

October 26, 1948

MEMORANDUM TO THE BOARD

Subject: Israeli Loan Application

A meeting was held in Mr. Arey's office on Monday, October 25, Messrs. Gass and Ginsberg representing Israel and Messrs. Arey, Lockhart, and Lynch representing the Bank. Mr. Gass admitted that the presentation of the Jewish agency was not in all points clear as to the geographic demarcation of the area for which the loan is requested. The boundaries set up by the United Nations are those under consideration. Even if the Bernadotte Plan should be adopted, however, he stated that the general lines of development during the next four years would not be altered substantially. The total investment in agriculture and irrigation during the next four years is estimated at \$135 million, of which 40 to 50 percent will represent foreign expenditures. Should the Bernadotte proposals be adopted, the total investment program would be reduced slightly. The Bernadotte Plan would affect the manufacturing development plan very slightly. The major change that would have to be made in the original proposals would be in chemicals, since the Dead Sea resources are, for the most part, beyond the Bernadotte boundaries.

It was pointed out to Mr. Gass that according to his book, "Palestine Problem and Promise," capital imports, mainly in the form of contributions during the two decades ending in 1939, amounted to \$650 million and in the second of the two decades to perhaps \$50 million a year. The increase in holdings of foreign resources, chiefly pounds sterling, during the war years was, according to the same book, a result mainly of military expenditures by the Allied forces, which presumably will not be repeated. It was suggested, therefore, that the paper of Mr. Hoofien on "Israeli's Ability to Repay" requires considerable elaboration. It was also pointed out to Mr. Gass that no balance-of-payments forecast appeared in his book. Mr. Gass admitted that a balance-of-payments forecast was deliberately avoided and explained his decision by pointing to the very conjectural nature of any forecast of the future, particularly in a state the population of which will increase by about 40 percent during the next four years. He admitted that no savings had occurred prior to 1939 but pointed out that after 1939 the internal savings of Palestine and the external balances so obtained were the result not only of inability to import and of military expenditures by Allied forces in a narrow sense but of a tremendous increase in production.

In this connection, he indicated that agricultural output, exclusive of citriculture, had increased by more than 125 percent between 1939 and 1947, with no increase in the farm population. He also stated that the Middle Eastern markets had received during these years a veritable flood of Jewish manufactures.

Mr. Gass asserted that there was every reason to believe that the agricultural and industrial output of Israel would continue to increase. He admitted that the marketing of Israel's products might be difficult, especially in the short run. He also admitted that some of the manufacturing installations are of a speculative nature. He insisted, however, that there was enough slack in Israel's foreign trade to insure the Bank against default, particularly in view of Israel's determination to put its trade on a sound basis and the large contributions that it expects to receive from the United States for the next several years. In this latter connection, he conceded that contributions would probably decline and that the \$100 million or so received from the United States in 1948 will probably never be matched. Mr. Gass stated that if the value of Israel's exports of foodstuffs should reach two-thirds of the value of her imports of foodstuffs, the country would be doing very well. Although Israel will probably continue to be a net importer of foodstuffs, he believes that exports of manufactured products, tourist traffic, and oil refinery income will eventually exceed the net value of imported foodstuffs.

Mr. Gass indicated that some private capital is now coming into Israel and that it is his hope that an Export-Import Bank loan will give private investors sufficient confidence in the stability of the Israeli State to induce a much larger inflow of private investment funds.

Mr. Gass was reluctant to say at what time Israel would be independent of foreign capital, mainly because of his inability to forecast the end of the immigration period. He did say, however, that when immigration fell to 5 percent or less of the total Israeli population, the country would, in his judgment, be capable of supporting itself at a reasonable standard of living. It was requested that he demonstrate this.

Mr. Gass stated that he was authorized to say that Israeli would welcome any restrictions that the Bank might impose upon the use of any funds lent by it. In particular, he suggested that the Bank permit no funds lent by it to be used for other than investment purposes.

He would hesitate to submit an application on a project basis for the reason that as much play as possible to private initiative in Israel is to be accorded by the new State, which will therefore desire as much flexibility as possible in the use of funds that it receives from

abroad. Only in the agricultural sector are plans sufficiently fixed to render the project approach easy. During the next two years foreign expenditures for agriculture and irrigation are expected to amount to \$35 million.

Mr. Gass said that Israel will insure against the dissipation of any funds that it might receive from the Bank through external and internal controls. Rigorous foreign exchange control, taxation, and internal rationing of loanable funds will be used for this purpose.

Mr. Gass stated that the pound sterling holdings of the Palestine Currency Board, amounting to 46 million pounds, are in dispute. Thirty million of the old Palestine pounds have been turned in for the new Government's currency. It is his opinion that this matter will be settled very shortly after the U. K. recognizes the new State.

In summary, Mr. Gass added nothing substantial to what had already been submitted to the Bank.

Edward S. Lynch