Theoretical Lies of the World Bank

In 2019, the World Bank (WB) and the IMF will be 75 years old. These two international financial institutions (IFI), founded in 1944, are dominated by the USA and a few allied major powers who work to generalize policies that run counter the interests of the world’s populations.

The WB and the IMF have systematically made loans to States as a means of influencing their policies. Foreign indebtedness has been and continues to be used as an instrument for subordinating the borrowers. Since their creation, the IMF and the WB have violated international pacts on human rights and have no qualms about supporting dictatorships.

A new form of decolonization is urgently required to get out of the predicament in which the IFI and their main shareholders have entrapped the world in general. New international institutions must be established. This new series of articles by Éric Toussaint retraces the development of the World Bank and the IMF since they were founded in 1944. The articles are taken from the book The World Bank: a never-ending coup d’état. The hidden agenda of the Washington Consensus (Mumbai: Vikas Adhyayan Kendra, 2007), or The World Bank: A critical Primer (Pluto, 2007).

The World Bank claims that, in order to progress, the Developing Countries [1] should rely on external borrowing and attract foreign investments. The main aim of thus running up debt is to buy basic equipment and consumer goods from the highly industrialised countries. The facts show that day after
day, for decades now, the idea has been failing to bring about progress. The models which have influenced the Bank’s vision can only result in making the developing countries heavily dependent on an influx of external capital, particularly in the form of loans, which create the illusion of a certain level of self-sustained development. The lenders of public money (the governments of the industrialised countries and especially the World Bank) see loans as a powerful means of control over indebted countries. Thus the Bank’s actions should not be seen as a succession of errors or bad management. On the contrary, they are a deliberate part of a coherent, carefully thought-out, theoretical plan, taught with great application in most universities. It is distilled in hundreds of books on development economics. The World Bank has produced its own ideology of development. When facts undermine the theory, the Bank does not question the theory. Rather, it seeks to twist the facts in order to protect the dogma.

In the early years of its existence, the Bank was not much given to reflecting upon the type of political economy that might best be applied to the developing countries. There were several reasons for this: first, it was not among the Bank’s priorities at the time. In 1957, the majority of the loans made by the Bank (52.7%) still went to the industrialised countries [2]. Secondly, the theoretical framework of the Bank’s economists and directors was of a neo-classical bent. Now neo-classical theory did not assign any particular place to the developing countries [3]. Finally, it was not until 1960 that the Bank came up with a specific instrument for granting low-interest loans to the developing countries, with the creation of the International Development Association (IDA).

However, the fact that the Bank had no ideas of its own did not prevent it from criticising others. Indeed, in 1949, it criticised a report by a United Nations’ commission on employment and economics, which argued for public investment
in heavy industry in the developing countries. The Bank declared that the governments of the developing countries had enough to do in establishing a good infrastructure, and should leave the responsibility for heavy industry to local and foreign private initiative [4].

According to World Bank historians Mason and Asher, the Bank’s position stemmed from the belief that public and private sectors should play different roles. The public should ensure the planned development of an adequate infrastructure: railways, roads, power stations, ports and communications in general. The private sector should deal with agriculture, industry, trade, and personal and financial services as it is held to be more effective than the public sector in these areas [5]. What this really meant was that anything which might prove profitable should be handed over to the private sector. On the other hand, providing the infrastructure should fall to the public sector, since the costs needed to be met by society, to help out the private sector. In other words, the World Bank recommended privatisation of profits combined with the socialisation of the cost of anything which was not directly profitable.
An ethnocentric and conservative vision of the world

The World Bank’s vision is marked by several conservative prejudices. In the reports and speeches of the first 15 years of its existence, there are regular references to backward and under-developed countries. The Bank sees the reasons for under-development from an ethnocentric point of view. In the World Bank’s 8th Annual Report, we read that: “There are many and complex reasons why these areas have not been more developed. Many cultures, for instance, have placed a low value on material advance and, indeed, some have regarded it as incompatible with more desirable objectives of society and the individual…” [6]. One of the causes of backwardness identified in the Report is the lack of desire or absence of will to make material progress and to modernise society. Hindus’ deep respect for cows becomes shorthand for the inherent backwardness of India. As for Africa, World Bank president Eugene Black declared in 1961: “Even today the bulk of Africa’s more than 200 millions are only beginning to enter world society ” [2]… The reactionary nature of World Bank vision has by no means been attenuated by the passing years. In the Global Development Report of 1987, the Bank wrote: “In his Principles of Political Economy (1848), John Stuart Mill mentioned the advantages of ‘foreign trade’. Over a century later, his observations are as pertinent as they were in 1848. Here is what Mill had to say about the indirect advantages of trade: “A people may be in the quiescent, indolent, uncultivated state, with all their tastes either fully satisfied or entirely undeveloped, and they may fail to put forth the whole of their productive energies for want of any sufficient object of desire. The opening of a foreign trade, by making them acquainted with new objects, or tempting them by the easier acquisition of things which they had not previously thought attainable, sometimes works a sort of industrial revolution in a country whose resources were previously undeveloped for want of energy and ambition in the people: inducing those who were satisfied with scanty comforts and little work to work harder for the gratification of their new tastes, and even to save and accumulate capital, for the still more complete satisfaction of those tastes at a future time.” [8]

The massive return of the neo-conservatives in the administration achieved by G. W. Bush (2001-2008) exacerbated its deeply materialistic and reactionary tendencies. The appointment of Paul Wolfowitz, one of the leading neo-cons, to the presidency of the Bank in 2005, has further entrenched this orientation.

Growth and development planning (in both industrialised and developing economies) is given remarkable importance in World Bank documents and the literature of the time dealing with development issues from the 1950s until the 1970s. Until the end of the ‘70s, planning was considered important for several reasons: first, planning emerged during the prolonged depression of the 1930s as a response to the chaos resulting
from laisser-faire policies; secondly, the reconstruction of Europe and Japan had to be organised; thirdly, this was still part of the thirty years of continuous economic growth that followed the Second World War and had to be managed and planned for; fourthly, the success, real or supposed, of Soviet planning undoubtedly exercised a great fascination, even for the sworn enemies of the so-called “Communist bloc”. The idea of planning was completely rejected from the early ‘80s, when neo-liberal ideologies and policies came back with a vengeance.

Another major preoccupation in the early days which was rejected after the 1980s was the decision by several Latin American countries to resort to import substitution and the possibility that other newly independent countries might follow their example.

Let us briefly review some of the economists whose work had a direct influence on and in the Bank.

**The HOS model** (Heckscher – Ohlin – Samuelson)

Ricardo’s theory of comparative advantages gained force in the 1930s through the studies of Swedish economists, Heckscher and Ohlin, later joined by Samuelson. It is the synthesis produced by the latter that is known as the HOS model. The HOS model raises the issue of factors of production – these factors are work, land and capital – and claims that each country has an interest in specialising in the production and export of goods which make greatest use of that country’s most abundant production factor – which will also be the cheapest. Free trade would then make it possible to balance out what the factors earn among all the countries taking part in free trade agreements. The abundant factor, which would be exported, would grow scarcer and thus more costly; the rare factor, which would be imported, would increase and its price would fall. This system of specialisation would bring about optimal
distribution of factors in a now homogenous market. This model would enable all economies to aim for maximal integration in the global market with positive outcome for all the trading partners. Various studies carried out later, especially those by Paul Krugman [9], to test the HOS model have shown it to be inaccurate.

In 1960, Walt W. Rostow [10] postulated five stages of development in a book entitled The Stages of Economic Growth: a Non-Communist Manifesto [11]. He claimed that all countries fell into one of the five categories and that they can only follow this route.

The first stage is traditional society characterised by the predominance of agricultural activity. Technical progress is nil, there is practically no growth in productivity and minds are not ready for change.

Next, in the stage before take-off, exchanges and techniques begin to emerge, people’s mentalities become less fatalistic and savings rates increase. In fact, this is how European societies evolved from the 15th to the early 18th century.

The third stage is take-off, a crucial stage corresponding to a quality leap, with significant increase in savings and investment rates and a move towards cumulative growth [12].
The fourth stage is the “march towards maturity”, where technical progress takes over in all fields of activity and production is diversified.

Finally, the fifth stage coincides with the era of mass consumerism [13].

Walt W. Rostow claimed that at the take-off stage, an influx of external capital (in the form of foreign investments or credit) was indispensable.

Rostow’s model is marred by over-simplification. He presents the stage of development reached by the USA after the Second World War both as the goal to aim for and the model to reproduce. Similarly, he considers that the British take-off model, with the agricultural revolution followed by the industrial revolution, should be reproduced elsewhere. He thus completely ignores the historical reality of other countries. There is no reason why each country should go through the five stages he describes.

Insufficient savings and the need to resort to external funding

In neo-classical terms, savings should precede investment and are insufficient in the developing countries. This means that the shortage of savings is seen as a fundamental factor explaining why development is blocked. An influx of external funding is required. Paul Samuelson, in Economics [14], took the history of US indebtedness in the 19th and 20th centuries as a basis for determining four different stages leading to prosperity: young borrowing nation in debt (from the War of Independence in 1776 to the Civil War of 1865); mature indebted nation (from 1873 to 1914); new lending nation (from the first to Second World Wars); mature lending nation (1960s). Samuelson and his emulators slapped the model of US economic development from the late 18th century until the
Second World War onto one hundred or so countries which made up the Third World after 1945, as though it were possible for all those countries to quite simply imitate the experience of the United States [15].

As for the need to resort to foreign capital (in the form of loans and foreign investments), an associate of Walt W. Rostow’s, Paul Rosenstein-Rodan, found the following formula: “Foreign capital will be a pure addition to domestic capital formation, i.e. it will all be invested; the investment will be productive or ‘businesslike’ and result in increased production. The main function of foreign capital inflow is to increase the rate of domestic capital formation up to a level which could then be maintained without any further aid” [16]. This statement contradicts the facts. It is not true that foreign capital enhance the formation of national capital and is all invested. A large part of foreign capital rapidly leaves the country where it was temporarily directed, as capital flight and repatriation of profits.

Paul Rosenstein-Rodan, who was the assistant director of the Economics Department of the World Bank between 1946 and 1952, made another monumental error in predicting the dates when various countries would reach self-sustained growth. He reckoned that Colombia would reach that stage by 1965, Yugoslavia by 1966, Argentina and Mexico between 1965 and 1975, India in the early 1970s, Pakistan three or four years after India, and the Philippines after 1975. What nonsense that has proved to be!

Note that this notion of self-sustained growth is commonly used by the World Bank. The definition given by Dragoslav Avramović, then director of the Economics Department, in 1964, was as follows: “Self-sustained growth is defined to mean a rate of income increase of, say, 5% p.a. financed out of domestically generated funds and out of foreign capital which flows into the country…” [17].
Development planning as envisaged by the World Bank and US academia amounts to pseudo-scientific deception based on mathematical equations. It is supposed to give legitimacy and credibility to the intention to make the developing countries dependent on obtaining external capital. There follows an example, advanced in all seriousness by Max Millikan and Walt W. Rostow in 1957: “If the initial rate of domestic investment in a country is 5 per cent of national income, if foreign capital is supplied at a constant rate equal to one-third the initial level of domestic investment, if 25 per cent of all additions to income are saved and reinvested, if the capital-output ratio is 3 and if interest and dividend service on foreign loans and private investment are paid at the rate of 6 per cent per year, the country will be able to discontinue net foreign borrowing after fourteen years and sustain a 3 per cent rate of growth out of its own resources” [18]. More nonsense!

Chenery and Strout’s double deficit model

In the mid-1960s, the economist Hollis Chenery, later to become Chief Economist and Vice-President of the World Bank [19], and his colleague Alan Strout, drew up a new model called the “double deficit model” [20]. Chenery and Strout laid emphasis on two constraints: first, insufficient internal savings, and then insufficient foreign currency. Charles Oman and Ganeshan Wignarja summarised the Chenery – Strout model as follows: “Essentially, the double deficit model hypothesises that while in the very first stages of industrial growth insufficient savings can constitute the main constraint on the rate of formation of domestic capital, once industrialisation is up and running, the main constraint may no longer be domestic savings per se, but rather the availability of currency required to import equipment, intermediary goods and perhaps even the raw materials used as industrial input. The currency deficit can thus exceed the savings deficit as the
To resolve this double deficit, Chenery and Strout propose a simple solution: borrow foreign currency and/or procure it by increasing exports.

The Chenery – Strout model is highly mathematical. It was the “in thing” at the time. For its supporters, it had the advantage of conferring an air of scientific credibility upon a policy whose main aims were, firstly, to incite the developing countries to resort to massive external borrowing and foreign investments, and secondly, to subject their development to a dependency on exports. At the time, the model came under criticism from several quarters. Suffice it to quote that of Keith Griffin and Jean Luc Enos, who claimed that resorting to external inflow would further limit local savings: “Yet as long as the cost of aid (e.g. the rate of interest on foreign loans) is less than the incremental output-capital ratio, it will ‘pay’ a country to borrow as much as possible and substitute foreign for domestic savings. In other words, given a target rate of growth in the developing country, foreign aid will permit higher consumption, and domestic savings will simply be a residual, that is, the difference between desired investment and the amount of foreign aid available. Thus the foundations of models of the Chenery-Strout type are weak, since one would expect, on theoretical grounds, to find an inverse association between foreign aid and domestic savings” [22].

The wish to incite the developing countries to resort to external aid seen as a means of influencing them

Bilateral aid and World Bank policies are directly related to the political objectives pursued by the USA in its foreign affairs.

Hollis Chenery maintained that “The main objective of foreign assistance, as of many other tools of foreign policy, is to produce the kind of political and economic environment in the
world in which the United States can best pursue its own social goals” [23].

In a book entitled *The Emerging Nations: their Growth and United States Policy*, Max Millikan [24] and Donald Blackmer, both colleagues of Walt W. Rostow’s, clearly described in 1961 certain objectives of US foreign policy: “It is in the interest of the United States to see emerging from the transition process nations with certain characteristics. First, they must be able to maintain their independence, especially of powers hostile or potentially hostile to the United States (...) Fourth, they must accept the principle of an open society whose members are encouraged to exchange ideas, goods, values, and experiences with the rest of the world; this implies as well that their governments must be willing to cooperate in the measures of international economic, political and social control necessary to the functioning of an interdependent world community”. [25] Under the leadership of the USA, of course.

Later in the book, it is explicitly shown how aid is used as a lever to orient the policies of the beneficiary countries: “For capital assistance to have the maximum leverage in persuading the underdeveloped countries to follow a course consistent with American and free-world interests the amounts offered must be large enough and the terms flexible enough to persuade the recipient that the game is worth the effort. This means that we must invest substantially larger resources in our economic development programs than we have done in our past” [26]

The volume of loans to developing countries increased at a growing pace throughout the 1960s and 1970s, as the consequence of a deliberate policy on the part of the USA, the governments of other industrialised countries and the Bretton Woods institutions, whose aim was to influence the policies of countries in the South.
Priority on exports

In one of their main contributions, Chenery and Strout claimed that resorting to import substitution is an acceptable method of reducing the deficit in foreign currency [27]. They later abandoned this position, when maintaining import substitution policies as practised by certain developing countries became one of the main criticisms levelled by the Bank, the IMF, the OECD and the governments of the major industrialised countries.

This is how other studies by economists directly associated with the World Bank turned to measuring the effective rates of protection of economies and the resulting bias in terms of utilisation of productive resources and of profitability of investments. They favoured redirecting strategies towards exports, abandoning protectionist tariffs, and, more generally, a price-fixing policy more closely related to market mechanisms. Bela Balassa, Jagdish Bhagwati and Anne Krueger [28] systematised this approach and their analyses were to leave their mark on the international institutions and become the theoretical justification for opening up trade during the 1980s and 1990s. Anne Krueger [29] wrote: “A regime promoting exports can free a country’s economy from the Keynesian yoke of under-employment since, unlike a regime of import substitution, the effective demand for its products on international markets may be virtually infinite, and thus it can always get closer to full employment, unless there is a world recession. A small export-oriented economy will be able to sell whatever quantity of goods it may produce. In other words, the country’s only constraint will be its capacity to supply the goods.” [30]. More eyewash.

The trickle-down effect
The trickle-down effect is a trivial metaphor which has guided the actions of the World Bank from the outset. The idea is simple: the positive effects of growth trickle down, starting from the top, where they benefit the wealthy, until eventually at the bottom a little also reaches the poor. This means that it is in the interests of the poor that growth should be as strong as possible, if they are to be able to lap up the drops. Indeed, if growth is weak, the rich will keep a larger part than when growth is strong.

What are the effects of this on the World Bank’s conduct? Growth should be encouraged at all costs so that there is something left for the poor at the end of the cycle. Any policy which holds back growth for the sake of (even partial) redistribution of wealth or for the sake of protecting the environment reduces the trickle-down effect and harms the poor. In practice, the actions of the World Bank’s directors are conducted in line with this metaphor, whatever the more sophisticated discourse of certain experts. Moreover the World Bank’s historians devote about twenty pages to discussions of the trickle-down31 theory and acknowledge that “This belief justified persistent efforts to persuade borrowers of the advantages of discipline, sacrifice, and trust in the market, and therefore of the need to hold the line against political temptation” [31]. They maintain that the belief gradually fell into disrepute from 1970, due to cutting remarks from an impressive number of researchers concerning the situation in both the United States and the developing countries [32]. Nevertheless, the historians note that in practice, this did
not have much effect [33], particularly since, from 1982 on, trickle-down theory made a triumphant comeback at the World Bank [34]. Obviously the trickle-down issue is inseparable from that of inequality.

The question of inequality in the distribution of income

From 1973 on, the World Bank began to examine the question of inequality in the distribution of income in the developing countries as a factor affecting the chances of development. The economics team under the direction of Hollis Chenery gave the matter considerable thought. The major World Bank book on the subject, published in 1974, was co-ordinated by Chenery himself and entitled *Redistribution with Growth* [35]. Chenery was aware that the type of growth induced by the Bank’s loans policy would generate increased inequality. The World Bank’s main worry was clearly expressed by McNamara on several occasions: if we do not reduce inequality and poverty, there will be repeated outbursts of social unrest which will harm the interests of the free world, under the leadership of the United States.

Chenery did not share Simon Kuznet’s point of view [36], that after a necessary phase of increased inequality during economic take-off, things would subsequently improve. The World Bank was firmly convinced of the need for increased inequality. This is borne out by the words of the president of the World Bank, Eugene Black, in April 1961: “Inequalities in income are a necessary by-product of economic growth (which) makes it possible for people to escape a life of poverty” [37]. Yet empirical studies carried out by the World Bank in Chenery’s day disproved Kuznets’ claims. [38]

However, after Chenery’s departure in 1982 and his replacement by Anne Krueger, the World Bank completely abandoned its relative concern about increasing or maintaining inequality to the extent that it decided not to publish relevant data in
the *World Development Report*. Anne Krueger did not hesitate to adopt Kuznets’ argument, making the rise of inequality a condition for take-off of growth, on the grounds that the savings of the rich were likely to feed into investments. Not until François Bourguignon became chief economist in 2003 did the Bank’s show any real renewal of interest in this question [39]. In 2006, the World Bank’s *World Development Report* subtitled *Equity and development* again refers to inequality as a hindrance to development [40]. At best, this approach is considered to be good marketing by J. Wolfensohn (president of the World Bank from 1996 to 2005) and his successor, Paul Wolfowitz.

*Translated by Vicki Briault*

**Footnotes**

[1] The terms used to designate the countries targeted for World Bank development loans have changed through the years. At first, they were known as “backward regions”, then “under-developed countries”, and finally, “developing countries”. Some of these have gone on to be called “emerging countries”.

[2] “The period during which the Bank held firm views on the nature of the development process but did little to reach into it extended roughly up to the late 1950s, and coincided with a phase in Bank lending in which most lending was still made to developed countries (by 1957, 52.7% of funding still went to such countries) ”, Nicholas Stern and Francisco Ferreira. 1997. ‘The World Bank as “intellectual actor’ ” in Kapur, Devesh, Lewis, John P., Webb, Richard. 1997. *The World Bank, Its First Half Century, Volume 2*, p.533.

[3] “The instruments of neo-classical analysis can be applied in a general way, quite unspecifically, to the questions posed by under-development. Under-development or blocked development is not subjected to systematic analysis in neo-classical theory” translated from Azoulay, Gerard. 2002. *Les théories du*


[9] The predominance of exchanges between economies endowed with similar factors (exchanges of similar products between industrialised economies) was established in the work of P. Krugman and E. Helpman in the 1980s.

[10] Walt. W. Rostow was an influential economist. He was also a high-ranking political advisor, becoming advisor to Robert McNamara during the Vietnam War. Some of the notes he addressed to McNamara can be consulted on the Net, dealing with the politico-military strategy to follow with regard to the North Vietnamese and their allies in 1964. One note entitled “Military Dispositions and Political Signals” dated 16 November 1964 is particularly interesting for it shows quite impressive mastery of the arts of war and negotiation (www.mtholyoke.edu/acad/intrel/pentagon3/doc232.htm). It is
worth mentioning since it highlights once more the political stakes behind the operations of the IMF and the World Bank in countries of the Periphery. Thus economic policy has to be considered in the light of its political motivation and levers.


[12] Note that W.W. Rostow claimed that Argentina had already reached the take-off stage before 1914.

[13] W.W. Rostow also claimed that the USA had permanently reached the stage of mass consumerism just after the Second World War, followed by Western Europe and Japan in 1959. As for the USSR, it was technically ready to reach that stage but first needed to make some adjustments.


[19] In 1970, Hollis Chenery became advisor to Robert McNamara, then president of the World Bank. Soon after, in 1972, the post of vice-president linked to that of chief


[24] Max Millikan, who was a member of the Office of Strategic Services (OSS) then of the Central Intelligence Agency (CIA) as it became, was the director of CENIS (Center for International Affairs at the Massachusetts Institute for Technology), with direct links to the State Department.


[26] Ibid., p.118-119.


[31] Ibid., p. 218.


[34] On the change of direction of 1981-1982, they wrote: “Poverty reduction would thus have to depend on growth and


[38] More recently, in *Capital in the Twenty-first Century* (Harvard University Press, 2014), Thomas Piketty has presented a very interesting analysis of the Kuznets’ curve. Piketty notes that Kuznets originally doubted of the validity of this theory, but that didn’t stop it becoming well renowned, and for a long time.


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