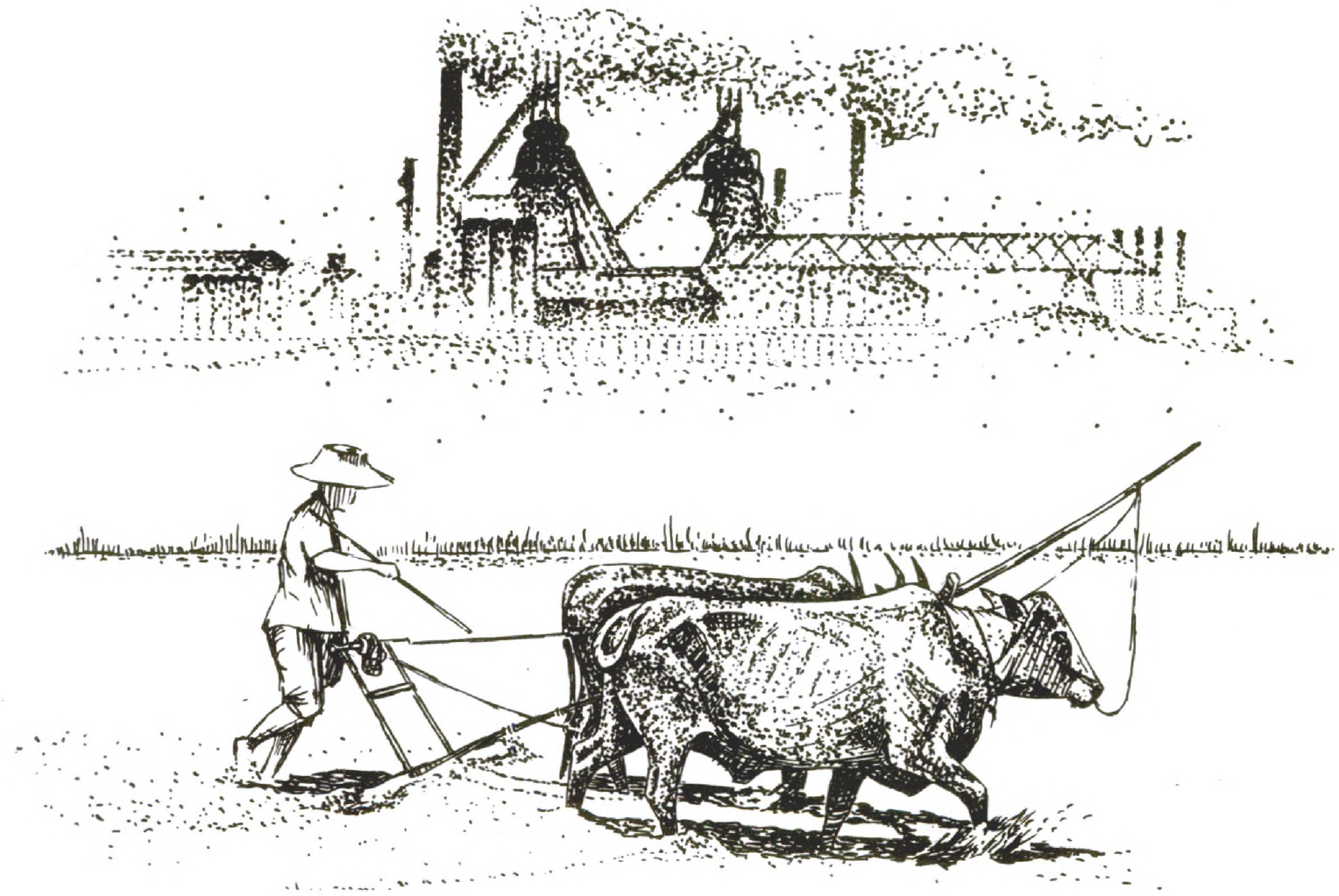
Seed Corn for Asia



THE Asian Development Bank (ADB) opened its doors for business in temporary quarters in Manila in December 1966. Some time may elapse before the Bank is able to carry on full-scale lending operations, but its appearance on the scene signifies the growing acceptance of the regional development-bank concept in the world of international finance.

The ADB is essentially an Asian institution, although any member of the UN or its specialized agencies can belong, and although its membership includes 12 non-regional members as well as 19 regional members. The original proposal for such an organization came from several Asian members of the Economic Commission for Asia and the Far East (ECAFE). Asian countries not only account for a majority of the membership but also control almost two-thirds of the authorized capital stock. The Asian members elect seven members of the ten-man board of directors, and this board in turn elects the president, who incidentally must be a citizen of one of the Asian member countries.

Regional banks—why?

The ADB's major purpose is to promote Asian development while adhering to sound banking practices. It is designed to act, in

the words of President Watanabe, "as a financial family doctor for Asia's billions."

The Bank's stated aims also include the promotion of regional co-operation and the stimulation of financial flows to Asia members. The Bank permits up to 10 percent of its paid-in capital (plus supplemental loans from members) to be used for soft loans or grants, and it permits up to 2 percent of its paid-in capital to be used for non-reimbursable technical assistance. (The 2-percent limitation will be dropped after the first five years of operation.)

The ADB is the third regional bank to be set up in recent years under international auspices, but it differs in some respects from the other two such banks, the Inter-American Development Bank (IADB) and the African Development Bank (AFDB). Developed industrial countries hold voting control in the Asian Bank but do not have a majority in the other two banks. This reflects the wide participation of industrial countries, both regional and non-regional, in the Asian Bank — whereas only one developed country (the United States) participates in the Inter-American Bank and none hold membership in the African Bank.

The Asian Bank has only one-half as much initial capital as the IADB but four times as much initial capital as the AFDB. The ADB plans to follow the IADB's example in floating bond issues backed by the Bank's callable capital, thus obtaining favorable terms in meeting its own financial needs. In the long run, at any rate, each of these regional development banks is designed to supplement its loanable funds by acting as a financial intermediary; that is, by borrowing in world capital markets and re-lending to regional borrowers.

But sufficiency of funds is not enough to assure the ADB that it can reach its goal of self-sustainable economic development of the huge area called Asia. To appreciate the problems facing the ADB, it might be well to look first at the nature of economic development itself.

Economic development — how?

Economic development is concerned with raising the average real productivity of a region's people. Many poorer countries suffer deficiency of resources or of knowledge

ASIAN DEVELOPMENT BANK—SUBSCRIBED CAPITAL AND VOTING RIGHTS

	Regional Members	
	Subscribed capital (millions)	Total votes
Afghanistan	$ 4.78	1,256
Australia	85.00	9,278
Cambodia	3.50	1,128
Ceylon	8.52	1,630
China (Taiwan)	16.00	2,378
India	93.00	10,078
Indonesia	25.00	3,278
Japan	200.00	20,778
Korea (South)	30.00	3,778
Laos	0.42	820
Malaysia	20.00	2,778
Nepal	2.16	994
New Zealand	22.56	3,034
Pakistan	32.00	3,978
Philippines	35.00	4,278
Singapore	5.00	1,278
Thailand	20.00	2,778
Vietnam (South)	12.00	1,978
Western Samoa	0.06	784
Subtotal	615.00	76,282

	Non-regional Members	
	Subscribed capital (millions)	Total votes
Austria	$ 5.00	1,278
Belgium	5.00	1,278
Canada	25.00	3,278
Denmark	5.00	1,278
Finland	5.00	1,278
Germany (West)	34.00	4,178
Italy	20.00	2,778
Netherlands	11.00	1,878
Norway	5.00	1,278
Sweden	5.00	1,278
United Kingdom	30.00	3,778
United States	200.00	20,778
Subtotal	350.00	44,336
Grand total	965.00	120,618

Note: Each member receives 778 basic votes plus one vote for each $10,000 of subscribed capital. Only one-half of the subscribed capital must be paid-in, and only one-half of that amount must be in gold or convertible currency; moreover, all paid-in capital is payable in five equal annual instalments.

and initiative in working whatever resources they have. Sometimes this means that new technologies are required. In addition, if the traditional economies are themselves basically inefficient, more efficient methods must be introduced as well. Where mechanization and industrialization are needed, heavy financial investments are a prerequisite to success.

Investment of course requires saving, whether in the form of domestic saving or in the form of direct foreign investment or foreign grants and loans. Poor countries have great difficulty amassing sizable volumes of savings voluntarily in advance of industrialization, and alternative means must be relied upon.

Saving is essential for economic development, but saving by itself is insufficient to promote growth. Some of the output produced is not consumed when an economy is saving. But such saved output must be put in a form suitable for investment: if economic development is to take place, pencils produced but not consumed (that is, pencils saved) cannot magically be transformed into the power lathes that may be needed. In real life, transforming the agricultural surplus found in underdeveloped countries into working capital for investment projects is far from an easy task. Among other things, political and social stability are required for the efficient transformation of savings into productive investment.

Indeed, in the real world, economic development is best seen as a combination of social, cultural, political, and economic changes which in turn bring about further changes in the economy. In this complex world, it is difficult to isolate any single factor as the prime mover in the development process. Suffice it to say that development is accompanied not only by the formation of investment capital, but also by a heightened spirit of enterprise, improvements in production techniques, and improvements in the economic qualities and productive capacities of labor.

The Japanese Case

The Japanese case would suggest that there are really no shortcuts to economic modernization—only a possibility of speeding up the process of industrialization when the environment is favorable. It also suggests that certain prerequisites — strong national solidarity, administrative and financial stability, good work habits, a strong propensity to save, high literacy, capacities for sustained agricultural growth, entrepreneurial skills, and the like — may be necessary before any great economic modernization is possible. It may take considerable time before enough of these characteristics have been developed in some Asian countries to permit them to move ahead rapidly with industrialization. Clearly if our policies of economic aid in Asia are to be meaningful, they should be aimed not at quick results, as in postwar Europe, but at a process of development over many decades.

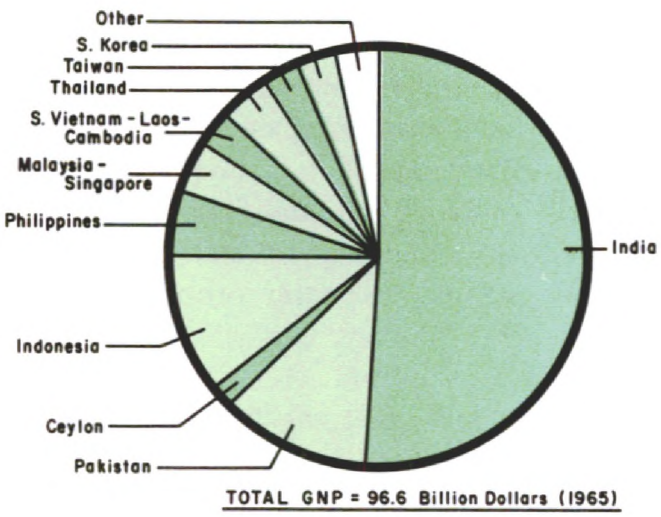
Edwin O. Reischauer
Beyond Vietnam: The U.S. and Asia

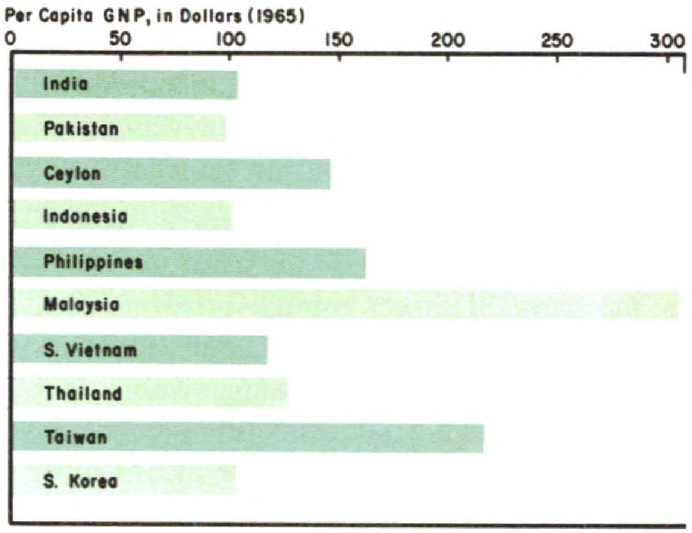
Development thus is seen as a process of change — technological, sociological, and economic change — where progress is constrained by a number of bottlenecks. These bottlenecks include shortages of human skills (for example, literacy), of advanced machinery, and of foreign exchange to import goods in short supply, along with a generalized lack of savings.

Finance — why and how?

The financial sector is deeply involved in each nation's drive to overcome the bottle-

Economies of underdeveloped Asian countries vary greatly in size, but almost all show a depressing sameness of per capita income





necks hampering development. When lending and borrowing opportunities are introduced into a modern money economy, both the efficiency of investment and the scope of entrepreneurial activity can be expanded. Larger projects can be organized and the best (highest yield) projects can receive the greatest supply of funds. Moreover, the great variety of instruments and institutions developed in a complex financial structure can increase both the amount of savings flowing into the market and the efficiency of the saving-investment transformation.

The diversity of instruments encourages the saver to save more, by confronting him with a wide range of yields, risk, and liquidity. The diversity of institutions also encourages savings by presenting the saver with competitive terms and conveniences. Such diversities also encourage entrepreneurs to borrow more; a wide range of loan contracts permits better terms on specific projects, and the provision of long-term funds for long-term projects circumvents the repeated transaction costs and future risks of short-term borrowing. The complex financial system which is taken for granted in the developed countries — but which is so woefully lacking in most underdeveloped countries — thus serves an essential role in smoothing the flow of funds from household savers to business investors.

Regional approach

The regional approach to development — the avowed aim of the regional development bank — is designed to stimulate a more efficient allocation of the world's limited resources in meeting its unlimited needs. This approach has several welcome features. Regional cooperation makes possible economies of scale through the expansion of trade, markets, and technological information. Regional cooperation, moreover, helps circumvent the regional boundary lines which cut across the unbroken seam of economic geography.

Disaster can result if this approach goes awry. Disillusion may breed distrust and stubbornness among nations, making develment more difficult than before. An overly broad plan may ignore special problems of participating nations, and thus stymie growth through conflicts of national self-interest. But

the existence of such difficulties only makes the basic task more urgent.

The ADB's approach is both a *regional* approach and an *Asian* approach. This is more difficult than it sounds, since Asian economies vary widely in their size, diversity, and scale of development. In fact, even their basic working methods differ; for example, Malaysia's development office is run energetically with Sandhurst efficiency, while Indonesia's program under the Sukarno regime concentrated on the preparation of a mammoth development plan — 8 books, 17 chapters, and 1950 pages, arranged so as to commemorate the founding date of the Republic (8-17-50).

Asia — how poor?

Despite certain statistical weaknesses, the available figures still paint a picture of an area containing a handful of prosperous and fast-growing economies (such as Japan and Australia), another handful of relatively poor yet growing economies (such as Taiwan and South Korea), but a much larger number of poor countries struggling to break free of their ancient chains of poverty.

The development experts, in concentrating their attention on the latter countries, see a group of nations which are plagued by underproduction of everything except people.

GNP estimates for 1965 show a wide range of income, from India with its $49 billion to

The Missouri and the Mekong

Americans know what can be done with natural resources. We know that a single river can transform the lives of millions. Properly developed, it can provide food, jobs, and transport. It can be an avenue to the bounty of modern life.

What has worked here will work in Asia.

Flowing through Thailand, Laos, Vietnam and Cambodia, the Mekong river drains an area 60% the size of the Missouri Basin. But only 8½ million people live in the Missouri Basin. Thirty million draw their sustenance from the lands surrounding the Mekong. The Mekong's flow is eight times greater than the Missouri's, and its hydroelectric potential is two to three times as great.

Ten solid years of work have already gone into careful and comprehensive planning for the Mekong area. The Mekong Coordinating Committee, along with 23 donor nations and 18 United Nations agencies, have:

—invested $30 million in the most detailed study of the area.

—invested $70 million in three major projects which set the stage for full development of the region.

—identified 34 potential tributary dam sites and completed detailed studies on 11 of them.

—conducted feasibility studies on 3 of the 12 potential mainstream dam sites.

These are examples of the sound ideas and projects which will be financed by the Special Funds I propose today. They are the Asian equivalents of the Erie Canal, the Transcontinental Railroad, and the land-grant college system which transformed our own society.

President's Message
September 26, 1967

Laos with only $200 million. On a per-capita basis, however, the figures show a depressing sameness of low income, ranging from $100 or less in India, Indonesia, and Pakistan to $300 and $500, respectively, in the relatively prosperous (or simply market-oriented) countries of Malaysia and Singapore.

The task of raising per capita growth rates is bedeviled by population growth; children, after all, are consumers and not producers. Population growth rates average 3 percent or more in such countries as South Vietnam, Thailand, Taiwan, and the Philippines, and although rates are lower — about 2 percent — in India, Indonesia, and Pakistan, the latter countries with their two-thirds of a billion people find their limited resources strained to the breaking point.

Where a large work force exists, the development of production is hampered by a basic lack of skills — three-fourths of the population of the Indian subcontinent is illiterate — and where the work force is so close to the subsistence level, it is hard pressed to set aside resources for capital formation. The ratio of capital formation to GNP, which ranges from 8 percent in South Vietnam to 20 percent in Malaysia and Thailand, nowhere approaches the level attained in such fast-growing nations as Israel, with its 30-percent figure.

These countries are underdeveloped too in their trade and other financial relations, not only with outside countries but also with each other. In 1965 only 7 percent of the production of the underdeveloped Asian nations was exported, and only 12 percent of that amount was traded among the regional countries themselves.

ADB and the breakthrough

The ADB's task is to support the economic breakthrough of this appallingly poor region. With the Bank's present limited resources, its best approach is to provide seed corn in the form of investment in basic industries, to channel technical assistance to various countries, and to serve as a forum for future planning. In the latter field, the ADB already is sponsoring a comprehensive study of Asian agriculture in order to identify specific projects needed to meet the food crisis of the next decade.

The Bank's direct lending ability is still limited. Its paid-in hard-currency capital stock is not much more than $100 million, and some time will elapse before it will be able to borrow on its own account or to assemble a sheaf of bankable projects. Moreover, in the words of President Watanabe, the ADB's first loans will be "sound" so that it can establish its own credit-worthiness for future borrowing. To supplement its efforts, the World Bank and the U.S. Export-Import Bank (among other agencies) can offer similar loans and loan guarantees.

Undoubtedly the major function of the ADB at this time is to provide technical assistance to underdeveloped Asian countries. Such assistance can be provided on a non-reimbursable basis, with spending limited to 2 percent of the Bank's paid-in capital stock for each of the next five years, and with no limitations on the amount thereafter. The assistance can take the form of project feasibility surveys, suggestions on project implementation, and *ex post* evaluations of project results.

The Bank's charter permits a certain amount of equity investment — a feature which should be a stimulus to young enterprises. For such firms, ADB participation (possibly with some repurchase option) may be the best means of acquiring working capital without the risk of bankruptcy or bond defaults in the first unprofitable years of operation.

ADB and the USA

The American interest in the expansion of the ADB was highlighted this September

COMPARISON OF REGIONAL DEVELOPMENT BANKS

	Inter-American	*African*	*Asian*
Start of business	October, 1960	November, 1964	December, 1966
Nonregional members	None	None	Twelve
Developed regional members	U.S.	None	Japan, Australia, New Zealand
Votes held by under-developed countries	57.5 percent	100 percent	35.4 percent
Capital structure (eventual)	$2,150 million authorized, of which $384 million paid in (Also $1121 million in Fund for Special Operations)	$250 million authorized, of which $125 million paid in	$1,100 million authorized, of which $550 million paid in
Debt outstanding (securities issued)	$449 million	none	none
Operations: 1. Methods of operation	Direct investment; technological assistance	Direct investment; technological assistance; grants; investment in stocks	Direct loans; investment in stocks; technoligical assistance
2. Eligible institutions	Governments; government agencies; private enterprises; financial institutions for development	Governments; public enterprises; private enterprises; financial institutions for development	Governments; government agencies; political subdivisions; enterprises operating in the territory of any member; international or regional development groups
3. Maturity of loans	Ordinary capital, 8-20 yrs.; special funds, 10-30 yrs.; trust fund, 20-30 yrs.	Undetermined	Undetermined
4. Interest rates	Ordinary, 6½%; special funds, 4.00%; trust fund, 1.25-2.75%	6%	Undetermined
5. Limitations on Bank participation	Normally, less than 50 percent of project funds, also joint financing for large projects	Normally, less than 50 percent of project funds; for stock investment, less than 10 percent of the paid-in capital of an enterprise	Normally only the foreign-exchange costs of a project

when President Johnson proposed a $200-million, four-year contribution to new special funds designed to provide Asian countries with long-term, low-interest financing. The Administration proposed this type of contribution because of its interest in supporting the ADB's long-term financing capabilities, primarily through the provision of assistance for infra-structure projects.

In the President's words, "Where there are factories and power plants, there must also be dependable all-weather roads, farm equipment, and clean water supplies. The Bank must be able to lend for these long-term, as well as for short-term, necessities." Specifically, the Bank with this support should be able to move ahead in the fields of agriculture, river development, transportation, and communications.

The Administration made its $200-million pledge contingent upon other nations' pledging at least an equal amount in special-fund contributions, and upon the earmarking of U.S. funds for the purchase of U.S. goods and services for use in Asia. No cash disbursement is envisioned for fiscal 1968, and Congressional appropriations will be sought only as other nations pledge contributions to the fund. (Japan has already pledged $100 million, and Canada has also expressed a desire to contribute.)

As the ADB moves ahead on this and other fronts, it should become a very useful organization for promoting economic development in Asia. In the short run, it may play less of a role in lending than in providing technical assistance and support to demonstration projects. But in the long run, a generation hence, the Bank should be one of the most important intermediaries in channeling the flow of funds from the developed world to the less-developed countries of Asia.

—*Ronald Promboin*