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Review

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Twenty-five years of the Inter-American Development Bank

*Felipe Herrera**

From 1974, under pressure from the new trends in the world economy, international public financing began gradually to lose its relative importance for the Latin American countries. The growth of international monetary liquidity gave the international banking system an unfamiliar weight in absolute and relative terms. However, the world recession persisted, and it became evident that our countries must again seek a response to their needs in bodies such as the Inter-American Development Bank.

In the author's view, the experience of the last 25 years in Latin America shows that international public financing, from whatever standpoint, is an essential form of co-operation for the advancement of the region.

CEPAL Review wished to draw attention to the importance of the role played by the Inter-American Development Bank at a time when this institution has just completed a quarter of a century of activity on the regional and international scene. This article by its first President, Mr. Felipe Herrera, is published as a tribute to a sister institution.

*First President of the Inter-American Development Bank-

I

Some of the background to the founding of IDB

A few years after the Second World War the countries of Latin America found themselves taking second place, in their efforts to obtain a greater amount of financial co-operation, to the great international priority which was given to the reconstruction of Europe and the economic development of Africa and some regions of Asia. The inflexibility of the working policies of the public authorities of the time was also subjected to universal criticism in the continent. Both these sources of dissatisfaction, together with the region's ancient aspiration to have its own regional financial system, transformed the establishment of a regional bank into a fighting banner in the inter-American economic forums. This aspiration was not shared by the rulers of the United States in those years, who saw no point in creating new mechanisms and thought it preferable to make better use of the resources offered by private capital, by Eximbank and by the World Bank.

The initiation of the Marshall Plan in 1947 encouraged the hope that the United States, following the pattern of the programme announced for Europe, would soon make major resources available for Latin American development. These expectations proved false and a feeling of frustration surfaced at the Ninth International American Conference (Bogotá, 1948). At this Conference the countries of the region expressed their unhappiness with the amount of resources allocated to them by bilateral and multilateral public bodies. To remedy this situation they formulated the idea of establishing an inter-American bank. In March of the following year the Inter-American Economic and Social Council (CIES) completed a study of the arguments for and against the establishment of a regional financial organ, without giving an opinion either way. Later, at the special sessions held in March and April 1950, this body adopted a resolution which stated: "in the present circumstances it does not seem feasible or advisable to set up institutions of this kind".

At the Special Economic Conference (Quintandinha, November 1954) Latin America put forward for the first time some concrete ideas on

the forms which inter-American cooperation should take. Although there was a feeling of scepticism at the meeting with regard to the viability of the proposed institution, at least in the short term, a decision was taken to establish a committee of experts made up of representatives of the central banks of nine Latin American countries to prepare and submit to the Organization of American States within six months a plan for the creation of a regional financial body. The group of experts met at Santiago, Chile, in February 1955 and prepared draft statutes which were submitted to CIES so that consultations could be held with all the countries members of the inter-American system. Although this plan led to no immediate action and the idea of creating an inter-American bank was not taken up again until later, the Santiago meeting had prepared a suitable framework for systematic study of this ancient Latin American aspiration.

The OAS Economic Conference (Buenos Aires, August and September 1957) initiated a process of change in inter-American relations which culminated in Operation Pan America proposed by the President of Brazil, Dr. Juscelino Kubitschek, and supported by all the countries members of the system. Operation Pan America was a decisive factor in the establishment of IDB not only because it included a mechanism of this kind among the measures it proposed but also because it influenced the United States to decide to review its policy of co-operation in the economic and social development of Latin America.

It must be recalled that at that time President Eisenhower, by proposing the establishment of a Regional Development Agency for the Middle East, with financial participation by the United States, had accepted the possibility of incorporating regional development instruments in the existing global systems. On 12 August 1958, at a special meeting of CIES, the Under Secretary of State announced that the United States was ready to participate in a regional financial organization such as the one proposed for Latin America. This coincided with the convening of a meeting of Ministers of Foreign Affairs which was to be held in the following month with a view to analysing the proposals on which Operation Pan America was based. At that meeting the countries members of the inter-American system supported the

operation proposed by President Kubitschek and set up a group of experts to negotiate the agreement founding the new regional financial organ. That decision initiated the last stage in the establishment of IDB.

The establishment of the Bank made a reality of the ancient aspiration of the Latin American countries to have a regional financial instrument in the management of which they would have an effective role. The Bank's long period of gestation was due to the need to combine in the planned institution its Latin American characteristics and its incorporation in the inter-American system. Regionalism and multilateralism thus determined the nature and essence of the new body. The original regional characteristics of IDB were expanded from 1976, and the Bank was transformed into an international organization with the admission of West Germany, Australia, Belgium, Denmark, Spain, Finland, France, Italy, Israel, Japan, the Netherlands, Portugal, the United Kingdom, Sweden, Switzerland and Yugoslavia.

I personally had the honour from 1954 to 1959, on behalf of my country first of all and also on behalf of other sister nations, to play a part in building on this initiative, especially in my capacity as General Manager of the Central Bank of Chile and, later, as Executive Director of IMF, representing the Southern Cone. I was a member of the drafting and organizational committee of IDB and later, at the first annual meeting of the Board of Governors of IDB (San Salvador, January 1960) I was elected President of the institution, being re-elected in 1964 and 1968.

In my speech of thanks after my appointment in San Salvador I had the following to say about the challenge which lay ahead of us: "The size and quality of the Bank will be determined by human and organizational factors and by the volume of resources available and the modalities for their utilization. The Bank's success will depend basically on the people who run it. We must elucidate the true scope of the Inter-American Bank and stress that only a calm and solid beginning and clarity of purpose will enable the institution to grow and assume greater responsibilities. Those who expect so much of us must give us time and their good will in this period of formation and growth. We will search

diligently for the most suitable ways of making the Bank part of the collective awareness of our people. It has been judged necessary that the institution's headquarters should be in the United States, for convincing technical and practical reasons. This circumstance^ however, obliges us to be more vigilant than ever and keep in mind that the Bank exists to serve Latin America; the Bank and its staff must identify themselves with the vigorous and exciting reality of Latin America. We must create a sound and efficient institution which will win the trust and gain

the interest of the capital markets; but we must also be ready with the same decisiveness and the same conviction for the Bank to live and develop with its roots in our own communities. The various factors which will influence the work of the Inter-American Development Bank and the specific circumstances of the framework in which it will have to act point to the complexity of our institution. It is a banking organization specializing in the regional financing of economic development projects. However, while it is a bank, it is also 'something more than a bank'".

II

The task of IDB

The long process of gestation and negotiation described above produced a bank with clear objectives and characteristics laid down in its own Founding Agreement; however, it was the work of IDB itself which shaped its contours and determined its image and nature.

Attention must be drawn, first of all, to its capacity to mobilize resources, not only among its founding members but also in other developed countries. A regional body is in the best position, together with the countries receiving the assistance, to generate adequate local counterpart funds, IDB'S experience was very successful in this respect, since each unit of foreign currency made available was matched by the commitment of at least double the amount in local currency.

Clearly, the object of stimulating local investment around an external input is to improve the whole mechanism of savings and investment in the developing countries in both public and private spheres.

Furthermore it is clear that the institution performed effectively in areas of action not covered by other bodies. We should mention in particular:

a) The promotion of the balanced development of the continent; to this end policies were adopted which gave priority to the relatively less-developed countries and to the backward areas within each country. In my speech in San Salvador I had put my views on this topic in the follow-

ing terms: "It is a fact that our continent, made up as it is of developing nations and regions, has areas which for complex reasons are more backward than others. Our conception of the economic unity of Latin America cannot leave this reality out of account. Just as the backwardness of one part of a country can create serious problems for the whole national economy, so at the continental level areas or nations of marked underdevelopment can signify dangerous imbalances and tensions for the economic, political and social future of our community of nations. Accordingly, on the basis of the resources available and the modalities established in our statutes, we must give priority to the solution of these problems. We must not forget that we have not established an institution for individual nations but for a whole continent in all its vigour".

b) A high percentage of the Bank's portfolio was made up of loans for the strengthening of the region's physical infrastructure, because infrastructural shortcomings imposed a severe limit on the yield on any productive investment. The lack of an interlinked transport and telecommunications network and the underutilization of energy resources accentuated the distortions of a development process centralized on a few unconnected poles and hindered the conquest of the interior of Latin America and the processes of regional and national integration.

c) International financing of the agriculture

and livestock sector had been neglected before the establishment of the Bank; the Bank's work in this area therefore had a pioneering and stimulating value. The operations approved for projects of irrigation, agricultural diversification, development of cattle farming, and live stock raising and marketing make IDB the principal source of external capital for agricultural development in Latin America.

d) The solid support of the industrial sector took the form of the massive Financing of national enterprises through global loans made to promotional corporations and industrial banks and through direct operations and financing of intra-regional exports of capital goods. The importance of this latter programme should be measured not so much by the trade figures achieved as by its promotional effect. Latin American industry has also been stimulated by the purchase with Bank loans of goods and services in Latin American countries, many of which have been suppliers for project? "jianced by the Bank. In the San Salvador speech when I became the first President of the Bank I stressed that: "In the Bank's operations I give great importance to the ways in which it can work through national organs for the financing of economic development, such as promotional corporations, development banks, agricultural or industrial banks or similar financial bodies. The experience of these organizations and their knowledge of the economies and needs of their countries can make them useful channels for the Bank's resources. There are large areas generally served by medium and small private businesses where we can help with our funds and increase the number of projects. It is perhaps in agriculture and livestock and in industry that our action is most needed and can be most productive. For these purposes we must also seek the support of private sources of local financing, especially through lending institutions and stock exchanges. From what I have said it is clear that the

co-operation between the Inter-American Development Bank and promotional organs, private and central banking systems and the financial market in each country will naturally be very close".

e) The Bank has given priority to urban development in view of the intense concentration of population in Latin American cities resulting from the modernization of agriculture and the advance of industrialization. The Bank has attached great importance to financial, technical and institutional co-operation for the establishment and improvement of the infrastructure in member countries.

f) Since technological capacity is one of the most dynamic factors for development, financial support has been given for higher education and training. The Bank has joined in the efforts of the Latin American countries to increase the capacity and improve the quality and efficiency of their university and technical educational systems. The operations of IDB have been aimed mainly at strengthening those academic institutions which are most effective in the training of human resources in productive activities and at introducing or consolidating fundamental reforms in the organization of educational institutions and in teaching methods and scientific and technological research.

g) The importance of a regional bank in creating an institutional infrastructure for development cannot be underestimated. Lending activities serve as a stimulus to the whole planning process, which developed in an interesting way in the 1960s, and to the establishment and improvement of promotional organs of various kinds. A regional body also serves as a real university for development, not only because of the exchange of experience among its staff members but also because of the multiplier effect which they have when they return to take up key positions in their own countries.

III

IDB'S innovative plans

In all this work an effort has been made to act pragmatically, blending economic investment with social and "hard" financing of highly productive projects with "soft" financing. An attempt has been made to reduce the imbalance between countries with different levels of development and even between areas of unequal development within a single country. The aim has been to surmount the barrier between the public and private sectors, taking as the guideline the decisions of the Governments themselves: support has been given to state and public enterprises if in the opinion of the Government they are the main agents of national development, or to private business if the Government decided to channel international resources in that direction.

The guiding criterion has been more effective and better utilization of the resources. Together with this faithful interpretation of the objectives and targets established as their sovereign right by the countries themselves, efforts have been made to foster the capacity for innovation which is an essential requirement for success in a rapidly changing environment. The continuing search for new areas for financing, from education to tourism, from health to the financing of exports or exploitation of marine resources, despite the risks inherent in such innovations, has prompted other international bodies to follow in the steps of IDB. In the San Salvador speech I said: "These ideas lead us to the conclusion that in practice the Bank will surmount the artificial distinctions between the public and private sectors which in theory should grow stronger. The level of importance of one or the other in the economic organization of the country depends on its particular institutional structure. It is not for the Bank to interfere in this. The coexistence of public and private enterprises is a fact of our communities: in its lending policy the Bank must concern itself only with the degree of efficiency with which these activities are run and with the benefit which utilization of its funds can bring to them and to the whole national economy".

By increasing its "soft" lending the Bank was

quickly able to achieve a proper balance between its social operations and its fundamental activity of financing economic projects. This original feature of the Bank as an organ for financing social development in Latin America may be found in embryo in the regulations governing its Fund for Special Operations established in the Founding Agreement. When the idea of the Inter-American Development Bank was being discussed, the notion already existed that the balanced development of the countries of the region would require less-conventional projects or ones which were less directly productive; by their very nature such projects would need to be financed on more flexible terms. However, the Bank's work in the social sectors and the activities of the Fund for Special Operations increased considerably after the Act of Bogotá, signed at the end of the third session of the Special Commission of the Inter-American Economic and Social Council in September 1960, i.e. months before the programme of the Alliance for Progress of President J.F. Kennedy came into effect.

The Act of Bogotá meant for the Bank and for the whole of Latin America not only the adoption of previously unknown operational modalities but also the acceptance of new doctrines. The Act recognizes that the impact of economic development programmes on the welfare of the people tends to operate over the long term and, accordingly, it proposes a set of measures for social improvement, especially in rural development, housing, education and health. When the Act was signed, the United States announced that it was ready to contribute US\$500 million to the attainment of its objectives. The United States Congress allocated these resources as follows: US\$6 million to the Organization of American States for collaboration with member countries in the preparation of their development plans; US\$ 100 million to the International Co-operative Administration (ICA) for bilateral grants or aid in education, public health and technical assistance; and US\$ 394 million for the establishment of the Social Progress Trust Fund, which was to be administered by IDB, to support

the efforts of those Latin American countries which were prepared "to initiate or expand effective institutional improvements and take steps for the effective utilization of their own resources, with a view to achieving greater social progress and more balanced economic growth". On 19 June 1961, when IDB had just started operating, the Trust Agreement was signed by the United States Government and the Bank, authorizing the Bank to make loans from this Fund for the settlement and better use of land, housing for low-income groups, environmental sanitation and higher education and training. The Bank was also authorized to give technical assistance in those sectors. The Fund thus officially established the financing of social projects as one

of the Bank's operational policies.

In the early days there was some concern that the Trust Fund might distort the Bank's purpose and work by drawing it away from mainly economic projects. It must be remembered that at that time, when the member countries had hardly paid the first installment of their contributions to Bank's regular and special resources, the Social Progress Trust Fund represented a considerable increase in resources. Today we can see that no such distortion took place and that, although the Bank did considerably expand its role in the financing of social investment in Latin America, it did so without reducing the attention it gave to the economic sectors.

IV

The integration bank

Another of the Bank's functions, which was implicit in its Founding Agreement and which has been gradually developing over the years, was its role as promoter of Latin American economic integration. Although the use of the term "collective development" in the basic Charter already contained in a way the concept of regional integration, the provisions of the Agreement defining the Bank's functions referred essentially to the financing of national projects and activities. However, one of these provisions invests IDB with broader scope of action and assigns it the task of "co-operating with member countries in directing their development policies towards improved utilization of their resources in a manner compatible with the objective of a greater complementarity among their economies and promotion of orderly growth in their external trade". Although these ideas do not cover everything that is now understood by economic integration, they did provide a mandate which the subsequent development of Latin America and of the Bank itself helped to clarify.

To this end, the Bank participated in the rich intellectual process of determining the scope of regional economic integration, a concept which was only just coming into its own at the beginning

of the 1960s. Nowadays there is often talk in the United States of the "golden sixties"; this term is also very appropriate for the new coming-together in Latin America and the growth of prospects for the historic convergence of our countries in that decade.

As the intellectual influence of the Bank increased in the process of Latin American integration, there was increasing concern to invest these ideas with an operational foundation. At the fourth annual meeting of the Board of Governors (Caracas, 1963) a mechanism was set in motion for the financing of intra-regional exports of capital goods, the objective being to make them competitive with imports from other regions. The programme originally operated on the basis of lines of credit made available to national financial organs and at the start it had an allocation of US\$ 30 million from the Bank's regular resources. The programme's success can be seen by the volume of trade stimulated, by the nature of the goods traded, which represented an innovation in the region's traditional trade flows, and by the institutional improvements which resulted. The use of part of the Venezuelan resources made available to the Bank in 1975 to expand the financing of regional exports

and the establishment in 1978 of the Latin American Export Bank (BLADDEX), with its headquarters in Panama, constitute, in my view, interesting examples of the operation of this programme.

The final launching of IDB as an integration bank dates perhaps from the sixth annual meeting of the Board of Governors (Asunción, 1965). At that meeting unanimous support was expressed for the so-called "document of the four", i.e. the report on speeding up the establishment of the Latin American common market which, at the suggestion of President Frei, had been prepared a few weeks earlier for all the Heads of State of the hemisphere by Raúl Prebisch (ILPES), Carlos Sanz de Santa Maria (CIAP), José A. Mayobre (ECLAC) and the author of this article in his capacity as President of IDB. In the last part of the document we reaffirm our faith in the future of an integrated Latin America in the following terms: "We must learn to work together; we must build a community of Latin American peoples. We have still not been able to come to grips with this great task because we have not succeeded in breaking free from the mold in which our development began in the 19th century. Separated from each other and with no active relations to bring them together in a vital union, each of our countries was headed at that time along separate paths towards two great world economic, political and cultural centres. We lived in the light reflected from those centres, and this had profound consequences for the Latin America of the past which are still felt in the present. Important elements of that situation still persist; and we must break free of them if we are to cope with a changing world and with the growing tensions in our own development. We must unite our efforts to overcome these and other obstacles to Latin American development and focus our efforts on the attainment of great common goals. It is not merely a question of responding to the demands of technology or of having to work together to gain more economic room and extend the cultural, scientific and technological horizons. We must also do this in order to gain greater political weight in the international arena".

The Bank's role in the integration process was rendered more effective by two initiatives: the establishment of the Institute for Latin

American Integration (INTAL) and the subsequent establishment of the Preinvestment Fund for Latin American Integration. The idea of setting up an institute of this kind had already been proposed at the ALALC meeting in Mexico City in 1963. That meeting had discussed the need to create a mechanism to co-ordinate the various existing integration institutions in Latin America. As time was passing without anything being done along these lines, the Bank decided to set up an institution of its own to carry out training, research, dissemination and evaluation work in connection with regional economic integration.

The Preinvestment Fund for Latin American Integration was established in 1966 on the specific instructions of the Board of Governors. The Fund had an initial capital of US\$ 15 million taken from the resources for special operations, and the United States Government added a further US\$ 3.5 million from the Trust Fund for Social Progress. The Fund's primary area of action was the implementation of infrastructure projects of an integrational nature, especially in transport and communications, the organization of services at the regional level for the development of economic areas including territory belonging to two or more countries, and the establishment and expansion of basic industries which sold to multinational markets or used inputs from several countries, etc. The Fund was very useful in speeding up the integration of the region's economy, for it facilitated the identification of new multinational investment opportunities. These developments were again ratified in the 1967 Declaration of Punta del Este in which the Heads of State of the inter-American system recognized the priority which IDB should give in its work to the financing of multinational infrastructure projects, with a view to accelerating the attainment of Latin American economic unity. It is a challenge for IDB to transform itself effectively into an integration bank. Not more than 10 % of the Bank's total lending is for multinational projects; we thus reaffirm our conviction that IDB must be an instrument for promoting the financial integration of Latin America by means of joint initiatives on the part of two or more countries.

V

Final comments

Clearly, the Financial and political environment in which the Bank operates is different in 1985 from what it was in the early stages. It must be remembered that at the beginning of the 1960s economic inter-Americanism reflected a new concept of the responsibility of the United States towards Latin America; its best expression was the "Alliance for Progress". From 1968 Nixon and Kissinger changed the rules of the game by introducing a general policy of gradual abandonment of the transfer of public resources from the industrialized countries to the third world.

In the early 1960s the integration and regional unification of Latin America accelerated swiftly with the establishment of ALALC and the Central American Common Market. In recent years this trend has taken a different turn, with greater emphasis on sectoral convergence. The Latin American Economic System (SELA) is an expression of this reality, IDB has secured a permanent presence in this process and has financed major multinational infrastructure projects.

In May 1985 INTAL held a seminar to study the problem of financing the subregional organs. The Fund for the Development of the River Plate Basin (FONPLATA), the Central American Bank for Economic Integration and the Andean Development Corporation (CAF) took an active part in the seminar. This meeting noted the support which IDB had given to all the subregional financing systems and the present difficulties which those institutions were experiencing as a result of the restrictions imposed by the general indebtedness of Latin America.

The Bank was born at a time when Latin America had fluctuating development rates, a negative trade balance and low monetary reserves. In the 1970s the region achieved growth rates of 6 to 8 %; its exports increased and diversified; and its monetary reserves climbed from US\$ 3 thousand million to more than US\$ 30 thousand million. In that context the volume of lending available from international bodies declined in importance for many countries, for they had new sources of internal and external investment produced by the changing

terms of trade and of international financing. Unfortunately, with the emergence of new economic and political conditions during that decade, instead of progressing towards Latin American regionalism, the countries gave priority to poorly understood principles of economic freedom and abandoned a general tradition of democracy. In recent years, however, integrationist and democratic beliefs have been re-born in Latin America; paradoxically, this has been due in many cases to the new policies which were put into practice and which led to the excessive external financial indebtedness of the whole region.

The internal composition of the Latin American conglomeration also underwent major changes which influenced the activities of IDB. At the beginning of the 1960s Brazil was still considered a risk by international financiers (it was IDB which reopened the door to international public credit for that country). Although Venezuela was fighting to consolidate its democracy and stimulate its internal economic development, it was still a long way off from its spectacular bonanza. In South America, the conditions in Bolivia, Uruguay and Ecuador reflected a situation of acute underdevelopment which has tended to improve in these last 15 years. The nine countries of the Caribbean, now independent of the United Kingdom and the Netherlands or in the process of decolonization, were not part of the regional system and had very few links with the majority of the Latin American nations. In contrast, between 1967 and 1969 Trinidad and Tobago, Barbados and Jamaica, and more recently, Guyana, Bahamas and Suriname became members of IDB.

When IDB was established the only industrialized country to commit major resources to it was the United States. From 1962 the Bank began to win the financial collaboration of all the capital-exporting countries. In 1972 Canada became a member and since 1976 17 developed nations from outside the region have become share-holders; at this point the Bank ceased to be an organ limited strictly to the hemisphere and

became increasingly cosmopolitan.

One of the acid tests for the Bank was its access to the international capital markets, which it secured throughout these years on excellent terms and with the technical support of a first-class portfolio.

In the early days the Bank's operational activities were considered heterodox by many people, as it sought pragmatically to overcome the contradiction between conventional and soft loans, between public and private sectors, between financing and technical assistance, IDB was economic investment and social investment, between investment and preinvestment and between financing and technical assistance IDB was establishing itself in this way as the central bank for the development banks of Latin America, as the integration bank and as a truly thinking bank.

At times it has been criticized for being a bank run by its debtors, i.e. in a Latin American spirit and with a Latin America majority, and it was alleged to have become politicized. I had to rebut those arguments at the end of my term of office in March 1971 when I said: "If this Bank had not been concerned and anxious to speed up development in Latin America with a view to integration and for the benefit of the majority, none of that political motivation would be what it is. And since in the 1970s it is very probable that the pluralist framework of Latin America will become broader and more complex, I believe that we will have to harness our goodwill and intelligence in the search for agreed formulas for combining the increasing centrifugal forces; and the only way of achieving such agreement is by appeal to higher political considerations".

When I became President of the Bank in 1960,¹ I defined our responsibility towards a bank which was at the same time "something more than a bank". I tried to be consistent with that belief for a whole decade; at the conclusion of my term of office in March 1971 when I passed my functions on to the Bank's new President, my distinguished and capable friend, Antonio Ortiz Mena, I put it as follows: "Perhaps today we perceive with greater clarity all the things which we knew intuitively eleven years ago when we said that IDB was something more than a bank: a great regional public organ, with a solidly established reputation and financial capacity, which remains profoundly Latin American despite the participation of the industrialized countries, with the ultimate objective not only of modernizing production structures and merely achieving economic growth, but also of enhancing the well-being of the great masses of the Latin American people. It is something more than a bank in the increasing orientation of its institutional efforts towards the promotion of the integrated development of our peoples and in its assumption of the functions of sounding board and spokesman for the interests of Latin America. In this contribution which the Bank can and must make to assist the countries of the whole region to find their own path of independent development and prompt their creative daring, it is worth recalling the words of that unforgettable public servant, the Secretary-General of the United Nations, Dag Hammarskjöld: "Do not examine the ground before you take your next step: only the man who keeps his eyes fixed on the distant horizon will find his true path".