

CHAPTER 14

ECONOMIC DEVELOPMENT AND INTERNATIONAL INVESTMENT

THREE-FOURTHS of the people in the world live in countries that are still in the early stages of industrial development. In most of these countries, the span of human life is short and the level of living is extremely low. The expectation of life in the United States is sixty-seven years; in Latin America and in India it is thirty-five. Purchasing power per capita, before the war, was \$589 in the United States; among the 390,000,000 people of India it was \$28; among the 480,000,000 of China it was \$19. In all of the backward areas, there is an insistent demand for a better life. In almost all of them, there are ambitious plans for industrial development. Industrialization may be speeded or retarded as assistance is given or withheld by more highly developed states. But, sooner or later, it is bound to come.

The industrial countries, in their own interest, should assist in this development. In particular cases, the industrialization of backward areas may create new competition for established industries. Its total effect, however, will be substantially to increase demand for manufactured goods. Industrialization changes the composition of trade; it enlarges the volume of trade. As factories are built, machinery and equipment are required. As they come into operation, output grows, purchasing power expands, standards of living rise, and more consumers' goods are purchased from abroad. This has been the experience of the United States. Our own market for foreign goods grew as we industrialized; foreign markets for our goods have grown

as other countries have industrialized. Highly developed nations are our biggest customers. Three-fifths of our exports went to such nations before the war. Canada, with 12,000,000 people, to the north, afforded us a better market than the twenty Latin republics, with 120,000,000, to the south.

Opposition to industrialization would be bad business; it would also be bad politics. It is clear to every undeveloped country that there are two roads leading to industrial power. The one has been followed by the United States, the other by Soviet Russia. Traffic on the second of these roads might well grow heavy if obstacles were placed along the first. In contributing to the improvement of levels of living in backward areas, we serve our own interest in political stability.

American business has contributed heavily to industrialization abroad by exporting plant, equipment, and know-how, by providing managerial talent, and by lending capital funds. Upon request, the government of the United States has sent technical missions into other countries and has given them informational and advisory services. It has made extensive loans through the Export-Import Bank. It took the lead in establishing the International Bank for Reconstruction and Development and made the heaviest contribution to its funds.

In its first draft of the *Charter*, the United States did not propose that specific responsibility for the promotion of industrialization should be assigned to the ITO. It was assumed that this function fell within the jurisdiction of other intergovernmental agencies, such as the Economic Development Subcommittee of the Economic and Social Council and the International Bank. It was believed, moreover, that the *Charter* would contribute indirectly to industrial development. It was designed to open markets and thus should make it easier to earn the funds required to finance new industries. It recognized that public assistance might be required to enable such industries to get on their feet. It permitted direct subsidization and the imposition, for this purpose, of new or increased tariffs. But it banned the use of import quotas and the establishment of new preferences. It thus raised the issue that was debated for months at London, Geneva, and Havana. For, in the opinion of the undeveloped countries, industrialization will be impeded unless these

devices can be employed. The desirability of industrial development was never questioned. The issue was not whether it should be promoted, but how.

PROPOSALS FOR ECONOMIC DEVELOPMENT

Some of the proposals advanced in the name of economic development must be seen to be believed. For example: Industrial countries shall undertake "to facilitate by all means in their power" the industrialization of backward areas. Members shall "make every effort necessary to ensure that the underdeveloped countries are able to obtain on equitable terms the facilities required for their economic development." Members shall "supply one another . . . with technical skills, production goods, and the necessary credits." A member "with a favorable balance of payments and plentiful supplies of capital shall take the necessary steps to facilitate the obtaining of long-and-short-term credits by countries which request them." Recognition should be accorded to the fact that funds must be provided on a non-remunerative basis. Satisfaction should be given to the desire of local enterprise to participate in the administration and management of the developments concerned. The right of governments to make diplomatic representations on behalf of private investors should be foresworn. And where loans are refused by the International Bank, new applications should be supported by the ITO.

Other proposals were designed to preserve the freedom of undeveloped countries to impose restrictions on imports. It was proposed at London, for instance, that industrialization and diversification should be accepted as a sufficient justification for the application of such restrictions; that they should be imposed on the basis of decisions made by national tribunals in accordance with such criteria as they might employ; and that industrial countries should recognize the necessity of contracting particular industries as these industries expand elsewhere. It was further proposed, at Havana, that countries "which have not reached an advanced stage of industrialization as a whole" as well as those "in an early stage of economic development" should be free to employ import quotas "for the sole purpose of protecting the growth of industries," when "no other form of protection is available or considered satisfactory." It

was suggested, too, that such freedom should be retained during a transition period that would end when half of a country's population was engaged in manufacturing. It was urged, finally, that an autonomous Economic Development Commission should be established within the ITO. This body would have been so constituted as to resist pressure for the reduction of tariffs and facilitate release from commitments as to commercial policy.

None of these proposals was accepted. They serve, however, to reveal an attitude that is widely shared. Enthusiasm for industrial development is accompanied by little interest in the conditions that must be satisfied if such development is really to be achieved. The basic importance of natural resources, of agriculture, and other extractive industries, and of power, transportation, and communications is lost from sight; attention is centered on manufacturing. The dependence of manufactures on raw materials, skilled labor, managerial talent, wide markets, and marketing facilities is forgotten; factories are wanted whether or not they can ultimately face competition on the basis of comparative costs. The fact that construction must be carried on by local labor, using local materials, is overlooked; it seems to be assumed that factories can be imported from abroad. The obstacles to industrialization inherent in social and religious patterns, in lack of health and education, and in political instability and corruption are never mentioned; the fact that increasing population may cancel increasing output is ignored. These things are fundamental; their correction will take time. The undeveloped countries seek industrialization by some quick and easy route. By obtaining large loans with no strings attached and by offering enterprisers a monopoly of local markets, they hope to build new factories overnight. They do not believe that they must creep before they walk.

On this subject, the only affirmative proposal to come from any undeveloped country was offered by Colombia. It provided, in considerable detail, for the creation, through bilateral treaties or regional conventions, of technical institutions to study, plan, promote, and assist in conservation, industrialization, education, and general economic development. The proposal, as a whole, was not accepted, but the *Charter* was so amended as to incorporate certain of its details.

ECONOMIC DEVELOPMENT IN THE CHARTER

Affirmative provisions dealing with economic development were first drafted at the London meeting of the Preparatory Committee. At Geneva and Havana they were modified in detail and extended to cover the reconstruction of devastated regions as well as the development of backward areas.

Each member of the ITO agrees to take action designed to develop industrial and other economic resources and to raise standards of productivity within its own territory (9). Each member is to cooperate with other members, with the Economic and Social Council, with the ITO, and with other intergovernmental organizations in facilitating and promoting economic development and in providing or arranging for the provision of adequate supplies of capital funds, materials, modern equipment, and technology (10-1). This does not mean that governments themselves are under any obligation to provide such facilities; the *Charter* merely says that members of intergovernmental organizations must cooperate, within the limits of their powers, in such activities as these organizations may be authorized to carry on. It is assumed that facilities for development are normally to be obtained from private sources and it is provided that no member may impose unreasonable or unjustifiable impediments that would prevent other members from thus obtaining such facilities on equitable terms.

The ITO itself, at the request of any member, is authorized to study the resources and potentialities of the member's economy, to assist in the formulation of its plans for economic development, to furnish advice concerning the financing and carrying out of such plans, or to assist the member in obtaining such advice. It is to provide these services, in so far as its powers and resources permit, on terms to be agreed with the members requesting them (10-2). It is also authorized to promote and encourage establishments for technical training (72c). And it may make recommendations and promote agreements to facilitate an equitable distribution of skills, arts, technology, materials, and equipment (11-2). No member, however, is committed either to accept its recommendations or to participate in such agreements.

The ITO is instructed to cooperate with the Economic and Social Council and with other intergovernmental organizations on all phases of economic development, particularly those relating to finance, equipment, technical assistance, and managerial skills. Its own activities in this field will be subject to such arrangements as it may work out with these bodies and are to be carried on in collaboration with them (10-3). The division of labor between the ITO, on the one hand, and such agencies as the Economic Development Subcommittee and the International Bank, on the other, thus remains to be determined.

There is no implication in these provisions that the ITO will itself finance, construct, or operate developmental projects. The functions assigned to it are promotional and advisory. Within these limits, however, it should make an affirmative contribution to the development of backward areas.

INTERNATIONAL PRIVATE INVESTMENT

If industrialization is to be speeded, capital must be imported from abroad. If capital is to be obtained in ample volume, international private investment must be resumed. From the point of view of the undeveloped country, moreover, private investment has marked advantages: it is flexible; it is non-political; it may carry with it technical knowledge and managerial skill. Private funds, under present circumstances, are to be obtained predominantly from the United States. The belief apparently prevails, in many other countries, that Americans are under some compulsion to invest abroad. This is not the case. Ample investment opportunities exist at home. Foreign investment is voluntary; it cannot be coerced. Unless there is a reasonable prospect of profit and an assurance of security, it simply will not occur. In many undeveloped countries, though the prospect of profit is present, the assurance of security is not. Debts have been repudiated, property has been confiscated, and payments to foreign investors have been blocked. There is conspicuous reluctance to accept commitments that capital will be treated fairly, once it is obtained. Until such commitments are taken, a serious obstacle to economic development will remain.

The *Charter*, as first drafted by the United States, contained no

provisions to govern the treatment which nations should accord to foreign capital and enterprise. This subject was already covered in treaties of friendship, commerce, and navigation; a program of bilateral negotiations designed to extend and modernize this treaty structure was under way. It was feared, moreover, that investment provisions negotiated at a multilateral conference might express the lowest common denominator of protection to which any of the participants would be willing to agree. And such a watering down of the standards obtainable in commercial treaties would scarcely be acceptable to the United States.

When the chapter on economic development was written into the *Charter* at London, however, the inclusion of provisions relating to international investment was no longer to be avoided. The commitment to "impose no unreasonable impediments" to the provision of facilities for development was therefore paralleled by a commitment to "take no unreasonable action injurious to" business entities or persons supplying such facilities. In the opinion of the American business community, however, this provision proved to be inadequate. In response to suggestions made by such bodies as the National Foreign Trade Council and the National Association of Manufacturers, the inclusion of an additional article on international investment was therefore proposed by the American delegation at Geneva.

This proposal, as was expected, led to a prolonged debate. In the face of determined opposition, agreement to the incorporation of such an article was finally obtained. But the draft that emerged from the negotiations was an unsatisfactory compromise. The draft forbade discrimination against foreign capital and enterprise, but it made a number of undesirable exceptions to this rule. It required members to make just compensation for property taken into public ownership, but it recognized their right to block the transfer of such payments in accordance with their foreign exchange policies and the *Articles of Agreement* of the International Monetary Fund. These provisions, instead of promising to stimulate the flow of private capital, threatened to check it. At Havana, accordingly, the question was reopened and, after prolonged discussion, the article was thoroughly revised.

Encouragement of the international flow of capital for productive investment is now included among the stated purposes of the ITO (1-2). And recognition is given to the fact that international investment "can be of great value in promoting economic development" and that this process will be stimulated "to the extent that Members afford nationals of other countries opportunities for investment and security for existing and future investments."

These words are followed, however, by certain provisions that will arouse little enthusiasm in the United States. Members are required merely to "give due regard to the desirability of avoiding discrimination as between foreign investments." And it is recognized that any member, in so far as other agreements may permit, may "determine whether and to what extent and upon what terms it will allow future foreign investment"; that it may "take any appropriate safeguards necessary to ensure that foreign investment is not used as a basis for interference in its internal affairs or national policies"; and that it may "prescribe and give effect on just terms to requirements as to the ownership of existing and future investments" and to "other reasonable requirements" with respect to such investments (12).

But the provisions do not end here. Members must "provide reasonable opportunities for investments acceptable to them and adequate security for existing and future investments" (12-2). No member may "take unreasonable or unjustifiable action within its territory injurious to the rights or interests of nationals of other Members in the enterprise, skills, capital, arts, or technology which they have supplied" (11-1). It should be noted, moreover, that requirements as to the ownership of foreign investments must be "just" and that other requirements affecting such investments must be "reasonable."

These words, of course, must be interpreted; provision is made for their interpretation. A complaint that a benefit promised by the *Charter* has been nullified or impaired through mistreatment of foreign investors may be brought before the ITO and, upon appeal, before the International Court of Justice. If it is established that a member has violated its obligations, concessions made in trade agreements and other benefits extended under the *Charter* may be

withdrawn (VIII). There is thus provided, for the first time, the right to bring before an international tribunal cases involving the treatment of American investments abroad. There is also provided, for the first time, a powerful sanction to insure that mistreatment will not occur. The proceedings at Havana, moreover, establish a legislative history that will aid in the interpretation of the text. The objectionable provisions of the Geneva draft were deleted. Attempts to confine the concept of security to the provisions of national legislation were rejected. An effort to exclude the investment commitments from the nullification and impairment procedure was dropped.

The investment provisions of the *Charter* are but a beginning. They contain minimum requirements applying to all the members of the ITO. It is explicitly recognized that the development of particular countries may be promoted through bilateral or multilateral agreements containing tighter commitments and written in more specific terms. Members are therefore required, upon request, to participate in negotiations directed toward the conclusion of such agreements (12-2). The ITO, moreover, is authorized to formulate and promote the adoption of an investment code and to recommend and promote agreements designed to stimulate investment by eliminating double taxation and to assure just and equitable treatment to foreign enterprise (11-2).

ESCAPES FOR INDUSTRIALIZATION

In the chapter of the *Charter* that deals with economic development, more than three-fourths of the space is devoted to an elaboration of methods by which undeveloped countries may obtain release from commitments assumed in trade agreements and under the *Charter* with respect to commercial policy. The provisions there set forth are so long, so detailed, and so technical that their true import is difficult to understand. But it is in this very complexity that the major compromise essential to agreement was obtained.

The compromise, in its simplest terms, is this: an undeveloped country, wishing to establish a new industry, may use any method that is not forbidden by its trade agreements or outlawed by the *Charter*; it may not use any method forbidden by a trade agreement unless it first obtains the consent of the other parties to the

agreement; it may not use any method outlawed by the *Charter* unless it first obtains the consent of the members who would be affected or secures permission from the ITO; its freedom to use such methods may then be subject to prescribed conditions and limited in time. It is for two reasons that this simple idea is spelled out at such length: first, because release is sought, by several different means, from obligations that differ in character and are contained in different instruments; and second, because protection against unwarranted release is provided, in each case, by laying down conditions that must be fulfilled and criteria that must be satisfied and by prescribing the procedures that must be followed in minute detail. It is because they are so carefully safeguarded that these provisions are so complex.

The possible exceptions for industrialization are prefaced by two propositions: First, members recognize that "in appropriate circumstances" the employment of protective measures for the promotion of economic development is justified. Second, they recognize that "an unwise use of such measures would impose undue burdens on their own economies and unwarranted restrictions on international trade" (13-1). The provisions that follow may be briefly summarized.

The obligations from which release may be sought, in particular cases, fall into four categories: (1) commitments contained in trade agreements binding duty-free treatment or tariff rates, (2) commitments contained in the *Charter* forbidding the restriction of imports by such devices as quota systems and mixing regulations where these commitments apply to products covered in trade agreements, (3) *Charter* commitments forbidding the use of such devices where they apply to products not covered in trade agreements, and (4) *Charter* commitments forbidding the establishment of new preferences.

In the first of these cases, release may be sought in one of two ways. An undeveloped country may enter into direct negotiations with the other parties to a trade agreement and obtain release through their consent, subject to such conditions as they may impose. Or it may ask the ITO to sponsor negotiations with all of those parties to the trade agreement who would be materially

affected. If substantial agreement is obtained, the ITO may then grant a release subject to such conditions as may be agreed upon (13-3). In the second case, the procedure is the same, the only difference being that the negotiations will not be confined to parties to the trade agreement but will include all countries materially affected among the members of the ITO (13-5). Protection against unwarranted release is thus afforded by the right of affected parties to withhold consent.

For two-thirds of the world's trade, covered in trade agreements, these are the only methods by which release from obligations can be obtained. For the remaining third, not subject to such agreements, the procedures are more detailed. Here permission to employ import quotas or mixing regulations may be sought in one of three ways. First, the undeveloped country may enter into direct negotiations with members that would be affected. If these negotiations lead to agreement, it must then apply to the ITO. And if the ITO is satisfied that all members materially affected have been consulted, it may grant a release, subject to such limitations as it may impose (13-8*a*). Second, the country may apply directly to the ITO. The ITO will then inform all members that would be materially affected. If none of them objects, it will grant the release. If there is an objection, however, the ITO will consider the case presented by the applicant, the views of other members, the probable effect of the proposed measure on international trade, and its effect on standards of living within the territory of the applicant. On the basis of these considerations, it may decide to grant a release, subject to such conditions as it may impose (13-8*b*). The two procedures are thus protected either by the right of members to refuse consent or by the discretion accorded to the ITO.

The third method, like the previous two, has to do only with applications for permission to impose such devices as import quotas and mixing regulations on products not covered by trade agreements. Here, however, there is a presumption in favor of release if certain criteria are satisfied or certain conditions fulfilled. (1) Release must be granted if the ITO is convinced that the measure proposed is the one most suitable for the purpose and is "unlikely to be more restrictive of international trade than any other practicable and

reasonable measure permitted" under the *Charter*. (2) It must be granted if the ITO finds that the industry to be protected will engage in the processing of an indigenous primary commodity or a by-product that would otherwise be wasted; that the measure proposed for its protection is necessary; that it will achieve a fuller and more economic use of resources and raise standards of living; and that it will not harm international trade. In both of these cases, the criteria laid down afford a wide measure of discretion to the ITO.

In two other cases, however, release will be virtually automatic. (3) Release must be granted if the industry to be protected was first established between 1939 and 1948. (4) It must be granted if the industry processes an indigenous primary commodity and if external sales of that commodity have been sharply curtailed by new or increased restrictions imposed abroad. These two cases are thus limited in extent. In the last three cases, moreover, release must be denied if it would seriously curtail the exports of a primary commodity on which the economy of another member depends. In all four cases, the ITO is authorized to place a limit on the time during which the measure in question can be employed. During this period, the member using the measure must "avoid unnecessary damage to the commercial or economic interests of any other Member" (13-7). If this commitment is violated, the nullification and impairment provisions of the *Charter* can be called into play. Permission to impose import quotas and mixing regulations, even in these cases, is limited in time and its abuse is subject to penalties.

Three other provisions of the chapter are relevant to these escapes. In order to prevent knowledge of impending restrictions from inducing a flood of imports, applications are to be handled in secrecy (13-2). For the same reason, subject to numerous safeguards, temporary restrictions on imports may be imposed (13-4, 9). And where import quotas and other prohibited devices, affecting products not covered in trade agreements, are already in effect, they may be continued until the ITO determines whether they must be abandoned or may be retained (14).

New preferences may be granted for the promotion of economic development. But, here again, the obstacles that must be surmounted are numerous and formidable. The ITO must find that the terri-

tories of the members entering into a preferential agreement are contiguous or within the same economic region. It must find that each preference obtained on each product by each of these members is necessary to promote the economic development of that country by assuring it a sound and adequate market for a new industry and that it is sufficient to accomplish this purpose. It may not approve the agreement if it is not open to adherence by other members, if it jeopardizes the position of another member in world trade, or if it is likely to inflict substantial injury on another member, unless the agreement is modified, or the other member consents to it, or is awarded fair compensation. In approving an agreement, the ITO may require that unbound duties charged to outsiders be reduced and may fix specific margins of preference for particular products. It may not approve such agreements for an initial period of more than ten years or renew them for periods of more than five years. New preferential arrangements involving non-members or otherwise departing from these requirements are forbidden unless approved by a two-thirds vote. If preferences are inaugurated which do not conform to these rules, concessions may be withheld or benefits withdrawn from the offenders on the ground that the provisions of the *Charter* have been nullified or impaired (15).

Such is the character of the industrialization escapes. In the opinion of the undeveloped countries, their provisions are onerous in the extreme. The rules controlling import quotas were characterized by one delegate at Havana as "completely inadequate and totally unjust." Those relating to preferences were said by another to be so restrictive that permission to set up new preferential arrangements is never to be obtained. It is to be doubted that the safeguards contained in these permissive exceptions will make them as ineffective as these critics would contend. But they do serve to establish a new principle in international economic affairs: devices such as import quotas, mixing regulations, and preferences are not to be employed, without international sanction, for the development of infant industries.