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Volume Author/Editor: Walther P. Michael

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Chapter Author: Walther P. Michael

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4

THE PATTERN OF CAPITAL MOVEMENTS, 1950–54

We now proceed to the discussion of the pattern of capital flows during the period 1950–54. In the first four sections of this chapter the relative shares of the sources of the supply and the distribution of the various types of capital are considered. This discussion is based on Table 1 and on Appendix Tables B-I through B-VII, covering the individual types of capital. The next section discusses to what extent the capital supply of the United States, the United Kingdom, and the Continental countries of Group 1 was concentrated in the countries of the respective trade orientations. Differences in the composition of the capital supply of the U.K. and the Continent are also discussed. The last section of this chapter examines the distribution of government aid and private investment between the advanced and the underdeveloped countries.

An Over-All View

Total capital flows for the five-year period are shown in Table 1. As can be seen, the bulk of all capital was provided by the industrial countries (Group 1). If one eliminates the International Institutions as independent suppliers (since they were more or less intermediaries through which funds largely provided by Group 1 were channeled),[1] Group 1 supplied close to 90 per cent. For government capital and the major types of private long-term capital the percentages are even higher, from 92 to 96 per cent. But short-term movements flowing to Group 1 from the other groups raise the share of the latter to 10 per cent. These flows consisted mainly of increases in the dollar re-

[1] The European Institutions have been eliminated from Table 1 as independent suppliers (see the notes to Table 1).

serves and other liquid assets of all three of these groups and of a $2 billion growth in the colonial sterling balances (Group 4).

The United States provided over half of all capital (55 per cent if the institutions serving as intermediaries are excluded), the United Kingdom approximately 9 per cent, and the Continent and Japan over 25 per cent. In the share of the Continent and Japan short-term movements again play a considerable part. These movements consisted of two flows: one within Group 1 to the U.S. in the form of an increase in dollar reserves and other liquid assets of $3.5 billion (of which Japan accounted for $.6 billion); the other consisting—apart from EPU financing within Europe—mainly of export credits and payments agreement balances extended to the other three groups. The Continental credits, on the order of $1 billion, went mainly to developing countries in Group 3, while Japan's ($200 million) went to Far Eastern countries in Group 4. On the other hand, the United States and the United Kingdom, as "key currency" countries, experienced more moderate changes in their liquid currency assets; and short-term credit extended by the U.S. was comparatively small, while that of the U.K. decreased. The U.S. and U.K. were also the main recipients of funds for repayments, redemptions, and repatriations, which reduced their long-term capital outflows accordingly. The share of the U.S. in the supply of grants and gross long-term capital and that of the U.K. in the supply of private investment were thus considerably larger than the over-all percentages indicate[2]; the shares of the Continent were correspondingly smaller. Japan provided virtually no long-term capital or grants during this period.

Aside from movements of reserve balances, the capital provided by lenders outside Group 1 was supplied mainly by Group 2. It consisted of direct investment in all groups, the largest of which was, however, Canadian investment in the United States. Another component was the grants extended by Canada, Australia, and New Zealand under the Colombo Plan to Asian countries in Group 4. Among the Scandinavian countries, Finland paid reparations, and Sweden extended a large loan, to Russia. But all these flows, other than the Canadian investment, amounted to no more than one per

[2] The U.S. shares of grants and direct investment, the largest types of supply, were 80 and 60 per cent, respectively; the U.K. supplied 21 per cent of direct investment.

cent of the total. As lenders, except to Group 1, the other groups were therefore unimportant.

Virtually all of the capital provided to the rest of the world thus came from the industrial countries of Group 1. The capital supply of the United States was, however, the only one with global dimensions. Almost all countries received U.S. aid of some kind, and almost as many attracted American private investment. The capital supplied by the U.K. and the Continent was not only smaller, but also went to far fewer recipients.

The Distribution of Government Grants and Loans

Government grants and loans are shown in Appendix Tables B-I and B-Ia.[8] Government capital exceeded private investment in the total supply and in the supply to all groups except Group 2. The United States accounted for almost three-fourths of total government capital supplied. While U.S. government capital had many aspects and wide geographical distribution, the political forces of the time led to a high concentration of U.S. aid in several areas. The prime concern was still with European recovery, followed by mutual security and military build-up in the later part of the period. Close to 60 per cent of total U.S. aid consequently went to the industrial countries, Western Europe, and Japan (Group 1). A substantial part of U.S. grants and loans flowing to Group 2 was likewise in this category: recovery and mutual security aid to Scandinavia and loans for the production of strategic materials to Sterling Area countries.

While government aid for the development of backward countries had already been recognized as a necessary policy, the larger part of U.S. aid to the underdeveloped areas consisted also of aid for reconstruction and military emergencies. Of the countries of Group 3, those in Southeast Europe on the periphery of the Soviet bloc received the greater part of U.S. aid (Greece, Turkey, and Yugoslavia). Of the

[8] In Appendix Table B-I, grants and loans net of repayments are shown, while Appendix Table B-Ia gives grants and gross loans. In Appendix Table B-Ia grants and loans are classified by types and purposes. There are, of course, no sharp dividing lines between some of the categories. The distinction between aid to "strategic countries," where large aid was given in response to urgent cold war emergencies, and that to Iran and India ("development aid"), for instance, is perhaps one of degree only.

countries in Group 4, those in the Far East received the most (Korea, Taiwan, Philippines, and Indochina). What might be called "pure" development aid constituted only $2.1 billion, or 15 per cent of the total U.S. government capital supply of $14.7 billion during this period. The greater part of it, moreover, was in the form of loans, while most other U.S. aid was in the form of grants.[4]

U.S. aid to Europe may be said, however, to have done double duty. First, it gave rise to intra-European aid, which was directly induced by, and largely contingent upon, American aid. Second, it enabled the European countries to provide aid outside the OEEC region. The metropolitan powers supplied substantial aid to their dependencies. Aid received from the U.S. was far in excess of the aid extended by European countries, except in the case of France; even in this case, however, U.S. aid came close to the exceptionally large metropolitan aid. While the European aid also included emergency aid, like British aid to Malaya, it was largely development aid, and the combined European supply of this type of aid was absolutely larger than the corresponding American aid. Thus, although the pure development aid of the United States itself was small, the aid to Europe helped to generate aid to underdeveloped areas.

Relatively few independent countries received aid from European governments, apart from British-French participation in aid to Yugoslavia. What there was, moreover, consisted largely of contractual obligations, such as German and Italian reparations to Israel, Greece, and Yugoslavia. Virtually no European aid was extended to Europe's former colonies or spheres of influence in Asia and the Middle East. It was to these countries that the United States extended the larger part of its development aid, assuming to some extent responsibilities that had been vacated by the former colonial powers. The Greek-Turkish aid program is a celebrated example, but the pattern was widespread. Colombo Plan aid by Canada and Oceania also fulfilled this role.

On the other hand, the traditional American sphere of interest, Latin America, received only a small part of the development aid dispensed by the United States, and virtually all of it was in the form of loans, mainly Export-Import Bank loans. This Latin American aid, moreover, clearly contained the element of export promotion. Many

[4] See the recapitulation in Appendix Table B-Ib.

of the loan commitments dated back to the early 1940's before aid had become an official policy. Both in kinds of projects and in country distribution they were akin to the commercial loans of the period.[5] While total U.S. development aid was inversely related to the level of development, i.e., the absolute amounts increased from Group 2 downward,[6] much of the aid to Latin America went to the advanced countries of the region. All the Latin American countries in Groups 2 and 3 borrowed from the U.S., while only four of the eleven in Group 4 did so. This distribution is similar to that of private loans, which also covered the export of American equipment to the developing, rather than the underdeveloped, among these nations.

Aid by the International Institutions, IBRD loans, and UN grants constituted only 7 per cent of the total, of which IBRD loans accounted for two-thirds. While the first loans of the Bank had been for European reconstruction, during this period IBRD loans were made mainly for development, and the share of Group 1 was only 8 per cent. In the other groups the advanced countries were, however, the chief borrowers. The shares declined with the level of development, Groups 2, 3, and 4 receiving 44, 30, and 17 per cent, respectively, as did the ratio of the number of borrowers to member countries in each group.[7] The average size of the loans was also several times larger in Groups 2 and 3 than in Group 4. IBRD loans, the granting of which depends on the existence of well-planned, economically feasible projects, thus went mainly to more advanced countries which had a greater abundance of such projects. In view of this problem, the Bank had already instituted a policy of aiding underdeveloped countries, through technical missions, to plan feasible projects.[8] But the results of this policy were not reflected in the distribution until the later 1950's when close to half of the total amount of loans was made to Group 4. During the earlier period, the Bank provided, in effect, capital for expansion

[5] Over one-third of the Latin American aid total, a $300 million Export-Import Bank loan to Brazil, was in fact for the purpose of funding short-term debts to American exporters, i.e., for trade which had already taken place.

[6] See p. 79, below.

[7] In Group 2, 8 of 11 members borrowed; in Group 3, 5 out of 10; in Group 4, 10 out of 25. Moreover, the nonborrowers in Group 2 were Canada, which was not eligible since it had unlimited access to the market, and Sweden and Denmark, which were receiving American aid.

[8] For a discussion of the early policies of the IBRD, see Raymond F. Mikesell, *United States Economic Policy and International Relations,* New York, 1952, pp. 199–206.

of the overhead sector of the countries which also received, as we shall see, large manufacturing investment. The loans thus performed mainly the function of complementing private investment in those countries where it was concentrated rather than substituting for it in the least developed countries.

UN grants were of even less importance as aid to underdeveloped areas. Apart from Korean relief, they consisted, to a large degree, of refugee aid, mainly in Europe and the Arab countries. Since in the latter case the aid was in the form of imports for the refugee camps, it probably had little effect on the countries concerned (with the possible exception of Jordan where the refugees were somewhat more integrated with the economy). Economic and technical assistance was small. UN aid was thus more humanitarian than economic in nature, and the amount going to the underdeveloped countries themselves made up only a small fraction of their aid receipts.

The Distribution of Private Long-Term Capital

PORTFOLIO INVESTMENT

Portfolio investment, i.e., the underwriting of foreign securities in the financial centers ("Issues" in Appendix Table B-II), the chief form of international lending prior to the depression of the 1930's, did not regain its previous importance after the war. It accounted for only 20 per cent of the total private investment during this period, while direct investment made up 70 per cent and loans extended by the private sector, 10 per cent. The obstacles to the revival of portfolio investment lay in the widespread defaults of the interwar period and the restrictions on lending in European markets. To some degree the lack of demand by countries receiving large-scale aid also seems to have played a role, particularly in the case of the Western European countries. These countries borrowed only moderately in the Swiss market during this period, while they had floated some issues in New York before the Marshall Plan and did so more extensively after aid had ceased in the second half of the 1950's.

The underwriting of new issues was, therefore, highly selective. Apart from the issues of the IBRD (which was, of course, established because of the expected dearth of portfolio lending, and whose own

borrowings accounted for more than one-fifth of total new issues), the issues of independent countries and those of the dependent territories must be distinguished. The latter were floated under favorable conditions in the metropolitan markets[9] and served largely to supplement aid (particularly in the British colonies and the Congo), but accounted for only one-fourth of the total (excluding IBRD issues).

Among independent countries, the advanced countries were the chief borrowers, with the countries of Group 2 more prominent than the industrial countries. Nine of the fifteen countries in this group were borrowers (three in two markets) compared to six in all other groups. Only two small new issues were floated by underdeveloped countries, Peru and Ceylon (the Panamanian issue represented refunding). Group 2, with 70 per cent of the total (excluding the IBRD), had the largest share in all of the three main markets where independent countries could or did borrow: the U.S., the U.K., and Switzerland. In the U.S., where Group 2 countries were the only borrowers, Canada and Israel accounted for most of the money raised. One may argue that these represent special cases, in that Canadian securities are not considered "foreign" by American investors,[10] and the Israeli issues had an emotional appeal. Yet the high economic level of Canada is, of course, responsible for the investors' attitudes, while the large inflow of skilled labor and managerial ability into Israel represents a condition that is absent in underdeveloped countries. The advanced economic level of these borrowers must be considered a precondition for their access to the market.

For balance-of-payments reasons, the British capital market was virtually restricted to the Sterling Area, but the domestic demands on the market curbed lending there also. Apart from the colonial and Rhodesian government issues, lending was confined to investment that would aid the balance of payments.[11] Under this criterion, mainly enterprises in the advanced sterling countries seem to have qualified,

[9] See, e.g., OEEC, *Sixth Report of the OEEC,* Paris, March 1955, Vol. II, p. 215.

[10] See Hal B. Lary and associates, *The United States in the World Economy,* U.S. Department of Commerce, 1943, p. 94; Ilse Mintz, *Deterioration in the Quality of Foreign Bonds Issued in the United States, 1920–1930,* New York, NBER, 1951, p. 10; and Paul Meek in *U.S. Private and Government Investment Abroad,* Raymond F. Mikesell, ed., Eugene, Ore., 1962, p. 241.

[11] *Midland Bank Review,* February 1952, p. 12; 1954, p. 12.

particularly the South African and Rhodesian mining companies with long-established markets.

With the exception of Switzerland, the Continental markets were generally closed to outsiders (except the dependencies) because of the domestic demand for reconstruction and balance-of-payments pressures.[12] While there were few restrictions in Switzerland until later,[13] the experience of defaults and unsatisfactory prewar debt agreements [14] also confined Swiss lending chiefly to advanced countries.

The outstanding securities that were bought (the positive entries for "Redemptions and Trading" in Appendix Table B-II) were also mainly those of the advanced countries, particularly those of the United States and Canada and, to a lesser extent, of Group 2 sterling countries.[15] Substantial purchases were also made of a few international blue chips, chiefly shares of the Shell group (in the Netherlands and the U.K.), British Petroleum (in the U.K.), and South African mining companies.[16]

While even among the advanced countries there were few whose securities were bought, among the underdeveloped there were fewer still, and most of the amounts were extremely small. Moreover, for the most part, these purchases do not seem to have been genuine portfolio transactions, but rather were connected with direct investment or were a by-product of other transactions. In the case of India, for instance, where the largest security purchases in Groups 3 and 4 were made, the amounts partly represent purchases of subsidiaries'

[12] The French and Italian markets were completely closed to outsiders, and the Dutch until 1954 (Paul Meek, "The Revival of International Capital Markets," *American Economic Review,* May 1960, p. 286; and UN, *The International Flow of Private Capital, 1956–1958,* New York, 1959, p. 65). The Dutch IBRD issue was floated in that year. There was possibly also a small issue by Surinam and one by the Belgian government, perhaps included in government loans.

[13] During the Suez crisis from 1956–58 the Swiss market was closed to foreign borrowers (see UN, *op. cit.,* p. 62); afterwards foreign access was rationed (see Charles P. Kindleberger, "European Economic Integration and the Development of a Single Financial Center for Long-Term Capital," *Weltwirtschaftliches Archiv,* Band 90, 1963, p. 200).

[14] See "Swiss Capital for Export," *Three Banks Review,* September 1951.

[15] Since the data for Redemptions and Trading in Table B-II are net totals for the five-year period, large redemptions or sales conceal substantial purchases in several cases, apparent from annual totals or other data, viz., Canada, where U.S. purchases were upward of $400 million; U.K. (by U.S., $26 million); and Australia and Rhodesia (by U.K., $23 and $11 million).

[16] See Paul Meek in *U.S. Private and Government Investment Abroad, op. cit.,* p. 247, and in *American Economic Review,* May 1960, p. 284.

obligations by foreign parent companies or by other buyers of the parent's nationality, and partly represent credit (by accepting shares) extended by foreign suppliers of machinery and equipment to Indian companies.[17] Acquisitions of securities are also the by-product of technical assistance when it is paid for in the shares of the assisted foreign enterprise.[18] Portfolio purchases in the ordinary sense were thus negligible in underdeveloped countries.

In brief, portfolio investment provided development capital only for the dependencies, not for the independent underdeveloped countries. How much access even the territories will have to the markets after independence remains to be seen.

DIRECT INVESTMENT

In contrast to portfolio lending, direct investment (Appendix Table B-III) was widely dispersed. The dispersion was greatest in the case of the United States, which accounted for 60 per cent of the total. While almost all countries received direct investment, it was the advanced countries (Groups 1 and 2) that attracted almost 70 per cent of the total.[19] Substantial investment was made in the industrial countries themselves, both by the U.S. in Europe, and by the latter in the U.S. There was also large Canadian investment in the U.S. and, to a smaller degree, Canadian investment in the United Kingdom. Intra-European investment was comparatively small, on the other hand, much smaller than trans-Atlantic investment by Europeans.

All the same, the direct investment capital inflow to Group 1 amounted to less than one-fourth of total direct investment. Group 2 again attracted the largest share, almost half of the total. Both the United States and the United Kingdom made their largest investments in the countries of this group—the U.S. in Canada, and the U.K. in the sterling countries, particularly in Australia and South Africa. It was characteristic of direct investment, moreover, that countries attracting large investments from the center of their trade-

[17] See Reserve Bank of India, *Report on the Survey of India's Foreign Liabilities and Assets as on 31st December 1953,* Bombay, 1955, pp. 11–12, 84; and *Report . . . 31st December 1955,* Bombay, 1957, p. 11.

[18] See Jack N. Behrman, "Promoting Free World Economic Development Through Direct Investment," *American Economic Review,* May 1960, p. 271.

[19] The distribution of receipts by groups was: Group 1, 24.3 per cent; Group 2, 44.6 per cent; Group 3, 12.6 per cent; Group 4, 18.5 per cent (of which the Overseas Territories accounted for 9 per cent).

orientation often received additional direct investments from other sources, except in cases where the investment was primarily or exclusively in primary production. Thus, Canada attracted substantial investment from the U.K. and the Continent; the sterling countries from the U.S., the Continent, and each other. The large share of Group 2, therefore, was not only due to the very large U.S.-Canadian investment, but also to the fact that these advanced countries were generally attractive to investors.

In the underdeveloped areas, the largest U.S. investment was made in the more advanced Latin American countries of Group 3, exceeding the combined American investment in all other underdeveloped areas. These countries, especially Mexico, also received additional investments from other sources. The main European investment in the underdeveloped areas went to the overseas territories, the British investment in the dependencies being the largest. Few European investments were made in the independent underdeveloped countries other than the Latin American countries of Group 3. India was the only country to receive substantial British investment, accompanied by American and other investment. The independent countries of Group 4 received the smallest share of U.S. investment and very little direct investment from other countries. Direct investment was highly trade-oriented, moreover, so that Latin American and other U.S.-oriented countries obtained most of the American funds that did move to Group 4.

We defer a discussion of the industrial composition of direct investment until later. The question of the extent to which the investment was made in production for the market of the host country and the extent to which it consisted of investment in raw material production for export helps to explain the distribution between groups described above. This question will be treated below, where capital flows in relation to levels of development are considered in more detail.

PRIVATE LOANS

Loans by the private sector (shown in Appendix Table B-IV) were typically of intermediate-term maturities and largely offset by repayments. They were thus not a major vehicle for long-term capital transfers. The lenders were mainly American, Swiss, and other European banks (accounting for two-thirds of the total), and approxi-

mately two-thirds were made to governments or were guaranteed by the government of the borrower. Some large movements occurred between private concerns, chiefly of advanced countries, and a few loans to underdeveloped countries were extended by American and European firms supplying equipment and materials to, or operating in, these countries.

The loans were extended mainly to industrial or other advanced countries (72 per cent to Groups 1 and 2). In part these loans were connected with recovery aid (e.g., Export-Import Bank–guaranteed loans to Japan), and in part they replaced it, as aid diminished in the later years of the period. Among the underdeveloped countries only a few of the more advanced Latin American countries received major loans. The share of Group 4 amounted to only 5 per cent of the total.

REDEMPTIONS AND REPATRIATIONS

To what degree did return flows of private capital modify the distribution of the supply? Redemptions by, and foreign sales to, the residents of the debtor country of portfolio securities (the negative entries in Appendix Table B-II) [20] were largest for Group 2, which was also the largest recipient of private capital. While a number of underdeveloped countries made such payments, these were substantial only in the case of Brazil, and they were generally larger for the more advanced countries than for the least developed.

There were other return flows which came mainly from Groups 3 and 4, however. We have called them Extraordinary Repatriations (shown in Appendix Table B-V) because they took place largely as a result of political events or under political pressure.[21] Apart from special movements (such as the liquidation of Italian investment in settlement of reparations and the sale of German real estate by former refugees when the proceeds became transferable), they were repatriations largely of British capital from Latin America and, in the wake of independence, from former colonies. They consisted of com-

[20] Although a separation of redemptions from trading in Appendix Table B-II was not possible, the negative entries mostly seem to represent redemptions. In the case of the United States, which reports receipts of redemptions by area, these amount to over 80 per cent of the total.

[21] These transactions are reported in the host countries' records or other sources with indications that the entries were of this kind. They do not include ordinary repatriations of investment, which are netted out in the appropriate types of capital.

pensation payments for nationalizations and proceeds of sales, often to the host governments, of railroads, utilities, and other enterprises largely engaged in primary production. In the case of former colonies they included the liquidation and transfer of savings of departing personnel.[22]

The repatriation of ownership of railroads and utilities, mainly of British investment in Latin America, represented part of a process which started after the war and included the well-known sale of the Argentine railroads in 1947 to the Argentine Government for over £250 million. Many of these enterprises had become unprofitable, it is true, and the owners were willing to sell.[23] But in view of the continuing nationalizations of American and European utilities in Argentina, Brazil, and Colombia, for instance, sometimes by seizure, sometimes after a rate increase had been refused, one can assume that the British firms would have suffered the same fate.

In former dependencies, on the other hand, unfavorable investment climates led also to liquidations of previously profitable agricultural enterprises, particularly in Ceylon and to some degree in India,[24] while nationalizations occurred in some other countries.

Compared to the direct investment made during this period, the repatriations were small. They resulted, however, in net capital outflows from a number of the U.K.-oriented countries of Group 4 and reduced the net receipts of others substantially. The Latin American repatriations constituted, together with the large sterling bond redemptions by Brazil, a withdrawal of British capital in an area which had once been a major field of British investment.

Short-Term Capital Movements

In a number of countries short-term inflows supplemented long-term capital receipts. These movements consisted of cumulative short-term credits and, in some cases, of substantial drawings on currency reserves.

[22] This accounts for three-fourths of the outflow from India, and for the repatriation from Indonesia.

[23] See "British Investment in Latin America," *Three Banks Review,* June 1949.

[24] For the conditions that led to sales and breakups of efficient tea estates and rubber plantations in Ceylon, see IBRD, *The Economic Development of Ceylon,* 1953, pp. 24–25, 75 ff., 143, 516. Regarding the liquidation and sales of foreign enterprises in India, see Reserve Bank of India, *op. cit.,* 1955, pp. 19–20.

SHORT-TERM CREDITS

As far as short-term credit represents the customary financing of international trade or results from trade through the time element involved in transportation and payments procedures, it consists of temporary financing rather than capital movements. With increasing trade such short-term credit outstanding must necessarily increase, but normally for both the assets and liabilities of a country. Appendix Table B-VI shows, therefore, net inflows or outflows by groups of countries and for individual countries with major transactions in order to indicate where cumulative inflows occurred.[25]

Such cumulative credits were on the order of $1.3 billion. The lenders were mainly Germany and other Continental countries (approximately $900 million) and the United States and Japan ($200 million each). The credits consisted partly of formal export credits, mainly in the case of the Continent, and partly of "forced" credits in the form of payment arrears resulting from a lack of foreign exchange (mainly in the case of credits extended by the U.S.) and of payment agreements balances (Continent and Japan). The chief recipients of the U.S. and Continental credits were the more advanced underdeveloped countries in Latin America and Southern Europe (Group 3), where rapid development induced such movements. Brazil and Turkey were particularly heavy borrowers. The Japanese credits, covering largely textile exports, went to Far Eastern countries, three-fourths of the amount to Indonesia.[26] The Continental credits considerably exceeded all other capital provided by the Continent outside

[25] Appendix Table B-VI shows an over-all discrepancy, after all possible adjustments, between changes in assets and liabilities of $1.2 billion. From the pattern of discrepancies between areas in the matrix constructed on the basis of the IMF area system (mentioned above in the explanation of Type VI), it appeared that close to $1 billion of the total discrepancy represents credits provided, but not reported, by the Continent, well over half of this amount by Germany. This conclusion is supported by the error items in the German and other Continental countries' balances of payments and by other evidence (see e.g., UN, *The International Flow of Private Capital, 1956–1958, op. cit.*, pp. 71–75; Paul Meek, *American Economic Review*, May 1960, p. 287). We concluded that the Continent, instead of the net inflow of residual credit of $105 million shown in Appendix Table B-VI, had a net outflow on the order of $900 million to the other groups, mainly Group 3. For a fuller explanation, see Walther P. Michael, *op. cit.*, Appendix B, Matrix IX, pp. 354–366.

[26] Over-all, however, Japan was a net borrower, receiving credits from, or falling in arrears to, the U.S. ($60 million) and Europe ($90 million) in addition to net purchases from the Fund. Indonesia, on the other hand, made large repayments, mainly to the Netherlands.

the dependencies. To a large degree the Continental capital supply was, therefore, directly connected with export promotion.[27] In the case of Japan these credits were virtually the only capital provided.

RESERVES AND CORRESPONDENT ACCOUNTS

The increase in reserves and other liquid assets (Appendix Table B-VII) during this period occurred largely in the holdings of the advanced countries. The later Marshall Plan aid was used, as is well known, to build up reserves in both dollars and gold. But other advanced countries also showed substantial increases. While the majority of the underdeveloped countries also increased their reserves, the increase by group becomes smaller toward Group 4 (excluding dependencies), where it was negative, and where two-thirds of the decreases occurred. The large decreases consisted mainly of reductions in sterling balances, a good part of which had been accumulated during, and blocked after, World War II, but were then gradually released by the United Kingdom.[28] Sterling accumulations of the later 1940's, particularly by Continental countries, were then also decreased, so that there was a net reduction in the liabilities of the United Kingdom to independent countries of $.5 billion.[29] While the cases of over-all decreases in reserves are thus partly due to the withdrawals of excessive and involuntarily held sterling balances, balance-of-payments pressures led also to reductions in dollar reserves in Brazil and some other countries.[30]

The case of Ireland is of special interest because the larger part of external finance for its development was provided by the liquidation of Irish assets abroad. To the reduction in sterling balances (commercial bank assets in this case) must be added large sales of British securities by Irish investors. A comprehensive development program by

[27] See Paul Meek, *op. cit.*

[28] At the end of 1949, some $3.6 billion of World War II balances were still blocked, over half belonging to India, with Egypt and Pakistan accounting for another fourth. See "Who holds the Sterling Balances?", *The Banker,* May 1950, pp. 93 ff.

[29] The large increase in the colonial sterling balances represents a special case, which is discussed below.

[30] See also IMF, *International Reserves and Liquidity,* Washington, D.C., 1958. "In some countries, such as India, the reduction in reserves represented heavy spending on development" (p. 51); ". . . many non-industrialized countries have decreased their reserves. In some countries these decreases were planned and used to finance development" (p. 92).

the government caused extensive domestic investment by the private sector which was financed to a considerable degree by these repatriations of private capital, which had been invested in Britain during years of economic stagnation at home.[31] The Irish case suggests that other flight capital, such as the billions of dollars of Latin American capital supposedly placed in the United States and Switzerland,[32] may return if political and monetary stability is achieved in such countries.

Substantial inflows of short-term capital thus occurred in a number of cases, both in the form of credit and by drawing on reserve balances or other liquid assets. For some countries, movements in one form were cancelled out, however, by changes in the other (e.g., Colombia received large credits, but increased its reserves by a similar amount; the reduction in India's sterling balances was largely offset by a credit outflow). For others, the net addition to the long-term capital inflow was relatively small. It was only in Ireland (counting the portfolio repatriation), Brazil, Turkey, Pakistan, and Egypt that the additions were substantial. For the underdeveloped countries as a whole, these short-term movements increased the capital supply only moderately and mainly for the more advanced of these countries. For Group 3 it meant an addition of approximately 20 per cent to the long-term inflow of government and private capital, but for the independent countries of Group 4 the addition was less than 3 per cent.

The large increase in the sterling balances of the British Colonies, on the other hand, had a drastic effect since it offset by far British aid and investment in the territories, resulting in a net outflow from the Colonies to the United Kingdom of $600 million. The larger part of the balances represented the collaterals of currency boards and the funds of marketing boards and other official bodies, which were required by statute to be held, wholly or partly, in sterling securities.[33] While all the various territories increased their balances, three-fourths of the total was accounted for by West Africa, the Malayan region,

[31] See Chapter 3, footnote 9. The following amounts are involved: U.S. aid, $79 million (Appendix Table B-I); U.K. purchases of Irish bonds, $44 million (Appendix Table B-II); total foreign capital, $123 million; repatriation—sales of British securities, $131 million (Appendix Table B-II), repatriation—reserves, $29 million (Appendix Table B-VII), total Irish repatriation, $160 million.

[32] See, e.g., "Economic Development in South America," *JEC*, 87th Congress, 2nd Session, Washington, D.C., 1962, p. 1.

[33] See Ida Greaves, *The Colonial Sterling Balances*, Essays in International Finance, No. 20, Princeton, 1954, *passim*.

and Hong Kong. In Hong Kong the increase seems to have been due to large inflows of refugee capital and gold hoardings from mainland China.[34] In West Africa and Malaya the large sterling accumulations were due to high commodity prices and relatively low ratios of capital formation to gross product.[35] Particularly in West Africa exceptionally high cocoa prices caused large increases in sterling balances. These areas received also less aid and investment than East and Central Africa and the West Indies, which had higher capital formation ratios. This suggests that the receipt of external finance does lead to higher capital formation even though domestic resources may be available. Development plans have to be made in advance and depend on the funds which are expected to be available in grants and loans in the London market. Budget surpluses which are the result of commodity price rises, on the other hand, cannot be foreseen. It may not be possible to accelerate development as a result of such windfalls. Surpluses of marketing boards resulting from price increases must be held as a safeguard against future price declines. The resources which these colonial sterling balances represent were thus not available, or could not be utilized immediately, for the purposes which external financing was designed to accomplish.

Capital Flows and Trade Orientations

In this section we examine to what extent the aid and investment of the three centers, the United States, the United Kingdom, and the Continental OEEC countries, were concentrated in the countries whose trade relations were oriented towards them.[36] Some of the reasons for the distribution of capital which we observed will also be discussed.

The distribution of the long-term capital flows of the three main suppliers according to trade orientation is shown in Table 3. Since we are interested in the distribution of the capital supplied during this period, repayments have been eliminated from the table, i.e., loans included in government capital and private loans are shown gross,

[34] See the *New York Times,* November 8, 1959, p. 7.

[35] See OEEC, *Economic Development of Overseas Countries and Territories Associated with OEEC Member Countries,* Paris, August 1958, pp. 249–265, where the question of the sterling balances is treated in detail and which the discussion here follows in part. The capital formation data are for 1956, but they are unlikely to have changed much, and a time lag between receipt of funds and investment must be considered.

[36] For the classification of countries by trade orientations, see Appendix Table A.

TABLE 3

Distribution of Long-Term Capital of Group 1 Countries by Trade Orientation

To	From: United States, Millions of Dollars	United States, Per Cent	United Kingdom, Millions of Dollars	United Kingdom, Per Cent	Continental OEEC, Millions of Dollars	Continental OEEC, Per Cent
U.S. and U.S.-oriented						
Government capital	3,226	22.5	107	10	139	4
Portfolio issues	1,175	99.0	–	–	19	4
Direct investment	4,936	72.0	625	25	678	53
Private loans	514	50.0	27	37	154	37
U.K. and U.K.-oriented						
Government capital	2,780	19.5	522	48.5	99	3
Portfolio issues	14	1.0	666	98.0	64	12
Direct investment	1,134	16.0	1,736	71.0	135	11
Private loans	212	20.0	46	63.0	17	4
Cont. OEEC and Cont. OEEC-oriented						
Government capital	8,218	58.0	447	41.5	3,057	93
Portfolio issues	–	–	14	2.0	428	84
Direct investment	795	12.0	98	4.0	460	36
Private loans	316	30.0	–	–	245	59

SOURCE: Matrix tables.

and redemptions and trading (Appendix Table B-II), consisting mainly of redemptions, and repatriations (Appendix Table B-V) have been excluded. For short-term credit the distribution could not be calculated.

The number of countries (including the countries of the centers themselves) in each of the three trade-orientations is approximately the same: twenty-seven in the U.S.-, twenty-six in the U.K.-, and twenty-nine in the Continental OEEC-oriented groups.[37] Thus, if the

[37] The British dependencies were counted as five units (Central Africa, West Africa, Western Hemisphere, Far East, Other); the French dependencies as three units (North Africa, Other Africa, Other); the Belgian, Dutch, Italian, and Portuguese dependencies as one unit each.

centers only supplied approximately one-third (or less) of a given type of capital to countries whose trade was oriented toward them, we would conclude that the distribution of this type of capital did not depend on the trade relationship of the recipient countries with the center. In Table 3 there are two of the twelve cases which fall in this category: the government capital of the U.S. and the direct investment of the Continent, where only 22.5 and 36 per cent, respectively, were supplied to their own trade orientations. In the other ten cases there was a definite concentration of the supply in the own trade orientations, ranging from approximately 50 to close to 100 per cent, which appears to indicate dependence on the trade orientation, although with considerable variation. In order to ascertain the reasons for the variation and to see how much meaning can be attached to the various percentages, we must examine the distribution of each type of capital more closely.

GOVERNMENT CAPITAL

The distribution of government capital may be assumed to depend on the political involvements of the donor country during the particular period. The small share of U.S.-oriented countries in American aid was, of course, the result of the global role which the United States had assumed. Recovery and mutual security aid to the Continental and Sterling OEEC countries was the major part, but American government capital went also to most other U.K.- and Continent-oriented countries. The share of the U.S.-oriented countries was thus less than one-fourth. A large part of this $3.2 billion, moreover, went to Far Eastern and other countries whose trade orientation toward the U.S. was, in considerable part, of recent origin and was, in fact, largely determined by this American aid, e.g., Korea, Taiwan, and Israel, where emergencies had arisen or new obligations had been assumed. Latin America, on the other hand, the traditional sphere of U.S. commercial interests, received only one-fourth of this amount.[38] Thus the global commitments which the United States assumed after World War II had the result that only a small share of American aid went to U.S.-oriented countries, particularly those in Latin America with the older trade ties to the U.S.

In the United Kingdom and the Continental OEEC countries, which

[38] See also the discussion on pp. 48–49 above.

had long-standing political and commercial ties with the colonial territories, the shares of countries oriented toward them were higher. In the case of the U.K. it was still less than half of the total, but in the case of the Continent it was over 90 per cent. British aid to the territories and to independent Sterling Area countries was relatively small. British grants and loans under the OEEC arrangements (IEPA and EPU grants and consolidation loans of payment arrears), aid to Yugoslavia, a loan to a Canadian corporation for the production of strategic materials, and various settlements with U.S.- and Continent-oriented countries accounted, therefore, for somewhat more than half of the U.K. total. Continental governments also had obligations to countries outside their own trade orientation (e.g., the German compensation payments to U.S.-oriented Israel). But the fact that grants and loans under OEEC arrangements were mainly extended between Continental countries and the large size of the French colonial aid (close to $2 billion) resulted in the high concentration of Continental government capital in their own trade-orientation group.

PORTFOLIO ISSUES

Portfolio lending showed a very high concentration in the trade orientations of all three centers. There seems to be no prima facie reason for this, however, since security flotations, largely funds raised by governments, do not necessarily finance trade directly and may not even be spent abroad. If there are no other constraints, interest rate differentials presumably determine the market in which a borrower floats an issue. In the past, the main financial centers, New York and London, had been global lenders. In the last peak period of portfolio lending, the decade of the 1920's, some fifty countries borrowed in New York.[39] The explanation of this high concentration during the 1950–54 period lies in the factors curbing portfolio lending mentioned previously, namely, the experience of defaults during the Depression, which resulted in very selective lending, and the restrictions of the European markets because of balance-of-payments pressures. The issues floated in the U.S. were thus virtually only those of the two special cases, Canada and Israel, while borrowing in the U.K. and in Continental metropolitan countries was mainly or entirely confined to their

[39] Ralph A. Young, *Handbook on American Underwriting of Foreign Securities*, U.S. Department of Commerce, Washington, D.C., pp. 11, 20, 75–137.

respective currency areas. The trade orientations underlie, of course, the currency areas, but it was the confinement of lending to the latter which was the determining factor. Switzerland alone resembled the markets of the past by lending to countries in all three trade orientations, although on a modest scale.

DIRECT INVESTMENT

Direct investment has a closer connection with trade than portfolio investment, since machinery and equipment for subsidiaries and branches are often supplied directly by the parent companies, investment in finance and trade are frequently connected with imports and exports, and investment in primary production is usually made for the purpose of supplying agricultural and mineral products to the center. Consequently we do find a fairly high concentration of this type of investment by the United States and the United Kingdom, the main suppliers, in countries of their respective trade orientations, although not for the smaller Continental investment. The high percentage in the case of the United States is of particular significance because, in contrast to the other lenders, the U.S. spread its investments very widely and the pattern is, therefore, less influenced by random factors. An industrial breakdown is also available for U.S. investment,[40] which makes it possible to ascertain the extent of the concentration by industrial sectors. In every sector over half of the investment was made in the U.S.-oriented countries, although with considerable variation in the percentages. The concentration was highest in primary production (agriculture, 100, petroleum exploration and extraction, 90, mining, 86 per cent) and in utilities and transportation (99 per cent). It was over 70 per cent in services (trade, 72, and other, 79 per cent), and it was least in manufacturing (61 per cent) and petroleum refining and distribution (51 per cent). This

[40] The *Survey of Current Business* provides breakdowns into seven sectors. Petroleum, which is reported as one sector, was divided into (1) exploration and extraction, and (2) refining and distribution, with information contained in the *Oil and Gas Journal*. This was done in order to separate (1) investment mainly for export from (2) investment for consumption in the host country. For major oil-producing countries the petroleum investment was considered to be entirely in exploration and extraction, since refineries in these countries mainly serve export.

In some cases where several sectors are combined in *Survey of Current Business* tables, the divisions were estimated from regional totals or other evidence. For references see Appendix B, Statistical Sources for Appendix Tables B-I to B-VII (United States).

variation is due to the fact that the investments in the different sectors were also dependent on the level of development of the countries in which they were made. In order to examine the relative importance of trade orientation and levels of development in the distribution, it is best to exclude Canada (Group 2, U.S.-oriented), which accounted for 42 per cent of total U.S. direct investment and for almost half of the investment in primary production. Its proximity to the United States was, one may assume, a more important factor than its level of development in attracting large investments in primary production. If Canada is excluded, still as much as 52 per cent of U.S. direct investment went to U.S.-oriented countries, but in manufacturing and petroleum refining and distribution the percentages fall to 37 and 30 per cent, respectively. Table 4 throws light on the relative importance of trade orientation and level of development in the distribution of the investment in each sector by relating the concentration of the investment in U.S.-oriented countries to that in Groups 3 and 4. As the table shows, investment in industries that went mainly to underdeveloped countries was highly trade-oriented. This is particu-

TABLE 4

Partial Distribution of U.S. Direct Investment, by Sectors, Between Trade Orientation and Economic Levels of Host Countries, 1950–54

(per cent)

	Percentage of U.S. Direct Investment Going to	
	U.S.-Oriented Countries	Group 3 and 4 Countries
Agriculture	100	100
Mining	73	73
Petroleum exploration and extraction	79	99
Utilities and transportation	99	99
Trade	58	64
Other	56	38
Manufacturing	37	37
Petroleum refining and distribution	30	29

NOTE: Excluding Canada.

larly true of investment in the production of primary goods, which generally constitute the main exports of underdeveloped countries to the center, and of investment in utilities and transportation.[41] Investment in manufacturing and in petroleum refining and distribution, on the other hand, was attracted to the markets of the high-income countries and was, therefore, more related to the advanced level of the countries in which it was made. Manufacturing investment is often made to "jump over tariff walls," while oil refining may use crude oil originating in third countries. These industries are, therefore, not especially associated with trade with the center.

In the Trade, Other (services), and Manufacturing sectors, substantial investment was made in the U.S.-oriented Latin American countries of Group 3. In other words, the investment in these sectors made in the underdeveloped countries was mainly in the more advanced among them, and the dependence seems to have been as much on the more advanced economic levels as on the trade orientation of the countries. This is particularly true of Manufacturing where Group 4 alone received only 4 per cent of the total investment (excluding Canada), indicating the strong dependence of this investment on more advanced levels of development.

For the other two centers, the United Kingdom and the Continent, the relation of the composition of investment to trade orientation and levels of development seems to have been similar.[42] Investment in primary production was very largely made in countries of their own trade orientation—chiefly in the dependencies, which received the major part of European investment in the underdeveloped areas. Investment in secondary and tertiary sectors, on the other hand, was chiefly in Groups 1 and 2 and was less dependent on trade orientation. The bulk of British investment outside the Sterling Area went to the U.S. and Canada and was mainly in manufacturing and services, including large insurance investments in the U.S. In the case of the Continent relatively large investments in secondary and tertiary industries outside countries of their own trade orientation made up, in fact,

[41] Utility and transportation investments as well as agricultural investments were small, however, accounting together for only 3 per cent of U.S. investment. Such investments were encountering increasing animosity in the host countries.

[42] Breakdowns by sectors are not available in these cases, but the approximate composition of the major part of the investments could be ascertained from partner data or other evidence.

the greater part of the total. It was mainly the sizable investment in the United States by two smaller countries, the Netherlands (in the petroleum refining and distribution sector) and Switzerland (in manufacturing), which accounted for the low share (37 per cent) of the Continent and Continent-oriented countries themselves. The distribution by sectors of the U.K.'s and the Continent's investment is, therefore, not inconsistent with the findings in the case of the United States. We shall come back to the distribution of investment by industries in relation to economic levels in the next section.

PRIVATE LOANS

The percentages of private loans indicate dependence on trade orientation in all three cases. The United Kingdom, where the concentration was largest (63 per cent in the U.K.-oriented countries), extended few loans, however, and the high percentage may not be very meaningful since these loans went entirely to one country, South Africa. The United States, the largest lender, showed the lowest concentration (50 per cent in the U.S.-oriented countries), while that of the Continent in the Continent-oriented countries was 59 per cent. The distribution of the loans of these two lenders by countries was quite similar, however. A large part of the American loans outside the own trade orientation was extended to Europe. These loans were chiefly for general balance-of-payments purposes (i.e., hard currency loans) and they served to supplement or replace the diminishing aid (as mentioned above). The Swiss loans, which made up the greater part of the Continental loans *within* the own trade orientation, were of the same nature and went roughly to the same countries. On the other hand, the American loans *within* the own trade orientation went mainly to developing countries in Latin America, but the Continental loans extended *outside* the own trade orientation also went chiefly to these same countries. These latter loans were more directly connected with exports, often financing equipment for development projects. In the case of the Continental loans, they resulted, therefore, from the efforts of the European countries to re-establish their export trade and conquer new markets. Although one would expect these export loans to follow the trade orientation this was not the case. Thus, the relation of private loans to trade orientation seems to be rather weak and not clearly established.

The apparently high dependence of capital flows on trade orientation observed in Table 3 is, therefore, somewhat misleading with regard to private capital. The high concentration of portfolio lending in the respective trade orientations was largely due to special circumstances. For direct investment the relationship varied by industrial sector: Investment in primary production and utilities—which predominated in underdeveloped countries—was highly trade-oriented; investment in manufacturing and oil refining and distribution, which was attracted mainly by advanced countries, showed little dependence; and investment in trade and other services, which also went largely to more advanced countries, showed a relatively weak dependence on trade orientation. For private loans no firm conclusions could be drawn.

SOME OTHER ASPECTS OF THE PATTERN

There are some other aspects of the pattern of capital flows during this period which deserve comment, namely, the capital supply of the United Kingdom and the Continent to the underdeveloped areas and differences between them. In contrast to the United States, the European countries extended aid to few underdeveloped countries outside the dependencies. The early fifties were, of course, still a period of reconstruction in Europe. The demands of the home economies continued to be great. In Britain, the center of the Sterling Area, it seemed particularly imperative to minimize drains on reserves and to guard against inflation lest the pound be endangered. British government aid was not only small in comparison to the large French aid, but also in relation to its private capital supply. The countries of Asia and the Middle East were very largely in the Sterling Area. A number of them were Commonwealth members, and others were within the British sphere of influence. Yet few of them received British aid. The British considered releases of the sterling balances that had been accumulated by a number of countries during the war as a kind of aid, since the resulting "unrequited exports" put a strain on the British economy. But such releases were of some substance only in the cases of Egypt and Pakistan during this period. The demands of home investment and defense, and the domestic demand for consumer durables, seem to have also prevented an increase in export credits. Such

credits, mainly finance capital goods and British exports of these goods, generally did not rise, and sometimes declined, during this period.[43] The extraordinary increase in export credits which took place in the case of the Continental countries thus did not occur in Britain.

However, having been historically the chief capital market of the world, Britain relied mainly on private capital to aid underdeveloped countries.[44] Thus, colonial aid was supplemented with London bond issues of colonial governments. The British also felt an obligation to give the Commonwealth members access to the market,[45] but few government issues resulted; among underdeveloped countries only Ceylon qualified for, or chose to float, a small issue. British delegations to the Colombo Plan conferences pointed to the investment being made in India as evidence of the contribution of British private investment.[46] The British investment in India was, however, the exception rather than the rule. British direct investment abroad was indeed considerable, but it went in large part to advanced countries. In the underdeveloped areas it was chiefly made in the territories which were still under British control and which also received most of the aid.[47] Thus, British investment cannot be said to have taken the place of aid in the former empire.

In Latin America, where British investment had been large, there was also a retreat rather than an expansion of British capital. And colonial aid and investment were more than offset by the capital inflow into the U.K. in the form of colonial sterling balances. As a result of these uphill flows, the United Kingdom's net capital supply to the underdeveloped areas as a whole was, in fact, negligible.

Continental aid and investment in the underdeveloped areas were concentrated in the dependencies. By far the largest part of this flow during the period under review consisted of $2 billion in French

[43] See Peter B. Kenen, *British Monetary Policy and the Balance of Payments, 1951–1957*, Cambridge, 1960, pp. 24–26.

[44] Cmnd. 237, July 1957, *The United Kingdom's Role in Commonwealth Development;* see also A. R. Conan, *Capital Imports into Sterling Countries*, London, 1960, pp. 98–100.

[45] See *Midland Bank Review*, February 1954, p. 12, and *Colombo Plan, 3rd Annual Report*, Ottawa, 1954, p. 103.

[46] Cmd. 9622, October 1955, "The Colombo Plan," U.K. section.

[47] It may well be that the lack of adequate data on British investment led to a misinterpretation of its direction.

colonial aid. The explanation of this large aid to the dependencies—on an even larger scale in subsequent years—is to be found in the French policy to induce the territories to maintain close political, cultural, and economic relations with the mother country after independence. As M. Pompidou has put it more recently: ". . . for us Frenchmen it is somehow a need to defend the French tongue . . . [against] . . . a strengthening of the position of the English language" (to which multilateral aid would lead).[48]

The bulk of the Continent's capital supply to the independent underdeveloped countries consisted of the $1 billion in export credits, which went, however, mainly to Group 3, the more advanced among these countries. These countries received, as mentioned previously, similar loans and credits from the United States, while the other aid they obtained consisted largely of IBRD loans. Since the "capacity to repay" is presumably greater for more advanced countries than for the least developed,[49] there is some justification for supplying aid through loans rather than grants to these countries. Nevertheless, the extent to which this kind of finance was resorted to has a number of disadvantages. Short-term credits are at best a haphazard way of financing development, since planning requires knowledge of the extent to which external finance will be available.[50] And the cumulative short-term credits and the bunching of intermediate-term and long-term loans have caused continuous balance-of-payments problems in a number of countries.

Capital Flows and Levels of Development

PRIVATE CAPITAL

In the previous sections we saw that the larger part of private capital went to the advanced countries. The receipts of government and private long-term capital by countries and country groups are shown in Table 5 both in absolute amounts and per capita. Of the total supply of private capital of $12.9 billion, net, only 28 per cent

[48] Quoted by Goran Ohlin, *Foreign Aid Policies Reconsidered,* OECD, Paris, 1966, p. 32; see also pp. 27–33 for a discussion of the controversy over foreign aid in France.

[49] See P. N. Rosenstein-Rodan, "International Aid for Underdeveloped Countries," *Review of Economics and Statistics,* May 1961, p. 109.

[50] *Ibid.,* p. 144.

TABLE 5

Receipts of Government and Private Long-Term Capital, Net of Repayments, Total Aggregative and Per Capita Amounts, 1950–54

	Total Receipts (millions of U.S. dollars)			Receipts Per Capita (U.S. dollars)		
	Total	Govern-ment	Pri-vate	Total	Govern-ment	Pri-vate
Total	28,897	16,015	12,882			
GROUP 1	9,521	6,578	2,943	21.05	14.55	6.50
US	1,792	-	1,792	11.80	-	11.80
UK	1,742	1,189	553	34.65	23.65	11.00
Continent	5,301	4,872	429	31.70	29.15	2.55
Japan	686	517	169	8.30	6.25	2.05
GROUP 2	8,146	1,799	6,347	89.00	19.65	69.35
Canada	3,915	74	3,841	285.75	5.40	280.35
Israel	781	478	303	600.80	367.70	233.10
Chile	143	22	121	23.45	3.60	19.85
UK-oriented	2,534	584	1,950	78.95	18.20	60.75
Iceland	38	37	1	265.50	258.50	7.00
Ireland	123	79	44	41.05	26.40	14.65
Australia	859	190	669	104.80	23.20	81.60
New Zealand	138	−1	139	72.60	−.55	73.15
Rhodesia	394	86	308	61.55	13.40	48.15
S. Africa	982	193	789	78.50	15.40	63.10
Cont.-oriented	773	641	132	20.20	16.75	3.45
Denmark	114	165	−51	26.55	38.40	−11.85
Norway	336	299	37	101.80	90.60	11.20
Sweden	86	66	20	12.30	9.45	2.85
Finland	−26	−24	−2	−6.50	−6.00	−.50
Argentina	172	91	81	10.00	5.30	4.70
Uruguay	(91)	44	(47)	(36.40)	17.60	(18.80)
GROUP 3	3,766	2,545	1,221	20.55	13.90	6.65
US-oriented	1,921	683	1,238	19.10	6.80	12.30
Brazil	818	456	362	15.70	8.75	6.95
Colombia	157	56	101	13.90	4.95	8.95
Cuba	154	14	140	28.55	2.60	25.95
Mexico	394	149	245	15.30	5.80	9.50
Panama	49	5	44	61.25	6.25	55.00
Venezuela	349	3	346	64.60	.55	64.05

(continued)

TABLE 5 (*continued*)

	Total Receipts (millions of U.S. dollars)			Receipts Per Capita (U.S. dollars)		
	Total	Govern-ment	Pri-vate	Total	Govern-ment	Pri-vate
GROUP 3 (continued)						
Cont.-oriented	1,845	1,862	−17	22.40	22.60	−.20
Greece	811	803	8	106.70	105.65	1.05
Portugal	83	65	18	9.90	7.75	2.15
Turkey	311	301	10	14.90	14.40	.50
Spain	63	77	−14	2.25	2.75	−.50
Lebanon	5	7	−2	3.85	5.40	−1.55
Yugoslavia	572	609	−37	35.30	37.60	−2.30
GROUP 4	7,464	5,093	2,371	8.40	5.75	2.65
US-oriented	2,120	1,516	604	25.25	18.05	7.20
Latin America	320	105	215	11.45	3.75	7.70
Costa Rica	7	4	3	8.75	5.00	3.75
Dom. Rep.	31	1	30	14.80	.50	14.30
El Salvador	12	13	−1	6.30	6.85	−.55
Guatemala	3	1	2	1.05	.35	.70
Haiti	28	13	15	8.75	4.05	4.70
Honduras	42	3	39	30.00	2.15	27.85
Nicaragua	14	6	8	12.75	5.45	7.30
Bolivia	37	34	3	12.35	11.35	1.00
Ecuador	32	13	19	10.00	4.05	5.95
Peru	114	17	97	13.40	2.00	11.40
Philippines	330	255	75	16.55	12.80	3.75
S. Korea	746	746	–	35.20	35.20	–
Taiwan	359	342	17	47.85	45.60	2.25
Liberia	46	9	37	57.50	11.25	46.25
S. Arabia	262	2	260	43.85	.50	43.35
Ryukyus	57	57	–	81.45	81.45	–
UK-oriented	2,512	1,354	1,158	3.60	1.95	1.65
Independents	1,126	991	135	1.80	1.60	.20
Burma	−30	−12	−18	−1.60	−.65	−.95
Ceylon	−5	12	−17	−.65	1.50	−2.15
India	445	326	119	1.25	.90	.35
Pakistan	195	169	26	2.60	2.25	.35
Iraq	59	9	50	12.30	1.90	10.40
Jordan	148	148	–	113.85	113.85	–
Libya [a]	43	43	–	43.00	43.00	–

(*continued*)

TABLE 5 (*concluded*)

	Total Receipts (millions of U.S. dollars)			Receipts Per Capita (U.S. dollars)		
	Total	Govern-ment	Pri-vate	Total	Govern-ment	Pri-vate
GROUP 4 (continued)						
UK-oriented						
Independents						
Afghanistan	24	24	–	2.40	2.40	–
Indonesia	62	91	−29	.80	1.20	.40
Iran	137	137	–	7.20	7.20	–
Nepal	1	1	–	.15	.15	–
Thailand	36	39	−3	1.95	2.10	−.15
Ethiopia	28	12	16	1.65	.70	.95
Sudan	−17	−8	−9	−1.95	−.90	−1.05
UK Overseas Terr.	1,386	363	1,023	18.00	4.70	13.30
Cont.-oriented	2,832	2,223	609	27.25	21.40	5.85
Independents	20	27	−7	.80	1.05	−.25
Egypt	1	10	−9	.05	.50	−.45
Syria	9	8	1	2.80	2.50	.30
Paraguay	10	9	1	7.15	6.45	.70
Cont. Overseas Terr.	2,812	2,196	616	35.85	28.00	7.85
French	2,444	1,995	449	49.00	40.00	9.00
Belgian	223	79	144	14.40	5.10	9.30
Dutch	59	43	16	53.65	39.10	14.55
Ital. Somali[a]	51	51	–	42.50	42.50	–
Portuguese	35	28	7	3.20	2.55	.65

NOTE: Excluding Soviet Bloc, Indochina, and Australian New Guinea. Parentheses indicate the figures are questionable. They are reported as "estimates," which are probably overstated; the identified private capital cancels out approximately.

SOURCE: Appendix Tables B-I through B-V; population data (1950), U.N. *Demographic Yearbook*, 1955, pp. 115 ff., and 1963, Table 4.

[a] Includes budgetary aid.

went to the underdeveloped areas (Groups 3 and 4). Among the advanced countries it was those of Group 2, however, that received the main share, close to one half of the total. Both major types, portfolio and direct investment, favored Group 2, as did both major suppliers of private investment, the United States and the United Kingdom. The underdeveloped areas as a whole account, however, for two-thirds of the world population (excluding communist countries), and Group 4 alone for over half, while Group 2 makes up only 6 per cent. Per

capita receipts of private capital declined, therefore, sharply from Group 2 downward, i.e., the lower the per capita income of the group, the smaller was the inflow of private investment per capita (see last column of Table 5).

We pointed out previously the reasons why portfolio investment has by and large avoided the underdeveloped countries since the Depression and the war. Presumably, however, direct investment, the dominant form of private capital, is especially suited to the needs of the underdeveloped countries because technological knowledge and managerial skill are provided with the capital. Yet, the underdeveloped areas attracted only a small share of the total. An explanation for the relative sparseness of foreign investment in underdeveloped areas was provided by the late Ragnar Nurkse, who gave two reasons. First, underdeveloped countries do not attract investment for the domestic market because their low per capita incomes yield insufficient aggregate demand. The investment in these areas is, therefore, frequently in raw material production for export—an often observed phenomenon. But, Nurkse continued, the markets for raw materials are not expanding to the extent that they did in the nineteenth century, and synthetic substitutes have diminished the demand, curbing this form of direct investment also.[51]

We have already discussed the industrial composition of direct investment in the context of trade orientation. We found that (if Canada is excluded) U.S. investment in primary production was mainly made in underdeveloped countries, but that the more advanced among them, those in Group 3, also attracted substantial investment in manufacturing and services. By groups, the distribution of U.S. direct investment between primary production and other sectors is shown in Table 6.

On a per capita basis[52] the largest investments were made in ad-

[51] Ragnar Nurkse, *Problems of Capital Formation in Underdeveloped Countries*, New York, 1953, pp. 24–31, 82–89; see also UN, *International Capital Movements in the Inter-War Period*, 1949, p. 32.

[52] Per capita receipts of direct investment alone were, in U.S. dollars:

Group 1	6.20	*Group 3*	8.70
		US-oriented	13.60
Group 2	55.70	Cont.-oriented	1.10
US-oriented	160.60		
UK-oriented	44.20	*Group 4*	2.40
Cont.-oriented	9.40	US-oriented	7.40
		UK-oriented	1.70
		Cont.-oriented	3.10

TABLE 6

Distribution of U.S. Direct Investment Between Primary and All Other Sectors, 1950–54

(*per cent*)

Country Group	Primary Production	All Other[a]	Not Specified
Group 1	–	100	–
Group 2	36	64	–
Group 2 ex. Canada	21	79	–
Group 3	27	70	3
Group 4	70	28	2

NOTE: The evidence for the other investor countries suggests that the composition was similar, viz.: primary production was nil or negligible in Group 1, constituted the smaller part in Groups 2 and 3 (and a smaller proportion in Group 3 than in Group 2), but accounted for two-thirds or more of the investment in Group 4 (see Walther P. Michael, "International Capital Movements, The Experience of the Early Fifties (1950–1954)," Ph.D. dissertation, Columbia University, 1965, pp. 163–172).

SOURCE: See footnote 40 in text.

[a] Including petroleum refining and distribution.

vanced countries with expanding markets, particularly those of Group 2 and to a smaller degree in the intermediate Latin American countries of Group 3. But, while investments in the manufacturing and service sectors of the countries in these groups were generally large, substantial investments in the primary sector were also made in several of these countries. Where investments of the latter type were large in these countries they were accompanied by still substantial investments in other sectors. Among the countries where both kinds were combined were particularly Canada, South Africa, Cuba, and Venezuela. On the other hand, investment was relatively smaller in those groups of countries where it was only made in nonprimary sectors, as in the Continent-oriented countries of Group 3, or mainly in the primary sector, as in Group 4. Group 1 also falls in this category, in that only nonprimary investment was made, but here more limited opportunities for foreign investment during this period were presumably the main reason for the lower per capita figure. The Scandinavian countries (in Continent-oriented Group 2) are on the Group 1 level with the exception of Norway where investment in shipping was large.

The first part of Nurkse's explanation seems, therefore, to be borne out: investment for the domestic market declined with per capita incomes.[53] In the majority of the underdeveloped countries, those in Group 4 with the lowest incomes, it was generally small and scattered. As far as the flow of capital into primary production is concerned, however, it is not so much that this investment was small but that it went to a considerable degree to more advanced countries. The American mining and oil extraction investment in Canada alone, in excess of $1 billion, exceeded the whole U.S. investment in Group 4.

A further factor accounting for the low receipts of some areas was an "unfavorable investment climate" or the existence of military emergencies in a number of countries. Particularly in several U.K.-oriented countries of Group 4 whose receipts were among the lowest, and where raw material investment had previously been important, no investment was made or repatriations occurred.[54]

This pattern of private investment was not unlike that of the half century before World War I. Data on capital movements during that period are far from complete, particularly with regard to the underdeveloped countries of today. But there seems little doubt that the largest investments were made in the "areas of recent settlement." [55] These are the countries that are included in our Group 2, except that the largest capital importer of that period, the United States, has replaced Britain as the largest supplier. As several writers have pointed out,[56] the capital flows to these countries complemented enormous immigration of skilled labor, providing the overhead capital which opened up the new lands and gave their products access to the world market.

This description does not fit the conditions in the early 1950's except in one case, the newcomer Israel, with its large immigration. Although we noted special motivations in the supply of portfolio capital to Israel, that country does present some similarities to the

[53] See also Peter B. Kenen, *Giant Among Nations,* 1962 edition, p. 128–129.

[54] For example, Iran under the Mossadegh regime, and Indonesia, where small investments were offset by disinvestments; see also Appendix Table B-V.

[55] See Ragnar Nurkse, "International Investment Today in the Light of Nineteenth Century Experience," *Economic Journal,* December 1954, pp. 744–758; see also Douglass C. North in *U.S. Private and Government Investment Abroad, op. cit.,* pp. 31 ff.

[56] Nurkse, *ibid.;* North, *ibid.;* A. K. Cairncross, *Home and Foreign Investment, 1870–1913,* Cambridge, 1953, p. 209.

areas of recent settlement of the nineteenth century. Its receipt of private capital per capita greatly exceeded those of all other countries except Canada, and if one includes government aid, its per capita receipts of $600 for the five years were more than twice even those of Canada. But immigration does not provide the explanation for the continued concentration of private investment in the other countries of this group. Having achieved a modern infrastructure and generally high living standards, these countries now attracted investment mainly in manufacturing and services, although in some cases substantial raw material investment continued or was begun. This situation was not wholly unique to Group 2. It also prevailed in the more advanced Latin American countries in Group 3, especially Brazil, Colombia, and Mexico.

Conditions in the underdeveloped areas, however, are very different from those in the developing countries of the past. Consequently, in the majority of the underdeveloped countries private capital provided neither for social overhead development nor for industrial diversification. Colonial administrations had access to the metropolitan capital markets, it is true, but these were restricted by the heavy demand placed upon them by reconstruction at home. The territories involved accounted also for only 14 per cent of the population of Group 4. In a few cases oil companies made substantial investments in refineries for the domestic market, namely in India and the Philippines, but in the latter case the inducement was mainly the granting of exploration franchises which were contingent upon the refinery. Otherwise private capital was attracted mostly by primary production in these areas, investment in secondary and tertiary industries being generally small and scattered. This conforms also to the pattern of the past.[57]

The disadvantages of this kind of investment for underdeveloped countries have often been pointed out. It is said to create or perpetuate "dual economies," in which the efficient export sector, utilizing foreign technology and often foreign personnel, may not induce further development in the indigenous subsistence sector.[58] Moreover, the establishments are usually much larger than in other industries. During the

[57] Ragnar Nurkse, *Problems of Capital Formation, op. cit.*, p. 84; see also North, *op. cit.*, p. 34.

[58] H. W. Singer, "The Distribution of Gains between Investing and Borrowing Countries," *American Economic Review*, May 1950, pp. 475–477; see also Nurkse, *Problems of Capital Formation, op. cit.*, and P. N. Rosenstein-Rodan, *op. cit.*, p. 110.

period 1951–57, for instance, primary investment accounted for 49 per cent of the *value* of new establishments founded by U.S. parent companies, but for only 19 per cent of their *number*.[59] The diffusion of the effect of the investment on the economy is thus likely to be much smaller than for other industries. The very scale of the operations requires equipment that cannot be produced in these countries and has to be imported.[60] On the other hand, in countries where modern technology and scientific methods have not penetrated at all, this kind of investment may provide new social services, such as education and medical services, as in the well-known case of Aramco in Saudi Arabia. Furthermore, royalties and tax receipts provide the government with important sources of development funds, and export proceeds supply needed foreign exchange. While raw material investment for export is, therefore, certainly not without benefit, it is not likely to have as great and direct an effect on the development of the host country as does investment for the domestic market.[61]

Although the share of the underdeveloped areas in private capital was relatively small, per capita receipts varied considerably within groups. Such variation is attributable, of course, to a number of factors, but it is accentuated by raw material investment, since large amounts of such investment are frequently made in countries with relatively small populations. The sixteen U.S.-oriented countries in Group 4, for instance, had the highest per capita receipts of direct investment in that group ($7.40 as given in footnote 52 above); but if Peru and Saudi Arabia with large mining and petroleum investment are excluded, the figure falls to $3.90.

GOVERNMENT CAPITAL AND PRIVATE INVESTMENT

In view of the fact that private investment was largely attracted to advanced countries, how did the distribution of government capital compare to that of private capital? Due to the massive European recovery aid, the share of Group 1 was, of course, the largest, 41 per cent of the total of $16,015 million shown in Table 5. But this was

[59] U.S. Department of Commerce, *U.S. Business Investments in Foreign Countries*, Washington, D.C., 1960, p. 100. The petroleum sector includes refining and distribution; if only exploration and extraction were included, the phenomenon would probably be more pronounced.

[60] Kenen, *op. cit.*, p. 118.

[61] See also Nurkse, *Problems of Capital Formation*, *op. cit.*, pp. 24–25 and 84.

peculiar to this period. For the three capital importing groups the shares increased downward, from 11 to 16 to 32 per cent for Groups 2, 3, and 4, respectively. This pattern was true of each major donor-lender, the U.S., the U.K.,[62] and the Continent. In the latter two cases, however, the distribution was influenced by reparations and other contractual payments, while their development aid went mainly to the dependencies where their private investment in the underdeveloped areas was also concentrated. The distribution is more interesting in the case of the United States, which supplied the larger part of both aid and investment, and whose capital was globally dispersed. In this case the distribution of government aid was inversely related to that of private capital in the three groups, the shares of private capital decreasing, and those of government aid increasing with the declining level of development, as seen in the text table.

	Government Aid (*per cent*)	Private Capital (*per cent*)
Group 2	21	68
Group 3	35	18
Group 4	44	14
Total	100	100

While these figures include emergency aid, which is influenced by factors exogenous to economic level, development aid showed a similar distribution (24, 33, and 42 per cent). The available supply of U.S. aid was thus distributed so as to somewhat offset the inverse relationship between receipts of private capital and level of development.

Returning to Table 5, we find, however, that per capita receipts of government capital, like those of private capital, declined with the level of development from Group 2 downward. On a per capita basis, Group 2 had the highest receipts not only of private capital, but also of official capital. (If the U.S. population is excluded, Group 1 showed the highest per capita aid receipts.) While Group 2 includes most of the countries which were least eligible for government aid (e.g., Canada and the sterling countries), IBRD loans and government loans for the supply of strategic materials raised the per capita

[62] For the U.K., Group 2 aid was larger than that extended to Group 3; but the former includes a consolidation loan, i.e., not new capital.

receipts of official capital above those of most underdeveloped countries. In Groups 3 and 4, moreover, all aid receipts over $10 per capita were cases of aid for reconstruction, political or military emergencies and famine relief, or aid to dependencies or countries under Allied administration. The countries and territories involved accounted for only 17 per cent of the population of Groups 3 and 4 (excluding the Soviet Bloc). The more or less pure development aid to independent countries resulted in the lowest per capita receipts. Moreover, these declined with the level of development. Thus, on a per capita basis, government aid did not compensate the underdeveloped areas for their small share of private capital.

The question whether the aid to the underdeveloped areas during this period was inadequate can be answered, however, only with reference to the "absorptive capacity" for capital of these countries. Unfortunately, there is as yet no generally accepted method of calculating the amounts which these countries could productively employ. The estimates of capital requirements which have been made are generally projections for the 1960's and 1970's. Some of these are based on parameters of past economic performance of individual countries with assumptions about possible growth rates limited by absorptive capacity. Others are estimates of the projected "foreign exchange gap." [63] The estimates vary widely in the magnitude of the required aid. A comparison with even the lowest of these estimates, those by Rosenstein-Rodan,[64] which assume extremely moderate growth rates for most countries, would suggest that the aid actually extended during 1950–54 was grossly inadequate. It amounted to 30 per cent of the estimated requirements of the underdeveloped countries as a whole. But since aid was highly concentrated, for most countries the discrepancies between aid and requirements were much larger than this average, while in the few countries with very high receipts the requirements were exceeded. In the countries with the lowest per capita incomes, the U.K.- and Continent-oriented independent countries of Group 4, the aid receipts came to approximately 10 per cent of requirements estimated by Rosenstein-Rodan.

[63] See Goran Ohlin, *op. cit.*, pp. 76–80, for a comparison of the various estimates.

[64] Rosenstein-Rodan, *op. cit.;* these estimates are also the most suitable for comparison because they were made for individual countries; for the comparison see Walther P. Michael, *op. cit.*, pp. 266–270.

5

THE FEASIBILITY OF CONSTRUCTING CAPITAL FLOW ACCOUNTS FOR LATER PERIODS

The pattern of capital movements described above covers an early part of the postwar period. While some aspects of this pattern, particularly the concentration of U.S. aid in Europe, were peculiar to this period, the distribution of private investment and aid among the capital importing groups is not. How this distribution works out for later years, after aid to Europe had ceased and European recovery had been accomplished, must remain for further study.

A continuation of this study would very likely encounter problems similar to those for the early 1950's, although improvements in the reported data have taken place. The staff of the Balance of Payments Division of the Fund has, of course, exerted steady efforts in this respect, and new information has become available in many cases. The U.K. balance of payments, which included only net figures for private capital, distinguishes, from 1958 on, assets and liabilities, and direct and other investment. A country breakdown of direct investment (including reinvested profits) is also available beginning with 1958, although there are some gaps in the coverage.[1] While the procedure in this case obviously will be simplified, the British account still will have to be supplemented with partner data and other sources, even from 1958 on. The records of the continental countries seem to have improved also, as spot checks of balance-of-payments reports reveal, and as is also indicated by the tables of aid and investment flows to the underdeveloped countries in the OECD studies, which are based on member countries' reports.[2] Private investment seems generally better covered and identified by type. Regional distributions by cur-

[1] H. M. Stationery Office, *Board of Trade Journal,* 6 October 1961, pp. 715–720.

[2] See, e.g., OECD, *The Flow of Financial Resources to Less-Developed Countries. 1956–1963,* Paris, 1964.

rency areas, which were of very limited use, have been replaced by more meaningful ones. While these improvements have come only gradually (Sweden, for instance, omits all direct investment until 1962), the identification of the Continental transactions will be made easier for later years than for the early 1950's.

On the other hand, there is the evidence, discussed above, which seemed to indicate that the Continental countries continued to understate their outflows in 1963 and 1964. The procedure will, therefore, still have to rely heavily on partner data and other sources to identify the capital flows of the European suppliers and supplement their data not only for the years directly following 1954 but probably for later years as well. There are always details of information available in the balance-of-payments statements, investment censuses, or other sources of some countries that make it possible to identify transactions and to fill gaps in other records. The publications of the OECD and the UN will also be very useful, particularly regarding the flow of official capital.

One problem in any attempt to reconstruct capital flows for recent periods is the length of time which elapses before the reported data are firm. At present each of the Fund's Yearbooks carries revisions of the data for the four years preceding the latest one covered. There is, therefore, always a lag of five years at the time of publication of the most recent data. In the process of this study substantial revisions were encountered in a number of important accounts. Very large revisions in the U.S. direct investment figures, particularly of the data for foreign investment in the U.S., did not appear until 1963.

It is hoped that the data can be further improved, especially those of the Continental countries. It would also be very helpful if for the transactions of these countries more detailed breakdowns could be provided, particularly of private capital, of the kind which the United States supplies, and which are also now available for the United Kingdom. It should be possible to improve balance-of-payments data to the point where one can construct integrated accounts of world capital transactions on an annual basis. Such accounts would be of obvious value to students of international trade and economic development. It is hoped that this study will contribute in some measure toward this end.