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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

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REPORT AND RECOMMENDATIONS

of the

PRESIDENT

to the

EXECUTIVE DIRECTORS

on the

PROPOSED LOAN

for the

DEVELOPMENT OF SOUTHERN ITALY

October 5, 1951

CONFIDENTIAL

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

REPORT AND RECOMMENDATIONS OF THE PRESIDENT
TO THE EXECUTIVE DIRECTORS CONCERNING THE PROPOSED LOAN
FOR THE DEVELOPMENT OF SOUTHERN ITALY

1. I submit the following report and recommendations with regard to an application from the Republic of Italy for a loan of \$10 million.

PART I - OPERATIONAL BACKGROUND

2. The present would be the first loan by the Bank to Italy. Possible Bank participation in a ten year development plan for the depressed areas of Southern Italy came to the fore in Spring 1949. Almost a year later a mission went to Italy to look into the question. Thereafter, on the occasion of a visit to Rome, I suggested to government officials that the Bank would be willing to discuss the matter further with the agency administering the Plan, along the lines of development loans which might be of a continuing character and based on the dollar component of the foreign exchange impact of the Plan. The Executive Directors were informed, and received a report on the Creditworthiness of Italy dated August 15, 1950.

3. A letter from the Bank to the Governor of the Bank of Italy, dated August 21, 1950, has provided the basis for all subsequent discussions. It stated that the Bank's interest would lie in the development plan as a whole; a figure of \$10 million was mentioned as possible participation by the Bank corresponding to the dollar impact of expenditure of the first annual appropriation for the Plan; it implied that the Bank would have a continuing interest over the life of the Plan; stated that the extent of the full Bank participation over a period of years would depend upon the general evolution of the Italian economy and on satisfactory progress of the development plan; and expressed the Bank's wish to select representative projects for financing in part through the lira counterpart of the loan.

4. Following the visit of a further mission to Italy in March of this year, three reports (R-491) of the Loan and Economic Departments were submitted to the Executive Directors on July 31, 1951, appraising Italy's economic position in general, and the Development Plan for the South in particular.

5. On September 19, 1951, negotiations were opened at the Bank. Professor Ferrari-Aggradi, Secretary General of the Committee for Reconstruction, (a committee of the Italian Cabinet), was designated by the Italian Government and the prospective Borrower to negotiate the loan.

PART II - DESCRIPTION OF THE PROPOSED LOAN TO THE CASSA

Borrower

6. The Borrower would be the Cassa per Opere Straordinarie di Pubblico Interesse nell' Italia Meridionale, more familiarly known as the Cassa per il Mezzogiorno, a governmental authority which administers the Plan. It is further described in a later section.

Guarantor

7. The Guarantor would be the Republic of Italy, a member of the Bank.

Amount

8. The loan would be in the amount of \$10,000,000, in dollars.

Terms of the Loan

9. The loan would be amortized by semi-annual payments, on the basis of equal payments of principal and interest combined, the first of the principal payments being due on November 1, 1956 (5 year period of grace), and the last on November 1, 1976 (25 year maturity).

10. The loan would bear interest, including 1% commission, at the rate of $4\frac{1}{2}\%$ per annum. The first interest payment date would be May 1, 1952. A commitment charge of $3\frac{1}{4}\%$ per annum has been provided for, accruing from December 31, 1951, whether or not the loan becomes effective by that date.

Purpose

11. The Plan is noteworthy in that it seeks to develop an underdeveloped area in a country which already possesses important industrial facilities. The Plan is very large in relation to Italy's resources and will have a measurable impact on the country's balance of payments. Italy depends to a considerable extent on imports of fuel, vital foodstuffs (wheat and fats) and raw materials. Some increased imports will be required to carry out the Plan itself, but more importantly, the Plan will provide increased employment and income for a substantial number of workers whose larger consumption will in part be translated into a higher demand for imports of consumer goods. It has been estimated that expenditure of the first 100 billion lire annual appropriation for the Plan will create a demand for

additional dollar imports of all kinds amounting to about \$10 million. The direct purpose of the Bank's loan would be to meet the dollar impact of the initial stages of the Plan.

12. The impact is of course felt by the whole economy and not by the Cassa. The Bank of Italy would buy the dollars from the Cassa, against lire. When the whole loan is disbursed the Cassa would have obtained 6.25 billion lire (the equivalent of \$10 million). In the circumstances the Bank felt it should have a voice as to the uses of the counterpart. Accordingly it has been agreed that the Cassa would lend the counterpart to private companies for the financing of industrial projects which are supplementary to the Plan. These supplementary projects are connected with the Plan but they would not be financed from the Cassa's governmental appropriation because the Cassa is confining itself to basic works of a public character such as roads, irrigation, and land reclamation. Thus, as with the loans the Bank has made in the past, the proposed loan would be directed primarily towards meeting needs in foreign exchange. As a second step the Bank would concern itself with the use of the local currency counterpart. Hence separate arrangements have to be made for disbursement of the dollars and of the lire equivalent, and for the control of their use.

PART III - LEGAL INSTRUMENTS AND AUTHORITY

13. There are attached hereto, as Appendices I and II, drafts of the following documents:

- (a) Loan Agreement between the Bank and the Cassa
- (b) Guarantee Agreement between the Republic of Italy and the Bank

14. The agreements incorporate Loan Regulations No. 4 with necessary modifications. They follow the general pattern of the Bank's Loan and Guarantee Agreements, except to the extent that they give effect to the special features of the loan which are described in this report.

15. Appendix III attached hereto contains the Report of the Committee provided for in Article III, Section 4(iii) of the Articles of Agreement.

PART IV - THE DEVELOPMENT PLAN FOR THE SOUTH

Cassa per il Mezzogiorno

16. The Cassa is a government agency, established for the purpose of administering the Plan by virtue of a law of August 10, 1950, and possessing independent juridical status. It operates under the supervision of a special Cabinet Committee composed of the Ministers of Agriculture, Treasury,

Industry and Trade, Public Works and Labor and Social Security. The management of the Cassa is in the hands of a Board of Directors, to whom the General Manager is responsible. The Board is composed of a chairman appointed by the President of the Republic and of two vice-chairmen and ten members appointed by the Prime Minister. The organization is relatively small. It will have the ultimate responsibility for the execution of the Plan which, however, will be carried out through regional and local agencies both within and without the government.

Description of the Plan

17. The title of the Plan is explanatory: "The Ten-Year Plan for Economic and Social Advancement of Southern Italy."

18. The 1000 billion lire (\$1.6 billion) expenditure to be made over ten years is for the depressed part of the country to the south of a line drawn across the middle of the peninsula from a point between Rome and Naples, and including the islands of Sicily, Sardinia and Elba. This area is 40% of the area of the country. The Plan aims at the development of agriculture through reclamation, irrigation and improvement of land, and at investment in public utilities, such as aqueducts and roads. A limited investment is planned in tourist facilities and installations for storing and processing agricultural products.

19. The works and their cost, in broad categories, will be as follows:

	<u>Ten Year Plan</u>	
	<u>In billion lire</u>	<u>Equivalent in million dollars</u>
Land reclamation and irrigation	440	704
Flood and erosion control	50	80
Land transformation and settlement in land reform districts	280	448
Aqueducts and sewers	110	176
Roads	90	144
Tourist facilities	30	48
Total	1,000	1,600

Disbursement

20. Since it would be the purpose of the loan to meet the impact of expenditures distributed over a wide area, a "list of goods" would not be appropriate. The basis for withdrawals would be expenditures incurred on the Plan as a whole, as reported to the Bank in summary accounting statements. Withdrawals would be at a rate that would see the \$10 million disbursed when 100 billion lire had been expended.

Appraisal of the Plan

21. The Plan to which the proposed loan would lend aid is a realistic attempt to come to grips with a basic Italian problem - the low standard of living in the South. As a result of the Plan agricultural output should eventually increase and the better grading and processing facilities provided should make the area's products more marketable. Development of the basic facilities provided by the Plan, and the increase in purchasing power, should lead also to the establishment of industries in the area, including the industrial enterprises which would be financed in part by the lira counterpart of the proposed loan. Although the loan in itself is not likely to strengthen Italy's dollar position, it should eventually improve her overall balance of payments by saving imports and increasing exports. It will, I believe, bring added employment and help to stabilize economic and social conditions, not only in the south, but in the member country as a whole, all at a dollar cost small in relation to the size of the Plan and to Italy's balance of payments.

PART V - THE SUPPLEMENTARY PROJECTS

22. One result of expending large sums of public monies in the area should be that private capital is attracted to the South. To accelerate the process, the Cassa will be authorized to borrow funds from foreign sources and to lend the counterpart to private companies whose activity would advance the general purposes of the Plan. The lire equivalent of the proposed Bank loan would be Cassa funds supplemental to regular appropriated funds, to be lent for projects supplementary to the Plan.

23. Supplementary projects satisfactory to the Bank and the Cassa have been tentatively approved, final approval being subject to negotiation of loan contracts between the Cassa and the private companies. These loan contracts would in their general terms be subject to approval by the Bank. Private capital would participate substantially in each project; in the aggregate, participation by the Cassa and the private companies would be about equal. The total amount to be invested in each project has been discussed by the Bank and the Cassa and the maximum amount which the Cassa would advance to each has been agreed. The Cassa could propose substitutions of other projects for those that have been agreed.

24. The supplementary projects tentatively approved, among which some have higher priority than others, would be:

<u>Company</u>	<u>Type of Plant</u>
S. Ligure per l'Industria dell' Acido Tannico	Tannic acid plant in Campania
Manifatture Tessili Meridionali	Woolen mill in Campania
S. Manifatture Laniera della Calabria	Woolen mill in Calabria
Unione Nazionale Oleifici	Vegetable oil refinery in Campania
Industria Meccanica e Chimica del legno	Fiber board plant in Calabria
S.A. Centrali Agricole Meridionali	Two fruit and vegetable collection centers in Campania
S.A. Centrali Ortofrutticoli Siciliane	Fruit and vegetable collection center in Sicily
S. Montecatini	Superphosphate plant in Sicily
S. Rhodiaceta	Nylon yarn and fiber mill in Campania
S. Dalmine	Welded tubes plant in Campania

Disbursement of Lira Counterpart

25. General provisions with respect to disbursement of the lire are set forth in Sections 4.05 and 4.06 of Article IV of the draft Loan Agreement. The counterpart would be credited by the Bank of Italy to a special account of the Cassa at one of the big commercial banks, which bank would release funds against documents submitted to it by other commercial banks making payments for work done. Disbursements would be subject to the corresponding payment of the proportionate amount of private capital to be invested in each supplementary project. The International Bank would receive regular statements certifying to disbursements made, and progress reports. In the event progress of any supplementary project was not satisfactory, the Bank would reserve the right of prior approval of subsequent lira withdrawals.

PART VI - PROSPECTS OF FULFILMENT OF OBLIGATIONS

26. Despite formidable obstacles, the Italian economy has shown a steady improvement in the years since the end of the war. After a severe inflation in the early postwar years, internal financial conditions have remained fairly stable. Increases in output, particularly in industry, have brought income and consumption per head at least to prewar levels and have enabled investment to go forward at a substantial rate. The rising trend should continue, though at a modest rate in view of the rapid growth of population and the added burden of rearmament.

27. The severe disequilibrium which appeared in the Italian balance of payments after the war has been substantially reduced. The current account deficit, which was equivalent to about \$700 million in 1947, was almost eliminated last year. There was still a deficit of around \$200 million with the dollar area which was met, as in earlier postwar years, by financial assistance from the U. S. Government. This deficit, however, was only half as large as it had been in 1948, and was almost completely offset by a surplus with other countries, particularly in Europe.

28. Nevertheless the international economic position of Italy remains basically vulnerable since, broadly speaking, she imports essentials and exports non-essentials. Her major markets are in Europe whereas particularly since the war she has been heavily dependent on imports from the Western Hemisphere. After Korea, reflecting a shift in pattern of trade and deterioration of terms of trade, an overall deficit on current account reappeared, and the deficit with the dollar area increased somewhat.

29. It is still reasonable for Italy, at her present stage of development, to import capital. Consequently, her balance of payments could be said to be in equilibrium if there were a moderate inflow of long term capital to offset the current account deficit. With some further U. S. assistance, especially to cushion the impact of rearmament on the balance of payments, Italy should be able to achieve overall equilibrium in this sense, in her international accounts, in the next few years. This equilibrium may well continue to involve deficits with the dollar area balanced by surpluses with other areas, notably Europe. While the speedy resumption of full convertibility of European currencies cannot be safely assumed, there is reason to hope that such a dollar problem as may then arise could be resolved under a healthily functioning system of international payments.

30. The external debt owed or guaranteed by the Italian Government amounts to the equivalent of about \$500 million, practically all payable in U. S. dollars. If the service payments on this debt were not so largely in dollars, they would cause little difficulty, since such service amounts to only about 2% of the country's external earnings in all currencies. Since it can not be assumed that Italy will be able to convert her surpluses in other currencies into dollars, some risk attaches to lending to Italy in dollars. Nevertheless new obligations which are so small in relation to existing dollar service charges should not be beyond Italy's capacity to bear.

31. Italy's record of service on external debt is good. Already by 1947, and on Italian initiative, a settlement had been reached on the major portion of the dollar bonds and on the small amount of sterling bonds outstanding, on which service was suspended when Italy entered the war. Agreement has since been reached on practically all the remaining privately held bonds.

32. I believe that due regard has been paid to the prospects that Italy would be in a position to meet her obligations under the proposed loan and that in making it, the Bank would be acting prudently in the interests of Italy and of the members of the Bank as a whole.

PART VII - COMPLIANCE WITH ARTICLES OF AGREEMENT

33. I am satisfied that the proposed loan would comply with the requirements of the Articles of Agreement of the Bank.

PART VIII - RECOMMENDATIONS

34. I recommend that the Bank at this time grant to the Cassa per Opere Straordinarie di Pubblico Interesse nell' Italia Meridionale, with the guarantee of the Republic of Italy, a loan of \$10,000,000 for a term of 25 years, with interest (including commission) at the rate of $4\frac{1}{2}\%$ and commitment charge at $3\frac{1}{4}\%$ and on such other terms as are specified in the form of Loan Agreement and Guarantee Agreement attached hereto.

Eugene R. Black
President

Washington, D. C.
October 5, 1951

STATUTORY LOAN COMMITTEE REPORT

To: The President, International Bank for Reconstruction and Development

Report of Loan Committee under Article III, Section 4(111), of the Articles of Agreement on the proposed loan to Cassa per il Mezzogiorno

The undersigned Committee, constituted under Article V, Section 7, of the Articles of Agreement of International Bank for Reconstruction and Development (hereinafter called the Bank) hereby submits its report pursuant to Article III, Section 4(111), of said Articles in respect of the proposal that the Bank grant a loan to the Cassa per il Mezzogiorno, to be guaranteed by the Republic of Italy, in the principal amount of \$10,000,000. The purpose of this loan is to assist the Cassa per il Mezzogiorno and the Republic of Italy in meeting the foreign exchange needs resulting directly and indirectly from the carrying out of the ten-year Plan for the economic and social development of Southern Italy.

1. The Committee has carefully studied the merits of the proposal to grant such loan and the purposes for which the loan is to be made.

2. The Committee is of the opinion that the Plan toward the financing of which the proceeds of such loan are to be

applied comes within the purposes of the Bank as set forth in Article I of said Articles of Agreement, that the said Plan is designed to promote the development of the productive facilities and resources of the Republic of Italy and that the proposed loan would be in the interests of the Republic of Italy and of the members of the Bank as a whole.

3. Accordingly, the Committee finds that the said Plan merits the financial assistance of the Bank and hereby recommends the said Plan for such assistance.

COMMITTEE

/s/ R. L. Garner

/s/ Alfredo Scaglioni

/s/ A. S. G. Hoar

/s/ D. Creña de Iongh

/s/ Leonard B. Rist

/s/ Davidson Sommers

Dated at Washington, D. C.

October 5, 1951

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

DRAFT RESOLUTION NO. _____

Approval of recommendations of the President that the Bank grant a loan to the Cassa per il Mezzogiorno in the amount of \$10,000,000, to be guaranteed by Republic of Italy; authorization to President or Vice President or Assistant to the President or Loan Director or Treasurer to execute Loan Agreement, Guarantee Agreement and other documents relating thereto.

RESOLVED:

1. THAT the Executive Directors hereby approve the recommendations of the President, dated October 5, 1951, that the Bank grant a loan to the Cassa per opere straordinarie di pubblico interesse nell'Italia meridionale (Cassa per il Mezzogiorno) (hereinafter called the Borrower), to be guaranteed by the Republic of Italy, in the principal amount of \$10,000,000, maturing on and prior to November 1, 1976, in accordance with the amortization table set forth in Schedule 1 to the form of Loan Agreement between the Bank and the Borrower which has been presented to the Executive Directors with such recommendations, with interest (including commission) and commitment charge at the rates specified in said form of Loan Agreement, and

upon such other terms and conditions as are contained in said form of Loan Agreement and the form of Guarantee Agreement between the Republic of Italy and the Bank which has also been presented to the Executive Directors with such recommendations.

2. THAT the rate of commission to be charged in connection with said loan shall be 1% per annum of the principal amount of said loan from time to time outstanding; that said commission shall be included as part of the interest and service charge on said loan and shall be payable semi-annually on the dates for the payment of said interest and service charge; and that the amount of said commission so paid to the Bank shall be set aside in the special reserve as provided in Section 6 of Article IV of the Articles of Agreement of the Bank.

3. THAT the form, terms and conditions of the said forms of Loan Agreement and Guarantee Agreement be, and they hereby are, approved; and

4. THAT the President or the Vice President or the Assistant to the President or the Loan Director or the Treasurer of the Bank be, and each of them hereby is, authorized in the name and on behalf of the Bank (a) to execute with the Borrower and to deliver a loan

agreement substantially in the form of the said form of Loan Agreement presented to the Executive Directors, with such changes therein as they or any of them shall approve, the execution of said Loan Agreement by any of said officers to be conclusive evidence of his approval of any such changes; (b) to execute with the Republic of Italy and to deliver a guarantee agreement substantially in the form of the said form of Guarantee Agreement presented to the Executive Directors, with such changes therein as they or any of them shall approve, the execution of said Guarantee Agreement by any of said officers to be conclusive evidence of his approval of any such changes; and (c) to take any and all such other action and execute and deliver any and all such other documents as they or any of them shall deem necessary or proper in the premises and in order to carry fully into effect the purposes of this Resolution.