, R. B., *A Changing of the Guard: Anglo-American Relations 1941-1946*, University of North Carolina Press, Chapel Hill, 1990. Pg. 229.

<sup>145</sup> Williams, J.H., 'Currency Stabilization: the Keynes and White Plans', *Foreign Affairs*, Vol.21, No.4, July 1943. Pg.655-8.

<sup>146</sup> Mikesell, R.F 'The Key Currency Proposal', *Quarterly Journal of Economics*, Vol.59, No.4, August 1945. Pg.569.

<sup>147</sup> Bitterman, H.J., 1971. Pg.83.

<sup>148</sup> Eckes, A.E., 1975. Pg.178.

<sup>149</sup> Block, F.L., 1977. Pg.52.



The bankers had a solid basis for their arguments: the problems of sterling were problems for the stability of any post-war monetary order and the viability of the Bretton Woods proposals. Under the IMF's Articles of Agreement, Britain was obliged to eliminate payments discriminations. To return to multilateral convertibility, Britain desperately needed funds to stabilise sterling at the head of the imperial trading bloc, and was attempting to obtain further budgetary relief by demanding write-downs of war-time debts to the US. Negotiations led to joint statements on trade and payments policy, and on the settlement of Lend-Lease. Under the Anglo-American Financial and Commercial Agreements, Britain achieved a loan of \$3.75 billion (although it had originally asked for much more, to Keynes' chagrin), and for an additional payment of £615 million, obtained a write-off of over \$20bn in assistance, and the transfer of \$6.5bn of US property located within her borders in 1945<sup>150</sup>. If London had not obtained a loan to this end, Parliament would have been unlikely to ratify the Bretton Woods Act, as it would have been put in the humiliating position of having to compete for dollars with other Fund members. Providing the liquidity sterling needed was essential – it was the capital the system needed.

Failing to provide this capital would have threatened the entire dollar-based blueprint for the post-war era. The Bretton Woods Act itself contained little in the way of specifics relating to how stable convertibility was to be achieved - the British loan and the Anglo-American Commercial Agreements constituted the essential 'nuts and bolts' of the achievement of the new settlement. The loan may have resembled an attempt to appease bankers by implementing the core proposal of the Williams plan; at any rate, it was strongly supported by the American Banking Association and the New York banking fraternity.<sup>151</sup> But it reflected a systemic imperative: its major purpose was to make Bretton Woods possible by deflecting the criticism which had been aimed at the Fund, and had threatened to scupper the entire settlement.

With the core of the Williams Plan in place, guaranteeing economic benefits to US industries and their financial backers, financiers' pressure groups were able to extract further crucial compromises concerning the role of the Fund to seal the passage of the Act. Firstly, moderate business leaders agreed to a proposal put forward by Beardsly Ruml (Treasurer of Macy and Co, and longstanding Roosevelt advisor) to the Committee for Economic Development think-tank to the effect that the Bank should take on the role of making short-

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<sup>150</sup> Mikesell, R. F., 'The Bretton Woods Debates: a Memoir', *Essays in International Finance*, No.192, March 1994. Pg.42.

<sup>151</sup> Ibid. Pg.50.

term stabilisation loans in lieu of the Fund<sup>152</sup>. The Fund, they agreed, would benefit from the protection of a narrower mandate which would prevent its exhaustion in relief and reconstruction, and potential accumulation of unstable currencies in the context of the instability of the immediate post-war years<sup>153</sup>.

Secondly, an interdepartmental committee was to be established to formulate US policy towards both institutions. The proposed committee eventually became the National Advisory Council on International Monetary and Financial Problems, chaired by the Secretaries of Treasury and Commerce, the chairmen of the Fed and the Export-Import Bank, although excluding the FRBNY. Secondly, policy coordination was to be further facilitated by uniting the posts of US governor in the Fund and the Bank, and likewise that of the American Executive Director. Ensuring that the proposals were accepted by the ABA was contingent upon Treasury agreement to seek an official interpretation confirming that the Bank could undertake short-term lending for stabilisation and balance-of payments support.

These twin compromises would come to define the subsequent character of the international monetary regime. The Bank would lend for stabilisation, at the expense of the Fund. Ultimately, the Bank emerged as the most important aspect of the international liquidity architecture and this would entail a particularly close relationship with the financiers who had sought to ensure that White and Keynes' vision was stillborn. Staff selection, governance, and lending practices were to be shaped decisively by this relationship. The new institution's first task would be to promote its bonds to American investors.

Financiers' opposition to the Fund ensured that the institution which emerged from the ratification process the strongest was not the institution which was capitalised by states. The Bank was – at least temporarily – to be the pillar of liquidity provision in the new international order, and it would draw its capitalisation from private financial markets. By enacting the core recommendation of the Williams plan, agreeing that the Bank would supplant the Fund in making short term stabilisation loans, and founding the NAC as a steering committee through which financial lobbyists would retain access to the US Executive Director of the Fund and the Bank, the Truman administration had secured the passage of the Bretton Woods Act through Congress and the British legislative apparatus – but had fundamentally altered the nature of its institutions.

That it was considered a political necessity to submit to the bankers' mauling of the Fund in Congress is suggestive of the extent to which it was considered a necessity to enlist financiers in the operation of the institutions which would govern the new international order.

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<sup>152</sup> Eckes, A.E, 1975. Pg.196.

<sup>153</sup> Chwioroth, J.M., 2006, Pg.16-19.

Without capitalisation from private investors, the infrastructure of the Bretton Woods regime would have been almost entirely impotent. The illiquidity of the international system was a problem for all fractions of the New Deal compact. Without the Bank's action as a stop-gap financier to Europe – which I will discuss in the following chapter – there would have been no exchange movements to control. The interests of financiers were indivisible from the interests of business and the state in this period, as the problem they faced was one they had in common.

Focusing on capital controls as the key determinant of the nature of the era is as misleading as focusing on the anti-financier rhetoric of the popular press and the Roosevelt administration itself – or the anti-Bretton Woods, or more accurately, anti-IMF rhetoric of financiers themselves. In so doing, the 'embedded liberalism' thesis and the many accounts which draw upon it, tend to underestimate the extent to which the very infrastructure of Bretton Woods required the enrolment of private finance. The place of finance in the story of Bretton Woods should more properly be understood as central and formative – not peripheral or oppositional. The success of the institutional framework demanded its enlistment.

## Conclusion

As we have seen, the depiction of the Bretton Woods order by Ruggie and Helleiner as a regime of 'embedded liberalism' in direct contrast to the 'disembedded' regime between the wars is somewhat misleading. Their understanding of New Deal anti-financier rhetoric as a signifier of a political programme which was antagonistic towards, and successful in repressing, the expression of financial interests in public policy follows from the emphasis they place on international capital controls. Yet from the US perspective, the financial movements of the era were not significantly destabilising and the US Treasury did not adopt capital controls in the manner of its counterparts across the Atlantic. Indeed, large flows into the US were actually favourable to the US agenda of building a new international order around the dollar: they were an essential aspect of the ability of the US to emerge as financier to European powers. For European economies on the other hand, the volatility of capital markets and the flight of European capital to the dollar was a significant concern. The centrality of capital controls as a signifier of the nature of the age may be argued to have been smuggled into accounts of the period via the protestations of Lord Keynes and his counterparts from the Treasuries of Europe in the feverish atmosphere of the Bretton Woods conference.

Taking a longer historical view uncovers a still more serious challenge to this narrative. Drawing on the work of Martijn Konings and Leo Panitch, I have illustrated that the anti-

financier rhetoric of the New Deal should be seen in the context of the problematique of the international financial order of the 1910s and 1920s. At the outbreak of conflict in 1914, European belligerents financed their munitions purchases through borrowing from the American public and American bankers. When the US entered the war in 1917, the government further tapped the American public through Liberty Loans and war bonds. During the inter-war period, J.P. Morgan and his associates were seen to have exerted direct political influence over the US government – and indeed over the entire international financial order in forcing the repayment of German reparations. This is the context in which Treasury Secretary Morgenthau's remarks on financiers must be situated. The New Deal programme was to be enacted in a society in which financiers had attained, through Progressive reforms aimed at increasing participation in financial relationships, an infrastructural power. During the 1920s, financiers were able to extend their reach into ever-broader strata of American society through innovation in credit products and the foundation of new investment institutions.

Crucially, this infrastructural power was reflected in the international order of the 1920s. Financiers were able to institutionalise a role as integral facilitators of the interactions of states at the international level – acting in concert with and on behalf of the formal institutions of states in international economic diplomacy. The problem of illiquidity in the aftermath of the Versailles settlement saw the conferences of Brussels and Genoa, as precursors to the successful transfusion of the international system with private American capital after the agreement of the Dawes Plan. Mass American participation in the purchase of foreign bonds followed this agreement – the default of which, after the Wall Street Crash of 1929 and the onset of the Depression, would set the immediate parameters of Bank action, once the necessity of basing its operations in private capital had been realised. More immediately, the proposals of financiers at Brussels and Genoa for an institution providing guarantees to private investors in order to inject liquidity back into the international system, would provide the intellectual foundations upon which the Bank was built. The infrastructural power of financial capital was steadily enhanced, becoming increasingly embedded at each institutional level.

This heritage could not be erased by administrative fiat. Even during the first New Deal as financiers' reputations reached their nadir in public political discourse during the Pecora investigations of the 1930s, they were not dislodged from their privileged positions as quasi-formal actors in the state apparatus. The Roosevelt administration courted the support of younger financial houses assiduously in its campaign against the Morgan empire. While the involvement of prominent private financiers in international negotiation was diminished during the Bretton Woods negotiations in comparison to the Dawes regime, they were not

displaced from the process. While financiers may have lost some of the direct leverage in the political process along with their roles as international negotiators, their infrastructural power endured. This infrastructural power had grown from structural necessity. This was largely because the central problem faced by the US and Europe endured throughout the efforts to return to orthodoxy in the 1920s and the turn towards nationalist macro-management in the later 1930s and the years of the second world war remained the same. The common obstacle was the basic illiquidity of the system and the problems of convertibility and attendant barriers to trade which that engendered. The refusal of the surplus economies to undertake the adjustment an automatic system dictated meant that continued capital transfers were required.

The objective of the 1920s was to reconstitute an external autonomous mechanism for the management of international transactions and trade, and the objective of the 1940s was to replace it with a mechanism capable of stabilising national macro-management and multilateral trade simultaneously. At each juncture, this required the reconstitution of the private capital markets. The consequences of this were dramatically demonstrated during the Bretton Woods era.

What is the importance of this evidence for our understanding of structural adjustment lending, and the narrative of the Washington Consensus? The impact of the features of the 1920s on the political climate of the 1930s is renowned. Yet the evidence of the strategic utility of finance, on the basis of its social importance, to the agenda of the New Deal has only recently been recovered through revisionist histories of the period. These illustrate the uniqueness of the American financial infrastructure, and its relationship to the US state. This was, these accounts have shown, unlike the *haute finance* of Europe: mass engagement in financial relationships was the basis of increasingly close linkages between the American state and financial markets. I argue that this transformation, in train through the Progressive era, was reflected in the foundation of the Bank.

In the form in which it emerged from the Congressional ratification process, the Bank had been decisively shaped by financiers ideas and strategic political support. The social basis of the Bank in the infrastructure of American finance, which I have illustrated in this chapter, would set the parameters within which management could pursue the imperial agenda of the US throughout the Bretton Woods era, and beyond, into the era of the Washington Consensus. This social basis in the infrastructure of American finance would shape the Bank's imperatives as an institution, in the development of the practice of structural adjustment just as much as in the Bank's earliest operations. The financial imperatives which had already begun to shape the

emergent parameters of Bank action in 1945, would mediate the imperial agenda of the US from the outset.

As I will show in the following chapter, this would have an immediate impact on its relationship with the US, its organisational structure, and its lending practices.

## Chapter 3: Morgenthau's Usurers and the Temple of International Finance.

*"Keynes always said you needed more money."*<sup>154</sup>

Emilio Collado, US Executive Director.

In Chapter 2, we saw that while the Bretton Woods conference was an affair of states and statesmen, the imperative of guaranteeing financiers' backing began to mediate the agenda of the US in the constitution of the post-war order even as the Act passed through Congress. Financiers were not displaced from the political process by the New Deal: the founders of the Bretton Woods institutions drew upon the practices of private financial planners in the 1920s in the design of the new order. Anti-financier rhetoric must be understood as an aspect of an effort to reorganise finance in support of national economic management in a multilateral international order. Thirdly, the leverage afforded by the imperative of guaranteeing their participation meant that financiers were able to secure compromises which constituted the IBRD as the principle source of liquidity in the new international system at the expense of the Fund. The visible legacy of the 1920s in the basis of the Bank's operation in private capital suggests that the balance of power in international finance was not tipped as decisively in favour of the state as Helleiner suggests.

In this chapter I will show how the foundation of the IBRD on the basis of private financial capital mediated its pursuit of the US agenda from the outset. This is visible in the struggles between the Executive Directors and management over a series of major changes wrought to management structure and lending practice of the new institution within the first five years of its operation. These features of the Bank owed more to the practices and problems of American financiers than to the idealists of the New Deal or the pragmatists of the Truman administration.

Finding a way in which to meet the immediate problem of capitalisation required further major changes to the Bank's personnel, structure, and strategies. The Bank could not look to the major economies of the pre-war era. In some respects, this is intuitive: the rationale of its very existence was to foster a liberal international trade regime by helping to overcome the shortage of foreign exchange among the old imperial European powers, whose monetary policies had been thrown into disarray by the exigencies of war, and whose currencies were inconvertible. Therefore, in order to do so, it would be forced to mobilise the

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<sup>154</sup> Wilson, T. A. & Richard D. McKinzie. *Oral History Interview with Emilio Collado*, New York, NY, 7<sup>th</sup> July 1971, Pg.38. <http://www.trumanlibrary.org/oralhist/collado1.htm>

support offered by financiers in exchange for the downgrading of the Fund during the ratification process.

Understanding the nature of the Bretton Woods order as a regime in which the agency of the US was mediated significantly by the imperatives of financiers is of signal importance for our understanding of the Washington Consensus. Rather than subordinating the power of American financiers to the Keynesian liberal compromise, Bretton Woods institutionalised the extension of its infrastructural power to the international level. As I will show, the era against which the Washington Consensus is commonly defined begins to take on a different complexion: the extent to which the US agenda would be mediated by the imperatives which had begun to emerge in the process of Congressional ratification would rapidly become clear in the course of the Bank's earliest operations.

The centrality of financial interests as a decisive factor in the transitions made by the Bank in its first five years of operation has been widely discussed in the literature concerning the governance of the Bretton Woods system. Yet the conventional frame for these discussions of financial interests remains the agenda of the US state, which is seen to overdetermine the agency of financiers in setting the trajectory of the Bank.

The account offered by the Brookings Institution historians of the Bank argues that the appointment of John J. McCloy as the second President after less than a year of operation represented nothing less than a coup executed by Wall Street.<sup>155</sup> His appointment was predicated upon the re-assignment of operational control from the Executive Directors – as representatives of member states – to management. As Kapur, Lewis, and Webb argue, McCloy wanted to send a positive message to Wall Street to the effect that subsequent decisions would be made on an economic rather than a political basis. Accordingly, he recruited a management team which was strikingly representative of the American establishment – lawyers, bankers, and corporate officers with impeccable credentials among the financiers of New York. Mason and Asher argue that financiers saw this move return some of the prestige that the Bank had so rapidly lost after Bretton Woods.<sup>156</sup> The institutionalisation of lending for productive projects was simply a strategic decision taken to appeal to this external constituency.<sup>157</sup>

However, these accounts still regard these developments as taking place in a framework delineated most decisively by the power of the American state. For Kapur, Lewis, and Webb, it represented a short term victory – a strategic move which permitted the Bank to

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<sup>155</sup> Kapur, D., Lewis, J.P., & Webb, R., 1997. Pg.79

<sup>156</sup> Mason, E.S., & Asher, R.E., Pg.129.

<sup>157</sup> Kapur, D., Lewis, J.P., & Webb, R., 1997. Pg.7



gain the capitalisation it needed to begin operations in earnest.<sup>158</sup> Ultimately, they locate this moment in the trajectory plotted by Helleiner's historical analysis<sup>159</sup>, and after Gardner, argue that the Bretton Woods institutions aimed to make finance subservient to 'human desires' in the international as well as the domestic sphere of politics.<sup>160</sup> The limited extent to which this 'coup' is considered to have meaningfully altered the trajectory of US-Bank relations is confirmed by their characterisation of the Bank's support for US' anti-communist 'development' agenda on the basis of ideological compatibility.<sup>161</sup>

It is surprising to note that although these histories of the Bank's early operations offer accounts which challenge the Polanyian narrative presented by Helleiner, their reification of the US as a hegemon in the Realist mode drives them to persist with the narrative of embedded liberalism. As a result the 'relative autonomy' approach cannot avoid casting the Bank as a passive recipient of the political agendas of states and narrow social elites according to fluctuating dynamics of direct political influence.

By depicting finance as antagonistic to the Bretton Woods regime, these accounts maintain an analytical blind spot which causes them to actively diminish the importance of the evidence which they present. I will show that the transition away from the governance of the Executive Directors to management specifically by Wall Street lawyers and bankers - which the Brookings accounts illustrate so vividly - reflected a necessary feature of the Bank's governance, not a temporary moment of relative autonomy rapidly subsumed within American state power. The enlistment of financiers in the governance of the institution reflected their centrality to the Bretton Woods project. Drawing upon the capital available through the deeply embedded infrastructure of US finance meant that any agenda the US sought to pursue through the Bank would be mediated by the interests of private American investors. In the specific processes of lending and conditionality, the impact of this infrastructural power can be seen - throughout the history of the Bank.

I will argue that the transformation of the Bank in the first five years reflects the underlying imperative of securing working capital. As Kapur et al show, a political struggle between Wall Street and Washington *did* occur over the governance of the institution. The enlistment of finance would have deeper consequences for the governance of the international order than the temporary addition of a role as liquidity provider. The key point is that this phenomenon is an aspect of the Bank's capitalisation problems - which is intimately related to the wider problematique of liquidity in the immediate post-war period. Financiers'

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<sup>158</sup> Ibid. Pg.912.

<sup>159</sup> Ibid. Pg.906.

<sup>160</sup> Gardner, R.N., 1980. Pg.76. Cited in Kapur, D., Lewis, J.P., & Webb, R., 1997. Pg.907

<sup>161</sup> Kapur, D., Lewis, J.P., & Webb, R., 1997. Pg.1773.

co-operation was integral to the Bretton Woods system: without it, the Bank would not have been able to function as an institution of governance.

From the outset the Bank was under pressure to fulfil two major objectives. Firstly, it was to provide liquidity to Europe prior to the mobilisation of Marshall Aid. Secondly, it was under pressure to expand its operations beyond Europe by South American members and the Truman administration under the 'Point Four' programme. In achieving these aims, it faced a barrier which could not be overcome by recourse to the public finances of its members: it was drastically under-capitalised.

Obtaining capital from private investors required the Bank to overcome a number of obstacles through a pragmatic political process across the first five years of operation, in order to demonstrate that it was a creditworthy institution. It required reconfiguring the original management structure to moderate state leverage, and adopting commercial lending practices in order to enforce financial discipline upon borrowers who had defaulted on dollar, franc, and sterling – denominated bonds in the 1930s. These changes to lending practice and managerial structure would become the established process of the day-to-day working of the institution until the later 1960s, and would enable the Bank to consistently tap capital markets in the US, Europe, and Asia.

This meant that any agenda the Bank sought to pursue in its early operations would be mediated by the interests of the financial community. This observation suggests the limitations of the narrative of financial repression advanced by Helleiner. By focusing on the imperatives which gave rise to the transformation of the Bank, rather than on the transformations themselves, we are able to see how they are derived from the broader structural problematique of the illiquidity of the international order and the Bank's resultant problem of capitalisation. From this perspective, the role of financiers cannot be seen as antagonistic to the objectives of the Bretton Woods era.

This suggests that the character of the era, and the role of finance in it were rather different. Instead of subordinating financial interests to broader social goals, the era is one in which the attainment of broad social goals is predicated upon the satisfaction of financial interests. Indeed, it is not possible to isolate financial interests or sustain the presentation of 'finance' as a 'constituency' external to the Bank. Financial interests were part of the very fabric of the institution, without which none of the objectives of the era could have been achieved. The defining feature of the international order – at least in the immediate post-war period – was not capital controls. Although it had not been possible to keep the global financial order open, financial interests were therefore not thwarted or repressed by such controls. Their imbrication into the foundations of the bank had extended their infrastructural power in

such a way as to ensure that the problems of financiers defined the agenda for the achievement of the objectives of the wider order.

Recently, Constructivist authors have made important challenges to the narrative of the 'coup' as put forward by Kapur et al. I will begin the chapter with an exploration of Chwioroth's intervention, in which he puts forward the argument that the 'coup' thesis offers a superficial account which does not allow us to grasp adequately how the Bank's strategy was actually changed in the most prosaic and practical terms. Chwioroth seeks to move the Bank out of the long shadow of US power, and reveal the importance of ideas and the agency of management. To this end, Chwioroth argues that the Bank is vested with substantive forms of authority which combine to give management autonomy in defining strategy and procedure through internal debate and contestation among employees.

This argument is rooted in his exploration of the transition from the Bank's earliest 'programme' loans to support the balance of payments of European members to the project model which became more usual from the early 1950s. As the legal authority to interpret its mandate had been vested in the Bank itself, and given that it drew its working capital from private investors not states, Chwioroth argues that the change is not attributable to pressure from either the US or private investors. It should be seen as a result of the expression of commercial norms by new recruits, into which they had previously been socialised in the course of their education or professional activities outside the Bank.

Chwioroth's intervention offers several important insights. Firstly, the Bank was the central organ of the international liquidity architecture before the Marshall Plan. Secondly, its basis in private capital is accorded central importance. Thirdly, it follows from this that by recognising the importance of finance as a key element of the Bank's agency as an institution Chwioroth contributes to a narrative which is capable of challenging the 'embedded liberalism' thesis. Financial ideas and practices, Chwioroth shows us, remained central to the Bretton Woods regime of governance.

However, by minimising 'external' factors such as investor pressure, and conceptualising the Bank as socially rooted only in narrow elite academic and professional groups, Chwioroth ultimately obscures the way in which these ideas are related to social forces at work in this wider field, and the material imperatives which animate them. As a result, the potential of the observation which Chwioroth makes is not fully realised. From this perspective material financial interests remain an external factor: Chwioroth cannot avoid ontologising an 'internal/external' divide. The compatibility of 'external' features - the US agenda and the financial agenda - with 'internal' features of Bank strategy relies upon the same consonance of intellectual paradigm and political paradigm which underpins the 'embedded liberalism' thesis.

This distinct domain of discrete external actors and ideas can only penetrate the internal world of institutional culture through recruitment. Ultimately, change in practice relies upon institutional capture - a similar conclusion to the 'coup' thesis of Kapur, Lewis, and Webb.

In the second part of the chapter, I will illustrate how the transformation of the Bank reflects the imperative of securing working capital. Firstly, the high expectations of the Truman administration revealed the lack of working capital. New Deal negotiators and financiers in the immediate Bretton Woods period envisaged that the Bank would be a highly conservative institution, linking private investors with borrowers and offering a guarantee on the investment. Its lending operations would be secondary, and both guarantees and loans would be offered on the basis of paid-in capital. However, the Truman administration's agenda immediately stretched the Bank, demanding capital transfers on a large scale – it rapidly became clear that the model worked out at Bretton Woods would be inadequate.

Secondly, at the Savannah conference the necessity to make the turn to the bond markets was clarified. As the conservatism of the initial design was out, the question under consideration was how best to appeal to financiers in order to obtain the capital Truman's objectives demanded. Further, it became clear that the Bank would have to lend on its own account if it were to be creditworthy enough to borrow to support the scaling-up of its operations.

Thirdly, once the decision to base the Bank's operations in private capital had been met it became clear that the initial management structure, in which Executive Directors exercised operational control on the behalf of member states, was a major obstacle to investment. The third step which would complete the turn to the bond market was the transfer of operational control to management, in order that lending decisions would not be made for 'political' purposes.

This final step took place after the departure of President Meyer and his replacement John J. McCloy – whose acceptance of the job was conditional upon the ousting of the US Executive Director, Emilio Collado. In the final section, I will offer a more detailed exploration of this third and crucial step towards the bond market. Firstly, I will discuss the programme-type lending of the early loans to Europe – and how, contrary to Chwieroth's intervention they were supported by financiers as is illustrated by their impact on the Bank's credit rating. Secondly, I will focus on the struggles between the Executive Directors and the Bank's management team over the Chilean loan application. The Chilean loan was at the core of this issue. It offers considerable insight into both how the agenda of the US – to rapidly expand lending in support of security – was mediated by the imperatives of financiers following the turn to the bond market. Indeed, both the early programme loans and the project mode

reflected the intertwining of financial and US interests, in the context of the problem of liquidity in the post-war international order – and the centrality of the uniquely deeply rooted infrastructure of the American financial system to its recovery as an open trading order.

In sum, the Bank of 1947 did not resemble the Bank of 1946, from which the Bank of 1952 was still further removed. By the time of the 1952 reorganisation it drew the majority of its working capital from private financial markets – a different funding model to that which had been imagined at Bretton Woods. It was managed differently, having transferred responsibility for operations from state-appointed Executive Directors (EDs) to the President and managerial team. It also lent differently – ceding its role as primary liquidity provider to the IMF and switching to a project-based lending strategy rather than programme lending for balance of payments support. In respect of these important transitions, the conflicts over the Chilean loan illustrate the importance of situating the agency of management within the parameters of the imperatives of the Bank's financial backers. Ultimately, it was the imperative of resolving the sovereign debt defaults of the 1930s – the key objective of international finance during this era – not the ideas of norm entrepreneurs which shaped management's decisions regarding the Bank's lending practice most definitively.

## **1: 'Relative Autonomy', Institutional Capture and 'Embedded Liberalism'.**

For Kapur, Lewis, and Webb; the appointment of President McCloy and his team constituted nothing less than a coup executed by Wall Street bankers and designed to demonstrate the marginalisation of the 'New Deal crowd'.<sup>162</sup> It is clear that a significant transition in personnel took place, and that new recruits at management level were quintessential Wall Street men. Further, if it can be seen as a coup, it was certainly Wall Street's affair, and not the Truman administration's. Yet this approach over-determines the direct influence of financiers as an external imposition: there is no room in this account for the agency of management. In this account financial leadership determines the action of the Bank – which had been occupied by Wall Street in a decisive victory against the New Deal, during the McCloy presidency at least.

Jeffrey Chwioroth argues that while the 'coup' concept may grasp the surface events of the transition, it does not allow us to grasp either the processes through which it changed Bank strategy – or even the nature of international organisations as institutions. In his analysis of the early lending practices of the Bank, Chwioroth makes an important observation: 73% of

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<sup>162</sup> Kapur, D., Lewis, J.P., & Webb, R., 1997. Pg.79

its lending across the period from 1946 to 1950 was programme lending for balance of payments support, whereas from 1951 to 1957 the quotient dropped to just 7%.<sup>163</sup> For Chwiero, the transition in the Bank's lending practices between 1947 and 1952 is a case study of the role of ideas in shaping organisational culture. In this account the ability to draw upon private finance in capitalising the Bank confers autonomy from member-state authority, allowing the agency of management to become decisive in setting policy.

The starting point of his account of this transition to the dominance of project lending is the authority which was conferred upon the Bank to interpret its Articles of Agreement. He begins by pointing out their ambiguity – and the use which was made of it.

The core of the Bank's mandate is described in the first and second clauses of Article 1: firstly, it was to assist in the reconstruction and development of war-damaged economies; and secondly to promote investment when private capital was not available directly to borrowers on reasonable terms. This latter aspect was considered of particular importance in the light of the high rates of inflation following from the scarcity of goods in the aftermath of conflict, and high government expenditures. However, Chwiero notes that it also opened up a further issue in relation to the ambiguous compromise language that had been built into Article 3 during the negotiations in Congress.

This concerned the Bank's mandate to offer general-purpose financing under 'special' circumstances:

Article III, Section 4: Conditions on which the Bank may guarantee or make loans:

*"The Bank may guarantee, participate in, or make loans to any member or any political sub-division thereof and any business, industrial, and agricultural enterprise in the territories of a members, subject to the following conditions:*

(vii)

*"Loans made or guaranteed by the Bank shall, except in special circumstances, be for the purpose of specific projects of reconstruction and development."*<sup>164</sup>

By Congressional request, a defined legal interpretation was sought to clarify that the Bank was in fact able to make such loans. At Savannah, this was referred to the governors, who in turn referred the issue to the Board. Ultimately, the Board concluded that the Bank had

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<sup>163</sup> Chwiero, J., 2008. Pg. 499.

<sup>164</sup> IBRD, *First Annual Meeting of the Board of Governors Proceedings and Related Documents*, Washington D.C., September 27 – October 3, 1946. Pg.120-1

the authority to make or guarantee loans for economic and monetary reconstruction, inclusive of long-term stabilisation lending, even if they were not for specific projects.<sup>165</sup> Loans could be made for stabilisation, and Bank management would judge what constituted 'special circumstances'.

Although the right to interpret them was conferred by the US Congress, Chwierothe indicates that this gave the Bank important power to set its strategy from the very outset. The persistently ambiguous wording of the Bank's foundational Articles conferred a degree of 'interpretative authority'. In combination with the decision to issue its own bonds, the delegation of the authority to interpret the Articles to management gave the Bank sufficient autonomy from its' principals for the agency of 'norm entrepreneurs' to become decisive. On this basis, he attributes primary causation in this transition to the development of a 'project culture' within the Bank. To support this argument, Chwierothe draws upon the early balance of payments programme loans as the context for the engagement of rival norm entrepreneurs in a 'battle of ideas' running across the first half-decade of the Bank's activities.

While France, the Netherlands, Denmark, and Luxembourg were all judged to fit the criteria of 'special circumstances', Chwierothe points out that this early lending strategy was altered significantly in the course of the later 1940s and early 1950s, to the extent that project lending dominated until the advent of structural adjustment in the 1980s. The Bank faced two sources of external pressure in relation to its strategy: the US government, and financiers. American officials pushed the Bank to lend to European applicants in order to bolster their governments against Communist parties; while Bank management, reliant on private finance for capitalisation, was concerned that programme lending would damage the institution's creditworthiness. Yet Chwierothe argues that these pressures were not decisive in shaping decisions about the form the Bank's lending should take.

While it is clear that American officials did drive Bank lending for the same strategic reasons as the Marshall Plan finance was eventually deployed, Chwierothe argues that they were entirely indifferent about the precise form it took. Nor, he continues, should the change in Bank lending practices be attributed to pressure from private investors.<sup>166</sup> If the change to project financing were attributable to the interests of financiers, he argues, it would be logical to expect the Bank to have made more project loans in the process of gaining AAA certification from the ratings agencies. Once it had been obtained, he contends, the constraint would diminish and more programme loans could be made. But the programme loans ceased after the AAA seal of confidence that management had been desperately seeking was obtained in

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<sup>165</sup> Chwierothe, J., 2008. Pg. 488.

<sup>166</sup> Ibid. Pg. 496

1958. For Chwioroth, this indicates that the agency of norm entrepreneurs was the decisive factor at work, not the imperatives of the Bank's private backers.

Chwioroth contends that in fact, the incidence of programme loans began to decline from 1951. The reason for this is that the most significant factor in the transition was neither sources of formal or informal external influence, but internal processes and collectively shared beliefs: *"early lending practices can be understood largely as a product of intra-organizational dynamics and change."*<sup>167</sup>

For Chwioroth, the emergence of the new commercially-oriented banker-friendly norm of project lending may be summarised as follows. Recruitment from a diverse pool of talent on either side of the Atlantic led to the burgeoning of subcultures within departments that reflected the 'beliefs' of new-hires according to their previous professional backgrounds<sup>168</sup>. Between these groupings, debates over strategy ensued in which leaders emerged relatively quickly. The victory of one conception of the optimum strategy and organisation depended upon the relative seniority of these leaders, the norm entrepreneurs, or their access to seniority.

The great strength of Chwioroth's account is in the way in which he is able to demonstrate the importance of the debates articulated within the institution in shaping an organisational culture, which shaped the Bank's form in a way which locked in the practices which sustained that culture. It is clear from the 66% reduction in programme lending from 1951-7 in comparison to 1946-50 that Chwioroth cites, that the adoption of the project approach was a critical turning-point in the development of the Bank – occurring as it did at a moment when the institution was undergoing a crisis of capitalisation and by extension of relevance to the order it was intended to express.

Yet the central problem with Chwioroth's account is that in depicting the social processes through which ideas attain a hegemonic status inside an institution, he divorces these ideas from the problem it was developed to overcome. He aims to address this by maintaining that recruitment is the key mechanism which builds constituencies behind new norms: the growth of a constituency behind the path-breaking 'entrepreneur' eventually causes a tipping point to be reached at which the new norm replaces the old. This leads to the conception that the Bank was only extremely narrowly socially anchored, in elite academic, managerial, and bureaucratic circles. In these respects Chwioroth's account bears significant similarity to the Polanyian embedded liberalism narrative expressed in Kapur et al's 'coup'

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<sup>167</sup> Ibid. Pg. 482.

<sup>168</sup> Ibid. Pg. 483.



thesis, in that it relies upon institutional capture to transmit the hegemonic paradigm into the Bank.

To an extent, he is forced to acknowledge this by offering an important caveat, to wit: *“The point here is not to deny that private capital market constraints were a crucial factor shaping Bank lending. Rather, the point is to suggest that private capital market alone cannot fully explain the Bank’s early lending practices”*.<sup>169</sup> This means that he misses the imperative which gave rise to the ideas over which the battle was fought. This imperative did not come from ‘within’: the action of norm entrepreneurs, while a key aspect of the Bank’s early history is a surface phenomenon which expresses a social and strategic interest, which is derived from a material problem. This was the problem of illiquidity and inconvertibility in the post-war era to 1958. Only the ability to draw capital from the uniquely deep American financial market allowed the Bank to inject more liquidity into the international system.

My point is precisely not to suggest that the private capital market alone provides a full explanation of the Bank’s early lending practices. The problems of the Bank and the private capital market were closely interrelated – and the solution to these problems was to be found only in adopting practices which were legible to financial agents and strategies which supported financial interests. Only then could the broader objectives of the coalition of interests which were mobilised in the creation of the Bank as an institution of governance be attained.

Financial interests set the imperatives of the Bretton Woods institutions, and were a crucial factor in the development of the project lending model. Yet this need not imply that the early programme loans ran entirely counter to financial interests. The early European loans were intended as stop-gap financing prior to the Marshall Plan – and crucially, they were principally used to pay American firms for import orders which had already been placed. The complementarities of state, financial, and business interest are demonstrable here: as I stressed in Chapter 2, the second New Deal was supported by a coalition of anti-Morgan financiers and internationally-oriented businesses. Ensuring that these contracts were upheld supported all three. I will return to this point in discussing the Bank’s creditworthiness in Part Three.

However, Chwiero is certainly correct to point out that lending to France was encouraged by the US as an effort to forestall the electoral advance of the Communists, and it is clear that the program lending to Europe reflected the logical outcome of Congressional insistence that the Bank should make such loans. It may be argued that this is an example of

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<sup>169</sup> Ibid. Pg.500.

the Bank serving American state imperatives. On the other hand, McCloy was highly concerned that the Bank obtain the best possible credit rating and insure itself against the possibility that it could be excluded from American capital markets – and the switch to project-oriented lending which was more easily comprehensible to commercial lenders was a central plank of his strategy in this respect.

Further, without additions to the Bank's working capital drawn from private investors, the Bank would have been exhausted after the European loans. This would have been problematic because it would have obstructed the 1948 loan to Chile (as I will show in the final section of this chapter) and the accommodation between the Chilean government and American private bondholders upon which it was predicated.

Just as the European program loans were not simply an objective of US state interests, so the Chilean loan was not simply a project of financial interests. It most certainly advanced financiers' cause by setting a precedent for the resolution of international debt defaults. But it also served the interests of the US more broadly by helping to reconstruct the international capital market as an arena for profitable investment based, of course, upon the dollar. Therefore, the 'battle of ideas' wasn't about the endorsement or negation of state or financial and commercial interests and practices – it was a pragmatic working out of the concrete politics of governance of the Bretton Woods order which should be seen as socially rooted in the financial relations of the US, rather than an ideational contest among elite technocrats governing an autonomous institution.<sup>170</sup>

Though the agency of Bank management and staff was crucial in translating these interests into a concrete political program of governance, the level of choice which they were able to exercise should not be over-stated. The Bank had to increase its working capital, or cease to work. It was essential that it demonstrate its creditworthiness, and promoting a commercial lending model which was familiar to investors was a necessary precondition.

The implication of this is that our exploration of the transitions which the Bank management forced the institution through in the earliest years of its operation should not begin with the transitions themselves. The phenomena which are associated with them, the 'battle of ideas' and the recruitment of staff from Wall Street in large numbers, are all part of the story – but the story must begin with the problems which gave rise to the imperatives around which the battle was joined and the recruitment drive was initiated. This is the

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<sup>170</sup> As I discuss in Chapter 4, the program loans continued – admittedly in reduced form – alongside conditionalities on project loans relating to defaulted debts, with a view to constructing and governing a dollar-based international order.

problem of capitalisation, which derives from the wider problem of illiquidity and inconvertibility at the cessation of hostilities in 1945.

## 2: Capitalising the Bank.

Getting the Bank organised to begin operations required addressing a thorny set of questions which had not been resolved at either Bretton Woods or Savannah. What would the Bank actually do, and who would run it? During the closing days of the Bretton Woods conference the exhausted delegates had frequently become confused. In the meetings of Commission I under Harry White's chairmanship, the process of minute-taking on the proposals for the International Monetary Fund was haphazard and almost careless. The meetings were a surprisingly disorganised affair, and no notes were taken at all during discussions in Keynes' Commission II on the Bank. In the short discussions that were held specifically pertaining to the Bank, some clauses of the Act were either dropped accidentally or adopted in different forms to those which had been discussed and agreed upon.<sup>171</sup>

Within a calendar year from its launch, the essential problematique of the Bretton Woods order as it related to the Bank was clear. The inability of members to pay in sufficient capital to support the Bank's operations entailed seeking funding in private capital markets, which required the transformation of the Bank's operational strategy and managerial structure in order to guarantee the participation of private investors.

In this section, I will offer a sketch of the three problems which had to be understood and resolved by management in order to address the Bank's primary problem – a chronic lack of operating capital – before exploring these issues in the context of a more detailed case study in the third section of this chapter. The first and second of these sections concern the process through which the capitalisation problem crystallised for the EDs, and recourse to the bond market was understood as a solution. The third details the process through which the EDs' control of the institution became understood, by management and the Truman administration, as the obstacle which would have to be overcome in order to execute this manoeuvre and set the Bank running on a sustainable basis.

### Great Expectations in Hard Times

Expectations of what the Bank would achieve were extremely high at Bretton Woods, and the first meeting in Savannah, Georgia in March 1946. This was particularly true of the

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<sup>171</sup> Oliver, R., *Interview with Mr. Aron Broches*, World Bank/IFC Archives, Oral History Program, July 11<sup>th</sup> 1961. Pg.2

EDs, whose eagerness to commence lending contrasted with the highly conservative vision which was originally laid out for the Bank at Bretton Woods by US officials and supported by financiers.

Initially, the vision of the Bank proposed by the New Dealers was that the Bank would function as a guarantor and cautious lender based on its paid-in capital. White had always intended that as far as the Bank was concerned *“The primary aim of such an agency should be to encourage private capital to go abroad for productive investment by sharing the risks of private investors in large ventures.”*<sup>172</sup> For Aron Broches, one of the first members of the Bank’s legal team *“there was no idea...that the Bank would supplement its paid capital by borrowing in the market so much as by guaranteeing loans made by others.”*<sup>173</sup> This had been a matter in which he felt there had been clarity from the outset: it had been strongly anticipated that the IRBD *“... would make loans out of its paid-up capital, but the principal activity would be to guarantee loans made”*<sup>174</sup>.

This conservative approach was designed to reassure financiers that the Bank would be a reliable partner in the reconstitution of the international capital market. By contrast, the Truman administration was extremely eager to get the new institutions up and running quickly and stated explicitly that large volumes of capital would be available through the Bank for this purpose.

It was anticipated that the Bank would begin operations by the end of the year, and that it would be capable of meeting global requirements in respect of international capital by the end of the calendar year of 1947. Treasury Secretary Snyder reiterated at the September 1946 meeting of the Board of Governors that the Bank would assume the principal responsibility for reconstruction financing. This would mean that the Bank would replace the programmes of the UNRRA and the Export-Import Bank. In fact, the US government repeatedly stated that a total of \$15 billion would be made available between the two Bretton Woods institutions – which would satisfy the needs of Europe and any further applicants<sup>175</sup>.

As the senior institution, the Executive Directors anticipated that the Bank would have \$10bn at its disposal.<sup>176</sup> Yet this sum was only available to the IBRD on paper. Its operating funds at this early juncture came from capital subscriptions only. When the Bank opened for

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<sup>172</sup> Quoted in Mason, E.S, and Asher, R.E, 1973, pg.18, cited in Gwin, C., ‘U.S. Relations with the World Bank, 1945-1992.’ in Kapur, D; Lewis, P; and Webb, R., *The World Bank: its First Half Century. Vol.2: Perspectives* 1997. Pg.197

<sup>173</sup> Oliver, R., *Interview with Mr. Aron Broches*, July 11<sup>th</sup> 1961. Pg.5.

<sup>174</sup> Oliver R., *Interview with Mr. Aron Broches*, July 11<sup>th</sup> 1961. Pg.5

<sup>175</sup> Gardner, R. N., 1980. Pg.290-3.

<sup>176</sup> Oliver R., *Interview with Mr. Daniel Crena De longh*, World Bank Project, Oral History Research Office, Columbia University, 1<sup>st</sup> August 1961. Pg.13-14.

business on the 25<sup>th</sup> of June 1946, 0.5% of the capital subscription had been made payable upon signature; and under the Articles of Agreement the first 2% of members' was due to be paid within sixty days in either gold or US dollars. A subsequent 18% was due to be paid in local currency; while the remaining 80% was callable should the Bank require it in order to meet obligations arising from guarantees or its own borrowings<sup>177</sup>. It was anticipated that the 20% call would be completed by late May 1947. By the middle of 1947, positive progress had been made, and \$8 of the \$10 billion which had been authorised had been officially subscribed.

However, the amount of capital which had been successfully paid in to the Bank amounted to considerably less: the US was the only member whose 18% contribution (\$571 million) was paid in full and available for lending<sup>178</sup>. The total sum available was \$1.6 billion of which \$727 million had been contributed in US dollars or gold. This latter figure represented the ceiling of the Bank's capacity to make guarantees or loans.<sup>179</sup> Such a small sum was far beneath the expectations of the EDs. The realisation that the Bank would not be capable, in the short to medium term, of lending to its members on the basis of its paid in capital was the first step in the turn to private investors as a source of capitalisation.

### **Financiers' Conservatism vs. Financial Reality.**

Although the EDs had emerged from the Savannah conference as the driving force in the management of the Bank's operations, a guiding concern of that gathering, as in the case of its precedent in New Hampshire, had been to appeal not to the representatives of less developed members - but to the financiers upon whose participation the new institution would be based.

However, there were problems with the financiers' preferred model, as Mason and Asher point out: guaranteeing private borrowing would not have increased the volume of globally available financial resources. It also had the potential to crowd the Bank itself out of the bond market. Worse, costs to borrowers may in any case have been untenably high and varied among borrowers. Daniel Crena de longh (the Bank's future treasurer), noted that if certain offerings were quoted at different prices, all the while backed by the IBRD's 100% guarantee this may have damaged the creditworthiness of the Bank itself<sup>180</sup>.

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<sup>177</sup> Kraske, J., with Becker, W.H; Diamond, W; and Galambos, L., 1996. Pg.17.

<sup>178</sup> Mason, E.S., Asher, R.E., 1973. Pg.105.

<sup>179</sup> Ibid. Pg.52.

<sup>180</sup> Oliver, R., *Interview with Mr. Daniel Crena De longh*, 1<sup>st</sup> August 1961, Pg.17, cited in Mason, E.S., and Asher, R., 1973. Pg.107.

As a consequence it was not possible for the Bank to act as a guarantor linking private capital with willing borrowers. This realisation put an end to the concept of the Bank as a guarantor to private finance – the second necessary step in the turn to the bond market as a source of capitalisation.

The only available solution to the capitalisation problem was that the Bank would have to become a borrower on behalf of its members. The change in strategy was accepted by September 1946: the Bank would issue its own bonds, and lend directly.

Executing the turn to the bond market entailed surmounting one further obstacle: the perception among the financial community that the Bank, if dominated by the EDs, would lend for political, not commercial reasons. At Bretton Woods, ex-BIS President J.W. Beyen, the leader of the Dutch delegation had put forward a conservative proposal that if the Bank were to lend at all, its lending limit should be capped at 75% of callable capital. The American delegation argued for 150%.<sup>181</sup> A compromise was struck at 100%, which Beyen warned was too much: financiers would not see the Bank as ‘sound’.

He was correct. At a social engagement in autumn 1946, Harold Stanley of the firm Morgan, Stanley informed Beyen’s colleague, Crena de longh that 100% *“was far too much, and that in practice the public wouldn’t buy more bonds than the amount that corresponded with the American and the Canadian guarantee.”*<sup>182</sup> Though the turn to the bond market would increase the lending power of the Bank, it still could not achieve the Truman administration’s objectives immediately.

### The power of the EDs

With the Bank’s strategy transformed from a guarantor institution to a lending institution, it was becoming less and less tenable to private investors that lending and borrowing operations would be directed by the EDs. Following his encounter with Harold Stanley, de longh took pains to convince Eugene Meyer, the Bank’s first president, that the borrowing ability of the Bank would be even less than its capital subscription and that this should be the first matter for management to attend to. The scepticism about the soundness of the Bank’s business practice which de longh had encountered was widespread.

Since the Bank had been ‘activated’ by the admission of Mexico as its thirtieth member on the 30<sup>th</sup> of December 1945, the EDs had begun a program of policy-formulation in the process of which they would meet formally as often as twice a week and confer informally

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<sup>181</sup> Oliver, R., *Interview with Mr. Aron Broches*, July 11<sup>th</sup> 1961. Pg.5.

<sup>182</sup> Oliver, R., *Interview with Mr. Daniel Crena De longh*, 1<sup>st</sup> August 1961. Pg.4.

on a daily basis<sup>183</sup>. According to Kraske, they “...believed that the exchange and financial markets in general, and private international bankers in particular had failed miserably in the late 1920s and 1930s” – and considered that due to the high price industrial economies had paid for this failure, the multilaterally governed and interdependent world economy of the post war era should be “guided by international institutions that had to answer to the governments which created and sustained them”<sup>184</sup>.

The Bank’s first task, in spite of the EDs’ ideas about the culpability of financiers for the Depression, and the importance of state power in governing the international order, was to court investors. For financiers, accepting the Bank and opposing the Fund was a tactical manoeuvre: they had held neither dear, but as it had become clear in the Congressional hearings on Bretton Woods that they would never ‘get’ the Fund, they had taken a particular interest in the Bank.<sup>185</sup> The immediate problem of the relationship between members and management was exacerbated by the pressure placed on US Treasury Secretary Vinson to name a pillar of Wall Street for the role of President.

With a New Dealer at the top, the Bank would be faced with difficulties selling its bonds. This was largely due to the opprobrium reserved for Emilio Collado, the US ED, who had been responsible for the Bank’s approach to financiers prior to the appointment of the first President. His role as the Bank’s principle agent in New York was made difficult by his reputation as a New Deal ‘planner’. The main problem with Collado, as far as financiers were concerned, was his sympathy for the objectives of his South American colleagues. They argued that the Treasurer should set up a system for the distribution of the Bank’s capital amongst its members in advance of the rush on the Bank’s assets they felt sure would follow its launch. Their primary fear was that the amounts which would be demanded for the reconstruction of Europe would deprive the developing economies of resources.

Collado was sympathetic to this concern. His experience in South American economic affairs was extensive. In 1937 he had been seconded to the Bank of Mexico from the Department of the Treasury, and in 1938 to the Federal Reserve, where he became assistant chief of the Division of American Republics. From 1943 he worked for the State Department as associate advisor for International Economic Affairs 1943-44 before rising to head the Division of Financial and Monetary Affairs, and further still to become Director of the Office of Financial and Development Policy from 1945-6. In these roles, he had worked closely with Harry Dexter White, and Morgenthau, and South American governments in the construction of projects

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<sup>183</sup> Kraske, J., with Becker, W.H., Diamond, W., & Galambos, L., 1996. Pg.26.

<sup>184</sup> Ibid. 1996. Pg.10-11.

<sup>185</sup> Oliver, R., *Interview with Mr Ansel F. Luxford*, World Bank/IFC Archives Oral History Program, July 13<sup>th</sup> 1961. Pg.24

such as the Pan American Highway and the putative Inter-American Bank (IAB). This latter project was formative in his approach to his role as US ED at the Bank – having also been present at the Atlantic City, Bretton Woods, and Savannah conferences, he was concerned to get the Bank acting quickly and anticipated that the IBRD's structural similarities with the failed IAB put the EDs in the driving seat.<sup>186</sup>

Collado's vote carried the weight of the largest shareholder - 35% - which was cast under the guidance of the National Advisory Council on International Monetary and Financial Problems (NAC) at the insistence of Congress. This body formalised the network of connections Collado had developed over the years of his service in both the Department of State and Treasury, whose secretaries sat on the Committee alongside the Chairman of the Fed, and lent significant authority to his words. As I have detailed in Chapter 2, the creation of the NAC was crucial in pacifying the American Bankers' Association whose president, Randall Burgess, had been Collado's manager during his time at the Federal Reserve Bank. Including prominent financiers such as Winthrop Aldrich alongside the bureaucrats of the Truman administration offered the investment community a voice at the very highest level of decision-making in state foreign economic policy.

The appointment of Eugene Meyer, made informally by President Truman after an embarrassing lack of applicants, appeared to offer a way out of the dilemma, and satisfy financiers and the EDs. He had forged a long career in finance with Lazard Frères and at the head of his own Wall Street brokerage house; and he had also served the US government under Wilson, Coolidge, and Hoover; before returning to government under Truman on the Famine Emergency Committee. He took up office in the Bank on the 4<sup>th</sup> of June 1946 aged 70 – at which point he was described as 'senile' by Luxford.<sup>187</sup> Worse, he was already an outsider to a group of Executive Directors who had a clearer set of ideas about the future of the Bank as an institution than he did.

Prior to Meyer's arrival, the Bank had been operated by the Executive Directors under the leadership of Collado. They had made the Bank's initial calls on members' capital, and invested the funds in received in US Treasury bills, notes, and certificates. They had secured the requisite amendments to enable wider private investment - first in New York State, and in New Jersey, with support from the NAC and the Securities and Exchange Commission. They had also elaborated an organisational structure and, most importantly, working procedures and relationships had been developed. The practices which had been

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<sup>186</sup> Wilson, T. A. & Richard D. McKinzie, *Oral History Interview with Emilio Collado*, 7<sup>th</sup> July 1971. Pg.9-10.

<sup>187</sup> Oliver, R., *Interview with Mr Ansel F. Luxford*, July 13<sup>th</sup> 1961. Pg.42.



developed under Collado and the EDs would bring the Bank into conflict with its new financial backers in a matter of months.

Meyer redoubled the Bank's efforts to engage the financial community. He had (like Collado) served the Federal Reserve and was able to exploit his extensive network of contacts in support of the Bank's objective to educate potential investors. He presented the Bank to representatives of insurance companies and commercial, investment, and saving institutions at a meeting at the Federal Reserve Bank of New York in 1946<sup>188</sup>. He was supported in this by Collado and his assistant Richard Demuth. Ultimately, they were able to successfully press financiers to lobby their state legislatures to obtain alterations to banking laws which would enable private financial institutions operating in their jurisdictions to invest in Bank paper.<sup>189</sup>

Shortly after Meyer's arrival and success in legalising Bank paper, the first annual report to the board of governors of September 1946 emphasised that the office of the President was responsible for "*operational, administrative, and organizational questions...*" The President's remit in these fields was qualified, "*subject to the general direction and control of the Executive Directors*", although endowed with a deciding vote should an equal division occur<sup>190</sup>. The central aspect of the Bank's function, the consideration of applications for lending, was also subject to the decision of the EDs and would proceed according to three stages. Firstly, the President would carry out 'preliminary conversations' with the applicant before receiving the judgement of the EDs as to whether the Bank could proceed with more formal negotiations. Secondly, where affirmation was given, the President would carry these negotiations out, and feed back to an *ad hoc* loan committee with a view to ensuring that the loan contract would be formulated in accordance with the Bank's Articles of Agreement. The committee would report to the President, and would maintain regular contact with the EDs to apprise them of the status of negotiations. Finally, the President would submit a proposal backed by a report developed by the Loan Committee to the EDs, who would make the final decision.<sup>191</sup>

The institutional responsibility for policymaking lay with the EDs, and this dominance emboldened the Dutch ED, J.W. Beyen, to announce a bold borrowing strategy in order to supplement the small volume of funds available to it through its members' subscriptions. In a speech to the New York Savings Bank Association Convention in Quebec on the 15<sup>th</sup> of October 1946, he claimed that the Bank would seek to borrow amounts up to \$2bn in 1947 alone. It

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<sup>188</sup> Kraske, J., et al, 1992. Pg.25-9

<sup>189</sup> Wilson, T. A. & Richard D.McKinzie, *Oral History Interview with Emilio Collado*, 7<sup>th</sup> July 1971. Pg. 58-61.

<sup>190</sup> IBRD, September 27<sup>th</sup> 1946. Pg.5.

<sup>191</sup> Ibid. Pg.9-10.

would do so by offering twenty-five year bonds for sale which he claimed would pay up to 50% more than US Treasury bills. Beyen's announcement threatened to throw Meyer's careful program of public relations into disarray: confusion reigned among bond investors. The Wisconsin State Banking Commission voted to prevent their financial institutions from purchasing the Bank's paper – unanimously, the following day<sup>192</sup>.

Beyen's speech had cut right to the heart of the Bank's claim to be a conservative institution which would operate on commercial lines. The pressure to lend, and lend rapidly, to less developed members which prompted Beyen's statement, was considered by the Bank's senior managers including Daniel Crenna de longh (Treasurer) and Robert Garner (Vice President under McCloy) to be coming from Collado, as much as the Latin American governors themselves.<sup>193</sup>

By the autumn of 1946, the tension between pressure to lend, and the pressure to conduct lending policy in the manner of a 'sound' commercial institution was coming to a head. In the course of the protracted negotiations over the Chilean loan, the struggle between management and EDs over the specific practices of borrowing and lending would reach its zenith. Its resolution, as I shall show in the following section, would transform both the Bank and the international capital market.

### **3. The Chilean Loan: Reconstituting the Bond Market, Disciplining Debtors.**

Emilio Collado's reputation as a New Deal 'planner' was, as we have observed, problematic for him in his efforts to market the Bank to the financiers of New York. His attempts to pursue the Truman administration's objective of rapidly expanding Bank lending would soon sharpen bankers antipathy toward him – and by extension, toward the governance of the Bank by the Executive Directors in general. The case of the Chilean loan application is instructive because it spans a period of eighteen months in which the Bank underwent its first major institutional crisis, largely brought on by Collado's desire to make the loan rapidly – in the face of financiers' objections in relation to Chile's default on foreign bonds in the 1930s. Ultimately, Collado would be a casualty of the procedural and structural reform through which the problem posed to financial interests by the power of the Executive Directors was surmounted. The Chilean case was the catalyst for the strategic reorientation of the institution

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<sup>192</sup> Oliver, R. W., 1977. Pg.232-3

<sup>193</sup> Oliver, R., *Interview with Robert Garner*, Oral History Research Office, Columbia University, July 19<sup>th</sup>, 1961. Pg. 12.

towards American financial capital. Financial imperatives were not repressed – they shaped the way in which the Bank was able to pursue the objectives of the Truman administration.

This case therefore offers a unique opportunity to explore the issues of external relationships and organisational culture raised by Chwioroth's interventions. In this section, I will present the way in which lending was made conditional upon the resolution of existing bond defaults – to private American and European investors.

On the 7<sup>th</sup> of October 1946, Luis Davila, assistant general manager of the Central Bank of Chile and alternate Chilean governor of the IBRD formally authorised the formal application of Corporacion de Fomento de la Produccion de Chile (Fomento) and Chilean State Railways for a loan of US \$40 million, initially submitted in a letter to President Meyer on the 30<sup>th</sup> of September. A loan was granted in March 1948, by President McCloy. In the intervening period, the EDs would lose control of the Bank.

By the time Meyer arrived at the Bank, the EDs had already begun to consider the first applications, or 'approaches', from Chile and Denmark.<sup>194</sup> Working parties considering these applications were convened by senior EDs such as J.W. Beyen, who had stepped forward as acting loan director. Meyer's assistant, Richard Demuth, offers remarkable candour on the working parties at this juncture: *"...we were all terribly inexperienced [...] Nobody knew where to begin [...] We didn't know what kinds of question to ask, what kind of investigation to make."*<sup>195</sup>

In this environment, Collado was keen to get a loan authorised by the end of 1946, to demonstrate that the Bank was open for business.<sup>196</sup> He pushed hard to get the Chilean loan approved, and engaged closely with US Treasury Secretary Snyder – exchanging memoranda on Bank policy and lending strategy on a daily basis.<sup>197</sup> Encouraged by Collado's suggestions that their application would meet with success,<sup>198</sup> the Chileans were eager to borrow. Demuth recalls that Collado was arguing that not only should the Bank issue bonds quickly, but that *"he knew Chile, he'd known them for a long time, and they were good for 40 million dollars and the Bank was darned well going to make the loan."*<sup>199</sup> In this respect, he was backed by Ansel Luxford, who felt that financial opinion mattered little and that if presented with a *fait accompli*, they would rapidly take the sanguine approach that *"business is business, and people buy government securities"* owing to his experience in getting a hostile banking community to

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<sup>194</sup> Oliver, R., *Interview with Mr. Aron Broches*, July 11<sup>th</sup> 1961. Pg.14.

<sup>195</sup> Oliver, R., *Interview with Richard Demuth*, World Bank/IFC Archives Oral History Program. August 10<sup>th</sup> 1961. Pg.5

<sup>196</sup> Kraske, J., et al, 1996. Pg. 29

<sup>197</sup> Oliver, R. W., 1977. Pg. 234

<sup>198</sup> Oliver, R., *Interview with Mr Ansel F. Luxford*, July 13<sup>th</sup> 1961. Pg. 39

<sup>199</sup> Oliver, R., *Interview with Richard Demuth*, August 10<sup>th</sup> 1961. Pg.4

finance US expenditure in the war years<sup>200</sup>. However, their application - which had arrived on the 7<sup>th</sup> of October – was held up by the outcomes of Beyen’s near-disastrous speech concerning the Bank’s likely borrowing strategy.

Following Beyen’s mis-step, the necessity of engagement with the financial community only deepened. Meyer pushed back against Collado with this in mind, arguing that the Bank needed to undertake a comprehensive program of ‘education’. This task was given to the Director of the Economics Department, Leonard Rist. With this in mind, Meyer encouraged Rist to engage ‘the copper people’ at Kennecot and Anaconda in order to attempt to gauge the viability of Chilean production for export, with a view to exploring the conditions under which lending to Chile could repair the Bank’s already fragile reputation.

Rist had a background in finance, having worked for the investment bank Blair & Company in New York under Jean Monnet, before moving to Paris to take up a role with J.P. Morgan & Co. He sought to sound out financiers’ ideas about creditworthiness, with the express intention of giving the ‘New York group’ the feeling – arguably not unfounded - that they were participating in the development of the Bank<sup>201</sup>. As Rist well understood, the issue of Chile’s international debts, in default since 1931, was of the highest priority. At the end of the financial year of 1946, the total outstanding external debt amounted to \$281,220,453 of which \$144,466,050 were owed to US bondholders.<sup>202</sup>

Unless the Bank were to deploy commercial practices in establishing the creditworthiness of an applicant, it was likely that it would not be able to establish its own creditworthiness. Potential borrowers could not be assessed in the way that had informed the prospectuses of the bond issues of the 1920s: through the simple enumeration of foreign trade balances, exports, imports, debt, budget and monetary structures and practices would not suffice. Hard conditions relating to the labour policy, foreign ownership, and the repatriation of profits would have to be established. Even more importantly, arrangements would have to be made for the resumption of payments on defaulted bonds.

Along with fostering the renegotiation of lapsed payment schedules, the Bank would have to build a more comprehensive and convincing picture of Chilean creditworthiness to present to bond investors. It would have to concern itself with policy and with the minute detail of projects as well as what Rist describes as the “...social pressures, on the political aspect of things, within the country, on the external political pressures that it may be subjected

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<sup>200</sup> Oliver, R., *Interview with Mr Ansel F. Luxford*, July 13<sup>th</sup> 1961. Pg.10

<sup>201</sup> Oliver, R., *Interview with Leonard Rist*, World Bank/IFC Archives, Oral History Program, July 19<sup>th</sup> 1961. Pg.22.

<sup>202</sup> IBRD *Chile Loan Application Report by the Working Party*, Washington D.C., 1947. Appendix III, Pg.26-8

to.”<sup>203</sup> Otherwise, the Bank risked gaining the same reputation as the Export-Import Bank - that it would lend to Latin American countries regardless of their defaults.<sup>204</sup>

The Executive Directors were in revolt over the usurpation of their authority implicit in Meyer’s downplaying of the readiness of the Chilean application and Rist’s efforts to find an accommodation with conservative investors. They began a public relations campaign of their own, briefing the media against Meyer’s management. On the 3<sup>rd</sup> of December 1946 Collado gave a speech to the Investment Bankers’ Association, in which he argued that there was already a big enough market for the Bank’s bonds. It could only get broader and deeper, when the remaining thirteen states of the union permitted their financial institutions to purchase Bank securities. It appears that this was the final straw for Meyer, who resigned the following day with a parting shot to the effect that he could “...stay and fight these bastards, and probably win in the end, but I’m too old for that.”<sup>205</sup>

With Meyer’s departure and the death of his Vice President, Harold D. Smith, the way appeared to be clear for Collado. Luxford felt that Collado had the backing of the US through the NAC: “I’m certain that Collado did not come into this fight without the backing of NAC. He was not carrying on a private little fight of his own. He was in here battling with the authority of NAC [...] In other words, the Meyer-Collado fight was not something where Collado didn’t have the backing of the United States.”<sup>206</sup> According to Demuth, the objective was to present the situation in such a way that the easiest solution appeared to be to make the US director temporary president, upon which he would rapidly issue bonds and carry out the Bank’s inaugural lending and on the basis of these achievements, be asked to assume the presidency on a permanent basis<sup>207</sup>.

With no small irony, even in the course of Collado’s campaign, his position as US ED required him to oversee the process of Meyer’s replacement and make approaches to potential rival candidates. One of these was John J. McCloy, a pillar of the American political and business establishment. He was familiar with several existing staff members including Richard Demuth from his time in the Pentagon as Assistant Secretary of War<sup>208</sup>; he had previously worked on Wall Street for Cravath, Swain, and Moore under Chester McLain (the IBRD’s General Counsel); and he had been in frequent contact with Meyer – who, with the help

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<sup>203</sup> Oliver, R., *Interview with Leonard Rist*, July 19<sup>th</sup> 1961. Pg.19-20.

<sup>204</sup> Ibid. Pg.23

<sup>205</sup> Kraske, J. et al, 1996. Pg. 31

<sup>206</sup> Oliver, R., *Interview with Mr Ansel F. Luxford*, July 13<sup>th</sup> 1961. Pg.51.

<sup>207</sup> Oliver, R., *Interview with Richard Demuth*, World Bank/IFC Archives ,Oral History Program, Columbia University August 10<sup>th</sup> 1961. Pg. 8-9

<sup>208</sup> Oliver, R., *Interview with Mr. Aron Broches*, July 11<sup>th</sup> 1961. Pg.2

of McLain, had been grooming him to accept a nomination for the Presidency. A partner of the Millbank, Tweed Wall Street law firm<sup>209</sup>, and an ex-employee of Chester McLain at Cravath, Swain, & Moore, McCloy had an exceptional network of contacts in the world of high finance. These included no meaner personages than Harold Stanley of Morgan, Stanley & Co.; Baxter Jackson of the Chemical Bank; Randolph Burgess (who at the time was vice-chairman of National City Bank); George Whitney, president of J.P. Morgan and Co.<sup>210</sup>; and Freddie Warburg, whose farm in Virginia he frequented in seeking advice on the IBRD. All advised him to take the role – subject to conditions.

These conditions had been elaborated with the help of Eugene Black, vice-president of the Chase National Bank, which McCloy had represented while in his post with Cravath, Swain, & Moore.<sup>211</sup> Black argued forcefully that McCloy would have to wrest managerial power from the executive directors. Any loan applications would be made to the management, with no obligation to seek a prior indication of the American position. All administrative matters would be the prerogative of the management and any hiring and firing of personnel would be the preserve of the Bank's president<sup>212</sup>. Accordingly, when McCloy began his negotiations with the EDs in February 1947 after two months of vacillation, the general principle of non-interference by the US government in loan negotiations was foremost in discussion.

As it became clear that the EDs, inspired by the UK's Sir James Grigg,<sup>213</sup> were about to elect Collado as temporary president at a specially convened meeting, a number of senior management threatened to resign. These included McLain, Richard Demuth, and Aron Broches,<sup>214</sup> who had been prominent in a faction organising against Collado. At the State Department's behest, Collado postponed the EDs meeting, and the Department informed McCloy that they would accept his conditions<sup>215</sup>. With Collado ousted after an executive meeting on the 28<sup>th</sup> of February, the EDs offered McCloy, Garner, and Black a verbal agreement that management would undertake their roles as they saw fit without interference.

Control over recruitment was particularly important for McCloy in terms of the US ED: the president would nominate a candidate as Collado's replacement, and that was to be

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<sup>209</sup> Bird, K., *The Chairman: John J. McCloy, the Making of the American Establishment*, Simon and Schuster, New York, 1992. Pg.282.

<sup>210</sup> Bird, K., 1992. Pg.285

<sup>211</sup> Oliver, R., *Interview with Mr. Eugene R. Black, President*, World Bank/IFC Archives, Oral History Program, Columbia University, August 6<sup>th</sup> 1961. Pg.2

<sup>212</sup> Gwin, C., 'U.S. Relations with the World Bank, 1945-1992' in Kapur, D; Lewis, P; and Webb, R., Volume 2, 1997. Pg.200.

<sup>213</sup> Kraske, J. et al, 1996. Pg.47.

<sup>214</sup> Asher, R. E., *Interview with Aron Broches*, World Bank Group Archives, Oral History Program, April 18<sup>th</sup> 1984. Pg.12

<sup>215</sup> Oliver, R., *Interview with Richard Demuth*, August 10<sup>th</sup> 1961. Pg.9

Eugene Black. To complete a management group which included Chester McLain, ex-Guaranty Co. banker Robert Garner was to be recruited from his position as financial vice-president of General Foods<sup>216</sup>. These four would constitute the 'intellectual doers' who would run the Bank.<sup>217</sup>

The structures and procedures of the Bank as laid out in the documentation of the second annual meeting of governors of the IMF and IBRD in September 1947 exemplify the contrast to those laid out in the 1946 meeting and express managerial control over lending procedure and organisational decision-making with great clarity. The constraints on the ambit of the President's decision-making by the EDs general 'direction and control' were replaced with a decisive statement to the effect that *"The President is the chief executive officer of the Bank"*. The responsibilities which now fell to Garner as Vice President were an even greater blow to the capacities of the EDs: not only did he *"act as a general manager with responsibility for assuring the effective operation of other offices and departments"*, he would *"...direct the formulation of policy recommendations for the President."*<sup>218</sup>

The greatest problem facing the Chilean loan application was the change of personnel at the Bank with the appointment of John J. McCloy and the resulting transformation of decision-making procedures. In his address to the governors on the 12<sup>th</sup> of September, McCloy was able to state that management had been offered the *"unstinted support and assistance in all its efforts by the Executive Directors"* who had relegated 'administrative matters' to the management while concerning themselves solely with issues of policy. In practice however, policy matters required their seal of approval rather than their active participation.

Garner had rapidly implemented an organisational structure which backed this managerial authority with the conventional features of a unitary, centralised organisation such as he had presided over at General Foods. Each of the functional departments had its specified remit, internal hierarchy, and a director reporting to Garner. This left little scope for the intervention of the EDs in either day-to-day matters or general strategy and direction: all matters of policy from bond marketing to economic research were clearly demarcated as falling within the purview of McCloy, Garner and their managerial team.

With managerial control established at the expense of the EDs, a further conflict was initiated – which Chwioroth has identified as the 'battle of ideas' between the academic economists of the Research Department under Leonard Rist, and the bankers and engineers of the Loan Department under Charles C. Pineo.

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<sup>216</sup> Oliver R., *Interview with Mr. Robert Garner*, 19<sup>th</sup> July 1961. Pg.3

<sup>217</sup> Oliver, R., *Interview with Mr Ansel F. Luxford*, July 13<sup>th</sup> 1961. Pg.55

<sup>218</sup> IBRD, *Second Annual Report to the Board of Governors*, Washington D. C., 1947. Pg.21

The Bank had been through a crisis of management, the resolution of which had re-constituted the politics of governance of the Bretton Woods order, before a single loan had been made. The nuts-and-bolts of the lending procedure were essentially untested, and the new team was determined to rescue the reputation of the Bank.

The French loan was authorised on the 9<sup>th</sup> of May 1947, before the first bond issue, with the application processed with markedly greater rapidity than in the Chilean case. Richard Demuth again offers striking candour on this matter:

*“...Mr. Garner [...] realized that the Bank’s reputation was at a low ebb and action had to be take, so he both organized the marketing campaign [...] and he decided to proceed rapidly with a number of European loans. Nobody at that time had any assurance that our loans to Europe would be repaid, but there was a desperate situation there [...]and McCloy decided that action had to be taken, and we made 500 million dollars of European reconstruction loans, on faith to a very large extent, without reasonable prospects of repayment that could be documented”.*<sup>219</sup>

This would appear to support Chwioroth’s argument that US officials were indifferent about the form which lending to Europe took, and that the management of the Bank was able to utilise the interpretative authority conferred upon it by Congress to set its own direction. As I have observed above, it is his argument that Bank lending practices should not be attributed to the ‘constraints’ of private capital markets which is problematic.

Chwioroth’s account shows that the Bank became an actor in its own right in a way which was driven by the agency of management in institutionalising a set of norms which most closely corresponded to the norms of their prior professional and educational environments. There is little doubt that these norms shaped the parameters of debate between the Research and Loan departments. For example, Paul Rosenstein-Rodan was recruited to the IBRD from the University of London via the ERP, and argued for a ‘general programming approach’ and lending in local currencies – as opposed to a business and commercial banking derived method. In lending for specific projects, the Bank would not be able to finance a sufficient quantity of a borrower’s total investment in order to influence their overall development policy. Failing to recognise that all capital was fungible, was *“not a question of misunderstanding, it’s a question of not understanding at all.”*<sup>220</sup>

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<sup>219</sup> Oliver, R., *Interview with Richard Demuth*, August 10<sup>th</sup> 1961. Pg. 12

<sup>220</sup> Oliver, R., *Interview with Paul Rosenstein-Rodan*, World Bank/IFC Archives, Oral History Program, Columbia University, August 14<sup>th</sup> 1961.Pg.14.



For Chwioroth, Rosenstein-Rodan was the opposite number to Vice President Robert Garner, who sat as chair of the Staff Loan committee. Drawing on Oliver's account of his years with the Bank, redacting *"terms like 'capital output ratio' out of reports, calling them 'economieze'"*<sup>221</sup>, Chwioroth contends that Garner fit Rosenstein-Rodan's depiction of a banker who neither understood nor sought to understand economists and economics at all. Garner was sympathetic to the Assistant Director of the Loan Department's calls to remove the Economics Department from its position of responsibility for Bank lending operations<sup>222</sup>.

Precisely as Chwioroth argues, Garner won out because he was in a strategically stronger position to advance his ideas, as Vice President of a new regime dominated by investment bankers and Wall Street lawyers. Rosenstein-Rodan was pragmatic enough to recognise that the Bank adopted its project-oriented approach to lending because of the appeal to management of a method which appeared more concrete and low-risk.

More importantly though, and contrary to Chwioroth's argument, Rosenstein-Rodan accepted that it was a necessity to adopt a method to which bankers were accustomed.<sup>223</sup> Although the consolidation of this approach to lending as standard Bank practice would see him leave his post in the course of the 1952 reorganisations, he was sanguine about the motivation. The Bank, he felt, had to be extremely careful in its operations, even when they were aware of strategic shortcomings because:

*"...issuing bonds in Wall Street has to take into account the mentality of other customers, and this should be a slow educational process which must necessarily take several years. Therefore the Bank ought to proceed in a cautious way, establish its good will and its creditworthiness for its bonds."*<sup>224</sup>

Both advocates of program lending and advocates of project lending recognised the importance of a conservative approach to creditworthiness, and a strategy of lending which was legible to potential investors. As I have pointed out above, the European loans expressed the interest of the New Deal coalition, of which financiers were an integral pillar. Within the Bank, their most significant proponents had a Wall Street background. Garner in particular was known to harbour hostility towards the 'liberals' at the Bank, whose ideas he considered to be

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<sup>221</sup> Oliver, R. W., 1977. Pg.239.

<sup>222</sup> Chwioroth, J., 2006. Pg.27.

<sup>223</sup> Oliver, R., *Interview with Paul Rosenstein-Rodan*, August 14<sup>th</sup> 1961.Pg.9.

<sup>224</sup> Ibid. Pg.20.

a legacy of Collado and “*Morgenthau and those clucks*”<sup>225</sup>; while an individual tainted by a history of government service would be derided by McLain as a ‘longhair’.<sup>226</sup>

Their former clients were reassured by the familiarity of the anti-‘liberal’, commercially-oriented attitudes of the new management and were able to be more forthright in their discussions of the problems of international lending as they saw it, as linkages between the Bank and the ideas of its founders became more tenuous. The Treasury and the wider Truman administration felt that they could work with McCloy, - but according to Luxford, the ‘bankers on the street’ had wanted a clear-cut victory and were of the opinion that whatever the Treasury thought, the appointment of McCloy and his team did not constitute a compromise<sup>227</sup>.

The re-orientation of the IBRD towards the financial community expressed nothing less than a pragmatic process of working-out the nuts-and-bolts of how the Bretton Woods regime would be governed in practice. Both state officials and private investors found their interests expressed in the operations of the Bank, and the shift from programmes to projects should be seen as a strategic working out of the processes through which the international order of the post-war era would be constructed and policed.

The notion that what transpired in the ‘clear-cut victory’ of management over the EDs emerges from the various rounds of interviews conducted with Bank staff under the rubric of the Oral History Programme of the World Bank Archives, in conjunction with Columbia University and the California Institute of Technology – and both the Brookings Institution histories which draw heavily upon them. These depict transition from the post-Savannah Bank to the McCloy presidency via the Collado interregnum as a financiers’ insurgency against New Deal ‘longhairs’, an inter-elite struggle to capture the leadership in which the decisive victory was delivered by means of a ‘McCloy coup’. According to this perspective the autocratic governance of the Bank in the period which followed saw the management impose the will of Wall Street on the practice of the institution and on its members.

The figure of Eugene Black provides both a partial affirmation and an important challenge to this narrative, in as far as his function in the institution transcended the dichotomy between agents of the state and agents of ‘the market’ which is retained in the Brookings histories and Chwierothe’s account. Renowned as a bond salesman on Wall Street and in government circles, Black united his role as an ED, the NAC’s interlocutor with the Bank,

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<sup>225</sup> Oliver, R.W., 1977. Pg.239

<sup>226</sup> Oliver, R., *Interview with Mr Ansel F. Luxford*, July 13<sup>th</sup> 1961. Pg.43

<sup>227</sup> Ibid. Pg.52

with his role as interlocutor for the Bank with the financial community, eliding the 'state' and 'financial' constituencies ostensibly battling for control of the institution at a stroke.

Although the Bank's director of marketing, E. Fleetwood Dunstan, had been installed in an office in New York; obtaining important regulatory concessions and developing an underwriting syndicate was largely attributable to Black's ability to draw on his exceptional connections in an informal role as the Bank's 'real' director of marketing. In May 1947, the Comptroller of the Currency permitted national banks of the Federal Reserve System to purchase IBRD bonds to the value of 10% of their capital and surplus<sup>228</sup>. Complimenting this, Black and McCloy elaborated a *'Memorandum with Regard to the Legality of the Bonds for Investment by Commercial Banks, Savings Banks, Insurance Companies, and Trustees in Certain Jurisdictions'* with a view to guiding state officials to secure interpretations of state legislation that would allow insurance, savings banks, and trust funds to participate. Crucially, Black was able to obtain the exemption of Bank securities from the 1933 and 1934 Banking Acts, through the formality of NAC consent rather than the legislative changes required for general permission from the Securities and Exchange Commission<sup>229</sup>. These achievements meant that commercial banks which were otherwise precluded from dealing in bonds of foreign governments, municipalities, and parastatals could deal in Bank securities. It was now possible to invest savings from all levels of American society in the bonds of the IBRD.

On the 15<sup>th</sup> of July 1947, four months from his appointment, the bond issue was made and rated 'AA' by Fitch Investors' Service and 'A' by Standard and Poor's Corporation<sup>230</sup>. So effective had Black and McCloy's sales drive been, that the issue attracted a high number of speculative investors – purchases from individual investors had taken place to a higher degree than expected.<sup>231</sup> Although Chwioroth focuses on the AAA rating, achieved in 1958, this illustrates that the Bank was engaged in what was effectively a process of negotiation for the support of the financial community almost from its inception. This suggests that, contra Chwioroth, the programme loans made to Europe were not received poorly by the financial community.

Settling foreign debt defaults was far more important to potential investors than the type of loans that were made. Black's ideas about lending had been shaped from the outset by his knowledge of the history of foreign bond markets. His colleagues were in full agreement with him that there could be no lending to countries which were in default if the Bank wished to engage productively with private capital. There would be no chance of retaining the 'AA'

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<sup>228</sup> Ibid. Pg.53

<sup>229</sup> Mason, E. S. and Asher, R.E., 1973. Pg.130

<sup>230</sup> Ibid. Pg.132

<sup>231</sup> Oliver, R. E., 1977. Pg.248

rating if lending took place which undermined the positions of the various bondholders' protective committees.

This had been an important reason why Collado's attempts to drive through the Chilean application had caused such outcry. The Export-Import Bank had been the principle source of capital for Chile since the 1931 default, and was accordingly negatively viewed from the office blocks of Wall Street. As a result, getting Chile to make a settlement with the US Foreign Bondholders Protective Committee (FBPC) was effectively a precondition to lending.

Existing Chilean bonds were subject to a 90% discount. Former colleagues and peers had prompted Black to be quite explicit with the effect that he *"told them that I wouldn't be willing to do it until they had made a settlement on their debt."* In the process of the negotiations, Black received a telephone call from an un-named 'important' New York bank *"...which said that they had heard that we were about to make a loan to Chile, and if we did make it they presumed that we would write the loan off to 10 cents on the dollar."*<sup>232</sup>

At this juncture the Bank's own creditworthiness was at stake as much as Chile's, and the report submitted to the working party adopts the position that Chile's method of handling the default had been problematic, and endorsed complaints to this effect on the part of the FBPC.<sup>233</sup> The application had been referred from EXIMBANK to the newly-founded IBRD, and this potentially transformative source of investment capital was now effectively embargoed.

The causes of the default were widely accepted as international, or at least intimately related to phenomena which did not have their origin in Chile. The political economy of Chilean development had been decisively shaped by the default – both in terms of its relations with the wider global economy and from a domestic perspective. These facts were accepted by the Bank, and the debacle of foreign lending in the later 1920s was understood in the 1940s as a period of excess and error in the financial community. This attitude towards Chilean bonds was not a novelty, but the institutionalisation of the demands of the FBPC in an international body sharpened the Chilean position. This was particularly the case as the interests of financiers, US business, the US government, and the IBRD were linked by the issue of the Chilean default.

For Chile, new lending was an urgent necessity: the cost of living index leapt upwards by 31% between September 1946 and September 1947<sup>234</sup>, while a persistent net balance of payments deficit (\$77m from 1945 to 1952) had been exacerbated by an embargo placed upon

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<sup>232</sup> Oliver, R., *Interview with Mr. Eugene R. Black, President*, August 6<sup>th</sup> 1961. Pg.6

<sup>233</sup> IBRD *Chile Loan Application Report by the Working Party*, Washington D.C., 1947. Appendix III, Pg.26-8

<sup>234</sup> Kofas, J. V., 'The Politics of Foreign Debt: the IMF, the World Bank, and U.S. Foreign Policy in Chile, 1946-1952', *The Journal of Developing Areas*, 31 (Winter), 1997. Pg.161

all credit to Chile by Assistant Secretary of State Braden (whose father had founded the Sewell mines, where Kennecott was struggling with strike action), unless strikes were settled in such a way as not to favour labour and taxation policies were 'simplified'.<sup>235</sup>

The Chilean government at the time of the application was a coalition formed by Congress in the aftermath of an inconclusive election. President Videla's cabinet contained, apart from his own Radical party; Communists, Liberals and independents. The coalition endorsed a populist programme promoting industrialisation and the nationalisation of strategic industries, insurance, and lowering rents, in conjunction with creating a state bank to control credit and target inflation.<sup>236</sup> This enabled the government to harness the strength of the union movement in areas such as copper mining and nitrate production, as a counterweight to the transnational might of the American corporations which dominated these sectors.<sup>237</sup>

While foreign ownership of these strategic industries constituted a problem for the Chilean government, it enabled Videla to stress the threat of a costly capitulation to Communism in an effort to extract new lending. US citizens and institutions held the lion's share of Chile's foreign debt and the US was Chile's single most significant trading partner. US officials demanded regular payments on foreign debt and non-discriminatory treatment of their companies, and Chilean officials intimated that additional revenues might have to be sought from the copper industry if credit was withheld.<sup>238</sup>

American businesses' complaints carried considerable weight with the Bank: On the basis of his discussions with the 'copper people' – Kennecott and Anaconda – in New York, Leonard Rist pointed out that these were *"practically the same people who would buy our bonds tomorrow."*<sup>239</sup>

Bondholders' complaints relating to Chile's diversion of revenues from the copper and nitrate industries into government spending programmes were also decisive in influencing the Bank's stance. Although Chile complied with the demands of the State Department and the US copper firms in simplifying its taxation practices, legal provision had been made by the Chilean government in 1932 to expedite service of foreign debt by transferring profits from sales of nitrates, and government taxes on income, copper, and petroleum. As of the 31<sup>st</sup> of December 1944, 90% of dollar bondholders, 99% of their Sterling-denominated counterparts,

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<sup>235</sup> Barnard, A., 'Chilean Communists, Radical Presidents, and Chilean Relations with the United States, 1940-1947', *Journal of Latin American Studies*, Vol.13, No.2, November 1981. Pg.369

<sup>236</sup> IBRD. *Chile Loan Application Report by the Working Party*, Washington D.C., 1947. Pg.6

<sup>237</sup> Barnard, A., 1981. Pg.347

<sup>238</sup> Ibid. Pg.349

<sup>239</sup> Oliver, R., *Interview with Leonard Rist*, July 19<sup>th</sup> 1961. Pg.22

and 94% of their Swiss peers had agreed to this arrangement and had duly been receiving interest payments.<sup>240</sup> The holdouts' chief complaint was that the Chilean government had founded Fomento - the very body which would have benefited from the loan that the government was attempting to contract with the Bank - on the basis of revenues from strategic industries which, under the terms of a 1935 memorandum between the Chilean Special Financial Commission and the FBPC, were payable to foreign bondholders in their entirety.<sup>241</sup>

The conjunction of US business, state, and financial interests is exemplified in a letter from US Ambassador Claude Bowers to president Videla in September 1947, to the effect that *"the slowing down of production inspired by Communists was a matter of deep concern to American bankers investigating the possibilities of investment."*<sup>242</sup>

Pressure from the Bank, the State Department, and the FBPC, prompted the Chilean Congress to give the President special powers to designate areas in which miners were striking as 'emergency zones'. Approximately 1,500 unionists were deported (with their families) by the military from these areas, and under the Law for the Permanent Defence of Democracy in September 1948<sup>243</sup>, Communist party members were prohibited from voting and some members were interned in concentration camps.

The final obstacle to IBRD lending was overcome through an agreement to re-schedule outstanding US private debt with the FBPC, which was publically announced on the 24<sup>th</sup> of March 1948.<sup>244</sup> Similar agreements had simultaneously been made with the Association Suisse des Banquiers and the Council of Foreign Bondholders of Great Britain.

The following day a meeting of the EDs was chaired by Robert Garner at which two resolutions were passed, with a single abstention, to accept the President's recommendation to make loans to Fomento and Endesa totalling \$16m. The press release notes that in 1947, the Chilean government undertook a change in monetary and financial policy. Deficit financing ceased, the money supply correspondingly tightened, and expenditures were 'consolidated' in line with receipts from taxation. These measures, the Bank noted, *"...are increasing indications that an adequate policy is being pursued and that stable economic conditions will be achieved."*

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<sup>240</sup> IBRD *Chile Loan Application Report by the Working Party*, Washington D.C., 1947. Appendix III, Pg.29-33.

<sup>241</sup> Ibid. Pg.32-3

<sup>242</sup> Letter from Claude Bowers to Assistant Secretary of State Norman Armour, Santiago, September 9<sup>th</sup> 1947. National Archive, State Department files 825.51/9-947 cited in Erickson, K.P., and Peppe, P.V., 'Dependent Capitalist Development, U.S. Foreign Policy and Repression of the Working Class in Chile and Brazil', *Latin American Perspectives*, Vol.3, No.1, Winter 1976. Pg.31

<sup>243</sup> Erickson, K.P., and Peppe, P.V., 1976. Pg.32-4

<sup>244</sup> IBRD, *Foreign Dollar Loans 1920 - 1947*, Washington D.C., July 26<sup>th</sup> 1948. Pg.13

*Such conditions might strengthen the foreign exchange position, and Chile has expressed the hope that private capital be directed towards investment in industrial and agricultural development.”<sup>245</sup>*

## Conclusion.

In this chapter I have sought to develop a non-functionalist perspective on the role of the Bank in the development and governance of the Bretton Woods order. To this end, I have drawn upon the insights offered by Chwioroth’s ‘strategic constructivism’ in terms of the importance of internally articulated debates and the significance of the processes of management and lending in the determination of the form of governance of the post-war order. My objective has been to demonstrate how these debates and processes are rooted in the social relations of the broad Fordist compromise, and express the inclusion of financiers rather than their ‘repression’ by government.

The staff testimonies which support Chwioroth’s intervention (and the Brookings histories) suggest that a ‘battle of ideas’ did indeed take place, and that the ‘interpretative authority’ of the management was a major factor in the decision to make general purpose loans to Europeans. The recruitment of a new managerial team from the world of New York finance was extremely important in the struggles which occurred around these issues, but its real significance lies in the transformation of the management relationships of the Bank upon which their recruitment was made contingent. This was nothing less than a re-configuration of the relationship of the management to the EDs – of the Bank to member states - visible in the reorganisation of the Bank’s policy and decision-making structures.

Without distancing the Bank from the New Deal administration in this way, it would have been impossible to draw on financial markets to support Bank activities. The turn to the project approach was not a transition made on the basis of the ability of a group of commercially-minded Wall-Streeters to overcome the Bank’s academic economists with the assistance of a contingent change in personnel. It was made on the basis of the Bank’s capitalisation problems.

This did not confer ‘autonomy’ upon the Bank: it necessitated the transformation of institutional strategy. The infrastructural power of finance was thereby institutionalised in the Bank, as the project approach was adopted on the basis of its similarity to commercial investment practices. This is not to say that the new management pursued the interests of financiers to the exclusion of the aims of the Bretton Woods settlement. Rather than a zero-

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<sup>245</sup> IBRD, *Press Release No.86*, March 25<sup>th</sup>, 1948.

sum conflict between state and market these cases demonstrate that while the Bank was a site of contestation it was also a site of pragmatic accommodation between bankers and state officials. Bank action therefore functioned to simultaneously support the objectives of its major donors, re-constitute the international market for foreign bonds, and to support its own creditworthiness.

Further, the Bank was an agent of the construction of a regime of international governance which reflected and reinforced these social relationships, and those of the economies of the periphery which supported them. This is evidenced by the practices of management in strategically managing these interests by deploying appropriate tools – hard conditionality on debt-defaults and project lending in Chile, and balance-of-payments support through programme lending in Europe.

The transition to project lending was not due to a ‘coup’, or to a ‘battle of ideas’ in an institution insulated from external pressures by ‘interpretative authority’. It reflects the pragmatic working-out of a concrete politics of governance which reflected the social relationships of the New Deal in which the Bank was anchored.



## Chapter 4: The Turn to ‘Development’: Making the World Safe for the Dollar.

In Chapter 3 we have seen that the imperatives following from the foundation of the Bank on the basis of private financial capital quickly challenged the ideas of its architects concerning how it would operate. We have seen, in conflict between Bank management and the Executive Directors over the Chilean loan, the way in which the Bank’s financial imperatives mediated its capacity to act on the hegemonic US agenda. The Bretton Woods regime may be re-conceptualised, on this basis, as an order in which the infrastructural power of American finance was institutionalised at the international level.

The most striking feature of the nineteen years under discussion in this chapter, from 1949 to 1968, is the ‘turn to development’: the expansion of Bank activities beyond Europe, to South American, African, and Asian members. I will show that pursuit of the ‘development’ agenda should not be read as a simple extension of the ‘embedded’ liberal nature of the financially repressive post-war regime. It was a contingent aspect of management’s pursuit of the Bank’s operational imperative to secure its capitalisation. Only through the foundation of the affiliates, the IDA and IFC, and the transformation of its lending processes to reflect the practices of the commercial banks that bought its bonds could the objective of expanding concessional lending to low-income members could be facilitated without damaging the Bank’s own all-important creditworthiness. In the process, the agenda of the Bank became increasingly closely interwoven with that of the US. Yet, by the end of the period, a new contradiction would emerge from the realisation of the objective of multilateral convertibility which both the Bank and the US had pursued, which would threaten the Bank’s ability to perform its role as an institution of global governance.

I will show that the objectives of the Bank, private finance, and member states were not implacably antagonistic, as the ‘embedded liberalism’ thesis contends. The epochal objective of the American state was to centre a multilateral trading order upon the dollar. The Bank’s objective was to secure its capitalisation by diversifying its sources of borrowing, and to obtain the subscriptions pledged by members New Hampshire in 1945. The objectives of financiers were to enforce commercial discipline on defaulted debtors, and to reconstitute and develop international capital markets as sources of liquidity and venues for profitable investment. I will argue that these objectives were mutually reinforcing, although their increasingly close interrelationship gave rise to a major contradiction with the development of

the Euro-dollar markets in the later 1960s. Crucially, their attainment remained mediated by the imperatives of financiers throughout.

The drive to turn the Bank into a development agency can be seen to have two sources. Firstly, President Truman's speech at his second inauguration in 1949 laid out a foreign policy vision in which the security of the heartland of the post-war order was linked explicitly to the development of the wider non-communist world. The administration remained eager, in spite of Collado's acrimonious departure, that the Bank expand its operations in support of this epochal governance objective. Secondly, while Marshall Plan funds supplanted it in Europe, the Bank was threatened with irrelevance by the commencement of negotiations in the UN to found a special low-conditionality fund for economic development which would enable low-income borrowers to escape the Bank's financial discipline.

These pressures shaped the Bank's problematique in the 1950s and 1960s. Its ability to meet these objectives was nothing less than an existential question for it as an agent of global governance – and thereby for the wider Bretton Woods regime. Retaining the support of its major donor, on the one hand, and avoiding marginalisation in favour of a new institution, on the other, required the Bank to draw upon the capital of private investors. Before its principals' needs could be met it would undertake significant transformations in three associated areas, resulting in a total transformation by the early 1960s.

Firstly, a major structural reorganisation was undertaken in 1952 to support the institutionalisation of the commercially-oriented 'project approach' as a lending model. This was a pre-requisite of the second area of transformation: the way the Bank funded its operations. Combining the project approach with strategic programme lending enabled the Bank to simultaneously meet its own objectives, and those of the US, without sacrificing its creditworthiness.

Secondly, management worked to achieve significant diversification of the Bank's investor base with a view to securing sufficient operating capital to expand its lending activities. Through diversification, the Bank could better guarantee the security of financing against currency fluctuations and individual capital controls – particularly as the US struggled with its balance of payments deficit.

Thirdly, the way in which the Bank disbursed its monies was significantly altered through the foundation of two affiliated lending organisations under the umbrella of the 'World Bank Group'.

In exploring these developments, I will show that the Bank's financial imperatives shaped its strategy in the 1950s and 1960s to a much greater extent than the agency of presidents and development economists.

Focusing on the complementarities of the objectives of the US, financiers, and the Bank; and the way in which the development of the US' hegemonic agenda was mediated by the imperatives of financiers helps to avoid a contradiction which bedevils the 'coup thesis' of the Brookings histories. This is the sharp dichotomy which it sets up between state and market – where the Bank was captured by market interests. Following the McCloy coup, so the story goes, the Bank acquiesced to a strategic development agenda handed down from the State Department in support of the imperatives of the Truman and Eisenhower administrations.<sup>246</sup> This neglects the imperatives of the transition to management governance of the Bank under McCloy, and thereby misreads its character and purpose as a blow struck for the market *against* the state. More problematic still returning to the 'embedded liberalism' thesis in this way suggests that the 'turn to development' was a reflection of the dominance of the imperatives of the US *state*, re-asserted at the expense of those of financiers in pursuit of the stabilisation of its hegemony in the post-war regime.

As a counter to the depiction of the Bank as an agent whose actions were defined by the agenda of its principles, Chwioroth's focus on the internally articulated processes of change which were at work inside the Bank across the period helps to illuminate the central failing of the Brookings thesis. Through focusing on the development of the project approach, he is able to demonstrate that the technology of institutional governance which was required to make development lending – and the continued centrality of the Bank to the post-war regime – acceptable to Wall Street and the US was not dictated by either. The technique of conditional lending for defined, productive projects rather than for broad-brush balance of payments support was a key step in the elaboration of the development agenda, and was adopted by the Bank in its specific form through the strategic agency of management.

I argue that Chwioroth over-states the autonomy of the Bank in pursuit of its own institutional objectives. In arguing that this transformation was effected through essentially internal processes of strategic change, Chwioroth divorces the ideas underpinning the project approach from the imperatives which necessitated its adoption. In his account, institutional change is linked to external social relations only via the ideational socialisation of the

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<sup>246</sup>Kraske points out that as a liberal internationalist with a conservative banking background, Black was firmly persuaded of the virtues of capitalism and shared the administration's views on the threat posed by communism. Mason and Asher also emphasise the 'harmony' between the Black-era Bank and the Truman administration; while Kapur, Lewis, and Webb posit a strong compatibility between the Bank's "*conspicuously Republican-style team*" and the Eisenhower administration – depicting both as defined by a 'republican internationalist' persuasion. See Kraske, J., with Becker, W. H., Diamond, W., and Galambos, L., *Bankers with a Mission: the Presidents of the World Bank, 1946-91*, Oxford University Press, New York, 1996. Pg.83; Mason, E. S., and Asher, R. E., *The World Bank since Bretton Woods*, Brookings Institution, Washington, 1973. Pg. 94; Kapur, D., Lewis, J. P., and Webb, J. R., *The World Bank: its First Half Century, Vol.1: History*, Brookings Institution, Washington, 1997. Pg.1172-3.

managers who advocated them in particular professional and epistemic communities. Where the interests of the Bank and external forces coincided, this was due only to the ideational harmony of the epistemic communities which guided them. Therefore, the adoption of commercially-oriented norms of lending was due to the agency of management alone.

The observation that the central transformation in the Bank's process during the 'turn to development', through which the character of development lending was constructed as conditional and based on 'productive' projects is a key insight, which I will take as my starting point in this chapter. Yet, as I will show, the fact that the programme loan model endured alongside the project approach until 1957 illustrates the interweaving of US, Bank, and financial imperatives. Further, locating the impetus for the adoption of the project approach overwhelmingly in management agency suggests that the elaboration of project lending as the key practice through which 'development' was realised was only one of an array of possible choices, in spite of the existence of powerful social interests which sought to pressurise the Bank from 'outside'. The fact that it concurred with the commercially-derived understanding of sound lending practice was a matter of choice and ideational coincidence. Here, the power of ideas floats free of the anchor of social interest.

I wish to clarify the material basis of the transitions identified by Chwiero, in order to illustrate how the agency of management was limited and shaped by the imperatives of the social forces in which its power as an institution was rooted. The turn to development was not impelled exclusively by the imposition of the agenda of the US and the Damascene conversion of Wall Street bankers and lawyers into humanists. Nor was it driven by the power of ideas and professional norms of managerial entrepreneurs. Each of the transformations undertaken to the Bank's processes of lending, and institutional structure, reflects the way in which the objectives of members and the Bank itself were shaped by the reliance upon financiers for capitalisation. At every turn, the agency of Bank management would be mediated by the imperatives of finance.

The 'turn to development' was a contingent aspect of Bank strategy. Firstly, I will explore how getting access to European capital markets entailed the closer and increasingly contradictory interweaving of the Bank's institutional imperatives with the objectives of the US government and those of US financiers. The objective which united all these requirements was the attainment of multilateral convertibility, and the Bank pursued strategic lending and non-lending in support of this aim.

Secondly, I will present the institutional transformations which were required in adjusting to the new problems posed by the Bank's success in promoting these interrelated interests. The foundation of the affiliates is conventionally taken to exemplify the Bank's re-

configuration as a development institution. However, I will show that the International Finance Corporation represented an effort to set forth a long-held commitment among Bank management to the primacy of private capital in development. The International Development Association also had its genesis in an effort to retain the Bank's primacy in multilateral aid transfers in the face of proposals to expand the UN's role in this field. Both are best understood as an effort to accommodate the contradiction caused by the Bank's success in facilitating the achievement of conditions whereby it could diversify its borrowings.

Ultimately, the affiliates which formed the vehicle for this ostensible strategic change became the source of a renewed crisis for the Bank as they reinstated the influence of members' legislative bodies over the institution's budget which McCloy and Garner had fought to resist.

## 1: Securing the Bank's Capitalisation

Europe's liquidity problem was the central problem of the 1950s for the Bank. For this reason, issues of 'development' were viewed by Bank management in the Black era through a primarily European prism. A minority of the forty-eight members had paid their pledged 18% tranches in full, and Bank bonds could not be marketed in most European financial centres due to emergency restrictions on investment. The problems facing members such as Brazil, Mexico, and Chile were also placed in a European frame: how could the conditions be created whereby their 'traditional' trade with the countries of that continent be resurrected? By far outstripping these issues was the problem of European recovery: it was imperative to get European producers selling in dollar markets again. Bilateral arrangements between currency blocs, and the stolid arrangements for capital transfers within the sterling and gold areas posed two major obstacles to the Bank.

Firstly, it meant that its lending capacity was limited to the US guarantee, and secondly, that it was only able to supplement paid-in US resources with recourse to the New York capital market. The paid-in portions of the largest members' subscriptions would not be released until the balance of payments condition of European members had improved satisfactorily to permit the achievement of multilateral convertibility. In this section, I will illustrate the strategic efforts made by Bank management to facilitate these conditions – to which end it would be forced to court both the US government and private financial capital assiduously. Their complex interrelationship in Bank strategy was manifest in a focus on European matters relating to debt default and blocked currency balances, exemplified by the engagement of the IBRD and the governments of Greece and Yugoslavia; and efforts to break

into the sterling currency bloc, exemplified in the Australian case. Addressing these cases would require a strategic admixture of the project and programme approaches to lending.

These cases were central to the Bank's ability to satisfy US and investor interests. A hard line stance on Greek debt defaults was combined with a flexible approach to Yugoslavia's defaults which enabled the Bank to support the US' overlapping security and monetary policy objectives. This strategic calculation proved essential to improving the Bank's access to the member subscriptions it desperately needed, while helping to foster moves in the direction of convertibility which could see those subscriptions realised as loan-able resources and guarantees which might offer further leveraging opportunities in capital markets.

In January 1951, all Greece's long-term external debts were in default apart from \$128 million in post-world war two credits from Britain and the US. These concerned loans contracted as far back as 1881. The Bank estimated that the outstanding publicly funded external debt to private sterling, franc, and dollar creditors was \$325 million.<sup>247</sup> The Bank position was clear: Greece was not eligible for IBRD lending. The clarity of the Bank's position was derived from the fact that *"The American foreign bondholders' council was very, very tough on the Greeks, writing very harsh reports about Greece's unwillingness to pay despite its' recovery."*<sup>248</sup>

The American interest was clearly expressed in 1947 by Under Secretary of State Dean Acheson, who informed Congress that *"a highly possible Soviet breakthrough might open up three continents to Soviet penetration. Like apples in a barrel infected by one rotten one, the corruption of Greece would infect Iran and all to the east."*<sup>249</sup> The same year, following an investigation conducted at the request of the Greek government, US Congressman Paul A. Porter reported to the House Foreign Affairs Committee that an American recovery mission would need \$300 million in the next financial year to fend off either a return to fascist governance or communist revolution.<sup>250</sup>

Financial imperatives were equally clearly expressed. Although the Greek economy remained in a parlous state following its liberation from Bulgarian occupation in 1944, and Bank management were clearly sympathetic to the anti-communist objective in Greece, their inability to authorise lending in support of this remained quite straightforward in the opinion of Bank vice president Robert Garner. In 1961, drawing on the Chilean example to explain the

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<sup>247</sup> IBRD, *Foreign Indebtedness of Greece*, Washington D.C., 12<sup>th</sup> March 1951. Pg.1-5

<sup>248</sup> Oliver, R.W., *A Conversation with Richard Westebbe*, Washington D.C., 25<sup>th</sup> January 1988. Pg.2.

<sup>249</sup> Acheson, D., *Present at the Creation: My years at the State Department*, Norton, New York, 1969. Pg.219, cited in Chomsky, D., 'Advance Agent of the Truman Doctrine: the United States, the New York Times, and the Greek Civil War', *Political Communication*, 17:4, 2000. Pg. 424

<sup>250</sup> Vetsopoulos, A., 'Efforts for the Development and Stabilization of the Economy during the Period of the Marshall Plan', *Journal of Modern Greek Studies*, Vol.27, No.2, October 2009. Pg.280

importance of the hard Bank line to the success of its on-going relationship with financiers and the impact of not making a settlement, Garner explained that: *"Having established the precedent with Chile, the objections were less vociferous. The only one that I know of that hasn't taken any real steps towards settling their obligations is Greece. That is still unsettled, and the Bank has never made a loan to Greece."*<sup>251</sup> This hard-line stance, while not directly supportive of the anti-communist effort, certainly went a long way towards reinforcing the perception of the Bank's probity among financiers. Greece would not see any funds from the Bank until 1967.

The necessity of appealing to both sets of imperatives is evident in the differential in treatment between Greece and Yugoslavia. The hard-line approach was necessary in Greece due to the way in which the Bank engaged with the case of Yugoslavia. The Yugoslav application linked not only American monetary and security interests, but the Bank's interest in obtaining paid-in subscriptions from European members whose currencies were still not convertible. In order to meet these objectives, the Bank took a far more lenient stance on the Yugoslavian defaults. Like Greece, Yugoslavia had defaulted on its private external dollar bonds in 1932, although it had been able to maintain partial service until 1939, total default took place in 1941 on bonds to the value of \$56,252,331.<sup>252</sup>

As Mason and Asher have noted, Eugene Black was quick to spot the opportunity that this potential crisis for the nascent post-war American sphere of influence in Europe afforded the Bank: US and Western European political interests in the survival of Tito's regime could be linked with hitherto thwarted trade interests in such a way as to provide for the release of the 18% paid-in subscriptions still outstanding among many European members.<sup>253</sup> During the early to mid-1950s, the scope for the IBRD's lending was extremely straitened by the bilateral and bloc-oriented monetary practices of the era. Already in 1951 a number of other prospective loans - to Iceland, Iraq, Pakistan, and Finland - were proving difficult to fund. Britain, France, and Belgium had previously refused to allow their 18% subscriptions to be drawn, expressing concerns about the balance of payments impact of the use of their funds for procurement in fellow European Payments Union (EPU) economies.

With the twin objectives of securing European members' capitalisation and reinforcing moves toward multilateral convertibility among European currencies in mind, Black took the extraordinary decision to work out a deal in principal with the Yugoslav ambassador in Washington, bypassing the FBPC. Against the precedent set in Chile and replicated in Greece,

<sup>251</sup> Oliver R., *Interview with Mr. Robert Garner*, 19<sup>th</sup> July 1961. Pg.14.

<sup>252</sup> Foreign Bondholders Protective Council, Inc., *Report 1965 through 1967*, Lenz & Riecker, Inc., New York, 1968. Pg.126-7.

<sup>253</sup> Mason, E.S., and Asher, R.E., 1973. Pg.111

Yugoslavia simply had to agree in writing to the Bank that a settlement would be made by a specific date.<sup>254</sup>

The latent leverage upon European members could be realised with this agreement and lending could go ahead due to the tough stance taken on Chile and Greece, and the apparent gravity of the security dimension to the situation. As 80% of the equipment required by the 25 projects identified in the Yugoslav plan was sourced from Europe, Black refused to loan Yugoslavia more than \$12m of a proposed loan of \$28 million unless Western European countries agreed to permit the use of their 18% subscriptions – or allow the Bank to raise funds in their capital markets.

‘Special Releases’ from twelve European countries followed the Yugoslav loan.<sup>255</sup> Yet the \$200m that the payment of outstanding subscriptions had secured was only a short-term shot in the arm for the Bank’s lending programme.

Although they permitted greater flexibility in terms of lending to members who were not creditworthy in dollar terms, the special releases could not displace capital market borrowing as its principle source of funds for this purpose. Lending to peripheral European countries which might have been creditworthy in their own or other local European currencies remained entirely dependent on the release of the 18% paid-in local currency portion of the member’s subscription, and the Articles of Agreement required the individual governor’s approval of further lending in that currency and its conversion into other currencies, while loans could also be tied to specific conditions relating to procurement.

The inability to re-lend during the first decade had cost the Bank in unearned interest and the lending ceiling was still fast approaching. As Kraske points out, the eventual release of the remaining 18% paid-in capital subscriptions in multilaterally convertible form in 1957 was dependent ultimately on the accumulation of large dollar balances outside the US, and the recovery of the balance-of-payments positions of members.<sup>256</sup>

For this reason, the Bank’s objective was to facilitate the accumulation of the dollar holdings of strategic trading partners, and this determined management’s strategic engagement with Australia. Although Chwioroth is correct to note that the arrival of Wall Street alumni drove the turn towards projects in the Bank’s lending, it is important to emphasise that the program loans continued – and that this neither represented the last hurrah of the New Deal ‘longhairs’, nor did it conflict with the interests of private financial

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<sup>254</sup> Oliver, R.W., July 12<sup>th</sup> 1961. Pg.56.

<sup>255</sup> Mason, E.S., and Asher, R.E., 1973. Pg. 110-12.

<sup>256</sup> Kraske, J., et al, 1996. Pg.85.



backers. As Mason and Asher point out, a further sixteen program loans to the value of \$1,055 million were made across the period 1950 and 1957.<sup>257</sup>

Such strategic mutability in the Bank's lending practice is underscored by its engagement with Australia during the 1950s. Australia appeared to be an unlikely candidate for a Bank loan, as it was highly creditworthy. Having never defaulted on its foreign obligations, it was thought to be a dynamically expanding economy in which high returns on investment could be found. Robert Garner, the Bank's General Counsel, considered it "*embarrassing*", to enforce the project approach with members such as Guatemala or Pakistan, when such large volumes of capital had been handed out to a wealthy government which was independently active in the private capital markets of New York with little scrutiny and for such general purposes.<sup>258</sup>

Australia's application nonetheless estimated that its capital needs ran to \$250 million, of which \$100 million was required immediately to sustain dollar imports<sup>259</sup> required for a development strategy designed to support population growth and production of raw materials for export to the dollar area.<sup>260</sup> A report on the Australian development programme noted that "*The Bank has not had an opportunity of studying the development projects which make up these programs nor of discussing them with the State and Commonwealth authorities and the business enterprises who will in fact carry them out [...] the mission did not make a technical examination of the projects.*"<sup>261</sup> As the relationship progressed further, a Bank study of the Australian economy observed that the conditions upon which the loan of 1950 had been predicated had not obtained, and that damaging inflation had undermined the government's growth strategy. Nevertheless, it went on to suggest that since "*[t]he Australians are a competent people with an ability to get things done once they have set their mind to it*", a further \$50 million credit should be extended.<sup>262</sup>

The contrast with the Greek case is illustrative of the wider importance of lending to Australia: whereas Greece was the cornerstone of the Truman doctrine for U.S. security, Australia was a key piece of the international monetary jigsaw with the capacity to strengthen

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<sup>257</sup> Mason, E.S., and Asher, R.E., 1973. Pg.264 footnote 7, 269-75, cited (incorrectly as 11 program loans) in Chwioroth, J., 2006. Pg.26.

<sup>258</sup> Oliver, R. W., *Interview with Davidson Sommers*, The World Bank/IFC Archives Oral History Program, Columbia University, 2<sup>nd</sup> August 1961. Pg.29-32.

<sup>259</sup> IBRD, *Report and Recommendations of the President to the Executive Directors on the Proposed Loan to the Commonwealth of Australia*, Washington D.C., August 18<sup>th</sup> 1950. Pg.1

<sup>260</sup> IBRD, *Australia: Economic Report*, Washington D.C., August 17<sup>th</sup> 1950. Pg.16

<sup>261</sup> IBRD, *Description of Australian Development Programs*, Washington D.C., July 3<sup>rd</sup> 1952. Pg.1

<sup>262</sup> IBRD, *The Australian Economy*, Washington D.C., June 27<sup>th</sup> 1952. Pg.iv.

sterling area dollar reserves and thereby facilitate the transition to a fully convertible international monetary system.

The strategic combination of program and project lending in the early years reflects the Bank management's simultaneous engagement with financiers and donor members. These interests, who had found common ground in these early program loans from a broader strategic viewpoint, focused upon the easing of constraints to international trade and transfers. The most concrete expression of this took the form of the Bank's efforts to ensure that the international monetary regime would be centred upon the dollar. Beginning dollar-based relationships with countries that were part of rival currency blocs and improving their dollar holdings would contribute to their return to multilateral convertibility and secure the primacy of trade in dollars.

## 2: A Victim of its own Success?

Successful pursuit of a strategy aimed squarely at replenishing the dollar holdings of European borrowers, re-orienting Sterling bloc members toward the dollar, and enforcing discipline on defaulted debtors had significant consequences for the form, lending processes, and structure of the Bank. In support of these aims, the first decade had been a period in which the Bank had worked desperately to broaden its investor base and expand the market in IBRD securities. Two major consequences followed from these strategies.

Firstly, non-European members sought to supplant the Bank through the UN: developing members clamoured for funds, and the Bank had to act quickly to deflect their critique and absorb their demands in order to retain its primacy in the governance of the early Bretton Woods order.

Secondly, support for dollar-based multilateral convertibility played a role in the development of the conditions for the foundation of the Eurocurrency markets. This caused two further problems for the Bank: US efforts to control the expansion of dollar balances outside its borders saw the Bank excluded from the US markets while Congress refused to fund the International Development Association (IDA) on the basis that it would exacerbate the budget deficit. Secondly, while the threat from the UN had been absorbed the threat posed by the Euromarkets could not be so easily accommodated: middle income borrowers began to develop a debt profile which boded ill for the future.

Ultimately, the Euromarkets would supplant the Bank among middle income members, laying the foundations for the debt crisis of the 1980s. In this section, I will explore the path to this outcome, illustrating firstly the Bank's success in its ability to translate the

interests of financiers and the US into a coherent politics of governance in the early Bretton Woods period. I will then turn to the institutional transformations which were required as a condition of this success, before discussing the pathological outcomes which they were unable to avoid.

### **Paying Dividends: the Success of the Diversification Strategy**

Initially, the Bank had been able to borrow solely in New York and Switzerland – the only capital markets which were able to offer convertible currencies. Beginning with the \$250m bond offering of 1947 the IBRD had long been a major borrower in the New York money markets – between 1946 and 1964 the Bank was one of the two largest issuers of securities, the other being the Canadian government. Between them they were responsible for more than half of the \$14bn of new foreign issues in this period<sup>263</sup>. 85% of bank bonds issued to 1957 were denominated in dollars<sup>264</sup>, and since borrowers were demanding dollar funds during this period of intense capital shortage and limited convertibility, this was not immediately problematic – for those states which were considered dollar creditworthy<sup>265</sup>.

Eugene Black and Robert Garner had enjoyed significant success in persuading US and Canadian state legislatures to permit their financial institutions to purchase Bank securities. The 1951-2 Annual Report placed the sum of bonds purchased by investors during that year at \$175.3m. Two issues had been made in the US totalling \$150m, supplemented by one in Switzerland for CHF 50,000 (\$11.6m) and one in Canada of C\$15m. Sales from portfolio contributed \$23.4m.<sup>266</sup> Black had issued a similar plea to the board of governors in 1949 – to take legislative action in their home governments to make Bank bonds saleable to central banks and more broadly, to institutional and individual investors outside the US.<sup>267</sup>

This was taken up enthusiastically in Germany, where only mortgage banks were barred from investing in Bank paper, and a healthy market developed among private individuals and the banking system. From 1950, IBRD dollar bonds were traded on the Paris and Amsterdam stock exchanges and with a sterling issue in London in 1950 and a guilder issue in Holland in 1954, the Bank was already an established actor in the international capital markets by the mid-1950s. In 1951 the Bank had \$536.7m in direct and guaranteed obligations outstanding, 20% of which – approximately \$130m - was held by investors outside the US. The majority of the approximately \$50m in bonds denominated in other member currencies was

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<sup>263</sup> Langley, P., *World Financial Orders: an Historical International Political Economy*, Routledge, Abingdon, 2002. Pg.67

<sup>264</sup> Mason, E.S., and Asher, R., 1973. Pg.106

<sup>265</sup> Kraske, J., et al, 1996. Pg.84

<sup>266</sup> IBRD, *Seventh Annual Report to the Board of Governors, 1951-1952*, Washington D.C. 1952. Pg.37-8.

<sup>267</sup> Kraske, J., et al, 1996. Pg.84.

held by non-US investors, alongside an estimated further \$69m in dollar bonds. In contrast to the American market, the principal foreign purchasers were central banks<sup>268</sup>. Across the period, the significance of European capital markets would increase significantly: in 1968, long term bank borrowing in West Germany exceeded funds raised in the USA<sup>269</sup>.

Expanding participation in bond issues and sales from the Bank's portfolio in European capital markets was the main reason that the houses of Morgan Stanley and First Boston were selected as underwriters of the IBRD's bonds<sup>270</sup>. The Parisian affiliate Morgan Grenfell gave the former strong links with Europe, and was renowned as a wholesaler. First Boston had one of the leading retail systems of any US bank outside the USA. The transition from the 1947 model of bond sales organised through a vast syndicate of almost 1700 security dealers in 1947 to direct negotiated sales to a preferred underwriter reflected an effort to find the issuing process which would give the Bank the best start in creating and maintaining an international market in its bonds<sup>271</sup>. Looking back on the period in 1961, the first Treasurer, Daniel Crena De longh reflected that *"if all that hadn't been done, now that the American market is, at present at least, not so favourable, and the balance of payments is not so favourable, the situation of the Bank would really be very, very different at present."*<sup>272</sup>

This represented an enormous success for the Bank. Figures compiled by Mason and Asher in their history of the Bank's first quarter-century show that net borrowings outstripped subscriptions as a source of income for the first time on June 30<sup>th</sup> 1958, from which point on they remained the largest source of income. Sales from portfolio similarly outstripped and continued to exceed subscriptions from 1964. Both of these remained individually larger sources of revenue than income from operations, and repayments from principal only marginally outstripped sales of the Bank's loans in 1971 – although remaining less than half the value of net borrowings in that year.<sup>273</sup> They argue that the period since the mid-1950s was characterised by a decline in the relative importance of the US markets as a source of borrowing. This is certainly true – across the period from 1955 to 1971, the Bank borrowed in Belgian francs, Canadian dollars, Deutschmarks, lire, yen, Kuwaiti dinars, Dutch guilder, Libyan pounds, Swedish kronor, and sterling, although its non-dollar borrowings were by far the most frequent in Swiss francs. By volume, Deutschmarks were the most significant – although only

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<sup>268</sup> IBRD, *Seventh Annual Report to the Board of Governors, 1951-1952*, Washington D.C., 1952. Pg.39.

<sup>269</sup> Mason, E.S., and Asher, R.E., 1973. Pg.140.

<sup>270</sup> Kapur, D; Lewis, P; and Webb, R., 1997. Pg.922.

<sup>271</sup> IBRD, 1952. Pg.38

<sup>272</sup> Oliver, R., *Interview with Mr. Daniel Crena De longh*, 1<sup>st</sup> August 1961. Pg.45

<sup>273</sup> Mason, E.S., and Asher, R., 1973. Appendix F. Pg.857.

slightly more than one quarter of dollar borrowings – and the German capital market was tapped more consistently than the Swiss from 1965 onwards<sup>274</sup>.

Black had wanted to transform the way in which Bank paper was viewed, commenting that *“I invented a word I’m not sure is in the dictionary. We tried to do what we called ‘pedestalize’ our bonds.”*<sup>275</sup> The government bond sector of the US capital market had begun to decline, and Black was concerned that going to the market in the US too frequently would result in the Bank paying higher rates. Accordingly, he sought to persuade other governments to hold IBRD bonds as part of their reserves. The Bank’s short-term issues were particularly important in developing the European market for its bonds and notes. Between 1956 and 1958 the Bank made seven issues, the first of which was a \$75m two-year bond offered for sale entirely outside the US. The Bundesbank snapped up \$17.5m, sixteen other central banks bought \$52m, with private purchasers taking the balance. From 1958, private purchasers were excluded from the market, as the Bank was confident of its ability to sell these short-term instruments to central banks – and could afford to pay a lower rate of interest. In 1966, these short term issues had become bi-annual and were worth more than \$200m per year, and were placed directly with central banks, governmental institutions and international organisations.<sup>276</sup>

Yet Black and Garner’s successes in the US and Europe had contributed to a problem for the Bank, which had been brewing amongst prospective borrowing members from the very outset when South American governors had expressed their concerns to Emilio Collado that lending to Europe would prevent developing economies from gaining access to the capital they needed.

### **Deflecting Critique from the South: the IFC & IDA**

In the 1950s a debate over development financing developed rapidly at the UN Economic and Social Council (ECOSOC). Hans Singer, of the UN’s Department of Economic Affairs, was receptive to the complaints of South American members who were concerned that as their economies grew, they would not be able to continue to benefit from concessionary financing.<sup>277</sup> Singer and V.K.R.V Rao argued for the development of a Special United Nations Fund for Economic Development (SUNFED) on the basis of the success of the large-scale transfers of Marshall Aid, and the observation that as the 1950s progressed, the terms of trade were tipping in favour of industrialised countries. In that year, further pressure was built up by

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<sup>274</sup> Ibid. Pg.859.

<sup>275</sup> Oliver, R., *Interview with Mr. Eugene R. Black, President*, August 6<sup>th</sup> 1961. Pg.16.

<sup>276</sup> Mason, E.S., and Asher, R.E., 1973. Pg.142.

<sup>277</sup> Ibid. Pg.349.

the adoption in the UN General Assembly of resolution 520A(IV) which required that ECOSOC submit a plan for the establishment of a grant-based or low-interest long-term financing body which could be tasked with financing non-self-liquidating projects by 1953.<sup>278</sup> This was supported by a report co-authored by eminent economists including W. Arthur Lewis and Theodore W. Schultz, who criticised the Bank heavily for its foreign exchange focus.<sup>279</sup>

The Bank was highly critical of the SUNFED proposal, and was joined in seeking to deflect serious discussion of the matter by US representatives who extolled the virtues of private enterprise – and the IBRD – as potential catalysts for growth. From 1953, the Eisenhower administration attempted to link the foundation of a grant-aid body to savings from multilateral disarmament.<sup>280</sup>

The pressure built on the Bank and the US from the South. Speeches at the Bank's 1954 annual meeting by Luis Machado of Cuba and other South American members drew upon an idea which had a long heritage in the Bank: a vehicle for investment in private enterprises.

This idea had been debated as far back as 1948, during the elaboration of the Truman Doctrine. It had been advanced in the NAC and the US Department of State, as well as among the McCloy-era Bank's top management, and in time, would come to unite the interests of financiers, US state bureaucrats, and the Bank itself.

McCloy, Demuth, Garner, and Black met frequently with US government officials to discuss a fund which could be offered to private enterprises in the form of equity as well as debt obligations – without government guarantees. This idea reflected a deeply-held conviction amongst the management to the effect that governments couldn't possibly run industrial enterprises effectively, and that a Bank affiliate could encourage members not to divert resources into the public management of industry. Bank management succeeded in convincing Truman's Advisory Board on International Development, chaired by Nelson Rockefeller, to adopt the idea of an 'International Finance Corporation' as a method by which the Point Four Program could be promoted.<sup>281</sup>

Popular as it was with borrowing members, the nascent IFC was initially considered by the US government and financiers as an essentially 'socialistic' undertaking: the provision of monies to a private enterprise in the form of equity investment by a public institution was equated to public ownership.<sup>282</sup> Financiers feared that the aspects of IBRD which they had

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<sup>278</sup> Shaw, D.J., 'Turning Point in the Evolution of Soft Financing: The United Nations and the World Bank' in *Canadian Review of Development Studies*, 26:1, 2005. Pg.47.

<sup>279</sup> Shaw, D.J., 2005. Pg.44-51

<sup>280</sup> Ibid. Pg.50

<sup>281</sup> Mason, E.S., and Asher, R.W., 1973. Pg.346.

<sup>282</sup> Oliver, R., *Interview with Richard Demuth*, August 10<sup>th</sup> 1961. Pg.44

lobbied against in the 1940s had returned under the Black presidency, and could potentially offer unwelcome competition for US investment banks.<sup>283</sup>

Financiers' criticisms gained important concessions from Black which would remove the major stumbling blocks – but ultimately stymie the IFC's operation. Firstly, its capitalisation would be reduced from \$450m to \$100m; and secondly, it would not offer finance on an equity basis. Thirty countries took up membership on July 20<sup>th</sup> 1956, contributing \$78,366,000 which rose to fifty-one member contributing \$92m by September the following year.

Therefore it was almost entirely hamstrung from the outset: its small capitalisation rendered it irrelevant to the large enterprises for which it was intended – those which needed the mobilisation of foreign capital. The terms it required were considered excessive<sup>284</sup> and a \$2m limit on individual investments rendered them marginal in terms of profitability and their contribution to the development of the industrial sector in question. Appeasing the Treasury and New York's financiers meant that the IFC endured a miserable start, and it invested only \$44m in its first decade. Most of its investments had gone to South American borrowers, but only 32 investments had become effective and only 13 of these turned a profit.<sup>285</sup>

However, the IFC would become the Bank's main instrument for dealing with private enterprise. Although the Kennedy administration oversaw the rationalisation of economic aid practices through the Foreign Assistance Act of 1961 – founding the Peace Corps, centralising programmes in USAID, formalising the Alliance for Progress – in 1961, appropriations for development assistance declined by more than \$300m. This meant that it was more important than ever to engage more closely with American financiers and bureaucrats who had perceived its equity investment as 'socialist'. Their reassurance took the form of an amendment to the IFC's Articles of Agreement to the effect that it would not exercise voting rights for managerial control.<sup>286</sup>

This was a significant success: in 1962 the IFC was able to hire George Woods, chairman of the IBRD's chief underwriters the First Boston Corporation and subsequent IBRD president, as an advisor. Alongside him were Dr. Hermann J. Abs, director of Deutsche Bank A.G (Frankfurt); Viscount Harcourt, MD of Morgan, Grenfell & Company (London); Mr. Andre Meyer, Senior Partner with Lazard Freres & Company (New York); and Baron Guy de Rothschild, partner of de Rothschild Freres (Paris).<sup>287</sup> As President of the World Bank Group

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<sup>283</sup> Kraske, J. et al, 1997. Pg.105.

<sup>284</sup> Oliver, R., *Interview with Richard Demuth*, August 10<sup>th</sup> 1961. Pg.46-7

<sup>285</sup> Haralz, J., 'The International Finance Corporation' in Kapur, D., Lewis, J.P, and Webb, R., 1997. Pg. 819.

<sup>286</sup> Haralz, J, in Kapur, D., Lewis, J.P., and Webb, R., 1997. Pg.822-3.

<sup>287</sup> IFC, *Sixth Annual Report 1961-1962*, Washington D.C., September 1962. Pg.5

from 1963, a central plank of George Woods program was to expand the scope of Bank lending to include more industrial projects. Overcoming the final obstacle to making the IFC a more attractive partner required giving the IFC access to greater leverage: Woods successfully amended the IBRD charter in 1964 to offer Bank lending to the IFC, giving it a leverage ratio of 4:1, with the first loan taking place in 1966.<sup>288</sup>

However, this was also the period – 1956-1961 – when the Euromarkets were taking off. US and European multinationals were able to find finance in the dollar markets of London without the complications of the IFC's awkward hybridity. Even though the IFC's annual commitments grew rapidly under Woods, the development finance corporations (DFCs) it aimed to fund were seen as competition to the IBRD so efforts were focused on investment in basic manufacturing industry: until 1971, DFCs received a total of \$53,174,705, compared to manufacturing industry's share of \$443,420,156.<sup>289</sup>

Deflecting borrowers' criticism and accommodating their demands for concessional financing therefore demanded an alternative solution, however popular the IFC may have eventually proven with financiers. The IFC had delivered only a trickle of capital in its first decade, and the agitation in the UN in the aftermath of the Singer group's proposal for a UN administered special concessionary development fund continued to threaten the Bank with marginalisation – and by extension, strengthen the hand of developing countries while decoupling them from anti-communist development strategies. From the mid-1950s, the debate turned to the foundation of another international body to finance projects which could not be undertaken on a loan basis. In doing so, yet again, the execution of the Bank's strategy would be mediated by the imperatives of finance.

The foundation of such a body had also been mooted in the 1951 US International Development Advisory Board report which had promoted the foundation of the IFC. It was viewed positively by the US as it would prevent the emergence of the SUNFED proposal's one-country-one-vote system in the UN and help to preserve US influence in development finance.<sup>290</sup> As far as the Bank was concerned, it could only meet the pressure to lend to developing members through the foundation of a new affiliate: the credit risk entailed by IBRD lending to less creditworthy members was too high. If the Bank, having obtained private capital at market rates, were subsequently to lend at lower rates, its own creditworthiness would suffer. Further, as the 1950s progressed it became that the developing countries carried

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<sup>288</sup> Haralz, J., in Kapur, D., Lewis, J.P, and Webb, R., 1997.

<sup>289</sup> Mason, E.S., and Asher, R.E., 1973. Pg.355, Table 11-3.

<sup>290</sup> Gwin, C. 'The International Development Association', in Kapur, D., Lewis, J.P, and Webb, R., 1997 (A). Pg.384.



an increasingly large debt-burden, while European members would shortly be able to turn away from the Bank to seek funding in private capital markets themselves.

For the Bank to be able to continue to tap private capital markets, any affiliate which would take on the task of lending to higher risk members for projects with lower returns would have to be entirely distinct. It was particularly important to clarify the different financial status of the IBRD and the proposed International Development Association (IDA) – the foundation of which was agreed at the Bank’s annual meeting of governors in 1959<sup>291</sup> – to assure investors in Bank bonds that their interest would not be diluted by diverting funds into soft lending channels.<sup>292</sup>

As a result, the IDA would have its own charter. This also meant that member parliaments would not have any opportunity to amend the charter of the IBRD itself in the course of processes of ratification. However, as Mason and Asher point out, the ‘affiliate’ status of the IDA was an “*elaborate fiction*”: in reality it was simply a fund administered by the IBRD but the illusion had to be maintained for the sake of the IBRD’s creditors, and to maintain its position of eminence as a development finance institution.<sup>293</sup>

With the advent of the IDA, the profile of the Bank Group’s lending was transformed: with significant contributions from the IDA, one third of total lending across the 1960s was undertaken in India and Pakistan. From 1961-69, IDA lent \$1,847m to low income members against the IBRD’s \$1,462m. Of the IDA low-income category \$1,044 was lent to India alone. While the IBRD committed no funds to program lending, the IDA lent \$555m of a total of \$2,218m for these more general purpose applications.<sup>294</sup> Mason and Asher note that across the 1966-1970 period, the IDA accounted for over 25% of combined Bank/IDA activity in new loans and credits. Of this share, Africa’s proportion increased to 25%, while the Western Hemisphere department disbursed 3% of the IDA total. 20-25% of IDA resources were spent in the agricultural sector, compared to only 10% of the IBRD, while the IDA also devoted a larger proportion to education.<sup>295</sup>

It is precisely this transition which leads the Brookings historians to depict the funnelling of non-project lending through the IDA as a transformation of the character of the Bank Group into that of a ‘development institution’. These struggles were taking place across the period which Chwioroth depicts as a ‘battle of ideas’ between internal constituencies

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<sup>291</sup> Resolution No.136: International Development Association, October 1, 1959, in IBRD, *Summary Proceedings 1959 Annual Meeting of the Board of Governors*, Sept.28-Oct. 2. 1959, Washington D.C.

<sup>292</sup> Oliver, R., *Interview with Burke Knapp*, The World Bank/IFC Archives, Oral History Program, Columbia University, July 1961. Pg. 34-5.

<sup>293</sup> Mason, E.S. and Asher, R.E., 1973. Pg.380.

<sup>294</sup> Kapur, D., Lewis, J.P, and Webb, R., 1997. Pg. 140-1, Tables 4-1 & 4-2.

<sup>295</sup> Mason, E.S., and Asher, R.E., 1973. Pg. 401-2.

advocating 'project' or 'programme' approaches to lending, from which the Wall Street-oriented project constituency emerged the victor.

However, I argue that this should be seen as a strategic move to stabilise the Bretton Woods order: management was able to sustain the orientation of the IBRD towards its private investors by incorporating IDA as a distinct entity, and secure the support of both the US and private finance through its efforts to foster private international investment through the IFC. Simultaneously the clamour from borrowing members for higher capital transfers for less directly productive purposes was successfully absorbed, and the Bank was able to retain its position at the heart of the Bretton Woods regime. It was the necessary social instrumentality through which these various political interests could be translated into a more-or-less coherent politics of governance.

The stabilisation of the interests of the US, private finance, Bank management, and vocal middle-income borrowers which Black and his cohort appeared to have achieved in the early 1960s was short-lived. In the course of the Woods presidency, contradictions would emerge from this settlement which, in conjunction with wider developments in the international financial system would undermine the Bank's centrality to the Bretton Woods regime.

### Pathologies of Success

The diversification of the Bank's borrowing had increased its working capital, and the foundation of the affiliates appeared to have secured its position as the foremost source of development finance. However the processes which it had supported and encouraged in order to achieve these aims created new contradictions which caused an institutional crisis.

Firstly, the basis of the IDA's capitalisation in public finance re-asserted the leverage which donors' legislatures had given up in the course of the struggle over the presidency of the institution and the negotiations on the Chilean loan of 1947. This would come to jeopardise the centrality of the Bank to the Bretton Woods regime in conjunction with a second factor – the development of the Euromarkets on the basis of the rising volume of dollars held in British and European banks. As the Kennedy and Johnson administrations battled to contain international movements of dollar-denominated capital, the Bank sought to facilitate it. I will discuss the impact of the explosion of Eurodollar lending in greater depth in Chapter 5, but I will close this section with an illustration of the way in which the Bank began to find itself supplanted as a lender towards the close of the Woods presidency.

An unintended, although perhaps not unforeseeable outcome of the attempt to defend the creditworthiness of the IBRD by founding the IDA, was that the legislatures of large donors had greater leverage over the institution than ever before.

The affiliate was to be capitalised with public monies. The Articles were brought into force on September 24<sup>th</sup> 1960, and by December 31<sup>st</sup> the following year, 56 members had subscribed, bringing its total capitalisation in convertible form to \$757m of a total \$912m.<sup>296</sup> Subscriptions were based upon 5% of IBRD subscriptions at the close of 1959, and members were to be categorised as Part 1 or Part 2 – contributors and borrowers respectively, based on per-capita income figures. The charter allowed the IDA to lend to public international or regional organisations, governments, and public or private entities in the territories of members. This wider mandate was nonetheless modified by a specific project provision – which was itself qualified in a similar way to the project clause in the Bank's AAs: paragraph 14 of Article V Section 1(B) permits financing for other purposes than specific projects under special circumstances.<sup>297</sup>

President Woods had noted in his inaugural speech in 1963 that the loan 'pipeline' was full: although undisbursed, project preparation was proceeding at full bore. This followed an enormous drop-off in loan disbursement in the year from June 1962, to a dispiriting \$442m.<sup>298</sup> Lending was slowing down to an unacceptable rate in relation to repayments. The Bank's reserves were building rapidly: almost \$1bn had accumulated through repayment. Attempting to cut these reserves by slashing interest charges or paying a dividend was potentially risky in respect of the on-going necessity of financiers' support – they were to be justified by riskier lending.

The liquidity sluicing into the IBRD's reserve funds was not paralleled in the IDA: when Woods joined in 1963, it had almost run out of funds – two years before the end of the anticipated five-year cycle. Irving Friedman's Economic Department had completed a study for Woods which suggested that the developing countries could make productive use of up to \$3bn more per year than was currently being supplied in all forms of ODA. The net flow of long-term capital from the industrialised countries was not reflecting the significant growth in their incomes at this point: it was stagnating at around \$6bn.<sup>299</sup>

By the mid-1960s, these problems would lead Woods to become entirely preoccupied by the IDA.<sup>300</sup> During the first replenishment, Black had been able to gain the Kennedy

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<sup>296</sup> IBRD, IFC, IDA, *The World Bank, IFC, and IDA: Policies and Operations*, Washington D.C., 1962. Pg.104.

<sup>297</sup> Mason, E.S. and Asher, R.E., 1973. Pg. 390-5.

<sup>298</sup> IBRD Washington D.C, September 30 – October 4, 1963. Pg. 9.

<sup>299</sup> Kraske, et al, 1996. Pg.140.

<sup>300</sup> Kapur, D., Lewis, J.P, and Webb, R., 1997. Pg 183.

administration's support by settling for \$750m over three years (rather than the \$1.5bn he had initially sought), in exchange for a token reduction in the US share of this deposit – from 42.34% to 41.89%.<sup>301</sup> However, in view of the decline in levels of ODA, Woods set as a target an increase in the amount of long-term financing available at concessional rates to \$1bn per year for the second round of replenishment of the IDA's capitalisation.

Such an increase combined with the expansion in the lending program and ambitions to increase un-tied transfers set Woods at loggerheads with Congress in 1964, as net lending to the developed industrial countries became negative for the first time. With the US mired in conflict in Vietnam, and struggling to develop effective policy in relation to the balance of payments deficit, the second replenishment could 'only' achieve \$400m per year. Worse, this would only come into effect in 1969 due to protracted negotiations which ensued as Congress demanded balance of payments safeguards and a further reduction in its share of the contribution, to be agreed at the 'end of the queue' after other Part 1 members had agreed their contribution.<sup>302</sup> Accordingly, Woods elected to transfer approximately \$200m to IDA across 1964-66.<sup>303</sup> However, the delay meant that IDA commitments would drop to \$107m in fiscal 1968, Woods' last year as President.<sup>304</sup>

His preoccupation with expanding IDA activities was motivated by a second, more structural problem which had been thrown up in the wake of the achievement of multilateral convertibility. With the growth of the Eurocurrency markets, middle income developing countries who were historically some of the Bank's biggest borrowers had been able to avoid Bank conditionality and obtain finance directly from private banks.

As Woods had noted in his inaugural speech to the governors, the level of debt which they were contracting was not problematic in itself. The potential problem lay in the structure of the debts: much of the borrowing had been undertaken through short-term instruments which concentrated repayment obligations to a troubling degree. During the later years of the Black presidency and the first year of Woods' term a further seventeen countries joined the Bank, sixteen of which were African countries – an entirely new class of debtors.

Rising levels of debt service payments among membership became a concern related to the ease and type of financing available in the booming Euromarket: the 1963-64 Annual Report notes that *"...some countries have assumed obligations which, although not necessarily excessive in total amount, are concentrated too heavily in the short term."*<sup>305</sup> A study authored

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<sup>301</sup> Gwin, C., in Kapur, D., Lewis, J.P., and Webb, R., 1997. Pg. 208.

<sup>302</sup> Ibid. 1997. Pg. 209-11

<sup>303</sup> Mason, E.S., and Asher, R.E., 1973. Pg. 128-9.

<sup>304</sup> Kraske, et al, 1996. Pg.141-2

<sup>305</sup> IBRD, IDA, *Annual Report 1963-1964*, Washington D.C. 1964. Pg. 8.

by the Bank's Economic Department for the United Nations Conference on Trade and Development (UNCTAD) in 1964 noted that from 1955 to 1962 the level of public and publically-guaranteed debt across a sample of 37 'developing' countries had increased from \$7 billion to \$18.2 billion. The level of amortization and interest payments incurred by this group of countries had increased by a far greater factor – from \$0.7 billion in 1946 to \$2.4 billion annually.<sup>306</sup> Of this group, seven African countries were among the most highly indebted, where the growth of service payments on their external public debt was also among the fastest, although the region with the highest proportion of debt to be paid within five years was Latin America, where it ran at 55%.<sup>307</sup>

The Bank/UNCTAD report observes that the debt service payments were constituted in large part by amortization payments – and that this was due to the fact that the majority of debt consisted of medium and particularly short-term privately-held maturities in contrast to the 'traditional' public international debt structure<sup>308</sup>.

The expansion of this borrowing was fuelled by the expansion of the Eurodollar markets in response to the US' attempts to control its balance of payments deficit. Both the Kennedy and Johnson administrations struggled to develop a coherent and effective strategy, applying a combination of restrictive monetary policy in support of the dollar, and loose fiscal policy in an attempt to overcome the effects of the 1950s recessions. The outflow of dollars was beckoned by the lower interest rates available in the Euromarkets – US MNCs and commercial banks would borrow cheaply in London and spend in the US, contributing to inflation.<sup>309</sup>

As this trend gathered pace the Bank became a victim of the disintermediation tendencies unleashed by the monetary practices of the US under Kennedy and Johnson in support of the dollar's role as a reserve. Efforts to make depositing funds in US Treasury bills more attractive than commercial bank deposits by lowering the maximum rate of interest paid by US banks under the New Deal's Regulation Q, and increasing the cost of investing in foreign stock and bonds through the imposition of a 1% Interest Equalisation Tax - thereby contracting credit<sup>310</sup> - simply drove still greater volumes of deposits into the Eurodollar market where the IET did not apply.

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<sup>306</sup> Avramovic, D., et al, *Economic Growth and External Debt*, Baltimore, Johns Hopkins Press, 1964. Pg.4

<sup>307</sup> Ibid. Pg. 100 Chart I; pg. 108 Chart 2; pg.114 Table 10.

<sup>308</sup> Ibid. Pg. 109.

<sup>309</sup> Seabrooke., L., *US Power in International Finance: The Victory of Dividends*, Palgrave, Basingstoke, 2001. Pg.59

<sup>310</sup> Alton Gilbert, R., 'Requiem for Regulation Q: What it Did and Why it Passed Away' *Federal Reserve Bank of St. Louis Review*, February 1986.Pg.25-6

These practices, as Seabrooke has it, meant that US policy in relation to the Bretton Woods order constituted an effort to “*not to internalize monetary or financial ‘negative externalities’ in order to provide a stable international monetary system, but to create dollar-denominated assets to achieve positive externalities for US interests.*”<sup>311</sup> The lack of external restraint on the US enabled the price of adjustment to be exported to minor deficit countries, as huge volumes of Treasury IOUs were created in Seabrooke’s terms ‘under the guise of convertibility’<sup>312</sup>, and private intermediaries borrowed short to lend long, without any particular concern about the value of the dollar or the creditworthiness of debtors. A boom in lending to developing countries took place which was cause and consequence of the enormous expansion of US banks beyond Europe and the Caribbean – from 143 branches to 399 across the 1965 - 1975 period<sup>313</sup> – bypassing the Bank.

Attempts to maintain the US’ policy autonomy by enabling it to sustained its payments deficit and an overvalued dollar, expressed an incipient monetary crisis. The efforts of the US to discourage foreign investment through measures such as the Johnson administration’s voluntary Foreign Credit Restraint Programme could not offset the pressure on the link between the dollar and gold created by the rapid expansion of foreign dollar holdings. Dollar holdings outside the US had increased by almost \$10bn from 1949-1958, from a shortage to a glut in the space of a single decade.<sup>314</sup> In 1968, Johnson was forced to enact a raft of measures in the face of huge gold outflows, which effectively closed US capital markets to foreign borrowers, including the Bank, which suffered enduring scepticism in relation to the quality of its paper.

A direct contradiction had emerged between the imperatives of the US and the imperatives of the Bank. US contributions to the Bank, and particularly to the IDA, were seen as factors in the deteriorating US balance of payments. During the Eurodollar boom, president Woods was forced to advise the governors of the Bank and IDA that finding the requisite monies to fund the continued operation of the Bank was a ‘dominant continuing problem’.<sup>315</sup> Having begun with a significant surplus, the Woods era came to a close in such straits that the president was, according to Richard Demuth “...*afraid the Bank wouldn’t get repaid and that it*

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<sup>311</sup> Seabrooke, L., 2001. Pg.59.

<sup>312</sup> Seabrooke, L., 2001. Pg.66

<sup>313</sup> Christophers, B., 2013. Pg.164.

<sup>314</sup> Battilossi, S., ‘International Banking and the American Challenge in Historical Perspective’ in Battilossi, S., and Cassis, Y., *European Banks and the American Challenge: Competition and Cooperation in International Banking under Bretton Woods*, Oxford University Press, Oxford, 2002. Pg.10

<sup>315</sup> George D. Woods, address to the Board of Governors and concluding remarks, annual meeting, Rio de Janeiro September 25<sup>th</sup> and 29<sup>th</sup>, 1967, Series 4530 (Information and Public Affairs – President George D. Woods speeches), World Bank Group Archives, pg.2 cited in Kraske, J. et al, 1996. Pg. 143.

would go bankrupt.”<sup>316</sup> Aaron Broches similarly noted that although the US was ‘happily’ voting in the Bank in favour of a greater loan programme, at the end of his tenure Woods “...became concerned that the Bank might not be able to borrow the funds it needed to meet its obligations to its borrowers.”<sup>317</sup>

In sum, sovereign creditworthiness at existing terms of lending was becoming problematic by the mid-1960s, and across the following three years Bank annual commitments declined from over \$1 billion to approximately \$850 million. Bank terms of lending were forced to reflect the rising costs of its own borrowing: during the later 1940s, the Bank lent at 4.5%, in the later 1950s at 5.5%, climbing in the later 1960s to 7% interest.<sup>318</sup> Net transfers declined from \$242.64 million in 1961 to \$41.63 million in 1962, peaking in 1967 at \$171 million before declining to \$23.14 million in 1969 and dropping to a negative net transfer of -58.85million in 1970.<sup>319</sup>

Realising the objectives of its stakeholders in the early years had required the Bank to facilitate the creation of a multilateral trading order centred on the dollar, and a profitable international capital market. Ultimately, successfully translating the interests of members and financiers into a more-or-less coherent strategy of governance had created a new contradiction rooted in a dollar glut, which inverted the post-war liquidity crisis to which Bretton Woods was a solution. Making the world safe for the dollar had set processes in train which would bring the Bank to a profound crisis of relevance.

## Conclusion

In this chapter I have sought to demonstrate the interweaving of state and financial interests with the Bank’s strategic objectives, and the impact the achievement of these goals had on the Bank’s role in the governance of the Bretton Woods order following the achievement of multilateral convertibility.

The Bank had actively sought to create the conditions for the re-emergence of international financial mobility, while the American state battled to contain it. Therefore, the diversification of the Bank’s borrowing increased its working capital, but the processes which it had encouraged in order to achieve this aim had outcomes which caused an institutional crisis.

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<sup>316</sup> Asher, R., *Interview with Richard H. Demuth*, World Bank/IFC Archives Oral History Program, March 19<sup>th</sup> 1984. Pg.3

<sup>317</sup> Oliver, R.W., *A Conversation with Aron Broches*, Washington D.C., November 7<sup>th</sup> 1985. Pg.24

<sup>318</sup> Mason, E.S., and Asher, R.E., 1973. Pg.228.

<sup>319</sup> *Ibid.* Pg.219 table 7-8.

This allows us to re-conceptualise the period in a way which captures the agency of the Bank in mediating the relationship between private finance and members – particularly the US – with the aim of consolidating its position in a framework of international financial and aid governance.

The ‘turn to development’ should be seen not as a moral imperative, but as a contingent aspect of the Bank’s strategy. The focus on European reconstruction and financial discipline with a view to facilitating processes supporting the attainment of multilateral convertibility was intended to resolve the twin issues of capitalisation with which the Bank continued to struggle.

Firstly, it needed to obtain the funds pledged to it by members. These were useless if they could not be lent, so management exercised the inducements afforded by lucrative procurement agreements among members of the European Payments Union, and the leverage offered by in strategic cases where Bank interests coincided with those of the US such as Yugoslavia, to gain ‘special releases’ and access to national capital markets.

This was the key to the second capitalisation problem: diversifying the Bank’s borrowings. Building up dollar balances in Europe and members of the Sterling bloc supported the US aim to centre the new multilateral order on the dollar, and helped to lay the foundations for the development of the Eurodollar markets. These had two benefits: the ability to draw on large institutional investors handling the financial products of the US working and middle classes, and secondly, it afforded some security from US efforts to control their balance of payments deficit by excluding the Bank from the capital markets of New York.

These successes entailed the transformation of the Bank’s institutional structure through the foundation of the affiliates – the IFC and IDA. Declining ODA flows and the early focus on European reconstruction had driven non-European borrowers to seek to supplant the Bank through the UN, to which the affiliates were a defensive reaction. By founding separate institutions as part of a ‘World Bank Group’, the Bank could retain its new-found ability to tap global capital markets while retaining its ability to play a leading role in ‘development’ financing.

Ultimately, these transformations – to the international financial system, and the structure of the Bank – would pose two problems which constituted an existential threat to the Bank. Firstly, the IDA required budgetary appropriations from the legislatures of donor members – restoring the state power which McCloy had sought to evade. Secondly, the Euromarkets began to supplant the Bank among middle income members – which began to develop a debt profile which threatened to undermine the private international banking system.



These problems constituted nothing short of a crisis of relevance. The Bank was no longer the most important of the Bretton Woods institutions in terms of international liquidity provision, and it was rapidly losing out to private capital markets while growing scepticism towards foreign aid among major donors had brought the concessional lending its members had demanded to a halt.

Overcoming the pathologies of the Bank's success in making the world safe for the dollar and adapting its structure and procedures to suit the changing demands of governance in the maturing Bretton Woods order would require renewed engagement with financiers and the development of new techniques of management. Under Robert McNamara's presidency, these processes and tools would form the roots of neoliberal governance which, from their origins in the 'basic needs' agenda, would outlast the Bretton Woods system itself.

## Chapter 5: Carabosse's Curse: Basic Needs and The Origins of Structural Adjustment.

*"You two brats shall grow up politicians; your every thought and act shall have an arrière pensée; everything you determine shall not be for its own sake or its own merits but because of something else."*

J.M. Keynes; speech at closing session of Savannah conference.

In Chapter 4 we have seen that the Bank's 'turn to development' was a contingent feature of management's pragmatic negotiation of the imperative of capitalisation. As the Bank sought to secure its access to private American capital, its strategy became more closely intertwined with the US hegemonic agenda. The re-emergence of international financial mobility was at first a blessing. Yet it became clear in the course of the 1960s that it had opened a contradiction between the Bank and the US. Outflows of dollars into the Eurodollar market through banks and MNCs exacerbated the US balance of payments deficit, and their recycling exacerbated inflation. In turn, this led to pressure to decrease aid spending as the Johnson administration battled to reduce the deficit and contain newly-mobile American capital. This all but choked the IDA during its replenishment negotiations. Worse, the easy availability of liquidity in the Eurodollar market meant that middle income borrowers could obtain finance directly and bypass the conditions placed on the Bank's loans. At the close of Woods' presidency in 1968, these dynamics had a simple significance for the Bank: it was highly liquid, but the imperative of remaining creditworthy meant that it was struggling to lend.

In this chapter we explore how the Bank met this crisis of relevance to its borrowers. Increasing the Bank's lending programme required management to develop new capacities of governance through which it could enforce financial discipline. By 1968, it was becoming clear that management could no longer rely upon the project approach as a tool of governance through which to meet this institutional imperative. To this end, McNamara deployed a specifically American technology of management in order to make the renovation of the Bank's concept of development legible to American financiers. As I will show, this entailed the wholesale transformation of the Bank's structure and lending practices. The structural adjustment loan was the consequence of the necessity of making McNamara's 'basic needs' lending programme acceptable to the American financial community in which the Bank is socially anchored. The threat posed to the American financial system by the debt crisis of 1982 saw the agendas of the Bank and the US once again become closely intertwined. The practices

of neoliberal governance which were deployed in this context were built upon the foundation of the new capacities developed by Bank management in the course of the 1970s – not on the basis of US power.

Conventionally, the transformations to the Bank's managerial and lending practices, structure, and concept of development in the period 1968 – 1981 are attributed to the force of McNamara's personality. In the account offered by Kapur, Lewis, and Webb, the development of neoliberal practices and concepts is a case of a powerful individual eventually being forced to yield to external pressures caused by a 'swing in global fashions' and losing the capacity to direct change within the institution '*sui generis*'.<sup>320</sup> This focus on the undoubted personal dynamism of the president obscures several crucial aspects of the enormous and significant transformations wrought to the Bank Group during his tenure. Most importantly, it is exemplary of a presentation of the Bank as a passive object of US state strategy, made familiar through widespread deployment of the 'embedded liberalism' thesis as a cipher for the governance of the Bretton Woods era; or as the victim of institutional capture by neoliberal intellectuals which constructed the institution as an adjunct to the US Treasury and Wall Street.

By contrast, Patrick Sharma's account of the development of structural adjustment focuses on the importance of endogenous bureaucratic imperatives in driving this change. The impact of the vast international expansion of liquidity through the Euromarkets on the Bank was to enhance the autonomy of its managers.<sup>321</sup> As he points out, during the later 1970s McNamara's team observed that the lack of good investment opportunities and the necessity of oversight of individual projects combined to reduce rates of disbursement dramatically.<sup>322</sup> As the project approach had reached its limits, in order to retain its authority as an international financial institution the Bank had to find a way in which to speed up its lending. By returning to the programme lending model and increasing the scope of conditionalities, the Bank was able to streamline the disbursement process. This absolved it of the responsibility of micro-management of individual projects and allowed the promotion of an export-oriented liberalisation package for which management expressed a preference. Although this overlapped with the preferences of the US, the structural adjustment loan was an innovation in managerial technology devised by McNamara and his team, in response to the limits of project lending – not as a response to the US agenda of liberalising trade and investment in the developing world.

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<sup>320</sup> Kapur, D., Lewis, J.P., & Webb, R., 1997 Pg.21

<sup>321</sup> Sharma, P., 2013. Pg.671

<sup>322</sup> Ibid. Pg.677

Sharma offers an acute observation of the limits of the project approach and the crucial agency of management as norm entrepreneurs. By emphasising the imperatives of the Bank as a bureaucracy, Sharma is able to illustrate the importance of managerial agency in negotiating the limits on the Bank's capacity to act, and designing new technologies of governance within this framework. Yet, by emphasising the autonomy afforded by the Bank's basis in financial relations, Sharma neglects the way in which this social grounding also functioned to limit the Bank's capacity to act. However, I will show that the development of structural adjustment lending did not only follow from bureaucratic imperatives. It was developed as management negotiated the limits to the Bank's capacity set by the Bank's social anchoring in American financial capital. In order to re-engage its clients, the renovation of the Bank's concept of development had to be translated into action via a specifically American technology of management which would render it legible to American financiers. Only by achieving this, could management successfully draw upon the liquidity of American financiers, and return the Bank to its central position in the governance apparatus of the international economy.

To this end, the strategy which management worked out pragmatically across the period 1968-1980 had three components. Firstly, in order to address the crisis of relevance to borrowers, the Bank would undertake massive expansion of its operations in the areas which it had entered under Woods in order to stave off displacement by a low-conditionality UN competitor. Conceptualised from 1973 as the 'basic needs' agenda, the Bank would aim to target its lending towards small farmers and promote redistributive policies alongside the more traditional focus on productive investment aimed at promoting growth. The hobbling of the IDA by Congress indicated that if such a programme were to be undertaken, it would have to be led by the IBRD. Borrowing operations would have to be expanded yet further. Therefore, as I will show, the form in which the 'basic needs' agenda was operationalised was mediated by the same financial imperatives which shaped the adoption of the project approach in the 1940s.

For this reason, the second aspect of the Bank's transformation would relate to its institutional structure and its lending processes. In order to render its objectives legible to the private investors upon whose capital it relied, McNamara's team would have to demonstrate that the Bank's commitment to financial discipline would not be eroded. A new set of practices was required in order to ensure that the Bank's investments – and thereby investment in the Bank – remained sound. The most important aspect of McNamara's presidency was therefore the 1972 reorganisation of the Bank on the basis of techniques of scientific management gleaned from his experience at the Ford Automobile Corporation and with the RAND

Corporation during his stint at the Pentagon. The new corporate structure and the use of quantitative performance measurement tools gave management the ability to exert greater functional control over Bank operations, assuaging financiers' concerns about the 'basic needs' agenda and enabling the Bank to expand its financial operations to meet McNamara's ambitious targets.

Thirdly, in the context of the rising debt-to GDP ratios of its middle and low-income borrowers, conditional project lending no longer functioned as a disciplinary tool. Conditionality which related to an individual project was meaningless if the borrower's wider policy package appeared to risk default. The close linkage between the creditworthiness of the borrower and the creditworthiness of the Bank compelled the rehabilitation of programme lending. As a consequence, the effort to directly target 'absolute' poverty in the developing world was the origin of the highly controversial practice of 'structural adjustment'. The attainment of either aspect of the response to the impasse of the late 1960s required a level of discipline and political intervention which could not be attained through the project approach.

It follows from this that the development of the technologies of governance most commonly associated with neoliberalism and the management of the 1982 debt crisis had a much longer history in the Bank as an institution than is commonly assumed. Structural adjustment was not a simple 'off-the-peg' solution to the debt crisis deployed by hard-line neoliberals on the basis of doctrinaire assumptions concerning the primacy of markets in development. The institutional forms and disciplinary tools which made neoliberal governance possible - and effective - not only pre-dated the proximate causes of the crisis and the ostensibly anti-state pro-market response to it. While they were re-articulated to different ends, they were rooted in McNamara's 'basic needs' agenda - commonly conceptualised as the most progressive moment in the Bank's history.

Firstly, I will briefly explore the outline of the Bank's new problematique: the impact of the expansion of the Euromarkets on the Bank, ideas about development, and Bank clients in the 1970s. The self-sustaining expansion of these markets posed a problem for the Bank, marginalising it as a lender. By borrowing directly, its clients were able to avoid the Bank's conditionalities and obtain funding for balance of payments support rather than specific projects. Simultaneously, the inflation which bedevilled the US economy in this period was a significant driver of the decline in the fortunes of the IDA: Congress became markedly reluctant to appropriate funds for its replenishment. The outcome of these dynamics was the creation of an incipient debt crisis in these countries, and significant decline in their creditworthiness. This was a major problem for the Bank, as Sharma has noted, slowing the disbursement of funds to a trickle. In an effort to renovate the Bank's concept of development

and re-engage its clients, McNamara undertook an extensive engagement with the academic community. The Bank would meet this challenge by turning itself into a 'Development Agency'. Befitting its new status, the Bank would develop a new lending programme aimed at ameliorating the negative outcomes of the industrial modernisation projects which had previously dominated development finance. Most importantly, many of these loans would not be directly productive. This last feature posed the greatest challenge to the Bank.

In the second section I will discuss how McNamara addressed this challenge and overcame the scepticism of finance, in order to obtain the vast increase in funding required to return the Bank to its central role in the international order. To make the 'basic needs' agenda legible to financiers, McNamara deployed the cutting edge technology of management which he had encountered at the Pentagon in his work with the RAND corporation. The Bank itself would be restructured on the advice of elite management consultants McKinsey, and run on the basis of a highly centralised hierarchical system of control predicated upon the quantitative analysis of budgets and the productivity of staff as well as the loans they made.

In the third section I will discuss the gradual moves toward the rehabilitation of programme lending - as the most important step in the development of the structural adjustment loan. The project loan could not deliver the massive increase in disbursement envisaged by the 'basic needs' concept. Development was conceptualised as an employment issue, and lending was to target the rural poor to offset migration to urban areas and stimulate agricultural production for export. Making loans of this type work as projects was highly problematic from a practical perspective, and under the rubric of 'basic needs' the Bank began to embrace the fungibility of development lending. Worse, the ease with which the conditions on project loans could be avoided threatened the creditworthiness of the Bank itself. Only the programme loan could achieve the policy leverage the Bank needed to satisfy its own creditors of the soundness of their investments. Basic needs and the employment-oriented development concept demanded macro-economic programming; and broad based macroeconomic conditionality in order to satisfy the Bank's financial imperatives. The security demanded by investors bound the performance of the Bank to the performance of its borrowers.

As I will show the roots of structural adjustment loans lie in the 'basic needs' agenda itself. This was not a radical break, a transformation following from US power. Rather, it stemmed from management agency in attempting to overcome the limits to the Bank's capacity to act posed by its social anchoring in American finance. The shift to neoliberal governance was not a direct offshoot of the requirements of the market; it was an institutional development which reflected the imperatives of the Bank. Ultimately, through the Baker Plan

the shift to structural adjustment would see the Bank Group of the 1980s step back into the role of the IBRD of the 1940s. This appropriation would thereby complete the institutionalisation of the infrastructural power of American finance, and the transformation of the Bank into the politician Keynes had warned against at Savannah.

## **1: The Bank, Development Theory, & Private Finance after the 'Decade of Development'**

The problematique of the 1970s was defined by the new contradictions arising from the achievement of the multilateral trading order centred on the dollar towards which the Bank had striven throughout the 1950s. For the Bank Group, the impact of these contradictions was most obviously manifest in the fact that in spite of Woods' efforts to counter the declining rate of disbursement by expanding the breadth of Bank lending to include sectors such as education and agriculture, the institution as a whole was more liquid in 1968 than ever before: repayments in respect of disbursed funds were running at a significant surplus.

The Bank was becoming marginalised as a lender. This was due to the impact of the Euromarkets on the American economy, the entry of the Bank's largest borrowers into the Euromarkets, and innovation in the lending practices of private banks. As a result of these dynamics, ODA flows declined while debt service payments and ratios of debt to GDP in developing countries increased rapidly.

In this section I will briefly sketch the factors and impact of the Bank's marginalisation, and the proposals from development practitioners, academics, and the Bank itself which aimed to counter it through a massive increase in lending. For the Bank, the most important factors motivating an increase in lending were precisely those which had caused it to slow down in the first place.

### **The Bank and the Eurodollar**

The rapid growth of the Euromarkets and the release of the dollar from its gold standard constraints had enormous implications for individuals, firms, and sovereign borrowers: through their pension funds and bank deposits as well as the bond issues of national states and the World Bank, the financial affairs of ordinary savers and pensioners were linked to the globalising network of commercial and investment banks, and multinational corporations. One of the most important sources of the influx of funds to the Eurodollar markets came from the OPEC countries in the course of the five-fold increase in oil price across

1970-1973. This offered a huge windfall for banks, while boosting to the US balance of payments through the increased receipts of the overseas oil operations and the relative affordability of the product of American oil majors. With the expansion of the Euro-dollar and Euro-bond markets during the 1960s, banking had been re-internationalised and privatised in advance of the wholesale liberalisation of financial transactions in the later 1970s and early 1980s. What did this vast expansion of credit mean for the Bank?

Under Robert McNamara, the World Bank sought to overcome the crisis into which it had descended in the last months of the Woods presidency by capitalising on the explosion of Eurodollar credit and funnelling it to its developing members. However, the figures involved show that at this point, it was virtually marginalised as a creditor – particularly with reference to its middle income group, who were the primary IBRD borrowers. Three factors drove the Bank's marginalisation.

Firstly, the entry of the Bank's borrowers into the Euromarkets. By seeking investment in private capital markets, borrowers were able to avoid the conditions which were attached to Bank loans, and obtain funding for more general purposes. The less the Bank was able to lend, the less leverage it had over its borrowers, and the less significant its role in the governance of the international order. More damaging still, the more exposed its members became to the risks of high cost short-term borrowing predicated on future returns from price-sensitive export industries – the more the Bank became exposed to the risk of a default. The creditworthiness of the Bank's borrowers was directly linked to the creditworthiness of the Bank itself.

A second driver of the marginalisation of the Bank was the impact of the expansion of the Eurodollar market on the American economy. Europe's dollar liquidity, bolstered by enormous sums from the OPEC countries in the early 1970s, was channelled through European branches of American banks back towards the US and onwards into the coffers of American multinationals. As expectations of future productivity growth were moderated, corporate cash holdings increased – and rising money market interest rates provided an opportunity to profit from the returns on financial instruments. US banks lobbied successfully for the deregulation of the New York Stock Exchange in order to allow them to compete with the market rates of interest paid on products offered by firms such as American Express and other unregulated securities companies which had begun to offer cash management accounts, competing directly with banks for deposits.<sup>323</sup> The profitability of financial assets drew funds not only from banks, but, in the context of the decline in industrial profitability which plagued Western economies

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<sup>323</sup> Helleiner, E., 1994. Pg.135



in the course of the later 1960s and 1970s (falling well below the 1975 level by 1981<sup>324</sup>), from corporations. Incentivised in their turn by the size of potential returns, small-scale financial institutions such as mutual funds contributed to the trend by pooling their savers' funds for investment in securities. The expansion of credit which banks' Eurodollar fundraising activities had allowed was a major driver of inflation in the US economy.

This had a direct effect on the fortunes of the IDA. As Michael Hudson has illustrated, the extent to which the inflation which the Fed and the Kennedy and Johnson administrations struggled with at home supported the power of the US state in the global political economy, as dollar-denominated credit expanded in the un-regulated Euromarkets, was not immediately understood until after the break between the dollar and gold.<sup>325</sup> This meant that the US sought to minimise the drain on the balance of payments attributable to their overseas development aid budgets: as far as US policymakers were concerned, developing countries that were creditworthy should apply to the World Bank or seek financing in the private credit markets.

The fact that the share of ODA in total financial flows to less developed countries fell from almost 40% to less than 30% between 1970 and 1981<sup>326</sup> indicates that as donors cut aid budgets, borrowers did turn to private markets. Foreign deposits from BIS-reporting banks rose from \$55bn in 1965 to \$650bn in 1975 and over \$2,100bn by the end of financial 1984. Excluding loans to other banks in this group, net international bank credit rose from \$260bn in 1975 to \$1265bn in 1984, considerably outstripping international inflation.<sup>327</sup>

A third factor was innovation in banks' lending practices, incentivised by high borrower demand and driven by the necessity to spread the risk of exposure to less creditworthy sovereign borrowers among private investors. This practice was the root of the self-sustaining dynamic of the inflation of the Eurodollar market, as it promoted a buoyant assessment of risk. The product which was developed to meet the demand – on the part of sovereign borrowers for larger loans, and on the part of the increasing number of internationally active banks for a piece of the profit – was the syndicated loan. This product enabled borrowers to contract bigger loans: 'jumbo loans' (over \$500m) and 'mammoth loans' (over \$1bn) entered the lexicon of international banking, and the average size of international bank loans increased

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<sup>324</sup> Armstrong, P., Glyn, A., and Harrison, J., *Capitalism since World War II: the Making and Breakup of the Great Boom*, Fontana, London, 1984. Pg.340-1

<sup>325</sup> Hudson, M., *Super-Imperialism: the Origin and Fundamentals of US World Dominance*, Pluto Press, London, 2002. Pg.14-21.

<sup>326</sup> Fryer, D.W., 'The Political Geography of International Lending by Private Banks', in Corbridge, S.E. (ed), Vol.1, 1999. Pg.108-9

<sup>327</sup> Lever, H., and Huhne, C., 'The Origins of the Crisis 2: the Supply of Credit' in Corbridge, S.E. (ed), *International Debt*, Vol.1, I.B. Tauris, London 1999. Pg.439

across the period.<sup>328</sup> Theoretically, syndication meant that banks were able to purchase pieces of a large number of different loans to different countries, which meant that they were not overly exposed to the default of a single debtor. What this meant was that the risk posed by the rising short and medium-term debt-to-GDP ratios of less developed borrowers was systemic.

Precisely because of this, private investors' attitude towards this feature of the landscape of the international capital market was cavalier; reflecting the infamous 'sovereign risk hypothesis' posited by Citibank's Walter Wriston. According to Wriston, it was impossible that a country would go bankrupt, unlike an individual debtor. Debts did not get paid – they were rolled over. Problems of cash flow would be cured through sound policy, and in the meantime more debt would be required.<sup>329</sup>

The innovation and expansion of American, European, and Asian banks in an effort to capitalise on this was a self-sustaining dynamic of the Eurodollar markets, in the absence of state regulation. The so-called petro-dollar glut was, although an enormous multiplier, not the only source of liquidity in the international money markets. European and Japanese banks activities were bolstered by their balance of payments surpluses, reflected in their predominance in this market: of the 50 largest global banks in the 1970s, 21 were European, 16 were Japanese, and only 6 were American.<sup>330</sup> The only check on a bank's lending was its own capital adequacy, and this was dependent on the individual bank's own assessment of the risk posed by its assets. Among US banks, capital adequacy ratios dropped to only 3.5% of assets in 1979.<sup>331</sup>

Where did this liquidity go? Primarily to the middle-income countries – precisely the group which had previously been the Bank's biggest borrowers. \$348bn was owed by all developing countries in the BIS reporting area to foreign banks in 1982. 21 countries accounted for 84% of the total, of which the ten largest accounted for 70% – and the five largest for 55%. Amongst American banks, 70% of lending went to Latin American countries, with the remaining 30% to East and South Asia, and Israel. The total outstanding from developing countries to US banks was worth 36% of total obligations to private banks in 1982, 40% of which was owed by Latin American governments. Of this debt, 23% of it was owed to

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<sup>328</sup> Seabrooke, L., 2001. Pg.95.

<sup>329</sup> Lever, H., and Huhne, C., in Corbridge, S., 1999. Pg.440-5

<sup>330</sup> Konings, M., *Development of American Finance*, Cambridge University Press, Cambridge, 2011. Pg. 115.

<sup>331</sup> Seabrooke, 2001. Pg.95.

just nine of the largest US banks. Venezuela and Ecuador, for example, owed a total of \$13.5bn in 1982 – or 68% of outstanding loans to American bankers.<sup>332</sup>

By contrast, almost 90% of the total debt of low-income African countries was owed to official bilateral and multilateral agencies. 60% was bilateral, 52% of which was non-concessional. Here, increases in American prime interest rates were less of a factor than in middle-income countries, and crisis came earlier. The exposure of international private banks in low-income Africa was less than \$10bn – and the majority of this was owed to, or guaranteed by official external creditors. The largest borrowers in terms of face value were, as in South America, middle-income economies such as Nigeria and Cote d'Ivoire. As Fryer has pointed out, this directly contradicts the notion that the most important dynamic in the development of the debt balances of the developing world was simply the recycling of OPEC surplus to non-OPEC countries to support their deficits and oil imports.<sup>333</sup> The majority of private commercial lending to these countries was short-term debt, undertaken to finance interest arrears on longer-term borrowings.<sup>334</sup> Although African debts were smaller, borrowers' debt-GDP ratios were still high. This led to the rescheduling of official claims on ten low-income African countries on nineteen occasions, and private debts on five occasions before the famed Mexican default of 1982, beginning with Zaire in 1976.

Although ODA flows increased in 1967 due to previously committed disbursements, the level of new commitments stagnated. Developing countries were not only suffering due to their dependence on primary commodity exports in the context of global slowdown from 1967 onwards, but there was no prospect that aid from the developed countries could bridge the gap.

What was the impact of these dynamics? While aid flows declined, debt service payments of the surveyed group of 92 developing countries increased at an alarming rate – by approximately \$185m in 1967. Taken together with an increase of \$400m in 1966, this was a major addition to the burden of public and publicly guaranteed external debt. The greatest increases in 1966 and 1967 had occurred in Africa, and Southern and Eastern Asia – while Latin American and European countries had begun borrowing heavily earlier in the 1960s and large debtors such as Argentina, Brazil, Chile, and Turkey had already undertaken a round of rescheduling.

In 1968 it had already become an article of common sense that these dynamics posed a serious threat to the viability of the international financial system. An UNCTAD agreement

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<sup>332</sup> Fryer, D.W., in Corbridge, S.E. (ed), Vol.1, 1999. Pg.113

<sup>333</sup> Ibid.

<sup>334</sup> Humphries, C., and Underwood, J., 'The External Debt Difficulties of Low-Income Africa', in Corbridge, S.E., 1999. Pg.345-54.

was met that the economically developed countries should offer a minimum aid commitment equal to 1% of their GNP.<sup>335</sup> Yet data reported by the OECD's Development Action Committee (DAC) indicated a considerable hardening of average aid terms through 1967.<sup>336</sup> Credit lines in private financial markets had been obtained on onerous terms, and the unfavourable market conditions of the end of the 1960s had begun to see debt service ratios rise to levels that were considered by the Bank to be potentially highly problematic.<sup>337</sup>

The erosion of creditworthiness among eligible borrowers which remained engaged with the Bank was reflected in the decline in Bank Group lending. The Bank's lending rate had been raised from 6% to 6.5% in early August 1968 as the Bank had found it difficult and expensive to raise funds in global capital markets due to strong competition and high rates paid on other tradable securities.<sup>338</sup> The Bank and IDA had lent \$953.5m in 1968 – a decrease of \$176.8m from 1967 attributable to the exhaustion of IDA resources. The problem of creditworthiness among low-income and middle-income borrowers was a problem for the creditworthiness of the Bank.

Creditworthiness was the central issue of the era. The drivers of the Bank's marginalisation were simultaneously to be harnessed for its rejuvenation. Downward pressure on ODA flows caused by the inflation of the Euromarkets meant that any response from the Bank Group would have to be led by the IBRD. This entailed new borrowing. For this reason, financial imperatives were again a highly significant mediating factor in the Bank's response to the latent threat of debt defaults in the developing world.

All these factors added up to an imperative to lend more - to prop up members, to offset the decline in ODA flows. However, from the Bank's perspective the expansion of the lending programme which followed was the expression not of the moral imperative, but of the financial imperative to retain the capacity to exert financial discipline over borrowers.

### **The Bank and Development Theory – Round 1: the Pearson Report and the Columbia Declaration.**

Accordingly, debate centred not on whether the Bank should lend more, but how it should be done and for what purpose. As lending ground to a halt in 1967-8, McNamara's predecessor had called for a 'grand assize', a taking stock of the progress, character, and

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<sup>335</sup> IBRD, IFC, IDA, *1968 Annual Meetings of the Boards of Governors Summary Proceedings*, Washington D.C. 1968. Pg. 32.

<sup>336</sup> Ibid. Pg. 38

<sup>337</sup> Ibid. Pg. 35.

<sup>338</sup> World Bank, IDA, *Annual Report 1968*, Washington D.C., 1968. Pg. 5-8.

direction of 'development' as a practice and concept with a view to revitalising the constituency for foreign aid among donors.<sup>339</sup> The ultimate outcome of Woods' final speech as President was that McNamara's first act in the role in 1968 was the foundation of a blue-riband commission on the revitalisation of international development, chaired by ex-Prime Minister of Canada, Lester Pearson and funded by the Bank.

The Pearson Commission was comprised of leading US development practitioners – Harvard's Hollis Chenery had served in USAID, from which he recruited Ernest Stern to the commission; and leading economists including W. Arthur Lewis and Goran Ohlin.

The commission's report, entitled *Partners in Development*, was published in September 1969 to significant scholarly condemnation. It offered wearily familiar conclusions: a 6% rate of growth should be attained by the developing world in the 1970s,<sup>340</sup> while industrial protection should be reduced to enhance free trade and export orientation.<sup>341</sup> The free movement of private capital should be encouraged,<sup>342</sup> and the role of the Bank and IDA should be expanded.<sup>343</sup> One of the greatest impacts of the Pearson Commission itself, Stern later reflected, lay in its recommendation that program lending be increased to at least 10% of total lending.<sup>344</sup>

By contrast, McNamara was determined from the outset that the Bank was a 'Development Agency'. Its remit, he considered, was not simply to pursue growth, but should be concerned with the capacity to provide leadership in 'development assistance' to donors frustrated with the lack of progress and poor countries marginalised by the exuberant post-war growth of the rich. Alongside financial assistance, technical assistance would be expanded in order to overcome the dearth of viable projects lamented by Woods, and a worldwide recruitment drive would be launched. The great 'productive machine' of capitalism which the world had created in 'the past few generations' could be directed by the Bank in such a way as to 'abolish' poverty.<sup>345</sup>

McNamara and his advisors had already calculated that abolishing poverty would require that from 1968 to 1973 the Bank group should commit double the volume of funds loaned from 1963 to 1968.

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<sup>339</sup> Blair, P. *Interview with William Clark*, World Bank/IFC Archives, Oral History Program, Washington D.C. October 4<sup>th</sup> 1983. Pg.1-4

<sup>340</sup> Commission on International Development, *Partners in Development: Report of the Commission on International Development*, Pall Mall Press, London, 1969. Pg.125

<sup>341</sup> Ibid. Pg.14-5

<sup>342</sup> Ibid. Pg.123

<sup>343</sup> Ibid. Pg.230

<sup>344</sup> Blair, P. *Interview with Dr. Ernest Stern, Senior Vice President for Operations on the Pearson/Brand Commissions*, World Bank/IFC Archives, Oral History Program, Washington D.C. March 2, 1983. Pg.6

<sup>345</sup> IBRD, IFC, IDA, 1968. Pg.13

McNamara's early programme was based on the acknowledgement that although the headline goal of the 'Development Decade' – an increase in annual national incomes in poor countries of 5% by 1970 – was likely to be achieved, the statistics supporting this notion were, unless disaggregated, a 'cosmetic'. Populous non-oil exporting countries had not seen the same growth as their oil-exporting counterparts, and growth was anyway skewed to urban industrial areas. Beyond these zones *"...the peasant remains stuck in his immemorial poverty, living on the bare margin of subsistence."*

The five year plan formulated with this in mind foresaw the greatest expansion of lending in Latin America (double) and Africa (triple). The sectoral makeup of lending would be altered: education and agriculture were singled out as the most important areas of expansion. The former would triple because *"...it makes a more effective worker, a more creative manager, a better farmer, a more efficient administrator"* and lastly *"...a human being closer to self-fulfilment."* Agricultural lending would quadruple in volume because bad diet meant that many people in the developing world were dependent on food imports and due to shortages could not *"...do an effective day's work..."* The single greatest problem, exacerbating all others, was the expansion in global population. Contemporary population trends would run down the per capita growth rates which development policy took as its objective to raise; to the extent that the benefits of consistent year on year growth would be imperceptible. Family planning programmes would be backed by research into the most effective methods of control and national administration. Lowering the birth rate would raise the standard of living, and prevent the 'dangerous' gap between rich and poor in developing countries from widening further.<sup>346</sup>

McNamara's programme had been developed prior to the publication of the Pearson Commission's report, which, in view of its underwhelming conclusions was guaranteed a bruising encounter with academia. In response to the Pearson Report an academic conference was convened at two sites, Williamsburg, Virginia; and Columbia University in February 1970. The tenor of the report was considered by the Institute of Development Studies' Richard Jolly to have been too optimistic, offering projections about the likelihood of success in closing the gap in output between rich and poor countries which were unrealistic – indeed, the policies advocated by the report would, he considered, see it widen further. The effort to integrate concepts of self-sustaining growth with export-orientation and import substitution while simultaneously raising domestic savings rates was conflicted and contradictory, and suggested that the report was *"a soft-sell of aid to the enlightened interest of the developed countries."*

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<sup>346</sup> IBRD, IFC, IDA, 1968. Pg.9-13

Rapid self-sustaining growth, to a target of 6%, would not deliver the results required: large scale transfers of income and development assistance were required.<sup>347</sup> For Samir Amin, its recommendations were nothing more than hasty conclusions and self-serving and pious wishes expressing the “...solutions that have been applied over the last two decades, even though their failure is evident.”<sup>348</sup> Rather than representing a new start, the Pearson Commission’s report simply argued that the international organisations should be doing more of what they had been doing before: pursuing growth above all else.

The Columbia conference was McNamara’s first significant encounter with development economists from outside the modernisation theory mainstream. As a response to the Pearson Commission, the ‘Columbia Declaration’ made at the close of the conference was defining moment of the first McNamara presidency. McNamara was substantially impressed with the emphasis on targeting lending towards the poorest by academics such as IDS’ Dudley Seers, Hans Singer, and Richard Jolly.<sup>349</sup> The declaration was of significant impact on McNamara’s views on the orientation of the Bank.<sup>350</sup>

Influenced in particular by Jolly and Columbia’s Barbara Ward, it argued that the targets set by the Pearson Commission and the means by which they would be attained, were designed simply to render minor increases in aid budgets acceptable and reasonable to public opinion in the developed world on the basis of a specious and illusory notion of developed-developing world partnership. Ultimately, it argued, “*Dependence in the modern world must be ended and give way to a framework which will allow genuine interdependence and partnership.*” (13) This required massive increases in aid above defence budgets, the foundation of a special fund for social objectives, significant restructuring of trade relationships, and flexibility on credit and debt – all of which should be organised through the UN and affiliated international institutions.

The primary conclusion of the academic opprobrium directed at the Commission’s report dovetailed with McNamara’s own conviction that the Bank should radically expand its operations. A number of the Columbia delegates would go on to shape the strategy of the Bank in achieving the objectives of the McNamara era – particularly by impressing upon management the need to dramatically increase transfers, and incorporate redistributive objectives into development policy. Ernest Stern would subsequently become Senior Vice

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<sup>347</sup> Jolly, R., ‘The Aid Relationship: Reflections on the Pearson Report’, in Ward, B., Runnalls, & D’Anjou, L., (eds.) *The Widening Gap: Development in the 1970s*, Columbia University Press, New York, 1971. Pg.284-92.

<sup>348</sup> Amin, S., ‘Development and Structural Changes: African Experience’ in *ibid.* Pg. 312.

<sup>349</sup> Kapur, D., Lewis, J., & Webb, R., *Interview with Robert S. McNamara*, World Bank History Project, Brookings Institution, Washington D.C, Session 2 April 1, 1991. Pg.24

<sup>350</sup> Blair, P. *Interview with William Clark*, October 4<sup>th</sup> 1983.

President for Operations, while Paul Streeten of Oxford would go on to develop the 'Basic Needs' approach with Mahbub ul Haq. Appointed during McNamara's second term to the role of Chief Economist, Hollis Chenery drew upon the work of Singer and Jolly with the ILO in conceptualising 'development' as a problem of employment – and orienting Bank development policy around the concept of 'Redistribution with Growth'.

From 1969 to 1973, Bank lending commitments increased by 131% in constant dollars.<sup>351</sup> This is a striking reversal of fortune given the stagnation of the lending programme in 1968. In the following section, I will show that the precise way in which management was able to implement the ideas of development economists such as Singer, Jolly, Seers, and Streeten as Bank policy was shaped by the requirement to make them comprehensible to financiers who invested in Bank paper in search of a steady return.

Rejuvenating the Bank in its ability to lend on the scale set out in the first five year plan would require that the Bank would obtain significantly greater volumes of finance in the global capital markets.

Support amongst the banking community was hard to come by. In order to meet McNamara's goals, the Bank had to find new ways to demonstrate – as ever - to financiers that although it was increasingly lending for non-cash-flow purposes it was still doing so prudently. In the context of the declining creditworthiness of the Bank's biggest client groups and the threat this posed to the creditworthiness of the Bank itself, this involved transforming the Bank's ability to quantify its impact. The implementation of the 'basic needs' agenda would be directly mediated by these imperatives.

Before the increase in lending could be achieved, McNamara had to demonstrate that the Bank as an organisation was under management control, and that the projects in which it was involved were financially sound. The first step which had to be taken was to demonstrate the probity of the Bank's practices of lending and operational control. The 'development agency' would only be able to attain the required capital to abolish poverty through the introduction of techniques of scientific management which had been pioneered in conjunction with the RAND Corporation at the US Department of Defense.

## **2: Quantifying Development and Managing the 'Development Agency'.**

The objective of undertaking progressive steps towards redistributive development strategies and simultaneously retaining the support of the Bank's private investors entailed improving the economic research standing of the Bank, while demonstrating that the

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<sup>351</sup> Kapur, D., Lewis, J.P., & Webb, R., 1997 (A). Pg.216



institution was scientifically managed and non-cash-flow or program lending would be rigorously controlled. From the outset, McNamara was at pains to emphasise that although this constituted a change in degree, it was not a change in kind: *“...we can carry out these operations within the high standards of careful evaluation and sound financing that my predecessors have made synonymous with the name of the World Bank.”* Sound development financing entailed seeking out the projects which would contribute ‘most fundamentally’ to the development of the ‘total national economy’.<sup>352</sup>

There were significant obstacles to these goals. Long term project lending became problematic in the light of the damage done to the creditworthiness of sovereigns seeking to repay longer-term debts with short-term private borrowing in Eurodollar markets. As member creditworthiness declined, the perceived likelihood of a default could threaten the Bank’s own creditworthiness, making it more expensive to borrow and resulting in higher charges to borrowing members. Lending more was therefore an imperative – to prevent the exacerbation of this vicious circle. McNamara’s first task would be to find a way to make lending to the poor acceptable to bankers.

Ultimately, the Bank would have to be re-arranged so that its structure facilitated a high degree of centralised control on the basis of decisions made by a small group of senior managers whose understanding of operations was derived from comprehensive data fed upwards from individual departments to divisional vice-presidencies. Adopting a structure of control which was common to the world of business, finance, and increasingly to government in the advanced capitalist countries was a key step in making ‘progressive’ lending objectives legible to private investors.

The scientific management practices of the McNamara era would become the foundations for the transition to the neoliberal political economy of structural adjustment in the Bank considerably before its return to centrality in international liquidity provision in 1982.

### **Financiers as Obstacle and Solution**

McNamara had a clear set of objectives from the outset regarding what needed to be done to obtain the financing with which to back the increased lending programme. Borrowings from foreign central banks should increase, the Bank should break in to the European pension trust market, and borrow more in Switzerland, Kuwait, and Italy. According to Kraske et al, the objective of the further internationalisation and diversification of the Bank’s borrowing was to

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<sup>352</sup> IBRD, IFC, IDA, 1968. Pg. 10-11.

*“achieve greater autonomy for the Bank”* from the requirement that it turn to an increasingly truculent US Treasury in order to tap the markets of New York.<sup>353</sup>

Such ‘autonomy’ from political vicissitudes of access to major markets could only ever be relative and contingent. The interests of financiers and their perceptions of risk were of paramount importance.<sup>354</sup> The discussion of the five year plan, increased borrowing, and technical assistance at the annual meeting had not improved the Bank’s standing in financial circles.

This rapidly became evident. Following the 1968 annual meetings, a bond issue was made in Switzerland in November that year. It was a failure the like of which the Bank had never seen: almost half the issue remained unsold, in a debacle which forced the Treasurer, Robert Cavanaugh, to resign.<sup>355</sup> In practical terms, the failure was due to the underwriting practices of the Swiss – the offering was not priced and placed in the market for a period of approximately fifteen days. Shortly beforehand, an issue had been made in Deutschmarks and while the Swiss issue was held by the underwriters, the exchange relationship altered in such a way as to make it more attractive to purchase the German issue.<sup>356</sup> However, McNamara noted that the Swiss bankers blamed the way in which he had spoken about the Bank as a ‘development agency’, casting him as a ‘red eyed socialist’ and causing *“...a tremendous undercurrent that, ‘McNamara is going to screw this thing up. We’re going to throw money away and you better be careful in buying Bank securities because they won’t do well.’”*<sup>357</sup> The financial press, particularly *Barron’s* in the US, ran enthusiastically with this story.<sup>358</sup>

While Cavanaugh’s successor Eugene Rotberg was aware of the disquiet within the Bank<sup>359</sup> and among the world’s money managers, he did not share his predecessor’s qualms about ramping up the Bank’s borrowing strategy. On the contrary, he shared McNamara’s view that the Bank was massively under-leveraged. The speculation surrounding the non-cash-flow lending which had contributed to the failure of the Swiss issue could be countered with a marketing campaign based on the financial structure of the Bank as an institution.

Rotberg embarked on an intensive round of presentations to financiers on purely financial matters – emphasising the liquidity of the Bank as derived from the steady and

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<sup>353</sup> Kraske, J. et al, 1996. Pg.180.

<sup>354</sup> Oliver, R.W., *A Conversation with Simon Aldewereld, II*, New York City, November 6<sup>th</sup>, 1985. Pg.31.

<sup>355</sup> Kraske, J. et al, 1996. Ibid.

<sup>356</sup> Asher, R., *Interview with William Clark*, The World Bank/IFC Archives Oral History Program, October 5<sup>th</sup> 1983. Pg.16.

<sup>357</sup> Kapur, D., Lewis, J., & Webb, R., *Interview with Robert S. McNamara*, Session 2 April 1, 1991. Pg.4

<sup>358</sup> Asher, R., *Interview with William Clark*, October 5<sup>th</sup> 1983. Ibid.

<sup>359</sup> Staff who had spent over two decades designing electric power projects considered that the trend toward projects which did not have an immediate cash product would not find the support of the financial markets. Where was the cash flow which would service a loan for the purposes of education?

increasing stream of cash flow from borrowers, the diversity of its borrowings, and its credit standing. At first, no reference was to be made to McNamara's objective to increase lending to the poor, and the non-cash-flow projects were to be underplayed. McNamara was similarly engaged, and began to return to the notion that the Bank had undertaken a change – but stressing that it would retain the financial probity which had characterised it to date. He assured the Bond Club of New York in 1969 that while the Bank was a development agency *"...I must make equally clear that the World Bank is a development investment institution, not a philanthropic organisation and not a social welfare agency."*<sup>360</sup>

Their campaign was a significant success. Bankers' concerns were assuaged that with the strategy sketched out by Rotberg - spreading the risk to the Bank across sectors and around the globe, with tight supervision and macroeconomic guidance - the Bank would not transform itself into a welfare institution.

Across the first five year period, to 1973, the Bank was able to borrow an average of \$780m net of repayments.<sup>361</sup> By the end of fiscal 1969, 60% of the IBRD's funded debt was held abroad. In 1970, the Bank borrowed in Japan for the first time: two issues of serial bonds denominated in yen at the value of \$100m each, yielding 7.14%, were followed by two further issues at the same value paying an even higher rate of 7.43%, both purchased by the Bank of Japan. Across 1970 and 1971, Japanese purchases of Bank paper added approximately \$600m to the Bank's loanable funds. In the US, the Bank made its first intermediate borrowings, issuing \$200m in five-year notes, paying 6.5% - in significant contrast to the Swiss issue of 1968, these bonds sold out rapidly, in spite of the fact that they were priced at par.<sup>362</sup> By 1973, less than one-sixth of the Bank's borrowing for the first five year plan had taken place on Wall Street.<sup>363</sup>

Appealing to the financiers in this way had significant implications for the Bank. Rotberg and McNamara considered that driving their programme to increase lending while retaining essential financial support would require more than simply building a *"...a financial structure in the early 1970s with lots of liquidity, diversity of loans and sectors, quality of lending, etc."*<sup>364</sup>

In order to really expand its programs into education, population control, and subsistence agriculture, it would have to undertake major structural reforms which would help

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<sup>360</sup> McNamara, R.S., address to the Bond Club of New York, May 14<sup>th</sup> 1969, cited in Kraske, J. et al, 1996. Pg. 80

<sup>361</sup> Kraske, J., et al 1996, Pg.182.

<sup>362</sup> Mason, E.S., and Asher, R., 1973. Pg.138 & 142.

<sup>363</sup> Clark, W., 'Robert McNamara at the World Bank', *Foreign Affairs*, Vol.60, Fall 1981. Pg.169.

<sup>364</sup> Webb, R., and Kapur, D., *Interview with Eugene Rotberg, Former Vice President and Treasurer*, World Bank History Project, Brookings Institution, Washington D.C., November 2<sup>nd</sup> 1990. Pg. 3-6.

to quantify the impact and effectiveness of each dollar lent. Modifying the project strategy towards a sectoral focus allied to a country-wide program in such a way as not to undermine the revitalised relationship with financiers, or in Rotberg's words, make it "*difficult for the Swiss*"<sup>365</sup>, entailed drawing upon the managerial strategies McNamara had learned and taught at Harvard Business School –and refined at the Ford Motor Company and the Pentagon.

### Importing Managerial Technology

The ability to quantify the inputs and outputs of Bank activity was one of McNamara's initial concerns on his accession to the Presidency. This lay at the core of his skillset as a manager, and had delivered his greatest successes with Ford and the Pentagon – as well as his greatest failures in Vietnam and with the troubled US Air Force jet, the F-111. He had gained his MBA from Harvard Business School at a time when methods of quantitative decision-making were at the cutting edge of management studies in the 'Business Statistics' course of Professor Edmund Learned and the 'Aspects of Budgetary Control' course of Professor Ross Walker. The techniques of cost accounting, control systems and 'decision science' learned at Harvard Business School were honed in the Army's Department of Statistical control where he developed a system for the tracking of materiel and men, before joining Ford with a small group of his Army colleagues – known as the Whiz Kids.<sup>366</sup>

The application of these control strategies at Ford drew not only on McNamara's expertise, but on the recruitment of senior managers from General Motors who had witnessed Alfred P. Sloan's rescue of the company – and its transformation into a model of scientific management frequently used as an example to students at Harvard Business School. This kind of change was also wrought at Ford: through the exertion of absolute control and the deployment of a defined statistical methodology, the loss-making manufacturer was rationalised and rejuvenated as costs were ground down through efficiencies found in the scheduling of production lines and in the use of resources throughout the company.

A major enhancement to this set of practices was the development of the 'Planning Programming Budgeting System' (PPBS), undertaken at the Pentagon with Charles Hitch of the RAND corporation, famed for its application of scientific methodologies to strategic bombing campaigns and the US nuclear posture. Hitch was a figure seen as a guru of modern management and was in charge of a highly unpopular team of statisticians hired to overhaul the American military budget, force posture, and strategy. While unpopular in the Pentagon,

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<sup>365</sup> Webb, R., and Kapur, D., *Interview with Eugene Rotberg*, November 2<sup>nd</sup> 1990. Pg.6.

<sup>366</sup> Rosenzweig, P., 'Robert S. McNamara and the Evolution of Modern Management', *Harvard Business Review*, December 2010. Pg.88-90.

PPBS was deemed exceptionally effective – and was extended to all federal agencies by President Johnson in August 1965.<sup>367</sup>

The method which had been developed by Hitch and his team in the Office of Systems Analysis was designed to produce explicit objective criteria for decisionmaking which excluded tradition, habit, and the institutional proclivities of individual services or agencies. This was achieved on the basis of an investigation of the objectives and processes of each department, generating a set of statements of their requirements and costs, which could be projected into the future. Once these data had been produced and analysed, highly rational decisions could be made about how to maximise capability at the lowest cost.<sup>368</sup>

The use of statistical data was a mechanism through which he would gain oversight of Bank operations, and enhance the ability of senior management to control policy. Due to the small size of the organisation on his arrival, McNamara felt that “...hell, I can control 3,000 people almost by myself...it’s easy to control once you’ve set up measures.”<sup>369</sup> The institutional basis of these ‘measures’ was twofold: firstly, a core of intellectual staff, who would perform a similar function to that of the Office of Systems Analysis, organised around Chenery, Mahbub ul Haq, and Ernest Stern. The second aspect of this was the foundation of a Program and Budgeting (P&B) department under Siem Aldewereld to operate as the practical control centre in terms of ‘input and output’. Chenery reflected that:

*“The real model for the Bank probably came out of his policy group in the Pentagon in which several very competent people from the Rand Corporation and elsewhere developed this kind of framework which could be applied to the analysis of weapon systems, to procurement, to budgeting, and so forth.”*<sup>370</sup>

P&B was intended as the vehicle for the quantitative analysis which would give the president greater insight into operations. This was the precursor to the foundation in 1970 of the Operations Evaluation Unit, which would audit loans after implementation – enabling McNamara to personally issue and police directives relating to the impact of lending.<sup>371</sup> The P&B department had an immediate impact through the systems-analysis derived design of

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<sup>367</sup> Amadae, S.M., *Rationalizing Capitalist Democracy: The Cold War Origins of Rational Choice Liberalism*, University of Chicago Press, London, 2003. Pg. 68

<sup>368</sup> Shapley, R., ‘Robert McNamara: Success and Failure’ in Doig, J.W., and Hargrove, E.C., *Leadership and Innovation: a Biographical Perspective on Entrepreneurs in Government*, Johns Hopkins University Press, Baltimore, 1987. Pg. 254-8.

<sup>369</sup> Kapur, D., Lewis, J., & Webb, R., *Interview with Robert S. McNamara*, Session 2 April 1, pg.23

<sup>370</sup> Asher, R., *Interview with Hollis Chenery*, World Bank/IFC Archives Oral History Program, January 27<sup>th</sup> 1983, Washington D.C. Pg.3.

<sup>371</sup> Kapur, D; Lewis, P; and Webb, R., 1997. Ibid.

McNamara's first five year plan, developed through analysis of relative priorities among countries and within sectors of each economy, to be 'directed from the top'<sup>372</sup>. As at the Pentagon, this was the central objective: to remove the politics from decisionmaking through a hierarchical and centralised apparatus which facilitated the production and control of large volumes of detailed quantitative data.<sup>373</sup>

The result of this was the introduction of the 'Country Program Paper' as a framework for Bank lending strategy in 1969. These confidential documents were not available to borrowers or Board members, and were to be prepared annually by regional departments, and would provide a comprehensive overview of a borrowers' politics, economic situation, their external financing, and a proposal for a five year lending program.<sup>374</sup> This innovation took place in the context of the abolition of the 'country working party', the ad-hoc groups which had their origins in a bid during the Bank's earliest years to improve communication between the Loan and Economics departments.<sup>375</sup> These had been partially formalised under the terms of the 1952 reorganisation as 'Loan Working Parties' to facilitate liaison between Aldewereld's Technical Operations Department (TOD) and the Area Departments.<sup>376</sup>

The objective in ending this practice was to extend presidential and senior management control over operations, while responding to economists' concerns about the relationship of project-based interventions to macroeconomic policy. The collegiate management style of the McCloy, Black, and Woods years was considered inappropriate to the new demands of accountability to higher management and transparency of process: there had to be a single individual who could be considered responsible for Bank strategy in a particular country.

In McNamara's view, the ability to derive quantitative information from Bank operations needed to be extended throughout the Bank's processes and systems in order to streamline the relationship between country programs, sectoral strategies, and individual projects. This imperative was complicated by the recruitment drive that had been set in train, and the opening of new departments and overseas offices. Between 1968 and 1971 staff numbers had increased by 75%. Therefore, a reorganisation of the entire institution was warranted, and in order to retain the confidence of the investment community and ensure that

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<sup>372</sup> McNamara, R.S., personal notes, item 16, May 25<sup>th</sup> 1968, Series 4541 (Presidents' papers – Robert S. McNamara – Chronological files [o]) World Bank Group Archives, cited in Kraske, J., et al. 1996. Pg.175.

<sup>373</sup> Amadae, S.M., 2003. Pg.65

<sup>374</sup> Kapur, D; Lewis, P; and Webb, R., 1997. Pg. 245.

<sup>375</sup> King, J.A., 'Reorganising the World Bank', in *Finance and Development*, March 1984. Pg.7.

<sup>376</sup> Galambos, L., and Milobsky, D., 'Organizing and Reorganizing the World Bank 1946-1972: a Comparative Perspective', in *Business History Review*, Vol. 69 (Summer) 1995. Pg.167.

it was implemented with the principles of scientific management in mind, McNamara would call in McKinsey & Co. in 1972.

Their report would not contain any surprises: he had already explained to them what he wanted to do. The outcome he sought was the creation of an organisational structure which reflected systems he had controlled at the Ford corporation, and was intended to give the office of the president what McNamara described as 'functional control' over area departments which would be run by vice presidents with 'administrative control' of their divisions. This would enable technical objectives, procedures, and standards to be set at the highest managerial level and enforced across the organisation by general managers. Should a manager in a particular area deviate from these procedures and standards, McNamara would be able to enforce discipline.<sup>377</sup>

The new structure created the position of 'Senior Vice President Operations', which was filled by Burke Knapp, who presided over six Vice Presidents. Five of these were the heads of regional departments: these posts were responsible for lending and technical assistance in their regions. The regional departments would operate in a similar way to the old pre-1952 Loan Department: they were responsible for their own project work, as well as assessment of creditworthiness and project supervision. The Central Projects Staff was the sixth VP position, to which Warren Baum was appointed; responsible for developing Bank Group-wide project policies, and providing operational guidance and support to the regions. The Central Projects group also contained those units which were too small to decentralise – and which were those targeted for expansion under McNamara: population and nutrition, agriculture, education, and environmental affairs; as well as further specialist departments in industry, tourism, urban project, utilities, and transport, which absorbed many technical and engineering staff from the disbanded TOD. Alongside the operational departments overseen by Knapp were a further six Vice Presidencies which reported directly to the President – in finance, general counsel, planning and personnel management, external relations, overseas offices, and internal auditing. Most importantly for the new direction of the Bank, a seventh VP position in Development Policy was created.<sup>378</sup> Organised under this VP, the Bank's economists were returned to the position of power that they had lost in 1952, perhaps even gaining – each regional office also had a chief economist on its management team.

The objective – simultaneously centralising functional authority in the office of the president, and decentralising administrative authority among operational divisions – was common to the US' largest multinational corporations. It was designed to render the great

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<sup>377</sup> Lewis, J., Webb, R., & Kapur, D., *Interview with Robert S. McNamara*, April 1, 1991. Pg.19-20.

<sup>378</sup> King, J.A., 1984. Pg.8

complexity of function which the increasing diversity of Bank operations entailed legible to the economists and managers in Washington.<sup>379</sup> The legibility of this structure of control was also extremely important to the Bank's investors, whose money was tied up for twenty years in Bank paper. McNamara's usage of the tools of quantification, econometric modelling, and regression analyses in order to reach a point at which a decision could be made reassured investors that the changes to the Bank's staffing and strategy were allied to a set of policies which would offer longstanding security and control that prevent the financial standing of the Bank and the price of its paper from being undermined by concerns over the quality of its credit.<sup>380</sup>

This was the broader objective – to support the extension of Bank borrowing in order to enable it to expand its lending operations among members who, thanks to their increasingly risky debt profiles, were less and less creditworthy.

The transformation of the Bank in this way was a key piece of the puzzle which would, once the debt crisis had struck, become known as the Washington Consensus. By 1973, McNamara could operate the institution as a highly centralised and hierarchical bureaucracy functionally controlled by a small team of senior management on the basis of detailed quantitative data concerning day-to-day operations. The broad oversight and tight control over operations exercised in this institutional form promoted the consideration of the individual productive projects the Bank was funding as 'programmes of projects', to be considered on a country-by-country basis under the Country Program Paper approach. During the second presidency from 1973-78, this would be an important aspect of the 'basic needs' approach: lending for purposes that were not directly productive and aimed to develop the agricultural base of the economy required greater insight into macroeconomic performance in order to ensure that the benefits of investment in education and technical training would be subsequently realised and offset by increases in productivity elsewhere.

McNamara's ability to remain in post for a second term as president and implement the second five year plan, with its focus on 'basic needs' as unveiled at the annual meeting in Nairobi in 1973, was predicated entirely on this foundation.

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<sup>379</sup> Galambos, L., and Milobsky, D., 1995. Pg. 186

<sup>380</sup> Webb, R., and Kapur, D., *Interview with Eugene Rotberg, Former Vice President and Treasurer*, November 2<sup>nd</sup> 1990. Pg.7-8.



### 3: 'Basic Needs' and the Consequences of Quantification

For Kraske, the 'Basic Needs' approach represented the Bank's most progressive moment, as it strove to attack the "*root causes of poverty and backwardness*". This coincided with the relaxation of IFC strictures prohibiting investment in firms that were publically owned, spoke to a concern about the disparity in incomes in the developing world, and saw the Bank enter into relations with countries such as Sri Lanka and Tanzania – which required the acceptance of 'socialist-type' premises such as Nyere's 'Ujaama' collectivisation scheme.<sup>381</sup>

Yet, as Kapur et al acknowledge, this was hardly a case of significant intellectual originality on the part of Bank management: the wider development policy world for some years had been arguing that concerns of distribution and equity had been neglected in a drive for growth which had anyway yielded unimpressive results.<sup>382</sup>

This 'progressive' moment would yield a second important step in the direction of structural adjustment. Quantification was not only important in terms of the control of the Bank as an institution – it would also make non-productive lending legible to financiers. Conceptualising development as an employment problem required the direction of Bank interventions at improving the productivity of the poor. These tenets of the 'basic needs' agenda would tie the performance of the Bank ever more closely to the performance of borrowers – necessitating a degree of leverage which the project model simply could not provide. Deploying 'basic needs' entailed macroeconomic reform – and the return to programme lending.

#### The Bank and Development Theory: Round 2 – Basic Needs and 'Redistribution with Growth'

McNamara's address to the governors at the 1973 annual general meeting in Nairobi drew heavily upon the work of the group of development economists McNamara had encountered at the Williamsburg Conference during the post-mortem of the Pearson Report: Dudley Seers, Hans Singer, Richard Jolly, and Paul Streeten, who were affiliated with the ILO and Sussex's IDS. It was profoundly shaped by Hollis Chenery, already appointed from Harvard to act as Economic Advisor and from 1972 promoted to the new VP Development Policy. Chenery's work in particular had attracted the President, as immediately prior to his appointment to the Bank, he had been running a research project at Harvard entitled 'Quantitative Research in Economic Development'.

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<sup>381</sup> Kraske, J., et al 1996. Pg.177-8.

<sup>382</sup> Kapur, D; Lewis, P; and Webb, R., 1997. Pg.16.

The use of quantification processes as a way to link research and policy had been deployed by McNamara's policy group at the Pentagon, drawing on Rand Corporation expertise and applying it to the analysis of weapons systems, procurement and budgeting.<sup>383</sup> Hiring Chenery meant that McNamara was able to demonstrate that the development policy research behind his lending programme was as robust as the scientific techniques he personally applied to the managerial transformation of the Bank.

Whereas early theorisation of the dynamics of late development had been essentially qualitative, at the close of the 1960s, efforts were made to create rigorous positive models of the process of rural-urban migration which accounted for widespread and chronic urban unemployment in the context of growth.<sup>384</sup> This had been an aspect of the research agendas which had followed from the ILO's Employment Policy Convention.

Drafted in 1964, it had committed signatory governments to adopt activist policies aimed at full employment. This agenda had gained momentum in the later 1960s and in 1967 the ILO initiated its World Employment Programme, under which a series of case studies were undertaken in an effort to provide guidance for the governments concerned, as well as for aid and trade policies among donors and international organisations. Specialists participating in the programme were drawn from UNCTAD, the ILO, the WHO, the Inter-American Development Bank (IDB), and the Organisation of American States (OAS); a number of UN agencies including ECLA, the Food and Agriculture Organisation (FAO), UNESCO amongst others; the IDS at the University of Sussex; and the World Bank.<sup>385</sup>

The 'Basic Needs' agenda which McNamara outlined in Nairobi was predicated on the Bank's achievement of a 100% increase in lending in real terms across 1964-8. This had been delivered through a four-fold increase in borrowing, which had increased the Bank's liquid reserves by 170%. For McNamara, it was a moral imperative to deploy these resources to target 'absolute' poverty, a phenomenon which he depicted as to a *"...condition of life so limited as to prevent realization of the potential of the genes with which one is born"*, in contrast to the simple observation of 'relative' poverty – the simple observation that some societies were more prosperous than others.<sup>386</sup> The 'absolute' poor were the large minority of the rural poor, who had seen no benefits from the productivity and income growth

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<sup>383</sup> Asher, R., *Transcript of Interview with Hollis Chenery*, January 27<sup>th</sup> 1983. Pg. 3.

<sup>384</sup> An example of this is Todaro, M.P., 'A Model of Labor Migration and Urban Unemployment in Less Developed Countries', *The American Economic Review*, Vol.59, No.1, 1969.

<sup>385</sup> ILO, *Towards Full Employment: a Programme for Colombia Prepared by an Inter-agency Team organised by the ILO*, ILO, Geneva, 1970. Pg.1-6.

<sup>386</sup> McNamara, R.S., 'Annual Address by Robert S. McNamara, President of the Bank and its Affiliates', in IBRD, IFC, IDA, *1973 Annual Meetings of the Boards of Governors: Summary Proceedings*, Washington D.C., 1973. Pg.17.

experienced by developing members had seen across the 1960s. Solving the problems of 'absolute' poverty in rural areas would require targeting lending towards small farmers, and encouraging redistributive policies which could assist in meeting the basic needs of the rural poor and the growth of the wider economy.<sup>387</sup>

The central tenet of this approach was that there was no trade-off between redistributive policies and growth. There was, in fact, a tight linkage: if the rest of the economy did not grow, farmers would anyway lack the required inputs or demand for their output.<sup>388</sup> Therefore, the Bank would increase its lending to \$4.4bn in agriculture from \$3.1bn in '69-'73, and advocate strongly that the governments of developing countries undertake the necessary redistributive reform in their spending policies in order to stave off the risk of revolution.<sup>389</sup>

While the Rostowian modernisation theory lineage is clear, by the early 1970s the 'trickle-down' approach to modernisation derived from the work of Arthur Lewis<sup>390</sup> and Simon Kuznets<sup>391</sup> - in which long-term equality was traded off for growth - had been comprehensively displaced.<sup>392</sup>

For the Bank, the most important feature of contemporary development theory was the way in which it reformulated 'development' as a problem of employment, not of growth alone. This followed directly from the work of IDS' Dudley Seers and Hans Singer. The ILO's research in Colombia and Kenya emphasised the inability of the 'modern' sector to create jobs. The policy implication of this was that rural-urban migration should be discouraged through public investment in rural areas with a view to raising rural wages and fostering small-scale entrepreneurialism in the 'traditional' sector.<sup>393</sup> The ILO argued that tax revenues derived from income growth of the top 1% of the population should be transferred to the bottom third of income recipients through crop technologies, rural credit institutions, and labour intensive technology in agricultural product processing.<sup>394</sup> The post-independence policies of growth and

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<sup>387</sup> Ibid. Pg.13-17.

<sup>388</sup> Ibid. Pg 22-3.

<sup>389</sup> Ibid. Pg.34.

<sup>390</sup> Lewis, A., *The Theory of Economic Growth*, Richard D. Irwin, Homewood, 1955. Pg.9

<sup>391</sup> Kuznets, S., 'Economic Growth and Income Inequality', *The American Economic Review*, Vol.45, No.1, March 1955. Pg.8

<sup>392</sup> Even *Foreign Affairs* and *Foreign Policy* both carried assertions that "The last two decades thus teach us that the poor will not obtain a proportionate share in the benefits of growth until the character of growth is radically altered" ( Shourie, A., 'Growth, Poverty, and Inequalities', *Foreign Affairs*, Vol.51, No.2 (January) 1973. Pg.350), and "We have seen that income distribution, welfare, and even population policies cannot readily be divorced from growth policies." (Grant, J.P., 'Development: the End of Trickle Down', *Foreign Policy*, No.12 (Autumn) 1973. Pg.63)

<sup>393</sup> Seers, D., 'New Approaches Suggested by the Colombia Employment Programme', *International Labour Review*, Vol.102, 1970. Pg. 380-1.

<sup>394</sup> ILO, *Employment, Incomes, and Equality: a strategy for increasing productive employment in Kenya*, Geneva, 1972. Pg.365

nationalisation within the inherited economic structure would have to be replaced with spending on programmes to absorb the rural labour force and promote investment in education, health services, and housing. Neither growth nor redistribution alone would suffice.<sup>395</sup>

The involvement of the Bank with this group of scholars had heavily influenced McNamara: the conclusions of the ILO projects, as well as the vehement denunciations of the highly conservative Pearson Commission and the highly popular (and populist) work of E.F. Schumacher,<sup>396</sup> had led him to task Chenery with supporting or rejecting the thesis that the productivity of the poor could be raised by focusing investment on them without reducing the growth rate of the economy as a whole.<sup>397</sup>

The ILO's approach, and endorsement of quantitative targets dovetailed with the Bank's own research project, organised by Hollis Chenery in collaboration with IDS and the Centre for International Affairs at Harvard, with the financial and logistical support of the Rockefeller Foundation. The Bank's report on these matters, *Redistribution with Growth*, appeared in 1974 and originated from discussions which arose from the involvement of Bank staff in the ILO studies, and Hollis Chenery's engagement with the academic research of Singer, Jolly, and Seers at Sussex's IDS. Orienting growth measures towards the enhancement of the productivity of the poor was selected as the mechanism through which it would be possible to "...make poverty...acceptable to the bankers."<sup>398</sup>

Bankers' acceptance of poverty-oriented lending was thus not only predicated upon the transformation of the institution and the introduction of quantitative methods into operational control. The Bank's development policy also had to be transformed to ensure that it drew upon the most cutting-edge positivist methodology. Positioning 'development' as a problem of employment facilitated a move away from the Bank's traditional exclusive focus on growth: the conventional requirement that each project should be self-amortising would not be dropped, but would be considered in terms of its contribution to the productivity of the wider economy. The reforms which Chenery's research advocated were not project-specific – they required large-scale macro-economic transformation of both inherited colonial economic structures and the nationalist programmes of post-independence governments.

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<sup>395</sup> Singer, H., and Jolly, R., 'Unemployment in an African Setting: Lessons of the Employment Strategy Mission to Kenya', *International Labour Review*, Vol. 107, 1973. Pg.104

<sup>396</sup> He had been particularly impressed by Schumacher's *Small is Beautiful: a Study of Economics as if People Mattered* - Kapur, D; Lewis, P; and Webb, R., 1997. Pg.229

<sup>397</sup> Kapur, D., Lewis, J., & Webb, R., *Interview with Robert S. McNamara*, World Bank History Project, Brookings Institution, Washington D.C, Session 4, October 3, 1991. Pg.73.

<sup>398</sup> Asher, R., *Interview with Mahbub ul Haq*, World Bank/IFC Archives, Oral History Program, December 3rd 1982. Pg.4.

The most important implication of this strategy was that the performance of the Bank, and its ongoing ability to borrow and lend, was ever more tightly bound to the macroeconomic performance of borrowers. This was a second important step towards structural adjustment lending: the oversight and discipline which was required could only be had through the 'Country Program Paper' system with extreme difficulty. The project approach was reaching its limits.

### **Operationalising 'Basic Needs': How the 'Country Program Paper' became the Structural Adjustment Loan.**

As a concept, structural adjustment lending was still some years from crystallisation. The project and productivity requirement stipulated by the articles of agreement remained. In the early 1970s, work was organised on the basis of projects which were productive on the basis of the 'Country Program Paper' approach, which had been introduced as one of McNamara's first reforms, prior to the 1972 reorganisation. This sought to aggregate groups of projects within an individual borrower, in such a way as to at least rhetorically meet the objectives of 'basic needs'. The object of this was to improve the Bank's ability to enter into dialogue with borrowers and exercise greater influence over sectoral and macroeconomic policy.

However, providing positive modelling to back up the redistribution-with-growth approach may have made the idea and rhetoric of 'basic needs' lending programmes acceptable to the bankers, but it did not necessarily feed in to Bank policy in the way in which had been anticipated. Further, the nature of the new lending programme and the turbulence of the international economy meant that it was extremely difficult to implement while holding strictly to the conditional project model. In the latter half of the 1970s it was rapidly eroded.

Firstly, 'basic needs' objectives cut across agriculture, health, education, and employment – it was difficult to 'projectise' these objectives while targeting a specific vulnerable social group. Accordingly, the delivery of primary health care, nutrition, and education projects was allowed to become an 'area' project. Mahbub ul Haq, one of the architects of basic needs commented that:

*"The project became a looser and looser concept. We could call a whole village development a project, including a lot of various elements in it. We brought in integrated rural development programs which included about ten different activities in a spatial sense, focusing on a certain vulnerable group. So that was continuing the previous process of loosening the project definition."*<sup>399</sup>

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<sup>399</sup> Ibid. Pg.14

The proportion of 'project' costs which were financed locally rose to 60 or 70% - permitting the borrowing government greater flexibility in utilising the foreign exchange provided by the loan. This gave loans under the rubric of 'basic needs' the character of program lending in many cases.<sup>400</sup> The Bank began to embrace the fungibility of development lending.

Secondly, the 'loosening of the project definition' was accelerated by trends in the international economy. The ability of clients to hire foreign exchange easily in international capital markets reduced the Bank's ability to enforce conditionality on its loans. Further, the Bank was forced to offer relatively soft program loans to countries whose ability to repay private creditors was jeopardised by inflation and declining terms of trade following the steep oil price increase in 1974. In this environment, it was impossible to utilise project lending to enforce conditionality. The essentially macroeconomic reforms required by the 'basic needs' and 'redistribution with growth' concepts demanded programme-level conditionality.

Brazil, Cote d'Ivoire, and Zaire provided object lessons. Following McNamara's speech in Nairobi the Bank made a highly determined effort to influence the government's policies in relation to poverty and inequality. Although a raft of projects were agreed in areas from hydroelectric power to agricultural research, the Bank considered that the government was not making a concerted effort to aim its policies at the rural poor, and McNamara argued that it was no longer justifiable to continue to lend. However, the extent to which the Bank had invested in Brazil meant that by 1975 the interest payments to the Bank had outstripped the Bank's total annual net income. Efforts to influence government policy were reduced to praising any activities with 'social objectives' as a concern, rather than substantive critique.<sup>401</sup> Stopping lending to Brazil was not an option – a default would have been catastrophic.

In Cote d'Ivoire the Bank had sought to engage with policymakers from the mid-1960s, financing a series of highway and agricultural projects from 1968 onwards,<sup>402</sup> and had produced a series of reports in the later 1970s which praised an 'Ivorian Miracle' in executing an export-oriented strategy with redistributive features.<sup>403</sup> The Bank suggested that greater development of the local private sector was required, with particular reference to the rural areas and the promotion of the 'informal sector' – a structural transformation of the income and incentive structure. Cost recovery was to be considered in services such as secondary

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<sup>400</sup> Ibid. Pg.13-14

<sup>401</sup> KIW. Pg 274-280

<sup>402</sup> World Bank, Operations Evaluation Department, *Cote d'Ivoire: Country Assistance Review*, Washington D.C., June 14<sup>th</sup> 1999. Pg.21-3

<sup>403</sup> den Tuinder, B.A., *Ivory Coast: the Challenge of Success: Report of a mission sent to the Ivory Coast by the World Bank*, Johns Hopkins University Press, London, 1978. Pg.4

education.<sup>404</sup> Yet on the basis of record export receipts, Cote d'Ivoire was highly credit-worthy in Eurodollar markets, and a Bank official employed there at the time noted somewhat peevishly that commercial banks were virtually queuing outside the Ministry of Finance to lend almost any sum on almost any terms – without asking what the money would be spent on.<sup>405</sup> The Bank's prescriptions went unheeded – until the defaults of 1982.

For high income countries such as Brazil and middle income countries such as Cote d'Ivoire, the unexpected interest rate hikes engineered by Volcker at the Fed from 1979 to 1983 were a major factor in their debt defaults and rescheduling. For low income countries, particularly in Africa, the majority of debt was fixed or lower rate and either owed directly to or guaranteed by official creditors. Although the sums outstanding were smaller than in other regions, indebtedness was both more severe than among middle income defaulters and low-income Asian countries measured by servicing ratios, and reached crisis proportions earlier.<sup>406</sup> Practices which would later fall under the rubric of structural adjustment have the longest history amongst these countries.

Indeed, Chenery comments that in terms of Bank policy “...I would not say that we ever adopted a basic needs approach in our project lending.”<sup>407</sup> Nor did its missions attempt to either persuade those countries which did not hold the basic needs concept as an objective of policy, or try and dissuade those which did already deploy some form of it. Further, the Bank's traditional cost-benefit analysis would not have captured enough of the benefits of ‘basic needs’-style lending as expressed by its advocates, who did not seek to stress making a calculation of a return as there were significant external economies which could not be measured. Among the wealthier borrowers, ‘basic needs’ was a chimera. Among the poorest, the outcome of the combination of quantification and ‘redistribution with growth’ necessarily looked much more like ‘structural adjustment’ than ‘basic needs’.

The Bank's engagement with Zaire throughout the 1970s exemplified both the shortcomings of the project-lending ‘country program’ approach, and a cautionary tale regarding the inability to move beyond the project approach to implement a coherent ‘basic needs’ programme due to the discipline demanded by financiers – having started down this route, the Bank was locked in. Although Zaire was an ideal candidate for ‘basic needs’ lending, it proved impossible to implement for two reasons – both of which are intimately related to the Bank's reliance on private finance. Firstly, abandoning the raft of existing projects would have damaged the Bank's AAA credit rating. Secondly, the extent of Zaire's private sector

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<sup>404</sup> Ibid. Pg. 296-9

<sup>405</sup> Oliver, R., *A Conversation with Richard Westebbe*, January 25<sup>th</sup> 1988. Pg.24

<sup>406</sup> Humphreys, C., and Underwood, J., in Corbridge, S.E., (ed) 1999. Pg.348

<sup>407</sup> Asher, R., *Interview with Hollis Chenery*, January 27<sup>th</sup> 1983. Pg.11

indebtedness required the Bank to act in conjunction with the IMF and the Paris and London creditor 'clubs' to enforce financial discipline in order to retain financiers' support for its increased lending programme.

Across the period 1973-88, the composition of Zairian debt would change dramatically. In 1973, the borrowing of Mobutu's CIA-supported regime in private capital markets peaked: private long-term external debt represented 78% of the total. This changed as world copper prices collapsed and a foreign exchange crisis ensued in 1975 and Zaire could no longer service its foreign obligations. By 1979, debts owed to bilateral creditors increased and private external debt had fallen to 44% of the total. Although Bank memoranda show that management were aware that the regime was siphoning the proceeds of loans and exports into personal accounts<sup>408</sup> and undertaking off-balance-sheet sales of natural resources, the level of Bank lending increased steadily.<sup>409</sup>

Following an agreement on a comprehensive 'Stabilisation Programme' with the IMF and a rescheduling agreement with the Paris Club of creditors and commercial bankers of London and New York, the Bank undertook a wide range of projects designed to support a 'basic needs' agenda. These included IDA financing for: development financing corporations; training primary teachers and agricultural technicians; promoting livestock farming, and smallholder maize production; and rail projects linking to major port rehabilitation projects to facilitate the export of the fruits of further projects to increase agricultural production in export crops such as sugar and cotton.<sup>410</sup> These did not yield significant fruit: By 1979, GDP had contracted by around 10% on 1972-4 levels, as inflation topped 100% and the economy saw chronic shortages of fuel and essential consumer goods.<sup>411</sup>

More significantly, following the IMF bailout, the Bank had founded the Office of Public Debt Management designed to oversee the spending of public funds. As an integral part of the surveillance of the public finances on behalf of multilateral donors, this new government

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<sup>408</sup> Blumenthal, E.M., 'Zaire: Rapport Sur la Credibilite Financiere Internationale' in Dungia, E., *Mobutu et l'Argent du Zaire: Les Revelations d'un Diplomate Ex-Agent des Services Secrets (annex 2)*, L'Harmattan, Paris, 1982. Also Kwitny, J., *Endless Enemies: the Making of an Unfriendly World*, New York, Penguin, 1984. Both cited in Ndikumana, L., and Boyce, J.K., 'Congo's Odious Debt: External Borrowing and Capital Flight in Zaire', *Development and Change*, Vol29, 1998. Pg.207. Blumenthal was a West German central bank official working in Zaire for the IMF.

<sup>409</sup> Ndikumana, L., and Boyce, J.K., 1998. Pg.197-99

<sup>410</sup> IDA credit numbers, in non-chronological order as above: 710 ZR (August 1977); 624 ZR (December 1978); 627 ZR (August 1977); 1040 ZR (October 1980); 571 ZR (July 1975); 1089 ZR (January 1981); 660 ZR (October 1980).

<sup>411</sup> World Bank, *Report and Recommendation of the President of the International Development Association to the Executive Directors on a Proposed Development Credit in an Amount of SDR \$42.2 million, and a Proposed African Facility Credit in an Amount of \$72.2 million to the Republic of Zaire for a Structural Adjustment Program*, May 29<sup>th</sup> 1987. Pg2



department would define borrowing policy and have direct responsibility for recording and servicing all projects financed with public and governmentally guaranteed debt.<sup>412</sup> World Bank officials also sat alongside IMF experts in the Bank of Zaire, the Finance Ministry, Customs Office, and Planning Ministry. Ultimately, the Bank was unable to exercise the leverage and political control which was required in order to effect the structural transformation of the economy. Ensuring that existing single-project interventions attained the productivity required to fund Zaire's debt to the Bank meant that these extensive interventions in the governance of the economy had little impact as a coherent programme.<sup>413</sup>

While the exigencies of default made it impossible for the Bank to overcome the project approach in Zaire, the case of the 1974 loan to Kenya provides an example of the step-wise incorporation of practices which would become familiar as structural adjustment loans after 1980. A programme loan was made conditional on the acceptance of an overall macro- and micro-economic plan within the 'basic needs' framework. Although Kenya's debt burden was comparatively light, the Bank was able to exercise considerable leverage as terms of trade deteriorated. The Bank was responsible for approximately 36% of its total external debt in 1974, and its debt service ratio (including members of the East African Community for which Kenya was responsible) was only 6%.<sup>414</sup> Without the hard constraint of default, in lending to Kenya the Bank was able to engage in 'structural adjustment' in all but name, in support of the 'basic needs' agenda, from 1975.

As in the case of Zaire, the Bank's intervention in Kenya took place alongside interventions from the IMF. However the differences in approach, which relate primarily to conditionality, are of signal importance here. As I noted in Chapter 1, Sarah Babb has pointed out that although the IMF is usually seen as the lead agency in terms of conditionality upon structural adjustment lending, the Bank has longer experience of the application of a wider range of conditionalities.<sup>415</sup> During the 1970s, the Fund had experienced a surge in lending to developing countries. Yet from 1975-1979, this lending was dwarfed by its disbursements in industrial countries. From 1974-1976 it made a short burst of lending to developing countries – of a specifically low-conditionality variety through its various specialised funds.<sup>416</sup> In respect of

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<sup>412</sup> World Bank, Eastern Africa Regional Office, *Economic Conditions and Prospects of Zaire*, Washington D.C., April 13<sup>th</sup> 1977. Pg.25.

<sup>413</sup> Callaghy, T.M., 'Restructuring Zaire's Debt, 1979-1982', in Biersteker, T.J., *Dealing with Debt: International Financial Negotiations and Adjustment Bargaining*, Westview Press, Oxford, 1993. Pg.109-110

<sup>414</sup> IBRD, *Report and Recommendation of the President to the Executive Directors on a Proposed Program Loan to the Republic of Kenya*, Washington, May 6<sup>th</sup> 1975. Pg.17

<sup>415</sup> Babb, S., 2013. Pg.276-277

<sup>416</sup> Boughton, J.M., *Silent Revolution: The International Monetary Fund 1979 – 1989*, International Monetary Fund, Washington D.C., 2001. Pg.558-564

Kenya, the Fund undertook a series of low-conditionality credits from 1974-1981, totalling \$190m, far outstripping the contribution of the Bank. But the Fund's involvement expressed hard conditionality only from 1981, when it insisted on a series of ineffective devaluations which signally failed to influence Kenyan monetary and fiscal policy.<sup>417</sup> Although the volume of lending was much lower, the Bank engaged much more deeply with Kenyan economic planning, in an effort to shape the macroeconomic policy environment so as to maintain its ability to negotiate its imperatives as an institution.

Within the framework of the 'basic needs' and 'redistribution with growth' strategies, the Bank had begun to build a policy-oriented 'dialogue' with the Kenyatta government from 1974, undertaking a series of reports and studies on the basis of a mission in February that year. As growth had begun to drop – falling to 3.4% (1999 pg.15) in 1973-6 due in large part to the OPEC price increase, the Bank was keen to prevent the 'momentum of development' from being lost. It considered that *"Kenya does not really have the option to continue the past pattern of growth, however successful it may have been, and that a material change in the structure or development would be required if Kenya's own development goals are to be achieved."*<sup>418</sup>

The programme loan of \$30 million which was agreed with the Kenyan government on May 30<sup>th</sup> 1975 was designed to offer support for increased expenditure on agricultural production and planning, and for the financing of essential imports.<sup>419</sup> It was envisaged that as urban employment levels fell, smallholder agriculture was to be emphasised: investment was to be increased, and consumer and producer prices were to be raised to reflect the increased cost of production. Wage increases were to be limited to 75% of price increases, with the poorest (mostly agricultural workers) granted full compensation for inflation and the richest (mostly urban sector workers) subject to wage freezes. Infrastructural projects and 'rural works programs' were designed to be labour intensive, and tax increases were aimed at the wealthy and on luxury consumption.<sup>420</sup>

Unlike in the Brazilian and Ivorian cases in which both borrowers were able to evade Bank conditionality in the private credit market, and without the complications posed by the crisis in Zaire, the Bank was able to deploy significant leverage upon Kenya. The Kenyan loan exemplified the McNamara Bank's adoption of the ILO's conception of development as an

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<sup>417</sup> Ibid. Pg. 589 - 596

<sup>418</sup> World Bank, *Report and Recommendation of the President to the Executive Directors on a Proposed Program Loan to the Republic of Kenya*, Washington D.C., May 6<sup>th</sup> 1975. Pg.1

<sup>419</sup> IBRD, *Loan Agreement (Program Loan) between Republic of Kenya and International Bank for Reconstruction and Development*, (Loan No. 1117 KE) Washington, May 30<sup>th</sup> 1975.

<sup>420</sup> World Bank, May 6<sup>th</sup> 1975. Pg. 7-14

employment and distribution problem. The operationalisation of this redistributive ‘basic needs’ package of reforms required Kenya’s structural transformation into an agricultural export – oriented economy. It required the use of hard conditionality in extracting commitments from the Kenyatta government to push through macroeconomic reforms in the form of politically unpalatable spending cuts which negatively impacted the popular standard of living.

In a 1975 report, the Bank noted that Kenya was faced with deteriorating terms of trade for its main plantation crop exports. Projections suggested that this would hinder the capital investment required to produce for export at sufficient volume to offset the deterioration in prices, and to absorb the expanding labour force – unless Kenya obtained increased external financing.<sup>421</sup> Accordingly, the Bank advised the Kenyan government that it would need to demonstrate its commitment to bringing its balance of payments under control before a loan could be agreed.

The outcome of this was evident in the budget presented for financial year 1975 – which aimed to curtail demand through new taxes, stringent credit restraint, increased interest and deposit rates, and a freeze on public expenditure. In the program which it subsequently presented to the National Assembly in 1975 as an official policy statement, the rate of expenditure growth in the development budget would be cut from 12 % to 8% per annum in the 1974-8 plan, and would be reallocated from infrastructure to agriculture and water.<sup>422</sup> It acknowledged that not only would this create conditions of real hardship as incomes would fall and unemployment would rise, but that these measures would not close the balance of payments gap – and increased ODA flows would be required, along with new types of assistance such as the Bank’s program loan.<sup>423</sup>

The depth of political involvement which the Bank required was the greatest stumbling block to the expansion of this mode of lending: while opposition from the Board was strong in view of concerns about overlapping with the mandate of the Fund, or the legal mandate in the Articles – the greatest problem was the lack of interest on the part of the targeted high and middle-income borrowers.

The trend among these borrowers exemplified by Brazil and the Cote d’Ivoire followed more generally: borrowings – even at high rates - in private international capital markets covered the cost of imports and paid down existing producer credits. While official credit grew across the decade, it was outstripped as a shift occurred to direct borrowing in capital markets

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<sup>421</sup> Ibid. Pg.2-4

<sup>422</sup> Ibid. Pg.8

<sup>423</sup> Ibid. Pg.5

through the issue of bonds and from private banks.<sup>424</sup> The Bank was not slow to apprehend that its falling share of financing equated to a limitation of its policy leverage, particularly in the case of middle income borrowers.

Structural adjustment was initially conceived of - in the words of Ernest Stern, McNamara's VP Operations - as a 'prophylactic', which could prevent such balance of payments problems.<sup>425</sup> The Kenyan loan of 1975 precedes the first officially designated structural adjustment loan by fully five years, and the decision to formally adopt develop 'structural adjustment lending' strategy as a Bank policy by three years.

The most important point to emerge from these case studies is not simply that the roots of structural adjustment are longer than generally conceived. The character of 'basic needs' and 'redistribution with growth' demanded macro-economic programming, in order to ensure that the elements of the agenda which were not directly productive were situated in a fiscally sound framework. Financial imperatives caused the adoption of the progressive agenda of the ILO and IDS to stretch the project approach beyond its limits. The security demanded by investors, without which the extension of Bank lending would not have been possible, bound the performance of the Bank to the performance of borrowers.

At the outset, it was a deliberately and carefully technicised mode of political engagement, designed to assist management regain the policy leverage which had become so precarious that, to paraphrase Stern once again, tougher conditionality was the only available tool through which the Bank could get a seat at the table for major sectoral and macroeconomic policy issues.<sup>426</sup>

That the macroeconomic analyses which the Bank staff had long carried out as background studies were transformed in the course of the 1970s into specifically structural analyses aimed at programmatic economic reorganisation - from balance of payments and capital flows to structural aspects of production, employment, spending, and the profile of sovereign debt - was a consequence of the strategy of introducing the principles of scientific management to the Bank in order to reassure financiers that 'basic needs' would not see the institution dabble in 'philanthropy'.

This problem was duly made the focal point the speech in which McNamara presented the policy to the Governors in Belgrade in 1979. The developing countries of the world, he noted, were increasingly looking to the Bank as the principal source of development assistance. The responsibility of the Bank would be to offer targeted assistance through

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<sup>424</sup> World Bank, *Annual Report 1980*, Washington D.C., 1980. Pg.19

<sup>425</sup> Kraske, J., Galambos, L., Milobsky, D., *Interview with Ernest Stern*, The World Bank Group Historian's Office, Oral History Program, January 5<sup>th</sup> 1995. Pg.28

<sup>426</sup> Kraske, J., Galambos, L., Milobsky, D., *Transcript of Interview with Ernest Stern*, January 5<sup>th</sup> 1995.

programs aimed at raising the productivity of the poor on the basis of comprehensive analysis of the situations of individual borrowers – providing external support on a program basis to countries willing to take ‘hard decisions’ to achieve internal structural adjustment before balance of payments problems arose.<sup>427</sup>

Those countries, he argued, had to implement effective policies to accelerate agricultural growth rates, and rates of saving and reinvestment. Growth was a basic essential, and developing countries should make every effort to increase it, but they must also develop “...their own plans of action to provide specific improvements in the standard of life of the absolute poor...” The major effort would come from developing countries themselves as “...no amount of outside assistance from the international community can substitute for determined internal efforts by individual developing societies.”<sup>428</sup>

The development decades had failed, even though growth targets had been met. It was time, McNamara argued, that the developing world acknowledged responsibility for this failure. The Bank could offer quantitative targets for the assessment of progress, and a framework for national programmes of action – but the primary responsibility for the governance of the international order should be taken on by the developing world in ensuring that their own policy frameworks reflected their comparative advantage.<sup>429</sup>

Opening the age of ‘structural adjustment’ with this claim appears paradoxical in view of the extent to which the political economy of borrowing members would be shaped by acceptance of the Bank’s strictures. Gaining the ability to influence policy had long been considered the most important objective in the relationship between Bank and applicant, as far as McNamara had been concerned. This was due entirely to the necessity of making ‘basic needs’ lending for activities which were not directly productive legible to the Bank’s financial backers.

## Conclusion

In this chapter I have argued that like the foundation of the Bretton Woods order, the development of neoliberal strategies was not a radical break from previous practices. It was not exclusively driven from outside the Bank, nor was it driven solely from within by a powerful figure on a moral crusade. McNamara’s Bank was not a philanthropic organisation, as

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<sup>427</sup>IBRD, IFC, IDA, 1979 Annual Meetings of the Boards of Governors, Summary Proceedings, Belgrade, Yugoslavia, October 2-5 1979, Washington D.C, December 1979. Annual Address by Robert S. McNamara, President of the World Bank. Pg.34-8

<sup>428</sup> Ibid. Pg.29

<sup>429</sup> Ibid. Pg.30-40

he was keen to demonstrate. The transformation of the Bank and its strategies were the outcome of the application of quantitative techniques of scientific management to redistributive 'basic needs' lending programmes, in order to make non-productive lending legible to financiers. The technology of the 1960s was no longer functional: it did not give the Bank the capacity to govern while executing its new programme while continuing to meet the institutional imperatives which followed from its social anchoring in US finance. This is clear from the cases of Brazil, Cote d'Ivoire, and most dramatically in Mobutu's Zaire. Rehabilitating the program loan furnished the Bank with the capacity to apply its conditionalities at the macro-economic level. Among the poorest borrowers, 'Basic Needs' had looked like 'structural adjustment' from the outset. From this perspective, the Bank emerges as more than the vehicle for the operationalisation of the political interests of dominant class fractions or ascendant epistemic communities.

While the Bank's reliance on financial capital did afford it a degree of autonomy from the US, drawing capital from these sources required adopting managerial practices that were derived from elite academia, and were common to large TNCs and the US government. This also tied it ever more closely to a commercial lending model, which required tougher conditionalities.

The rapid growth of the Euromarkets and the release of the dollar from its gold standard constraints had enormous implications for individuals, firms, and sovereign borrowers. Through their pension funds and bank deposits as well as the bond issues of national states and the World Bank, the financial affairs of ordinary savers and pensioners were linked to a globalising network of commercial and investment banks, multinational corporations, sovereign debtors, and international financial institutions. As the crisis of the 1980s unfolded, private financiers faced huge losses in the developing world, and the US government faced the collapse of the international banking system upon which its position in the monetary and financial order depended. To preserve this deep set of linkages, in 1985, the US government was able to seize upon the legible strategies and powerful tools for political intervention with which the Bank had redeveloped its capacity to meet its institutional imperatives and contribute to the governance of the international order across the preceding decade.

The defining techniques of neoliberal governance were not developed via institutional capture by the Wall Street-Treasury Nexus or the generation of a neoliberal culture by internal norm entrepreneurs. The novel technology of governance which McNamara brought with him was not a direct product of the needs of 'the market', but it spoke clearly to the Bank's investors. Neoliberal governance was a development of an institutional order. It was the

agency of Bank management, which, in managing these requirements while simultaneously meeting its own organisational imperatives, enabled the World Bank Group of the 1980s to step back into the liquidity-providing and financial discipline-enforcing role of the IBRD of the 1940s.

## Conclusion

The central claim of this thesis is that the Bank has never been a passive recipient of the American hegemonic agenda. Its ability to express the ideological preferences and strategic governance objectives of the US in a straightforward fashion is often taken for granted. In particular, the development of the structural adjustment loan is presented as emblematic of the ability of the US to use the Bank to meet its objectives: the 'Washington Consensus' is persistently interpreted as a product of US hegemony. Yet Bank management has charted a pragmatic course of its own. What this thesis shows is that US hegemony cannot be understood without the agency of the Bank.

There are two levels at which I articulate this claim. Firstly, anchoring the Bank in private American finance means that the relationship between the Bank and the US is defined by the growing reliance of the World Bank on access to US capital markets. The imperatives of financiers shape the strategy of the bank, and thereby frame the limits of its capacity to act on the US agenda. The second relates to the managerial practices of the Bank. The agency of Bank management emerges through the pragmatic negotiation of the institutional imperatives which follow from its social anchoring. While in pursuit of the Bank's institutional imperatives, management agency has been crucial in designing the tools through which American hegemony has historically been realised.

In respect of the first of these claims, it is clear that financiers did not attend Bretton Woods in the quasi-official capacity in which they attended the Brussels and Genoa conferences of the 1920s. But as I have shown, the outcome of the Bretton Woods conference was very vague and highly conservative. This was in line with the Roosevelt administration's vision of how the Bank should work in practice – which was far removed from what the institution would become. I argue that the development of the Bank can only be understood in terms of its reliance upon US financial markets. It should be considered an attempt to capitalise upon the deeply socially embedded infrastructure of financial relationships which were unique to the American political economy of the era. Yet this observation is frequently obscured by the mythology of the Bretton Woods conference. The achievements of the delegates at the conference itself have been widely overstated in support of a narrative that insists that the creation of new institutions through which the US would govern the international order expressed a social-democratic political vision, in which financial capital was subordinated to the needs of the real economy. As I have illustrated, in the 1940s, while financiers were displaced from the quasi-official roles they had held during the international



conferences of the 1920s and in the development of the Dawes plan; it was neither possible nor strategically desirable for the New Deal administration to negate the infrastructural power of finance. Drawing upon the deep reserves of liquidity created by mass participation in financial relations was explicitly envisaged from the outset.

The only question was how. The nuts and bolts of the new international order were not worked out at Bretton Woods. Understandings of what would actually be done to re-inflate the international economy remained fluid throughout the period of the negotiation of the Act, its ratification and even after the first annual meeting in Savannah. The 'blueprint' for the Bank, such as it was, drew upon the heritage of private financial planning which had shaped the 1920s - and recognised that American private financial capital would play a central role in the development and operation of the new dollar-based international order. But the specific practices of lending and structure of the Bank's governance had still to be worked out after the first annual meeting.

The way in which these questions were answered reflected the gradual apprehension of the practical implications of anchoring the Bank in the infrastructure of American finance. The limits of the Bank's capacity to act on the basis of state capital alone were rapidly made clear: European members were unable and unwilling to pay in the capital they had committed. Further, the Truman administration's objectives in relation to the Bank were far more ambitious than Roosevelt's. Linking American security and development, the Truman doctrine demanded that the Bank expand its operations rapidly beyond the borders of Europe. But the American contribution, though famously large enough to pay for a veto, would soon be exhausted. The illiquidity of the immediate post-war context would require, as in the 1920s, the enlistment of American financiers and through them, access to the liquidity of the unique infrastructure of the American financial system.

Making the machinery of Bretton Woods actually work towards the Truman Doctrine depended on the direct involvement of financiers in capitalising the Bank. The impact of this was visible immediately, in the transfer of operational control to the Bank's own management team during the struggle over the Chilean loan. With the operation of the Bank predicated upon its ability to access private capital, its viability as an organ of governance was predicated upon its creditworthiness. Affirming this required the Executive Directors to submit to the shift of control of day-to-day operations from their hands to the Bank's own newly-appointed management team of Wall Street lawyers and bankers. With this move, the infrastructural power of American finance was institutionalised at the international level.

From this point, the imperatives of American financiers became an important constitutive element of the imperatives of the Bank. The hegemonic agenda of the US during

the Truman and Eisenhower era required the Bank to expand its operations in support of security and anti-communist objectives. This required the Bank to borrow more – and in order to achieve this, it had to remain creditworthy. Therefore, the second claim I make in this thesis is that the technologies of management which the Bank deployed were designed by management in response to the imperative to render the Bank's agenda legible to the financial interests in which the institution was socially anchored.

We may be tempted to assume that the Bank's reliance on private US financial capital that this enabled financiers to direct the Bank's strategy. Although management were concerned to tap financial markets, they had to work hard to overcome the reluctance of financiers to invest. While the major representative organs of the financial community such as the American Bankers' Association had backed the Bank during the Congressional hearings on the Bretton Woods act, management had to undertake an intensive public relations campaign, lobbying to change the law to permit commercial banks to hold the IBRD's paper on a state-by-state basis. Although the Bank saw enthusiasm for its paper gradually build, even after obtaining the AAA rating in 1958 management still had to work to keep financiers engaged. I argue that this is a crucial causative factor in McNamara's experimentation with techniques of scientific management. Developing the quantitative data gathering mechanisms was designed to render every aspect of the Bank's activities transparent and legible to the mathematical modellers of Wall Street. As I have shown, these were crucial steps in the direction of structural adjustment lending.

The two major shifts which the Bank has made in this respect – from 'programme' to 'project' model during the 1950s, and from 'project' to 'structural adjustment' in the 1970s – should both be understood in terms of management's agency toward this end. The requirements placed upon the Bank to act in support of US hegemony had to be met within the parameters of financial imperatives. The impact of this was that the forms which the practices of lending took were not simply one choice from a number of possible options in this regard. This is particularly clear in the case of structural adjustment lending, but it may also be claimed to hold for the project approach.

The project model became by far the dominant mode of lending after 1958 once the twin objectives of achieving the AAA credit rating and diversifying the Bank's sources of borrowing had been achieved, until the development of structural adjustment lending during the 1970s. The purpose of the project approach was specifically to appeal to financiers – since it was a familiar model which evaluated potential investments in the same way as commercial banks. Prior to 1958, the strategic interests of the Bank, its financial backers, and the US, converged around the achievement of multilateral convertibility. Bank management was able

to satisfy the US agenda through strategic project lending to Yugoslavia, and financial interests by strategic-non lending to enforce financial discipline on Greece, while offering lax programme lending to Australia in order to help re-orient it toward the dollar and hasten the demise of the sterling bloc.

The Bank's imperative, underlying all of these, was the ability to unlock the subscriptions it was owed by its members which were outstanding due to the cumbersome monetary arrangements of the pre-'58 order. Although its contribution toward the achievement of multilateral convertibility should not be overstated, the Bank had a further strong interest in its achievement. With the re-opening of European capital markets, it was able to market its bonds outside the US for the first time – diversifying its potential sources of liquidity and safeguarding its operating capital in the event of the closure of the New York markets. Bank management did not only design the Bank's practice in response to the strategic concerns of financiers, but it also deployed its lending strategies pragmatically in order to meet financial imperatives and those of the Truman doctrine.

During this period we are able to see the interrelation of financial imperatives and the structure and practice of the Bank clearly. As I have shown, the Bank's role in the governance of the post-war international order was threatened in this period by the potential foundation of a competitor under the auspices of the UN. As this had the potential to subvert the anti-communist objectives of US foreign economic policy, the Bank was required to find a way to respond, within the parameters of the imperatives set by financiers. Management were able support the US agenda by founding two affiliates to offer lending on a more concessional basis. Concessional lending would have damaged the Bank's creditworthiness, and thereby potentially derailed its pursuit of its major strategic objective, the diversification of its capital base. The most important feature of these was that they were legally distinct entities, whose operations were funded through direct contributions by member states. This was not a 'turn to development'. It was a defensive action by management aimed at securing the apparatus of governance in support of US hegemony while maintaining the Bank's creditworthiness.

The limits to the project approach were exposed in the later 1960s and early 1970s by the same dynamics which had enabled the Bank to expand its borrowing and diversify its creditor base following the attainment of multilateral convertibility. The Bank's imperatives remained the same – but the changing political economic context demanded that management develop new tools with which to meet them. As in the 1950s, the Bank's centrality to the international governance apparatus was threatened – but in this case, by the ability of members to bypass the Bank and borrow directly in the Eurocurrency markets on their own account.

It is McNamara's response to the dynamics of the declining Bretton Woods system that enables us to reconceptualise the Washington Consensus. In arguing this point, I am not attempting to deny the nature of the political shift which was beginning to become visible in this era. But the Bank's response to the problems posed to the institution by the dynamics of the expansion of the Eurocurrency markets opened the way to the development of new institutional capacities – and ultimately laid the foundations for the possibility of the forms of governance which have become familiar as the 'Washington Consensus'.

In order to return the Bank to a central position in the governance apparatus, McNamara's intention was to expand the Bank's borrowing in order to facilitate a massively enlarged lending campaign in rural agriculture and education. The 'basic needs' programme was designed to reinvigorate 'development lending', and foster redistributive spending on education and agriculture projects that were not directly productive. Here, the Bank ran up against the limits posed by its basis in private financial capital – in the most clearly communicable way possible, through a disastrous bond issue.

The transformations which McNamara made to the Bank in order to make these indirectly productive investments legible to the Bank's financial backers as safe and profitable required management to effect two major transformations. These transformations were significant steps in the direction of structural adjustment. Firstly, the Bank had to be reorganised. To this end, McNamara deployed the tools of the RAND corporation, which he had learned at the Pentagon: systems analysis, and the foundation of a programming and budgeting unit which would generate large volumes of statistical data about the Bank's operations in the field and in Washington. These tools, as the cutting edge of American management science, allied to the transformation of the Bank into the structure of a standard multidivisional corporation, would make the new model legible to investors. Secondly, the enhanced ability to control the Bank's operations had to be reflected in the leverage the Bank could project over the macroeconomic policy settings of the borrower. Essentially, the 'basic needs' model and the project model were incompatible with the Bank's requirements. The primary criterion for its replacement was that it would facilitate the sectoral restructuring that 'basic needs' and 'redistribution with growth' demanded, and communicate the overall soundness of the investment to financiers. The only technology which could meet these criteria within the parameters set by the financial community in which the Bank was anchored, was conditional programme lending. Rehabilitating the programme model which the Bank had discarded as its principal lending strategy in the 1950s was essential, as it was the only technology which offered the scope for macroeconomic conditionality which the Bank's creditworthiness demanded. With these steps, McNamara had established the structure of

organisational control and the macroeconomic conditionalities which would become familiar as structural adjustment lending after 1980.

At each point in this transition, the limits to the Bank's capacity to pursue the agenda of governance are clearly visible, as are the limits to the agency of management in defining the nature of the tools through which the agenda of governance could be pursued. However, it should be clear that the turn to structural adjustment was not, any more than the project model, an extension of American ideology or policy. It is clear that the norm entrepreneurs of the 1970s behind the turn to structural adjustment espoused an agenda which was pro-free trade, pro-free capital movement, pro-private sector, and anti-state in general - in a way which coincided with the Washington Consensus agenda of the 1980s and 1990s. Structural adjustment lending was a practice which McNamara's VP Ernie Stern - who would remain a defining figure of the Washington Consensus era during the Clausen, Conable, and Preston presidencies - advocated strongly. But however well-suited it was for enforcing the austerity programmes the Baker Plan demanded, structural adjustment was not an off-the-shelf market-oriented US imposition.

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