

Oral History Interview

with

J. BURKE KNAPP

Economist, Federal Reserve Board, 1940-44; adviser on German economic affairs, U.S. Department of State and German Military Government, 1944-45; special assistant to the chairman, Federal Reserve Board, 1945-48; director, Office of Financial and Development Policy, Department of State, 1948-49; economic adviser U.S. delegation to NATO, 1950-51; U.S. president of the Joint Brazil-U.S. Economic Development Commission, 1951-52; and assistant director, economics department, International Bank for Reconstruction and Development, 1950-52, director, Western Hemisphere department, 1952-56, vice president, IBRD, 1956.

Bethesda, Maryland

July 24 and 30, 1975

by Richard D. McKinzie, Harry S. Truman Library

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MCKINZIE: Mr. Knapp, would you be good enough to talk about your early ideas about Government --your attitude, rationale, and your assignments?

KNAPP: Well, I'd have to start back a little earlier than that. Life in the international field really began for me when I went to Oxford as a Rhodes scholar in 1933. I spent three years at Oxford studying politics, economics, and philosophy. When I was ready to leave in 1936 I had the idea that I would probably go into Foreign Service, although I knew that in those years the opportunities for getting into the

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Foreign Service were very restricted. As it happened, in the summer of 1936 I went to Berlin to the Olympic Games, which I thought I'd take in before I came home. In Berlin, actually through the intervention of some German and American Rhodes scholars that lived in Berlin at the time, I was recommended for a job with an American banking firm that had a branch in Berlin. I decided to take a fling at that before I came home; it would give me an opportunity to learn German and some practical financial aspects. So, I took this job thinking of it as a pretty short term arrangement before coming home and pursuing my career.

This turned out to be a very interesting job, and I decided to stay with it. I spent just six months in Berlin, then moved to London and went into the City (where I carried an umbrella like everybody else, although I never got around to wearing a bowler hat). I spent a further

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three years in the City of London, which was sort of my indoctrination in international finance, which I have pursued as a career ever since then.

I was with an Anglo-American firm called Brown, Harriman & Co., Ltd. The managing director of the firm, as he was called, was a fellow by the name of Henry Mann, who was of German origin and had a lot of German connections. He'd gotten out of Germany very early in the game and set up his headquarters in London. I owe a great deal to him, as a man of immense integrity, experience, and a real aptitude for the banking business. I always think of him as my first mentor.

The business that I was in was concentrating on international banking and the underwriting of international bond issues, which was at that time pretty primitive, although it's grown to be a huge business in international

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finance now. This was really a pioneer effort in trying to build up international bond issues. The conditions were very difficult in Britain in the thirties; there wasn't that much capital and there began to be restrictions on the British capital market for foreign issues. This made our business somewhat difficult, although we also placed bonds in continental European markets as well as in the British market.

I remember particularly an operation in which we placed bonds of the River Plate Telephone Company, which was a subsidiary of ITT, and sold these bonds all over Europe. At the time the London market itself was closed to us. This operation happened to have been quite historic in the history of ITT, because ITT at that time had very large short term debts outstanding in the

United States and they were on the point of collapse. Through our efforts, and on the credit of their Argentine subsidiary, which was one of

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the most profitable of their operations, enough money was raised to tide them over the short term cash flow problem that they had at home and keep the ITT empire intact.

MCKINZZE: Were you aware of Lord Keynes?

KNAPP: Oh, yes. My Oxford education in economics was almost pre-Keynesian, Keynes was writing at the time and things were coming out, but of course, he was at Cambridge and not at Oxford. At Oxford they don't pay much attention to Cambridge economists, so I only really later came to appreciate the values of the Keynesian doctrine.

The war broke up the business that I was in. When the war broke out in September '39, the British market closed down completely, continental Europe was soon in turmoil, and my job went out from under me. I came back to the States in January 1940, looking for work. I talked a little at that time to the State Department, thinking of

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the old idea that I might like to go into the Foreign Service. But with my experience in economics and finance, I thought that I might have a better opportunity in one of the financial agencies. I shopped around among the Treasury and the Federal Reserve Board in Washington and in the Federal Reserve Bank in New York, and, to make a long story short, I ended up by taking a job with the Federal Reserve Board.

As a matter of fact, I got two offers at the time which were both very interesting. One was from the Federal Reserve Board, which I accepted, and the other was from the Treasury, where I had a long interview at the time with Mr. Harry White, who came later to be known as the real intellectual author of the Bretton Woods institutions. Harry White was very anxious for me to come to the Treasury, but I finally decided on the Federal Reserve, not really because of any considerations about money or career, but

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just because of the people over there. The people in the Federal Reserve at that time were the chairman, Mr. Marriner Eccles; the head of the research department, as they called it, Dr. [E.A.,] Goldenweiser; the assistant head, Woodlief Thomas; and then the head of the international work, Walter Gardner. All these men were very outstanding and interesting people, and I'll have a little more to say about some of them later.

So, I ended up taking this job in the Federal Reserve. They had a personnel form that asked you to specify the lowest salary you'd accept, which I always felt was a kind of a dirty trick. So, I decided finally that I really wanted this job, and put down \$2,500; and that was my starting salary at the Federal Reserve. Of course, I probably couldn't have gotten more than \$3,000 anyway, given the salaries of those days, but I think I probably understated a little my

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experience as a graduate in economics from Stanford University, a graduate from Oxford, and four years of practical experience in international finance.

I hadn't been there more than about two or three months when another very interesting proposition came along, which I think is worth mentioning. This was with the Bank for International Settlements, in Basle, Switzerland. Its director, Per Jacobsson, later became the head of the Monetary Fund, and he was really an outstanding economist; he had great size, both physically and intellectually. He came to Washington on a recruitment expedition, wanting to get a young American economist to come and work for the BIS in Basle. The Federal Reserve in principle was prepared to release me on a sort of loan basis.

I talked to Jacobsson very seriously about it, along in February 1940. I knew some languages,

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had had this European experience, and he thought it would be a very good fit. They wanted to add some Americans, at least one, to their staff. I told Per that I was interested in principle, but that I was concerned about what was going to happen to this job in neutral Switzerland if the war heated up and Switzerland became virtually isolated in a belligerent Europe.

This was in February or March. He said, "Well, we'll fix it for the first of July. You come to work on the first of July, if we're still in business, so to speak."

Well, then came the events of April and May 1940, the invasion of Belgium, the Netherlands, and then of France; the BIS really went into mothballs for the rest of the war period. They did a lot of useful research work there, but it wasn't the kind of active life that I had expected and looked for, and so I respectfully declined.

I came to know Per Jacobsson very well

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later, when he was the head of the Monetary Fund. We used to reminisce and talk about what might have been if the BIS had been able to continue its work, or if I'd come there to spend a while in the isolation of Switzerland.

But that didn't work out. Of course, the war clouds began to gather pretty fast over the United States, and my work at the Federal Reserve came to be dominated more and more by wartime considerations. I really think of my years there as being concerned with wartime finance and postwar planning.

On the subject of wartime finance -- that is to say, the financing of the United States war effort -- I didn't personally have anything to do with it; I was strictly on the international side. But I learned a lot about it by contact with my colleagues. The Federal Reserve essentially was called upon to underwrite the war effort, and the budget immediately began to run into huge

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deficits as war expenditures began, even as the preparations for war began. Certainly after Pearl Harbor there were huge deficits in the Federal budget, and they had to be financed in large part by the banking system. There were the savings bond drives, taxes were increased, and all that, but the huge requirements of the Federal budget required the banking system to move in, to buy war bonds on a vast scale, expand the money supply, and engage in what Marriner Eccles liked to call the "monetization of the public debt." What this meant was that large public expenditures were financed by the creation of money through the banking system. The Federal Reserve, which in normal times would be exercising restraints on the supply of money because of the fear of inflation, was turned into a veritable engine of inflation. It tried to organize this through the banking system, but it had no autonomous power to control events;

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it was simply the victim of events, and the money supply was vastly expanded. The inflationary impact of that expanded money supply was held in check by price controls and wage controls, but when that backed up money supply was let loose, it led to the very serious inflation that followed immediately after the end of the war.

There were two notable personalities that came down to serve as advisers to the Federal Reserve in those days. One was Alvin Hansen, who was a professor of economics at Harvard University and a great exponent of Keynes. He was the first Keynesian disciple in the United States, and he wrote and talked a great deal. He exercised a very powerful influence in Washington, not only in the Federal Reserve but in the Treasury and the White House, in arguing the Keynesian case and how Keynes would have handled a situation such as was confronted during

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the war. Keynes had, indeed, in his writings contemplated exactly the case of war finance. Then in London he was the principal author of the British system for financing the war effort, which again ran on very similar lines with the monetization of the public debt and the insulation of the consequences through price and wage controls.

The other adviser who spent a lot of time at the Federal Reserve was Gottfried von Haberler, who was probably best known for his work in the international field. He was one of those very distinguished Austrian economists who came to the New World, to America, and settled down. He is still alive and well at Harvard as a very senior professor of economics.

MCKINZIE: You mentioned the other aspects of the Federal Reserve, the postwar planning.

KNAPP: Right. That gets more into my own particular

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work. With the outbreak of the war or very soon thereafter (and I must say I wasn't responsible for launching this, but I always thought it was a pretty foresighted thing to do), all branches of the U.S. Government were organized to concern themselves with the future occupation of Europe by U.S. forces. Partly these studies were initiated to study what Germany, as the occupying power in Europe, was doing in the occupied countries and in Germany itself. But it soon

turned in the direction of planning for what was to happen after the war, always on the assumption, which nobody ever doubted or hesitated about, that this was going to be an Allied victory. The Americans would finally become an occupying power in Europe and they'd have European problems on their hands.

So, the different agencies of Government took over portions of this problem according to their functional responsibilities, and it fell to the

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Federal Reserve to prepare studies of the continental European banking systems (somehow we never assumed that Britain was going to be our problem).

At that time there were a great many refugees from the Continent who had come to the United States in one capacity or another. I was put in charge of a program utilizing them to prepare studies of the European banking and monetary systems, with an eye to turning these into what we called military government handbooks. These were information manuals that would be put at the disposal of military government as it was set up in the continental European countries.

Here was I, just a youngster. I did know some languages, which helped, but I was put in charge of a stable of refugee economists and financial experts. We had Germans, Belgians, French, and Italians, and we were writing all these essays and studies about financial systems

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in Europe. I will say that I think they eventually proved very useful and helpful to military government.

As time went along, I became typed as a fellow that knew about this subject, and I used to go down to the War College in Charlottesville, Virginia, where they had an institute for training officers in military government, to lecture on what the systems were in these countries, and to make suggestions on how they might be administered under a regime of occupation.

MCKINZIE: Were you aware at the time that they were also studying the whole problem of occupation and postwar developments in the State Department under Leo Pasvolksy and that in fact that Treasury also had something going on?

KNAPP: Oh, we all were. As I say, this activity was spread all over Washington among the different functional agencies, and we were

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assigned a particular role in banking and currency. The Treasury was doing studies more about fiscal systems, budgets, taxes, and that sort of thing, but when it came to money then we crossed paths. At that time a very interesting controversy developed about how the U.S. forces occupying Europe could best pay their way when they invaded a country.

The initial thought was, "Oh, you pay your way in dollars." But then it was said, "Well, that's very dangerous. In the first place, the dollars might fall in the hands of the enemy. Why should

we be throwing good dollars into Europe?" I'll say that I was one of the originators of this idea: "Why don't we print currency in the local denominations?"

For example, instead of going into Germany and throwing a lot of dollars around, why not go into Germany and print marks, and call them "occupation marks." Then in the peace treaty

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we would require the German Government to accept responsibility for the marks that had been issued and convert them back into regular marks. This came to be called occupation currency, and there was a great debate about it.

It wasn't particularly a debate between Federal Reserve and Treasury, although the Treasury seemed to lean for a while on the side of using a special dollar currency. Then they became convinced of the merits of this occupation currency. In the very first American invasion, which was in North Africa, this occupation currency idea hadn't yet taken hold and the American forces paid their way in dollars. But they were specially designated dollars with a yellow seal on them instead of a green seal. The idea was that if the territories were then lost and they fell into the hands of the enemy, these yellow seal dollars could be disowned, repudiated.

As our forces went further, I just don't

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remember how extensively occupation currencies, other than occupation marks, were employed. But when it came to Germany, the system that was established was to issue occupation marks.

I might say that that led in turn to a very, very difficult problem -- and I'm getting a little away now from things that I was personally concerned with -- because Germany was occupied not by the Western Powers, but by the Allies including the Soviet Union. We prepared all these plates for the printing of the occupation marks. Of course, it made sense for the occupying powers to follow a common policy and to all use the same occupation marks, rather than different brands of occupation marks printed by different countries. That was easy to agree upon with the British and the French, because there was a unified command and a unified accounting, but then the Russians said, "Okay, where do we come in?"

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So, the Russians insisted on getting a supply of these marks, and there was a great battle and a lot of well-founded fears about it. But the Russians insisted, "We want a supply of these marks, and furthermore, we want a duplicate set of plates that we can print our own supplies on." Like a lot of things that were done during the war in the interest of maintaining the quadripartite occupation and control of Germany, the Russians were finally given plates from which to print these marks.

Well, it had been feared that the Russians would, so to speak, abuse this privilege of printing marks and of course, what they did was to go ahead and print them on a vast scale. Every Russian soldier that went into Germany had his pockets stuffed with marks with which he could

buy up all the gold watches or anything else that they were looking for. The result was a great outpouring of these occupation marks in the Soviet

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zone of occupation. Of course, the money that was spent in the Soviet zone of occupation just floated over the other areas of occupation, and it meant, in the first place, that the real goods and supplies, such as they were, in the western part of Germany could be bought up by East Germans who had this flood of marks at their disposal. That caused a drain of supplies into East Germany, but even worse it set the fires of inflation going. It could have had very serious inflationary consequences if that money had been allowed to be outstanding for very long.

What happened was that within a fairly short period of time, the regular German currency was restored and all that occupation currency was called in. This was part of what they called the monetary purge of Germany; the old Deutschemarks and the occupation marks were all called in and people were given, in exchange,

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only a fraction of the amount they had deposited. Thus this great surplus of currency that threatened to drive up prices at a terrible rate was immobilized, and the new German currency was issued in amounts which put it on a sound basis. Indeed the new Deutschemark, right from that time, became one of the hardest and most solid currencies in Europe, later on even in the world. The German mark today is as strong a currency as it is because those original measures had been taken to restrict its issue to amounts which would establish its real value.

Now, I was also concerned somewhat with the exchange control measures which were introduced in the United States as part of the war regime. This was a Treasury function, and I was concerned only sometimes in an advisory capacity. The United States had to introduce exchange control first of all from the point of view of economic warfare -- to seize all enemy

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assets in the United States. And enemy assets were not only German assets; when France was occupied, for example, all French assets were under control of the enemy and they equally had to be immobilized in the United States. Then there had to be a series of measures introduced to avoid financial manipulation by the enemy in the United States markets, and to control the proceeds of exports to assure that funds paid for exports didn't fall into enemy hands. Quite a complex mechanism of exchange controls was introduced, many of them based upon the experience of the British, who had had the same problem but two or three years earlier, and who had by that time developed a very sophisticated system of capital and exchange controls.

Pretty early in the game, like about 1943, planning began for the postwar world and the postwar international monetary system, in particular. This was the pre-Bretton Woods planning,

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and here also I played a minor role. My job in the Fed was still concentrated pretty heavily on postwar planning for military government, and the people who were working on the postwar planning for the international monetary system were the people that I mentioned earlier:

Goldenweiser, who was the top economic adviser to the Federal Reserve Board; Woodlief Thomas; and Walter Gardner. The lead in this field was taken by the Treasury, but the State Department and the Federal Reserve were both considerably involved in it. The State Department was more concerned with -- they were thinking about the postwar international trade systems commodity systems -- but there was obviously a close relationship between these two. This was Harry White's heyday, when he was planning an international monetary system based on gold, but with a considerable degree of international management introduced into the gold reserve standard. The

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feeling was that the prewar system had shown itself to be very defective; that there had been anarchy in the international monetary system because individual countries pursued their own monetary, fiscal, and economic policies; that it was imperative to have some international coordination of monetary policy; and that in particular the great evil of competitive depreciation in exchange rates had to be brought under control. The feeling was that during the prewar years, as the world was emerging from the great depression, many countries had played the game of artificially manipulating the exchange rates of their currencies in order to gain advantage in the international market place. They would depreciate their currencies in order to sell their exports more cheaply in external markets. Of course, this was a kind of "beggar my neighbor" policy, because, as they depreciated, the countries buying their exports began to run into deficits, and they in turn would try to depreciate. This

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could easily have degenerated into a competitive race, with everybody trying to depreciate against everybody else in order to gain trading advantage. This was a pretty chaotic system.

So, the basic idea of Harry White was to establish an international mechanism by which countries would consult together with respect to their monetary policies, particularly their exchange rate policies, and to establish an international authority in this field, which subsequently became the International Monetary Fund. This would be the arbiter of exchange rates and would decide when a country was in such a chronic deficit position that its currency ought to be devalued in order to achieve equilibrium.

Countries would have to come to an international court to get a judgment before they engaged in exchange depreciation.

Of course, a very important question was just how much authority to vest in this central agency.

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If you vested sufficient authority in it, it would become in fact an international central bank; monetary policy and exchange rate policy in the individual countries would be subordinated to the will of this central authority.

Well, nobody really pursued the idea to such an extreme, although some people thought that, in setting up the Monetary Fund with limited powers of surveillance, discussion, and debate, it

might eventually accrue more and more power to itself and become a really dominant world monetary authority.

MCKINZIE: Mr. Knapp, do you recall at that time discussions about Lord Keynes' proposal, which vied for a short time? I think the U.S. Treasury indicated that it was not going to participate in such a program, but was it seriously considered by other people or by yourself?

KNAPP: Yes, it was very seriously considered and

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studied. The Bretton Woods Conference took place in October 1944, and there was a preliminary meeting at Atlantic City early in '44 or late 1943 where delegations came from the principal countries. In particular, Keynes came from Britain and White from the United States, championing the respective proposals which they had drawn up and had by that time exchanged. It was at Atlantic City that the basic decision was made that the White plan rather than the Keynes plan should be pursued. The Keynes plan was a far simpler and intellectually more satisfying structure for monetary affairs. He would have created an international currency, which was coined the "Bancor" ("or" for gold, to get a little French in it and to convey the idea that gold was the base of the currency). This bancor would be issued by an international agency, and countries would have had far more liberal access to this international money than they ever got to the

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resources of the International Monetary Fund.

I spoke of the Monetary Fund as being a forum for the discussion and negotiation of exchange rates, but I should also have said that the International Fund, from the beginning, was conceived as a source of credit. Countries were given drawing rights on the Monetary Fund, which they could exercise by selling their own currencies to the Monetary Fund. The Monetary Fund was endowed with a massive capital, contributed by all of the countries but mostly in their own currencies. Of course, the money that was in desperate need all over the world at the time was U.S. dollars. The idea was that this U.S. dollar contribution could be drawn by other countries from time to time by sale of their own currencies in exchange for dollars. The Fund would build up stock of currencies other than dollars to that extent. But all these drawings were to be made under pretty severe

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conditions. They constituted an international line of credit to be dispensed by the authority under pretty strict conditions with respect to the performance of the borrowing countries.

The Americans felt that at least potentially (it would have all depended upon how it was administered) the Keynes plan would provide a far easier source of credit. This touched on a very critical difference between the United States and the British positions. The United States view was that if one country had a surplus and another country had a deficit in its balance of payments, it was the responsibility of the deficit country to adjust its position and get out of the hole. There was no problem with the surplus country; the surplus country was just a godfather

that was carrying the other fellow over until he could put his house in order. So, the deficit country was exhorted to cut down on imports, push up exports, and cut back on the

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scale of internal economic development in order to dampen the demand for imports and release commodities for export rather than consumption on the domestic market.

Now, the Keynes approach was fundamentally different. He said that if there is an imbalance between the surplus country and a deficit country, each of those countries is equally responsible to clear up that situation. A deficit country has to do a lot of things, but a surplus country has a fundamental obligation to take measures to adjust its position and not force its surplus upon the world. It ought to, for example, to appreciate its currency, if necessary, in order to make its exports less attractive. This would also encourage imports by its people. It ought to adopt an expansive domestic financial and fiscal policy, in order to build up demand and keep some of those goods at home that were being exported and while creating new demands for imports.

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I must say that at the time I thought that this was just heresy. But, of course, we have observed that in recent years, when the United States was in massive deficit and the Germans and the Japanese were in massive surplus, it was the United States that was lecturing the Germans and the Japanese to take expansionary measures to avoid the surpluses they were accumulating.

Another way, of course, that you can remedy a balance of payments situation is for the country that has a surplus to invest that surplus abroad and thereby restore the balance in overall payments. The shoe has been on the other foot in recent years, and it's been rather amusing to see how the United States' position has changed radically as their economic situation changed.

I was close enough to this Bretton Woods preparatory work that when the Bretton Woods Conference was being organized I was designated to participate. This was about a year before

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Bretton Woods, but we were planning the conference already at that time. The secretariat for the Conference was primarily a United States secretariat. At least I don't remember that there were any representatives from other nations; it shows how far the United States dominated the whole scene at the time.

Frank Coe was designated as the secretary of the Conference. He later came into bad troubles. He was accused of being a Communist agent and, along with Harry White, fell from the scene; in fact, he ended up by going off to live in Communist China.

But he was the general secretary of the Conference, and then under him there was to be a secretary for Committee I, which was concerned with the Monetary Fund; a secretary for Committee II, which was to consider the World Bank; and a secretary for Committee III, which was to consider various other subjects that were offshoots of the

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Conference. One of these was to reach agreement on the liquidation of the BIS, the agency that I had almost gone to work for at the beginning of the war. The BIS, in the American view at the time, was condemned because they had been trading with the enemy during the war. They were sitting there in Switzerland and had maintained relations with both sides. As a matter of fact, the reason the BIS had first been created in the twenties was to distribute German reparations to the rest of Europe through the so-called Dawes plan and later the Young plan. And they administered these German monies even during the war; they could hardly not have traded with the enemy unless they were to have abandoned the basic function for which they had been created. So this was just a kind of political vendetta, but it was pursued very hard by Henry Morgenthau and some of his Treasury associates. The Federal Reserve always took the view that the BIS should

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not be condemned for this, that it was a very useful institution and its integrity should be maintained in the postwar period. There was even some feeling, I think, in the Treasury that the BIS was a potential rival to the International Monetary Fund and it would be just as well to get rid of this institution lest it impair the workings of the new dream organization, the Monetary Fund. So, a resolution was proposed by the United States at Bretton Woods to liquidate the BIS, and it was passed under very heavy pressure from the United States. The United States wasn't even a member of the BIS, which made it all the more extraordinary that they would sponsor and push through such a resolution. The resolution called for the winding up and extinction of the BIS, but it never happened; the resolution was never carried out.

About a year before the Bretton Woods Conference, in which I had expected to participate,

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I was called to the State Department to work on the preparations for military government in Germany. I wasn't very happy about this, but the call was made in terms of a wartime duty, and I decided to move to the State Department at the end of 1943. We had people there working on the German-occupied countries, but my assignment was to work on the postwar administration of Germany itself.

MCKINZIE: Had the handbook been written at that point?

KNAPP: Yes. We'd produced our materials and we had put them in the hands of the Department of the Army for use by the military officers who would be concerned with the occupation of, first, the occupied countries, and then of Germany itself.

MCKINZIE: Did you think at the time that you might go back to the Fed?

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KNAPP: I did think of it and I did do it.

I want to just add a footnote about the Bretton Woods planning and all that. As I say, I moved out of it about a year before Bretton Woods and at the time the Bretton Woods meeting was being held, I was in the State Department on other business. However, I took a vacation at that

time and took my family up to New England. I'd been planning to go up to New England anyway, but knowing that this conference was on, I thought it might be fun to go up there and hang around the conference in a purely unofficial capacity.

I wasn't an accredited representative, but I sneaked into a few meetings. I also used to attend the meetings of "Committee IV." I said earlier that there were three committees. Well, "Committee IV" met late at night in the nightclub downstairs in the Bretton Woods Hotel after the agony of the day was over. (I might say

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that the agony of the day sometimes included drafting sessions that ran into all hours of the day and night.) Usually, if you went along in the evening to "Committee IV," you could pick up the gossip as to what had happened during the day.

And then I wangled an invitation to the final dinner, which was to celebrate the conclusion of this arduous period. The Conference had been called originally for a week or ten days, and they actually finally took two weeks. By today's standards, when you have conferences that take literally months and months to produce a major international agreement, it was an incredibly fast piece of work to draw such sweeping and intricate plans for the postwar monetary system in such a short time.

When everything was buttoned up and the charter of the Monetary Fund and the World Bank were finally drafted, all the delegations (except

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the Russians) affixed their signatures, ad referendum to governments and to eventual legislative approval, because all of this would have to go through Parliaments and the U.S. Congress. The Russians had sent a delegation to Bretton Woods but didn't take a very active part in the whole thing, although they had some pretty good people. By the time of the final dinner, nobody knew whether they were going to sign the final declaration or not. But half way through the dinner -- in a very dramatic moment -- Secretary Morgenthau, who was the head of the U.S. delegation, got up to his feet, rapped on his glass for order, and made what at that time seemed like a most magnificent announcement, namely that the Soviet delegation had received instructions from Moscow to sign the Bretton Woods Agreement. And indeed they signed it, like everybody else, ad referendum. Furthermore, they pledged a billion dollars to the Fund and a billion

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dollars to the Bank as their capital contribution to the institutions, which made them the third largest participant. The United States was the largest, the British were second, and the Soviet Union third. Of course, all of that evaporated in the months and years that followed, and the Soviet Union never joined these international organizations. It has never shown, indeed, the slightest interest of pursuing that signature that their delegation affixed on the Charter at Bretton Woods.

As I've talked about the Bretton Woods Conference and the buildup of the postwar planning in the international monetary field, I haven't even referred to the origins of the World Bank, which

was a companion piece to the Monetary Fund founded at the Bretton Woods Conference. Even though most of my later career was in the World Bank, that omission is just a striking reflection of how little attention was paid to the Bank in the pre-Bretton Woods planning or in the Bretton Woods Conference itself. I suppose if one measured the time spent during those fourteen days of work at the Bretton Woods Conference, the Bank probably didn't take more than a day and a half.

There had, of course, been a lot of pre-planning with respect to the Bank. The Bank was exclusively a U.S. idea; there was nothing really corresponding to it on the British side. It's true that in the very early stages of the Keynes scheme, it had been designed also to provide funds for reconstruction, but that faded out fast. The concept was that the International Monetary Fund was going to be a monetary authority that it was going to provide resources to iron out fluctuations in the international balance of payments and in national reserves, but it was clearly and definitely not intended to finance long-term investments. A very clear distinction

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was made between the role of the Fund in the monetary short-term financial field and the role of some other institution, which turned out to be the World Bank, in financing long-term investment requirements.

So, very little attention was paid to the Bank, and in the end the Bank charter was thrown together in great haste. The Bank charter has clauses in it that don't make any sense as far as the Bank is concerned, because they were carried over literally from the Fund charter. I could give some examples of that.

Take, for example, the structure of the organization. The head of the institution is called the "managing director" in the Fund and "the president" in the Bank, but after that the whole structure is identical; the same terminology, the same provisions. As I say, it was put together as a kind of clip and paste job at the end of the day at the Bretton Woods Conference.

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Now, the thinking about the Bank, which was mainly on the U.S. side, was that there ought to be set up as a postwar institution an agency to provide long-term investment capital to the rest of the world. It really was almost to the rest of the world, because the United States was at that time absolutely dominating the whole scene as far as capital resources were concerned. The developing countries were languishing the way they had for centuries, and the other industrialized countries, Western Europe, Japan, and the United Kingdom, were in desperate straits. The whole world looked virtually to the United States, Canada, and to some slight extent to the richer countries of Latin America, like Argentina, for support.

So, the first thing was to give it the formal title; the formal title of the World Bank is the International Bank for Reconstruction and Development. The concept was that its initial task

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would be to finance the reconstruction of the war devastated areas, and after it had tidied that little problem up, it would then move on to become a development bank for the developing

countries. That's very revealing about how little was understood at the time of the vast requirements of European and Far Eastern reconstruction.

The Bank was set up with a capital of something like 10 billion dollars, and that's to be compared with the 18 billion dollars that got poured into the Marshall plan for Europe alone.

When the World Bank was formally established and opened its doors for business in June 1946, and after a period of getting organized, the first applications that came to the World Bank were from European countries, from the French, the Belgians, the Dutch. (The British requirements were handled by a special loan to Britain directly from the United States, and I'll have more to

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say about that later. There was also a direct loan to the French.) So, the Bank was relied upon, in the first instance, to start this task of financing reconstruction of Europe. Of course, it very rapidly became apparent that its resources were totally inadequate to that task that if it threw all of its resources into that work, there would be nothing left over for the long-term task which was assigned to the Bank to finance the developing countries. This put the Bank in an impossible position.

The Bank did lend about five or six hundred million dollars in its first operations for reconstruction loans to Europe. It was only a few months after that that General Marshall launched the Marshall plan in his speech at Harvard University, and the task of financing the reconstruction of Europe and subsequently the reconstruction of Japan was assigned to other channels. The Bank got out of the business right after those

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initial loans, because by that time it had also become apparent that the requirements of the developing countries were pretty vast, too.

One of the reasons it got out of the business was because, at that time, nobody felt that the creditworthiness of the European countries or Japan was sufficient to absorb more than a small amount of loans. Of course, the Marshall plan was basically set up on a grant basis. And the Bank was an afterthought. The Bank has since developed on a scale that was hardly anticipated at the Bretton Woods Conference, in its role of financing the developing countries.

The next chapter in my career followed my joining the State Department in the beginning of 1944, to work on plans for postwar Germany. This was a planning period that was concerned, first of all, with the occupation of Germany and the establishment of quadripartite control of Germany, and then the long-run task, as it was envisaged,

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of reincorporating Germany in a world community. I was concerned with economic planning in a broad sense -- I was, in this role, getting beyond finance, money, banking, and fiscal affairs and into questions of industrial development, agricultural development, production, employment, and the whole range of the problems of the German economy.

At the time that I went into the State Department there was already developing a great controversy between the State Department and the Treasury, with the Department of the Army, for the time being heavily preoccupied with fighting the war, in a sort of a middle position and a waiting position. The controversy centered on what came to be known as the Morgenthau plan. Henry Morgenthau, who felt extremely bitterly about Germany, advocated that when the time came and Germany surrendered, it should be, in his phrase, "pastoralized." Germany should be denied the right to develop any kind of industry beyond light

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consumer goods. Heavy industry in Germany should be suppressed; the coal mines should be flooded, and coal, which was the major German industrial resource, should be denied to future generations of Germany. Germany should be reduced to a pastoral state; an agricultural economy with a little light industry. If Germany could be held in that state of subjugation, the threat of a new rise of Nazism, militarism, and aggression in Germany could be permanently extinguished.

Now, I suppose it's obvious now, with the benefit of hindsight, how ridiculous such a thesis was. Indeed, there were many at the time who regarded this as a perfectly ridiculous proposition, and the State Department took issue with this in a very fundamental way. It took the view that this was a totally unrealistic policy and that other and better ways would have to be found to integrate Germany into the world community, specifically that the planning for the

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postwar occupation of Germany in the economic and financial sense should be to restore order, to begin giving employment, and to establish control over war industries. Germany was never again to be a manufacturer of armaments or of aircraft, but an outlet would have to be given to this very talented people to find a way in the world and to develop a normal economic life, subject only to your rather narrow restrictions (as compared with the Morgenthau concept to neutralize Germany as an aggressive force). This cleavage ran very deep through Washington and frustrated a lot of postwar planning, because until that sort of an issue got settled, a lot of planning was being done in a vacuum and without much conviction that it would really be employed.

Well, nonetheless, that was the atmosphere in which I was working. I personally felt that this Morgenthau plan was totally ridiculous. Yet, the advocates of the Morgenthau plan built it

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up to the point where anybody that contested it was obviously crypto-Nazi or was at least failing to do his patriotic duty to see that nothing like this ever happened again. It was a very difficult atmosphere in which to work, but we did get ahead with our planning effort in the State Department, including the economic and financial aspects. The main problem of planning the postwar occupation of Germany was to plan the political structure. What kind of a government should you have in Germany, what should be the responsibilities of the occupying powers, and how would they go about exercising them?

Everybody was pretty clear that, in the initial stages of the occupation, there would be no government in Germany other than local municipal authorities and possibly provincial authorities, that the functions of the central government of Germany should be transferred to the occupying powers. But that led to the question of who are the occupying powers and how are they going to work together to exercise this mandate? This wasn't too difficult as between the U.S., the U.K., and France, but there was a major difficulty in trying to decide how Germany would be administered by a quadripartite system of occupying powers including the Soviet Union. At the time the Soviet Union was the Noble Ally and we all shared the task of defeating the German aggression, but it was obvious that to have the three Western Powers and the Soviet Union working in harness to administer Germany was going to be a very difficult task. It became apparent early in the game that it would be impossible for quadripartite authority to be set up and administer Germany on a unified basis. Therefore, for purposes of military administration, but also for purposes of political administration, it was decided to set up the zonal system. Germany was divided into four

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zones, and each zone was to be occupied and administered by one of the four great powers. But it was also hoped and expected at that time that there would be a strong central coordinating authority. It was called different things at different times, but the basic title was the Allied Control Council. The concept was that this Allied Control Council (of course this would be an entirely military administration in the initial stages) would be a quadripartite military organization which would govern Germany and coordinate political, economic, and financial administration in the four separate zones. We had to have a center, and so the concept was that Berlin -- the old capital of Germany -- would be the capital of Germany again, and would be the central point of administration where the Allied Control Council would be established. Contrary to expectations, it turned out to be impossible even to have a unified Berlin. There was a unified Vienna when

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Vienna was occupied; it wasn't split into zones. But as far as Berlin was concerned, finally it was carved up into four sectors and each occupying power had a separate zone in Berlin.

Now, there was further the very awkward fact that Berlin was an enclave in the Soviet zone of Germany, so that arrangements had to be made for access to Berlin from the three Western zones. A lot of time was spent in working out these conditions of access and the subsequent crisis over the Berlin blockade arose simply because the Russians, at a certain point, denied access to Berlin from the West, and trade from the Western zones of Germany was cut off. Berlin was still accessible by air, and the access by air of the occupying powers was not challenged, but the Russians did establish a land blockade of Berlin so far as the movement of goods and German people were concerned. It happens that I had quite a

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hand in this affair, but that is a later chapter in my story.

MCKINZIE: Did you have anything to do with working out these original access arrangements?

KNAPP: Well, I sat in committees where these were discussed, but my role in the committees was limited. There was a lot of planning going on across the board in the economic field, political field, military field, and there were committees to bring these people together. But I was a bystander as far as the political side was concerned. I was concerned with the economic administration.

Take the questions of financial administration in Germany, which was part of the economic task. The advocates of the Morgenthau plan said, "The Allied Powers should assume no responsibility for money and banking." If there was to be a tremendous inflation as a

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result of these occupation marks, and if the banking system collapsed, so much the better. "Let the Germans stew in their own juice. Banking and finance is very important in building up an economy, and our task is not to restore the financial and banking mechanisms. The less they are restored, the more we are assured that Germany will collapse into this state of pastoralization."

Of course, that meant that all of the planning we were doing in the State Department on these matters seemed, at the time at least, to be threatened with frustration by the application of the "hands-off" Morgenthau plan.

I spent a year, approximately, on this planning work, and then I was sent overseas in an odd capacity. By this time (this was now in early 1945) the Supreme Allied Command had been established in Versailles, pending the move into Germany. General [Dwight David] Eisenhower was

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the Supreme Commander, and he had as his political adviser a State Department officer, Ambassador Robert Murphy. I was sent over to be economic adviser to the political adviser, that is to say, the economic adviser to Bob Murphy. We worked in Versailles, and then I was sent on some advance missions into parts of occupied Germany. Actually on V-E Day I was in Essen where the great Krupp works was burning to the ground. As the advocates of the Morgenthau plan would say, "It was never to be rebuilt."

Then with the collapse of Germany and the move of the Supreme Command to Frankfurt, I moved along with the advanced contingents that went into Frankfurt to establish military government in the U.S. zone of Germany, of which Frankfurt was the temporary capital.

MCKINZIE: As the State Department man, did you have contact with the Treasury Department man, who at this time was Bernard Bernstein?

KNAPP: Yes. The civilians, such as we in State and those in Treasury, were set up with uniforms and a "simulated" rank. Bernie Bernstein was a general, and I was a colonel. I didn't have very much to do with the Treasury activities, which at that time were very heavily concentrated on two or three lines of work, first of all recovery of war booty. They went into Frankfurt to seize the gold reserves. They were concerned with rounding up the German bankers and getting them into concentration camps. They just weren't bothering about the administration

of Germany. It was an interesting conflict, because the military had officers who had been trained at Charlottesville and were supposed to come in and run the banking systems. They didn't get any encouragement from the Treasury or any advice from the Treasury, which was dominated by the concept of the Morgenthau plan and wasn't paying any attention to getting

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key institutions, organizations, and mechanisms reorganized and back on their feet. I got very alarmed about the threat of inflation; just runaway inflation. Of course, the German economy had gone through this in the early twenties, when utter economic disorder had been created by the hyperinflation. I got very concerned about this, and I wrote a memorandum at the time which is about the only document that I retained from the time. I wrote a memorandum to Murphy and said, "For God's sake, let's get about the job of reorganizing the German banking and monetary system, because otherwise they're going to have raging inflation and total disorder."

At that time, just after the occupation, this was sort of crying in the wilderness. But it wasn't long (and here I can't give you the exact chronology) till General [Lucius D.] Clay was sent over as the Military Governor of Germany.

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General Clay was a military figure, but he was a statesman. He was taking the long run view of Germany, and he wasn't there merely as a commanding general that had come in with his troops. He was a military governor with a very great sense of responsibility.

It wasn't very long before he looked over the scene and decided that this occupation was going to be a total disaster unless something was done to bring order into the German economy. He feared that Germany would rapidly descend into starvation, unemployment, and violence and he concluded that the safety of the occupying forces would require that something be done to bring things into some semblance of order.

In other words, he felt that he was there as Governor and it would be an ungovernable situation unless something was done. It was his messages back to Washington, and it was finally [Henry L.] Stimson, as the Secretary of

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the Army, who came down hard on the side that the Morgenthau plan was unrealistic and unworkable. The rationale was not because anything was good or bad for the Germans, or for the long-run future of integrating Germany into the world community, but simply that here was an occupying force in Germany which had to be protected against the starvation, plagues, and violence that would be the consequence of a total neglect of the German economic recovery. It was Clay who then began to assemble a team of economic administrators, brought General William Draper over with many other distinguished people of military and civilian backgrounds, and began building a military government and an economic policy for Germany under occupation.

He was the one that began talking about getting the Ruhr coal mines back to work, getting steel production up, getting the railways running again, getting agricultural supplies so the

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Germans could start growing their own food instead of relying upon a handout from the occupying forces. And the Morgenthau plan just faded, because it had been totally impractical for an occupying power to be in a country and try to govern it in the state of disorder that would have resulted.

MCKINZIE: Did Robert Murphy seem to be impressed by what you were telling him about the possibilities of inflation and other problems?

KNAPP: Yes. He was a political officer and he didn't have much interest in, or professional competence in, economics, but he could understand the logic of that situation. I didn't really convince anyone, and I don't think it was Murphy that convinced anyone; people were convinced by events and by the really disastrous implications of the laissez-faire, do-nothing policy. You had to put people back to work, because if people weren't back to

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work they were rioting in the streets, and then you'd have to bring in GI's to knock heads and keep people quiet. In those days there was another very serious threat -- the medical officers were frightened of the consequences in terms of disease. The American troops in occupation couldn't be immunized against all the diseases and plagues which were feared if there was not some restoration of economic order.

Well, this was all a very chaotic time. We were trying to write rules and regulations and make contact with some Germans who could be put in positions of responsibility. You have to bear in mind that all the Germans of responsibility had been swept away because it was a Nazi administration. Then you had to find people that could be trusted in civilian capacities -- starting at the level of municipal government, starting at the level of administration of the railways, starting at the level of

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the administration of the power companies.

MCKINZIE: Did you approve the business of impounding the people of responsibility who had been members of the Nazi Party? I know that other areas, people who were in Agriculture for example, found it was very difficult to carry on, because people who knew how to carry on were carried off.

KNAPP: Basically, there was a rotten crowd that had been put in charge. True, they had learned their trade, and they were doing the business, but it was a rotten crowd. They had to be displaced, and there were a lot of heads and eggs that had to be broken.

I, myself, think that the war crimes trials and all that were perfectly understandable in the spirit of the time. But if you look at it all in retrospect, I'm not so sure that we had the moral right to condemn people to death or life imprisonment. But in terms of getting

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experienced people, the argument was made everyday; "If you want to get the railroads running, put back the longtime member of the Nazi Party, and forget that identified with the slave labor practices and all the rest of it." There's a trade-off here, but at some point you just have to say, "Well, let's get rid of that gang and see if we can find some decent people to put in charge."

I was reassigned back to the States in August, 1945, so I was only in Europe for a period of eight or nine months, and in Germany itself for just a period of five months. I came back to work in the State Department and at that time was approached by my old friends in the Federal Reserve, who said, "Well, now that the war is over, we've got a lot of postwar problems and postwar functions to discharge in which the Federal Reserve has an important role." In particular, what had happened in the

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interval was that the Bretton Woods Act had been passed by the United States Congress, approving the United States adherence to and support for the International Monetary Fund and the World Bank. There had also been established, by legislation, a so-called National Advisory Council, which was supposed to manage United States international financial policies, and in particular to provide the instructions to the United States executive director in the Monetary Fund and in the World Bank and coordinate the United States overseas lending activities of the Export-Import Bank and by other agencies of Government. This council was set up with the Secretary of the Treasury as the Chairman, and the other members were the Secretary of Commerce, the Secretary of State (I should have mentioned him second because he was the ranking member under the Secretary of the Treasury, who was chairman), and the chairman of the Federal Reserve

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Board. Marriner Eccles, who was at that time the chairman of the Federal Reserve Board and with whom I had had very happy relations in my previous incarnation in the Federal Reserve, asked me to come back as his personal assistant for international affairs, specifically to assist him in discharging his role as a member of the National Advisory Council. There was at that time no International Department in the Federal Reserve system; the international work was incorporated in the Research Department and was a sort of a sub-branch of that. So I decided to return to the Federal Reserve and to resume my career there.

I was established first in this role of personal assistant to the chairman, and then they finally decided that the importance of this work deserved setting up a separate International Department, and I was the first director of this Department.

The senior man in the Federal Reserve system in the international field, who had been my boss,

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Walter Gardner, left at about the same time to join the International Monetary Fund. It was when he left that I took over and they created this new International Department.

I'd like to say just a few words at this point about Marriner Eccles, because I think he was one of the most fabulous figures of Washington in that era. Marriner Eccles came from a Mormon family in Salt Lake City, and he was something like the 23rd child of his father, who had various wives. His father apparently always said, "Well, I'm glad I kept going because Marriner was my greatest boy." He became a banker in Salt Lake and then came into prominence when he came to Washington in 1933 to testify before committees of the new Congress as to what to do about the dismal state of the Nation, then in the depths of the depression with the collapse of the banks, the banking holiday, and all that. All the big moguls from the banking world came

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down from New York and from Boston and testified before the Congress as to what should be done to restore the banking system. (I'm dramatizing this a little and I wasn't a personal participant in these events.) But here came Marriner Eccles out of Salt Lake, Utah, and apparently he made such an extraordinary impression that just over night he became a Washington celebrity. He was promptly appointed as Assistant Secretary of the Treasury, and then Roosevelt asked him to take over as the chairman of the Federal Reserve Board.

Marriner Eccles was a most remarkable man; he was totally unschooled (he might have gone through high school), and at a very early stage in his life, 18 or so, he embarked, as every good Mormon, upon a missionary life. Every Mormon has to spend a certain number of years of his life on missionary work, and he went to Edinburgh, Scotland, because he was of Scottish

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origin. I remember him telling me how he lived in some ghetto area in Edinburgh or Glasgow.

The support he got from the church was an absolute pittance, and there he was for some two or three years passing out pamphlets for the Mormon Church. His father was a big landowner and sheepowner, and when he came back to Salt Lake he went into a business career. By the time he came to Washington, he was president of the bank which was controlled by his family in Salt Lake City. He was almost illiterate in the sense that his span of attention would not permit him to read any substantial piece of paper. I'm exaggerating a little bit; that was more in his first days. By the time I got into association with him, I'm sure he could read the newspaper and read memoranda, but the way he really learned things was by people talking to him. He had a magnificent capacity to absorb things and understand them, and to have insights into complicated issues.

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He had extraordinary instincts and insights. (I say "he had;" he's still alive, though quite elderly now.) He was a fascinating type to work with, and we had somehow hit it off from the first so I was his confidant and personal assistant in this work of the National Advisory Council in the years immediately following the war.

We had some very interesting things to deal with. Of course, the Monetary Fund was getting set up and the Bank was getting set up, but the things that I particularly remember with interest were the postwar financial negotiations on several subjects.

There was the liquidation of lend-lease. During the war vast supplies had been provided to the Allies, including the Soviet Union, under the so-called Lend-Lease Act, and everything was left open about how that was all going to be settled after the war. There ensued some very important negotiations after the war with the

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various nations, including the Soviet Union, regarding these so-called lend-lease obligations. To make a long story short, the lend-lease obligations were wound up on extremely generous terms; the general concept was that we would forget about anything that had been shot, consumed, or destroyed. The lend-lease negotiations had to do with the other remaining values of stocks that had been delivered under lend-lease. It was agreed that a valuation should be placed upon those stocks and that they should be the subject of repayment over a very long term and at liberal interest rates.

Parallel with these negotiations on lend-lease were negotiations on military surpluses which were held abroad. The U.S. Army, operating generally with a pretty huge pipeline of supplies, had immense stocks piled up all over Europe, stocks that were of peacetime value: trucks, blankets, foodstuffs, textiles. There were

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billions of dollars worth, even in those days when the dollar was worth more than it is today, of stocks that it just wasn't worth turning around and shipping back home. Again, we had to reach a settlement with respect to these amounts. First we had to get a valuation placed on them, and the valuation was generally pretty generous to the European countries.

Well, aside from the liquidation of these claims and properties that were hanging over from the wartime, it became quite apparent that the World Bank wasn't going to be able to pick up the main load of reconstruction requirements in Europe; and the Marshall plan hadn't yet been conceived. In this interim period negotiations were undertaken with various countries to provide loans from the United States for reconstruction purposes, and the key country was the United Kingdom. The British organized a very high level and special mission that came to Washington

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under the chairmanship of Lord Keynes to negotiate a postwar reconstruction loan. These discussions with the British extended, however, far beyond financial assistance and into the field of the organization of postwar international trade. The United States and Britain were the two principal world trading nations, and it was logical, perhaps, that these two nations should commence the discussions about how postwar trade was to be organized. What was to be done about the quotas and restrictions on trade which had grown up during the war and in the immediate postwar period, due to the fact that most nations outside the United States were in extremely difficult circumstances and had to impose very severe controls upon imports?

So, the question of how to dismantle this system of controls and how to develop a long-run international trade system was a second subject of these Anglo-U.S. discussions which

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was equal in importance to the loan negotiations, and in the long run perhaps more significant. This was all coordinated by the National Advisory Council. The State Department, where Will Clayton was the Assistant Secretary for Economic Affairs, conducted the trade discussions, and the financial discussions were conducted by the Treasury and the Federal Reserve. Then from time to time there would be group meetings in which the trade people and the financial people would be brought together for common discussion, trying to integrate the financial settlement with the trade settlement.

For example, the United States interest was to dismantle controls. The United States wanted to export, and particularly they wanted to export their agricultural products. The British, as one example, had introduced pervasive and intricate controls with respect to all their external trade, affecting especially the importation

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of agricultural commodities, with very heavy protection for British agriculture.

So, the logic of the U.S. position was that if the United States was going to provide finance to Britain on a large scale, Britain should dismantle these controls and open their market to more free international trade.

I was concerned particularly with the British loan discussions. This was really a fascinating negotiation. Just consider who the representatives were. On the British side we had Lord Keynes and the British Ambassador in Washington, Lord Halifax. Lord Halifax was the very epitome of the British aristocracy. He had come from the very highest order of the British nobility; he was an aristocrat to his fingertips. Keynes, by comparison, was a new arrival. Keynes came from middle class origins, but Keynes was also an intellectual of the highest brilliance. He spoke the English language with magnificent

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articulation. And these two Lords, Lord Halifax and Lord Keynes, were coming to Washington as supplicants, essentially, for aid.

Well, the principals on the United States' side were Fred Vinson, Secretary of the Treasury of the United States; and Will Clayton, the Assistant Secretary of State. Now, Fred Vinson was a former semiprofessional baseball player. He had come up through politics, he had been a member of Congress; a very shrewd cookie, a very tough negotiator, and a rough and tumble politician. Just as an example, when we would have meetings in his office, with Lord Halifax and Lord Keynes across the table in all their British elegance of speech and dress, Fred Vinson, chewing tobacco all the time, would occasionally clear his throat and let go into a spittoon at the side of his desk. It was an incredible contrast of traditions, cultures, and people.

Now, Will Clayton was another type out of

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the same earthy American mold. Will Clayton had started life as a court stenographer and had no formal education. I don't know whether he ever went to high school, I doubt it; certainly not to college. But he trained in shorthand, became a court stenographer, and worked for years in the courts in Texas. By this time, of course, he had far outgrown that early beginning. Somehow he had got into the cotton business and built up the Anderson-Clayton Trading Company in Houston, Texas, which had made him a multi-millionaire and a very worldly man, but still a man who obviously came from common clay.

This was quite a confrontation of the old world and the new world. And bear in mind that all the cards were in the hands of Vinson and Clayton because of the position of the United States. It had emerged virtually unscathed from the war physically, with a tremendous buildup of its industrial power, and with an agricultural output that made it

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virtually the granary of the world. This meant that the Americans had tremendous power and authority. So, it was a rather unequal contest in terms of the cards that were in their hands, although Keynes and Halifax played their cards with consummate ability.

Well, these negotiations on the loan had to do with the amount of the loan and with the financial terms; the period of repayment, the terms of amortization, and the interest rate. They also had to do with the dismantling of the British system of exchange and trade controls, including very importantly, the dismantling of the imperial preference system, which the British had built up even before the war in the depression years and maintained during the war. The British Commonwealth included a great many of the important trading nations of the world, such as Canada, Australia, New Zealand, South Africa, and India. These were all under the

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system of what was called imperial preference. It was a closed trading society in which the nations of the Commonwealth had virtually free trade back and forth among themselves, but with high walls of tariff protection, quotas, and restrictions against external trade. The United States saw its interest in breaking down the imperial preference system and opening up these countries to American trade and American exports. So, these issues were negotiated simultaneously with the British loan, and -- to put it bluntly -- the British loan was used as a lever to pry open this restrictive system that the British had adopted and to open up new opportunities for American foreign trade.

The negotiations were eventually successful. On the trade side lots of concessions were made and it was agreed that, like the Monetary Fund in the monetary and financial field, there should be set up an international

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authority in the field of international trade, to regulate tariffs, quotas, and other instruments of trade restriction. It was agreed in principle that there should be established a so-called International Trade Organization, ITO. And a year or so later the U.S. and the U.K. jointly

invited the rest of the trading nations of the world to come to a conference in Havana, Cuba, to draw up a charter for international trade. Indeed, it was a very ambitious charter, and it extended out not only to international trade but to international investment. A code of conduct was laid down with respect to international investment. Investors, on the one side, were to respect the laws and traditions of the recipient country, the so-called host country; the host country, on the other hand, was to provide free access, and to undertake not to discriminate against, and certainly not to expropriate foreign investments that came to

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their soil unless fair compensation was paid.

This ITO charter is another chapter, and I didn't have much to do with it myself. Suffice it to say that a far-reaching charter was negotiated at Havana, Cuba, but it never came into being; it was never ratified and it never became effective.

MCKINZIE: As I recall, the British asked originally for six billion dollars and they finally got three and three quarters billion. They contended that they needed the six billion to restore British industry and the whole British economy to normality because of the devastation of the war. Well, someone who is not sophisticated in matters of economics might say, "If they computed that it took six billion dollars to do that, and they only got slightly more than half of it, then obviously they couldn't undertake the task of reconstruction. Therefore, by giving them less than what they needed, it was simply a stopgap

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measure, and the crisis of the British economy was simply postponed." Was there any validity in that sort of argument?

KNAPP: Oh, yes. After all, it was the Marshall plan that came on later to provide some 18 billion dollars, and I dare say the British share in that was four or five, so that this initial British loan has to be regarded as just a tiding over. They did ask for more; there was very hard bargaining on the amount, and they always kept saying: "Now, if you're expecting us to dismantle all these controls, we can't do it unless we are assured that we have the money to import the volume of imports which will be required in a market unprotected by tariffs, quotas, and so on." That's why no really conclusive agreement was reached at the time of the British loan discussions on trade policy, although a very important foundation was laid for the eventual ITO discussions. But then the

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ITO discussions themselves finally foundered.

Let me go on to say that after these British loan discussions were concluded, the next customer to arrive in Washington was the French, and the French delegation was led by another extraordinary figure, Leon Blum. I don't know what capacity he had in the French Government at that time. He was an outstanding figure in postwar France. He was of Jewish origin, and I guess he had gone underground during the war. I don't remember that he actually emigrated

during the German occupation, but he had been no part of the [Henri Philippe] Petain government. Although he was Jewish by race, I always think of him as the very embodiment of French culture; an elegant man with very elegant speech. And so he was the next to arrive with his plea for assistance, and there were not nearly such long and extensive negotiations. International trade policy played a much lesser part, because

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the French role in international trade was very minor as compared with the British, particularly as compared with the British Commonwealth system. But I always think of Leon Blum as one of the most outstanding personalities that I've had an opportunity to meet. My personal participation in the British loan discussions was, as it happens, very extensive, but in the case of the French loan, it was over more quickly. The British loan, to a certain extent, had set a pattern and the French talks were concluded with a lesser amount, but with also very liberal terms.

I didn't mention that the British negotiations involved a lot of discussion as to what period of repayment and what interest rate would be suitable for the occasion. I can't quote the exact terms, but the British loan was made for, I think, a period of 35 or 40 years at an interest rate of something like 2 or 2-1/2 percent. Bear

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in mind that that was in another world when interest rates in general were very low, and yet obviously that was a very lenient interest rate. Furthermore, there were provisions for interest to be forgiven in certain years or postponed in certain years if the British economy fell into special difficulties -- and similarly with the French loan. These loans were on very liberal terms, and represented at that time a major concession and gesture by the United States toward the reconstruction of the European economies. They are not to be compared with the Marshall plan; they were, after all, loans, and not as generous as the subsequent Marshall plan aid, which was provided very largely on a grant basis.

MCKINZIE: Mr. Knapp, were there studies of the ability of these nations to repay the loans?

KNAPP: Oh, yes, but they usually came to pretty pessimistic conclusions. For example, nobody had

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any idea that all the assistance that was provided to Germany under military occupation would ever be collectible. There were vast amounts of food supplies and raw material supplies that were all just written off.

That does take me forward a bit to the Marshall plan, and I would like to say something about that. I was still at the Federal Reserve when the Marshall plan was inaugurated by the speech at Harvard University by General Marshall. Dean Acheson was the intellectual author of the Marshall plan and had a large hand in drafting that speech, and what it said, in effect, was, "We, the United States, have come to recognize that we have a very great economic interest, as well as a political interest, in the restoration of the economies of the war-devastated countries in Europe.

We would be prepared," said General Marshall, without a shadow of authority from anybody and certainly not from the U.S. Congress, which

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eventually had to provide the money, "to enter upon negotiations with the European community" (this included the British as well, but not the Germans, who were still under occupation) "provided they will get together and draw up a long term plan of reconstruction." The ball was thrown right across the Atlantic for the Europeans to get together and draw up this plan.

The response in Europe was very rapid and very positive. It was obviously positive, but it was surprisingly how rapidly a meeting was called in Paris of the European countries to draw up a plan for reconstruction. Marshall's offer included the Soviet Union as well, and the Soviet Union was invited to Paris to participate in the drawing up of these reconstruction plans.

It was like the earlier story of the Bretton Woods Conference. The Soviet Union participated, sent a delegation, but soon after that they faded out of the picture. This was about the time of

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the Iron Curtain speech, Winston Churchill's famous speech, in which he saw the Iron Curtain ringing down over Europe. The Soviet Union withdrew. There were all these problems in Germany where the quadripartite administration was collapsing, and the Soviet Union eventually took no part in the Marshall plan. But the nations of Western Europe -- and by that I mean the British, the French, the Italians, the Belgians, the Dutch, and the Scandinavian countries -- assembled and drew up a plan of action. The chairman of the working committee that drew up the Marshall plan in Europe was Oliver Franks. Oliver Franks was a very outstanding British civil servant who had a wonderful career during the war that I can't detail, but in the postwar period he became one of the outstanding British negotiators and statesmen. He subsequently came to serve in Washington as Ambassador, but at this stage he was sort of the intellectual creator of the

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European reconstruction plan that had been demanded by Marshall as a condition of United States aid.

Well, after this plan was presented by the European authorities, a committee was organized in Washington under the chairmanship of the State Department (I served as the Federal Reserve representative) to draw up an analysis of the European plan. I was only in the first phase because the job rapidly got taken over by the State Department; it wasn't anything that could be run by an interdepartmental committee. They prepared the legislation that went to the Congress, and when the Congress voted the funds the Marshall Plan Organization was established in the United States, of which Paul Hoffman became the head and Averell Harriman became the European representative. I then ceased to have any personal role in the administration of the Marshall plan.

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MCKINZIE: There was, of course, the question, even then on that committee, of exactly how much it would take.

KNAPP: Well, there was the question of how much it would take to do the job, and also on what terms this aid should be provided.

We were all convinced that the bulk of this aid would have to be provided on a grant basis. The World Bank has said that these countries were not creditworthy. We couldn't properly lend them money, and it would have to be put on a grant basis. Much was made of the earlier experiences with the war debts following World War I, when obligations had been put on European countries which they were never able to pay. It was said, "This is just not a bankable business," so we made the British loan and the French loan, but after that there wasn't thought to be any hope of collecting any money off these people. One aspect of this matter that I had a hand in

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arose when some people said, "Well, okay, if you give them food, clothing, or raw materials that are going to be consumed, you can't expect them to pay. That's eaten up, that's burned up, that's incorporated in things that are not of long term productive nature. But if you give them steel mills, if you give them tractors, or if you give them textile plants, then they ought to be able to pay for that because these are productive resources." I wrote a key memorandum for the original interdepartmental committee to demonstrate the fallacy of that approach. When you come to think about it, it doesn't make any sense. These countries were going to get, as they finally did get, some 18 billion dollars of assistance from the United States. During that period they probably bought in the United States (I'll just pick a figure out of the air), 40 billion dollars worth of things, of which they paid for 22 billion dollars out of the proceeds of their own exports.

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Now, if you say you're going to give them food and clothing and raw materials as a grant, and you're going to give them tractors and steel mills as a loan, what's going to happen? They're going to pay for the tractors and the steel mills out of their own money, and they're going to ask for the food and the raw materials as a grant.

The creditworthiness of countries has to be determined on the basis of their total capacity to service debt, rather than according to what particular commodities they're going to receive under an aid program.

We have this same argument, I might say, in the field of development, because people will say sometimes that if you're providing assistance for, let's say education, it ought to be a grant, whereas if you're supporting a project for a steel mill it ought to be a loan. There aren't many funds available for grants these days,

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but there are funds for soft loans and for hard loans; so, they say that you should make a soft loan for education, and a hard loan for a steel mill. Upon analysis that doesn't really make sense. The question is what kind of a country you're dealing with. If a country is fully creditworthy and fully bankable, it can pay for a loan for education as well as it can pay for a loan on a steel mill. The steel mill, you might say, earns its own way and generates revenues, but so does education. If you educate people, it builds up their talents and their income earning capacity, and that means

their taxable capacity. Governments can borrow and repay an educational loan out of the revenues they eventually get out of taxing better educated people earning a higher income.

On the other hand, if you've got a steel mill project in a completely broken-down country, it's no good arguing that this steel mill is going to be productive. If this country has a

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disastrous overall balance of payments and resource position, then it won't be able to generate the foreign exchange necessary to repay a loan, even for a steel mill. I'm not sure I've expressed this very well, but my general approach is to say that the question of whether you lend hard money or soft money should depend upon the country that you're dealing with and its overall capacity to mobilize resources and make repayment, not upon the particular nature of the project.

So, this same issue came up in the Marshall plan when we were talking about the kinds of commodities we were going to deliver to the European countries. The judgment was that, with a few exceptions, these countries were never going to be able to repay.

We went through the same thing with the vast American aid that was supplied to Japan in the early days. Nobody had any idea that the Japanese economy could recover as it has recovered,

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and would arrive at a state where it would not only recover equilibrium, but go on to generate surpluses and service large foreign loans. Of course, that's what has happened also in the case of Germany, and indeed most of the European countries. But at the time people were dominated by the near-term prospects, and couldn't summon up the imagination to envisage how, over a period of decades, the condition of a country could be transformed.

When I was standing in Essen at the end of the war and saw the whole of the Krupp works going up in flames, it never occurred to me that within ten years Germany would approach self-sufficiency and that within 20 years they would become, as they have become, one of the richest and most dominating countries in the field of international trade and finance.

MCKINZIE: I've heard it stated that the amount of money determined by the committee you sat on, the

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one that dealt with the CEEC plan, was based as much upon what they thought the Congress would appropriate as it was upon actual assessment of what Europe needed for recovery. Is there any truth to that?

KNAPP: Yes, I think so. I don't recall the exact figures, but I don't think anybody on the U.S. side talked initially about the 18 billion dollar figure that eventually emerged. I think the focus in the original discussion was upon the requirements for maybe the first three-year period. I do have some recollection that the European figure seemed to be so staggeringly large that it had to be cut back, but I don't think it was eventually cut back very much, say from about 24 billion to 18. What seems to me the most remarkable thing was not that the 24 was cut to 18, but that the

U.S. Congress faced up to 18, which even by today's standards is a fantastic amount. I believe I'm right in saying that during

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those Marshall plan years, the U.S. was devoting something like 4 or 5 percent of its GNP to external aid, and of course, today the figure's a fraction of 1 percent, about .25 percent. Now we're getting off on the question of aid to developing countries, which is a little different in terms of U.S. national interest than the reconstruction of Europe, or the reconstruction of Japan. But today, the highest expectations and highest demands by the developing countries are that the industrialized countries of the West, the rich countries, should devote 1 percent of their GNP to development assistance to the poorer countries. In the Marshall plan years, the United States made a vastly greater effort, proportionately, but again for a purpose which was far more clearly in its political and economic interest.

MCKINZIE: Mr. Knapp, I wonder if you could say something about your knowledge of the Soviet request

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for a loan that came at the end of the war.

KNAPP: Well, I speak with a little hesitancy about this because it's a chapter of the history of that particular period which is pretty obscure. Along about the same time that these requests were forthcoming from the British and the French, and you might say more or less out of the blue, there did come into the U.S. Government, through the State Department, a note from the Soviet Union asking for a loan of a billion dollars.

Now, this was already at a time when things were getting pretty tense in relationships between East and West, particularly in Germany. It was at a time when the lend-lease negotiations with the Soviet Union had just about collapsed. There were very substantial lend-lease supplies, of course, to the Soviet Union, and we were again following the same principle of asking repayment only for those goods and assets which remained intact at the end of the war. We weren't asking

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for any repayment on things that had been burned up, shot up, or eaten up. This is a matter I did have something to do with during my time in the State Department. We had tried to get some negotiations going with the Soviets on the lend-lease "bill" as we called it. Of course, in the first place, it was almost impossible to get any facts, but we drew up a bill of what we thought they still had in the way of stocks that were left over from the lend-lease deliveries. We then submitted a bill to them, but they were never prepared to discuss it. It just got lost in the whole deterioration of relationships that followed in the years after the war.

I can tell you this about the earlier Soviet request for a loan; that the NAC never functioned in the matter. It just got buried somewhere in the recesses of the State Department. The British and French loans were financed through special legislation for the U.S. Treasury, but I

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think the Soviet request was for a line of credit with the Export-Import Bank.

Anyway, all I remember about it is that everybody knew that it had come in and nobody knew what had happened to it. I dare say if there had been a more successful and reasonable discussion of the lend-lease bill -- even in the deteriorating relationships -- it would have set the stage for a billion dollar loan.

I can't really say much more about it than that. It was mysterious at the time what had really happened to it, and it's more mysterious to me after a lapse of 25 years.

MCKINZIE: Why did the National Advisory Council sort of fade out of prominence? It appeared that in 1945 or early 1946 the National Advisory Council seemed to have the ear of the President. It was in the top agency or interagency group in the Government dealing with these matters. Then, somehow in the next year or two, it significantly

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declined. Do you have any comment on that?

KNAPP: No, I can't really explain that. But just to relate it to my personal history, I left the Federal Reserve in 1948, after a couple of years there. Eccles, as chairman of the Federal Reserve Board, was a member of the National Advisory Council. Under the National Advisory Council was a so-called staff committee, and each of the principals named a member of his staff. I was the member representing the Federal Reserve on the NAC staff committee. The member for the State Department at the National Advisory Council was nominally the Secretary of State, but either for reasons of dignity or just because he was too busy, he practically never attended meetings and he designated as his representative the Assistant Secretary of State. Will Clayton had graduated from that position, moved upstairs to become Under Secretary, and the Assistant Secretary was Willard Thorp. Willard Thorp, in 1948,

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offered me the job of coming over to the State Department as director, under him, of a so-called Office of Financial and Development Policy. One of the functions of that officer was to serve as the State Department member of the NAC staff committee. I took that job and I just shifted chairs in the NAC staff committee from being the Federal Reserve representative to the State Department representative. That was the last job that I had in the U.S. Government before I joined the World Bank, and I served there again for about two years. At the end of '49 I finally moved over to the World Bank.

I consider that up until the end of '49, still only a short period after the war, the NAC and the NAC staff committee was kind of in command of the foreign financial policy of the United States. Even after I was in the World Bank, the U.S. director in the World Bank was subject to the guidance of the National Advisory

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Council, so I wasn't very far removed from it. It's quite right that the whole thing in time deteriorated. It probably had something to do with the basic relationships between Treasury and State. As long as they were close and cooperative, the NAC functioned. But to the extent that they moved apart and became rivals, the NAC council deteriorated in its effectiveness. It may have something to do also with the fact that the big issues of international finance moved out of the hands of the U.S. Government and moved into the international agencies, the Inter Fund and the International Bank lending activities of the United States moved over to the Export-Import Bank, which became more autonomous and independent. Things like the British loan and the French loan were made by the U.S. Government directly through the Treasury. After that, the Marshall plan and the assistance under the Marshall plan was heavily dominated by

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the State Department. They didn't want to have the NAC involved. The Marshall plan was very much in the hands of the State Department, or rather, of a semi-independent agency which came to be called the Economic Cooperation Administration, or ECA. It was closely linked with the State Department, and they probably didn't want to have much Treasury influence in that operation. Hence the NAC, of which the Secretary of Treasury is the chairman, began to get downgraded.

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Second Oral History Interview with J. Burke Knapp, Bethesda, Maryland, July 30, 1975. By Richard D. McKinzie, Harry S. Truman Library.

KNAPP: I'd like to go back to the negotiations we held with the British regarding a loan to Britain for postwar reconstruction. Lord Keynes was the head of the British delegation, and I have mentioned earlier what an overwhelming personality he was; a tremendously elegant intellect, with, of course, an immense reputation as an economist. During one of the discussions that we had in the Treasury Department, we had the British delegation lined up on one side of the table, with Keynes presiding, and the U.S. delegation on the other side. One of the problems that had come up related to the conditions under which the United States might be obliged to forego payments of interest on the loan.

Now, the British maintained that if their economic situation and balance of payments deteriorated to a certain point, as measured

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by various criteria, they should be entitled to a waiver of the interest payments due. This was finally accepted in principle, but there was a long and involved debate about just how to formulate these conditions. At a certain juncture we had had an overnight adjournment. Keynes came back "full of beans" the next morning and said that he had worked out a formula which might be used to determine whether this waiver of interest payments would be granted or not. He proceeded in a most effective and articulate presentation to present his formula, which had all kinds of numerators, denominators, and sections. After expounding this at some length, he finished and looked across the table to a slightly stunned audience, which was trying to figure out the ramifications of this formula. To everybody's surprise, since I was a relatively junior member of this delegation, I spoke up and said, "Sir, in that Section IV of your formula,

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don't you have the numerator and the denominator reversed?" I'll never forget it. He started looking at me almost scornfully, and then suddenly a kind of light dawned on his countenance and he broke out into a broad smile. I received from him (which at that time I took as quite an accolade) a sudden glance of great appreciation. He said, "By jove, you're right." He turned around to his aides, and said, "Has that cable gone off to London?"

And they said, "Yes, it has."

And he said, "Well, call it back; we've got to change it." Once he had appreciated the point, he was very generous in thanking me for having called this to his attention. He said that this was a stupid mistake, and was rebuking his aides who had allowed him to send the cable off in that form.

I never had that close a personal association with this great man, but I do cherish the memory

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of the time when he took a point from me and took it with immense grace and appreciation.

Well, let me proceed to the next chapter of my professional career. Toward the end of 1948 I left the Federal Reserve Board again to go to work for the State Department as the director of what they called the Office of Finance and Development Policy. General Marshall was the Secretary of State at the time; Bob Lovett was his very distinguished Under Secretary; and as Assistant Secretary they had a very distinguished economist, Willard Thorp. Willard Thorp had long represented the State Department on the National Advisory Council, and we'd become acquainted, since I had been serving as the Federal Reserve member of the National Advisory Council staff committee. He invited me to move over to the State Department and continue this work on the National Advisory Council staff committee. I found, although I had great loyalty to the Federal Reserve

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Board, that there was a change taking place at that time. Marriner Eccles, the chairman of the Federal Reserve Board, with whom I had been very close, was just retiring. The move opened up exciting possibilities, and I undertook to take on this new job.

Willard Thorp had as his deputy Paul Nitze, who subsequently went on to hold very distinguished positions in the State Department and in the Defense Department. Under Willard Thorp and Paul Nitze there were two main offices. There was the Office of Commercial Policy, which handled all affairs relating to international trade, commodity agreements, and such matters and then there was the Office of Finance and Development policy, which was concerned with such matters as the U.S. activities in the International Monetary Fund and the World Bank, the administration of the Export-Import Bank and other foreign lending agencies of the Government, and generally anything in the international economic field that had to do

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with financial matters or economic development.

I spent only about a year on this job and during that year an emergency arose which came to occupy, I should judge, something like a third to a half of my time. This emergency was the Berlin blockade. Now, it was somewhat anomalous that I had these extensive administrative responsibilities for a wide range of matters in the State Department, and yet got tagged as the United States economic and financial expert on the problems arising out of the Berlin blockade. Given the emergency conditions at the time, I simply had to give this top priority.

The Berlin blockade was, of course, essentially a political and a strategic move by the Soviet Union to try to make things difficult for the Western Powers and eventually to try to incorporate Berlin in the Eastern zone of Germany. But, oddly enough, the crisis was precipitated by issues having to do with the currency and trade of Berlin vis-a-vis the world outside.

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Berlin was set up as the capital of the whole of Germany, which was supposed to be governed by the quadripartite administration of the four powers. In 1948 a monetary reform was introduced in Germany. Within the three Western zones of Germany the old currency was withdrawn and a new West German currency was issued. There had been an attempt to introduce this monetary reform throughout the whole of Germany, and to have a unified currency in the whole of Germany. But this had failed in long, tedious, and painful negotiations with the Russians, and it had failed essentially over the question of who was going to control supply of the currency. The difficulty was that under a quadripartite administration, powers had a veto over any action when you come to the question currency and the support of the banking system, you risk serious economic disorder. You can't have lying in the hands of one party a

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veto over any effective action.

So the Western Powers finally decided they had to introduce their own currency (the West mark) in the Western zones, and the Soviet Union, as the administrator of the Eastern zone, countered by the introduction of an East mark. That left open, however, the question of Berlin, which was an enclave in the Eastern zone of Germany. It was the proposal of the Soviet Union that the East mark be introduced into the whole of Berlin. This was unacceptable to the Western Powers, who felt that the currency might not be available when it was needed by industry and trade in the Western sectors of Berlin. On the other hand, this currency could be so badly administered that it might lead to a rampant inflation; this would be equally damaging to the economy of West Berlin. It was very important to keep the economy of West Berlin going because on that depended the employment and the welfare

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of people who were the responsibility of the Western Powers. Hence when the Russians announced unilaterally that they were going to introduce the East mark in the Eastern sector of Berlin, thus effectively destroying the quadripartite administration of the city, the Western Powers responded by introducing the West mark in the Western sectors.

This issue of the status of Berlin in the monetary reform, and the associated problems about how to finance the trade of Berlin with both the Soviet zone of Germany and the Western zones, were the immediate occasion which precipitated the Berlin blockade.

I won't go through the story about the blockade itself and the airlift, which is common knowledge. Suffice it to say at this point that it was a very dangerous crisis in the relations between East and West, with the threat of a breakout of hostilities at any time. The United States,

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rather than try to break the blockade by land action which would have meant the outright use of force, decided to meet the problem of the blockade by the airlift. You could fly a plane from Frankfurt into Berlin without any overt use of force; force would be needed to stop it. The Soviet Union did not challenge the airlift by force, partly because they thought that it could never succeed. It was, of course, a major logistical undertaking to supply the food and the coal and all the requirements of the Western sectors of the city of Berlin through this airlift.

Now, the United States and the Western Powers, Britain and France, took the position that they were not going to negotiate about Berlin with a gun at their head. They weren't going to negotiate under duress. But whereas that was the formal position, in fact discussions began soon after the blockade was established, to see if through secret channels and contacts some

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way could be found out of this impasse relating to Berlin currency and trade.

Then the issue was taken up by the United Nations Security Council, or rather by the chairman of the Council at the time, the foreign minister of Argentina, Mr. [Carl Valdemar] Bramuglia, who was anxious to make headlines for himself. He announced that he was going to take it upon himself to find a solution. He nominated a "mediator" a distinguished Canadian civil servant, Norman Robertson, who was assisted by Charles Ritchie and Ed Ritchie (no relation), both of whom later served as Canadian Ambassadors in Washington. They in turn brought in a team of experts consisting of the top secretariat of the Economic Commission for Europe in Geneva. This was an agency that had been set up by the United Nations to Coordinate economic relations in Europe, but its function had been largely displaced in Western Europe by the Organization of European Economic Cooperation

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in Paris that was set up under the Marshall plan. The ECE kept working away in Geneva, however, with particular interest in East-West relationships. The executive secretary of the Economic Commission for Europe at the time was Gunnar Myrdal, a very well-known Swedish economist; his deputy was Nicholas Kaldor, a British professor of economics; and their principal technical assistant at the time was an American, Walt Rostow. All these men have had very interesting subsequent careers, and their names are probably familiar to most students of international economics of these days.

Well, the Myrdal-Kaldor-Orstow group set themselves up in Geneva and began to commence studies as to how the Berlin problem might be resolved. They came up with the bright idea that the way to resolve it was to set up a new central bank for Berlin, which would administer its own currency (a Berlin mark). The problem, however, was just in microcosm the same problem

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that had arisen for the whole of Germany. With the Eastern and Western Powers having such disparate interests in economic and financial matters, how could you run a central bank in Berlin on a basis that would assure the healthy and sound growth of the economy of the Western sectors of Berlin? How could you prevent a wild inflation on the one hand or such close currency controls that the monetary and banking system of West Berlin would be suppressed? Therefore, we on the U.S. side could not accept this as a negotiable proposition. I was designated to go to secret -- extremely secret -- meetings that were held in Geneva to discuss this plan. There was a Soviet representative, a British representative, a French representative, and myself. Not only was this secret, but the Western representatives were enjoined not to negotiate, not even to meet directly with the Soviet representative. What happened was that Myrdal, etc. would prepare draft schemes, and under Robertson's chairmanship,

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they would spend a day with the three Western representatives discussing them. Then they would have a parallel session with the Soviet representative. The only times we ever met together with the Soviet representative were at cocktail parties.

Now, the atmosphere at the time in Britain and France was of great alarm over the possible consequences of this Berlin blockade, great fear of a confrontation with the Soviet Union, and, in short, a strong tendency to seek a compromise solution. In the end it became my task, not only to convince Robertson and the Myrdal group that these plans were not feasible, but also to work pretty hard on my good British and French colleagues to maintain a common front.

I had some very interesting meetings, in particular a meeting that I recall vividly in London. Julius Holmes was the American minister in London at the time; Lewis Douglas, I believe,

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was the Ambassador, but I think he was ill at the time. So, Julius Holmes took me to go over to see Ernest Bevin, the British Foreign Secretary, and his team, to try to rally them to a common position with us, and to try to persuade them that if we didn't achieve a common position and just caved in to this solution being offered by the United Nations team, it could have disastrous consequences for our position in Berlin.

I spent a great deal of time shuffling back and forth, consulting and getting my instructions in Washington and talking to our Western colleagues. And all this time there was still another dimension to it. Here was the State Department carrying out these negotiations, but there was also the U.S. military government in Berlin, where General Clay and his advisers were very jealous of the fact that we were meeting off in Geneva and deciding the fate of Berlin while he was not having any part in it.

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So, this was all a very complex pattern of different parties with different interests and, indeed, different convictions about how this problem ought to be handled.

MCKINZIE: Did you have contact with General Clay?

KNAPP: Oh, yes, but I never visited Berlin during this period; my instructions were not to go to Berlin but that Berlin was supposed to come out to us. I think the State Department was afraid that if I went to Berlin I'd get taken into camp, because they had some of their own ideas in Berlin of how to handle this situation.

At the Washington end, I was advised and instructed by a group which was headed by the State Department but included also the Treasury Department and the Pentagon. That introduced still another dimension of complexity into the task. I used to go home and meet with them and then draft my own instructions for the next round.

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Still it was all a fascinating experience, extending over many months. It all ended in nothing, because to everybody's surprise the Soviet Union one day just terminated the blockade, following certain contacts that were made in the United Nations between Philip Jessup and the Soviet delegation there. So, we never did achieve a solution to the very perplexing currency problem that confronted us. We were condemned to keep stonewalling against unacceptable solutions -- the unacceptable solution of introducing the East mark in the whole of Berlin and the unacceptable solution -- though on the face of it it was quite appealing to some anxious to find a compromise -- of setting up a new Berlin currency under quadripartite control. In the end I must say that our ingenuity ran out, and the only solution we could find was to introduce the West mark into the Western sections of Berlin.

Going back a little bit earlier than that, I had been involved, both at the Federal Reserve and I believe later in the State Department,

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with the West German monetary reform itself. The proposals for the "monetary purge," as they called it at the time, were made by a team which had been organized mainly by the Pentagon, but with advice from the State and Treasury departments and the Federal Reserve. They picked a distinguished team of economic experts to go to Germany and propose what to do about monetary reform there. This team was a very interesting group of personalities, all of whom I came to know in this and other connections. Gerhard Colm was of German origin, a distinguished professor of economics who at one time became the chairman of the Council of Economic Advisors; Raymond Goldsmith was also of German origin, and also an outstanding monetary economist; and Joseph Dodge was the president of a bank in Detroit. He was supposed to bring practical banking experience to supplement the economic and financial expertise of Colm and Goldsmith. They

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worked out the so-called Colm-Goldsmith-Dodge plan, which was a very radical monetary purge in Germany, designed to cope with conditions that I think I mentioned in earlier parts of this discussion. There existed a tremendous so-called monetary overhang. The printing presses had flowed very freely in the immediate postwar period, and the amount of money piled up in cash and bank deposits was vastly in excess of the needs of the country. The inflationary impact of that mass of money had been held back by price controls and wage controls, but if the economy was to be freed and a liberal system of trade and investment was to be introduced, it was necessary to do something about this monetary overhang. So the Colm plan called for all the old currency and the old bank deposits to be repudiated and exchanged in limited amounts for a new currency to be established, called the Deutschemark. Cash amounts were converted only

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in small amounts, partly because a lot of the cash had been hoarded by war profiteers and through illegal channels. Even bank deposits were converted only in part to the new currency.

The idea was to establish a new currency which had a proper relationship to the economic needs of the country and to permit, at the existing price level, the removal of wage and price control. I was on the edge of this plan rather than any prime mover in it, but I spent a good deal of time in interdepartmental conferences with the authors of the scheme and the military government in Germany, regarding, first, the construction of the plan, and, secondly, its initiation in Germany. It has been said since by many historians and observers of the German economic scene that it was this monetary reform which laid the essential indispensable basis for the subsequent so-called economic miracle of Germany -- the very rapid recovery thereafter of German agriculture, industry, and commerce.

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MCKINZIE: With what certainty did the authors of that plan put it forward, and with what degree of success?

KNAPP: Well, they put it forward with force and conviction. Colm and Goldsmith were both old enough to have lived personally through days of acute raging inflation. They'd studied the subject academically, and they were quite solid and quite united. They eventually persuaded their lay colleague, Joe Dodge, to join in the recommendations. I think the whole concept of the monetary reform was a tribute to the abilities and experience of these men, and it was accomplished under the military government in Germany very effectively.

There is one other incident I might describe of my work in the State Department during that time which casts an interesting light on the spirit of the times and on some of the problems that we confronted in disentangling the wartime

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measures. This problem hit me about the first week that I took my post at the State Department. The situation was that when the United States forces occupied Japan, they seized the Bank of Japan and the gold reserves in the Bank of Japan. In due course these were declared by General [Douglas] MacArthur to be war booty which he proposed to ship back home to help pay for the costs of the war. This led to considerable discomfiture in Washington; again it was like the

Morgenthau plan. A lot of people felt that now that Japan was occupied, our task was to get Japan back on its feet and off the back of the occupying forces, and at least to a certain extent, they would need some monetary reserves to restore an orderly economy in Japan.

But the particular aspect of this matter that came onto my plate, was the fact that in the vaults of the Bank of Japan at the time, and mixed up with their own gold reserves, was gold

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that the Japanese had seized in countries that they had occupied during the war. In particular, there were boxes and boxes of gold in the vaults of the Bank of Japan which, it was quite clear from the labels on the boxes and from the records of the Bank of Japan, were the property of the Bank of Thailand. During the Japanese occupation of Thailand they simply looted these gold reserves and sent them back to Tokyo. The Thais knew, of course, that this gold was in Tokyo and immediately after the occupation and the seizure of the assets of the Bank of Japan, they filed a claim with the U.S. military government for the restoration of this gold. That claim was turned down by General MacArthur, who said that the Thais had collaborated, in any case, with the Japanese, and this was American war booty. It was going to help pay for the U.S. war effort.

So, the State Department was brought into the picture. As I say, in my first week in the

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Department, I was presented with a huge dossier giving all the background of this problem, and was asked to prepare a judgment on it for the Secretary of State.

Well, it was really fairly simple to determine that this gold was indeed the property of the Government of Thailand. We had no business taking as war booty something that was stolen property in Japanese hands. I should say that the only consideration in the case which tempted me to a different conclusion was that of the role of a couple of fellows, whose names I wouldn't mention if I remembered them, who were formerly Treasury lawyers. They had retired from the Treasury, set themselves up as a law firm in Washington, and offered their services to the Thai Government to help get the gold back. The only problem about this was that the value of this gold was about 70 or 80 million dollars, and they had negotiated a deal with the Thais that if they were to succeed

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in getting this gold back, they would receive a 5 percent commission. These lawyers kept coming in and beating at my door, and I just refused to see them. I saw them a first time to make their case, but after that I refused to see them again. All during the weeks that I was pondering and working with my associates to find a solution to this case, they were badgering us constantly, trying of course to show the Thais that they had been responsible for getting the United States Government to restore this gold.

Well, it was too bad that the Thais had entered into such an unwise arrangement with these fellows, but obviously that wasn't a reason to come to a wrong decision, simply to deny these fellows their commission. So, we did make a finding, in favor of the Thais, it was approved by

the Secretary of State, and there ensued a long period of negotiations between Washington and General MacArthur's administration in Tokyo to get them to give up the gold. That was

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finally accomplished, and the restoration of that gold in Thailand was very important in enabling them to proceed with their postwar recovery. It probably, in the long run, saved the United States a lot of money that they would otherwise have had to provide as aid to Thailand.

Among my responsibilities in the State Department was maintaining liaison with the World Bank, or, more strictly speaking, with the United States executive director in the World Bank, who was our channel into the Bank. I was thrown in contact with the leadership of the Bank, which at that time was Eugene Black, as the president; Robert Garner, the vice-president; and Leonard Rist, who was the son of the famous French economist Charles Rist and head of the economics department. Toward the end of 1949, they approached me -- Rist initially, and subsequently Garner and Black -- to invite me to come to the World Bank as the deputy director of the economics department.

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The World Bank by that time had assembled an outstanding team of economists from all over the world, but what they really were looking for was, so to speak, a manager. Leonard Rist was a very brilliant man, but he was devoted to his own economic analysis and problems. I was asked to come as a sort of executive head of the economic work to organize and administer this stable of interesting personalities which had been assembled from all over the world.

In another earlier incarnation, I had had something to do with the initial organization and founding of the World Bank, but it had never occurred to me at that time that I'd ever go to work at the institution. But they painted a very interesting picture, and I decided that I'd had a pretty hectic existence in the State Department, made all the more hectic by my diversion into this matter of the Berlin blockade. I could see the possibility of somewhat quieter

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waters and more orderly personal life, and yet a very challenging opportunity to work on international economic problems.

So I had a long final interview with Bob Garner, vice-president of the Bank, who had to be convinced that any economist could have any sense of managing affairs. He himself had been a businessman, the treasurer of the General Foods Corporation, before he came to the Bank. He had very brisk ideas about organization and management, but I finally passed muster with him and was designated to this post.

We were at that time engaged in the economic appraisal of the various countries that wanted to borrow money from the World Bank. The essence of our job was to try to appraise the creditworthiness of these countries and to render some judgment as to the limits within which the World Bank ought to lend money to countries all over the world in very different stages of

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development and very different economic and financial conditions.

Most of the countries with which we were dealing were, of course, developing countries, particularly in those early days the nations of Latin America. I remember vividly the day that we received a loan application from a big and important country for one hundred million dollars, which was considered a very large amount at that time. This came from Australia, and I was commissioned to produce an economic study of the creditworthiness of Australia. In terms of the economic prospects for the country, compared to many of the developing countries with which we dealt, this was a pretty simple proposition. We put together an economic study of Australia, presented it to our Board, and made them a hundred million dollar loan within a matter of weeks. This at least established that the Bank -- which at that time had been much criticized for having

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been very slow in getting itself organized and commencing lending operations -- could move pretty rapidly, with the right kind of client.

It happened that events soon intervened to put a temporary halt to my work with the World Bank, because during 1950 plans were being made for the initiation of the North Atlantic Treaty Organization, or NATO. The NATO Council, which was to be the principal civilian body in charge of the affairs of NATO, was to hold its first session in London in the fall of 1950. The outbreak of the Korean war in June, 1950, gave new impetus to this matter, and indeed precipitated a crisis in international affairs which at the time dominated people's thinking. The State Department (Dean Acheson was then the Secretary of State) in effect mustered me back into service after I had been only about eight or nine months in the World Bank. They went after Black and got him to release me to come

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back to the State Department and proceed to London with the first U.S. delegation to NATO, as their economic adviser. I spent about a year in London in that capacity.

This was a period during which the Council was just getting organized and on its feet. General Eisenhower was the Supreme Commander of NATO forces with his headquarters outside Paris, and the Council had to establish its authority as the civilian control over the very dynamic and powerful personality of General Eisenhower. It was for that reason, essentially, that the Council was established in London rather than in Paris, to have a degree of physical separation. It was thought that this might prevent the Council from falling completely under the domination of the military head of the NATO forces.

This was a pretty frantic year of just getting organized. People were not at all clear

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in their minds at that time whether NATO should have an important role in economic and financial affairs. There was still, of course, the Marshall plan organization (the Organization for European Economic Cooperation) which was working in Paris with its own high-level council. As it turned out, NATO never did take over any very substantial role with respect to the

coordination of national economic and financial policies, or with respect to international trade, investment, and monetary affairs. But I spent a great deal of time going back and forth between the OEEC in Paris and the NATO headquarters in London, discussing this question of our relationships.

We did have on our own plate in NATO one very important issue of an economic and financial character which took a great deal of time. This was the question of organizing financing for the so-called infrastructure facilities in Europe in support of the NATO forces. This meant airfields,

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telecommunications, roads, transport arrangements, and the stocks of war supplies that were maintained by the NATO forces. This issue led to what was perhaps the first coining of the word that one has heard a great deal more about since, "burden-sharing."

The question was, how should the financial support for the NATO installations and supplies be shared among the members of NATO? In the end, in spite of many attempts to work out actual burden-sharing formulae based upon national income, trade, reserves, and other tests of capacity to pay, the negotiations for the sharing of the costs of these installations was hammered out over the bargaining table, without much regard for specific economic and financial criteria.

My leave from the Bank to serve as economic adviser to the NATO delegation was for a term of one year, and I had expected to return to my post at the Bank at the end of that time. But

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again, events interceded and it turned out that I was to spend another year away from the Bank on another mission before I returned there.

It happened that Brazil, a nation of very great political and economic interest in the United States, had fallen into a state of rather severe economic disorder. Furthermore they wanted to borrow large amounts from the United States, and from the World Bank, to commence a development program in Brazil. One of the reasons they had fallen into economic disorder is that they had no development program; nobody had ever taken a systematic look at the country and decided what lines of development would be most fruitful and what investments, such as electric power, transport, agriculture, and industry, would be best designed to put the country on the road to economic productivity. It had been agreed, in the early part of 1951, to establish a new type of organization, a joint Brazil-United

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States Commission for Economic Development, to address this problem. What was new about it was that it was not just the provision of U.S. technical assistance, but rather a joint council headed by two co-presidents, a Brazilian and an American, with their respective staffs, who were to mount a jointly directed effort to formulate an economic plan for Brazil. The United States had designated as its co-president a very distinguished gentleman who came out of a New York investment banking background, Francis Adams Truslow. Truslow had spent some time in Washington briefing himself for his post in Brazil, and then set sail -- one went by boat in those days -- with the team that he had organized to Brazil. On his third or fourth day out, exercising

himself in the gym and in the swimming pool on the ship, he collapsed with a heart failure and died.

This precipitated a serious problem. The joint commission had been set up with great

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advance publicity, and great expectations had been placed upon it in Brazil. The United States had a great political and economic interest in seeing this task carried forward.

So, the State Department again put the arm on the World Bank and said, "Well, we have another emergency on our hands. We'd like to have this fellow Knapp take over a second assignment for us before he returns to the World Bank." I was consulted on this to some extent in London, but the first thing I knew I found myself under new orders to proceed to Brazil to pick up the task of heading the American contingent to the joint Brazilian-American Commission for Economic Development. I came back to Washington for just a few days to get a hasty briefing on what was in store for me and set off for Brazil. Whether they didn't want to risk me or whether they just wanted to get me there sooner, they insisted that I fly down,

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so I ended up arriving in Brazil by plane.

This joint commission, I would like to repeat, was quite an innovation and it had its awkward aspects, in the sense that the Brazilians had a pretty clear and firm idea of how they wanted to organize the work. In some respects, it might have been more healthy for the Americans to be just there as advisers, but we had assumed this co-responsibility for the execution of the work, and much depended, therefore, upon a close and collaborative relationship between the Brazilian and the United States heads of the organization. The Brazilian co-president was a man named Ary Torres, an engineer-businessman from San Paulo, a very bright and energetic and personable fellow, but totally without experience in macro-economic planning. On the other hand, he had with him a group of advisers of outstanding ability and capacity, and he was quite prepared to take their guidance. In the end, we worked out quite

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an effective working team, which, under the co-heads, became more and more integrated as we proceeded with our work. It wasn't a Brazilian staff working with an American staff, but became really a joint Brazilian-American team.

Among the outstanding advisers on the Brazilian side were two men that I might mention particularly. One was Roberto Campos, an outstanding international economist who many years later became the Finance Minister of Brazil. And it was really under the Campos regime that the recovery of Brazil from its chronic economic disorder was finally accomplished.

Another outstanding adviser was Lucas Lopez, who also subsequently became Minister of Finance. They had the advantage also of outside economic consultants, including Octavio Bulhoes, and Eugenio Gudín, head of the Getúlio Vargas Foundation in Rio, who both also became ministers

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of finance. Gudin was an older man of outstanding capacity as an economic and financial expert; a wonderful personality and a sort of guide and counselor to subsequent generations of Brazilian economists.

I spent a year with this team. We set about, under a great deal of pressure to show results rapidly, trying to draw up an inventory of the problems of the Brazilian economy, particularly designing an investment program to meet the most critical needs of the economy. These turned out to be very largely in the areas of the basic public services of electric power and transport. We drew up programs for the rehabilitation and restoration of the railway services, the highways, and the ports and coastal shipping, and we did a great deal of work in the field of electric power development. Looking back upon it, I must say that it was partly because of the great pressure in which we were operating

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that it was not a model of macroeconomic planning. People were impatient for practical results and for the drawing up of specific projects in which investment could be undertaken by the United States Government, primarily through the Export-Import Bank, and by the World Bank.

MCKINZIE: Was the impatience U.S. or Brazilian?

KNAPP: The impatience was primarily Brazilian. There had been such a fanfare of publicity about these "saviors" that were going to come in and design a magnificent plan. There was very little understanding of the degree of disorder which existed and the amount of work that would really be necessary to prepare a systematic and rational investment program. But perhaps that was also just as well, because if there had been the time, it might have been wasted in drawing up a too finely-tuned plan.

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What was perfectly clear was that there were serious bottlenecks which were just choking economic production and growth. The situation of the railways will illustrate that.

The railways were completely broken down both in their physical facilities and in their administration. The railways in Brazil, like those in Argentina and Uruguay, had been originally built mostly by the British. Then they had been nationalized and put into the hands of the Government administrators, usually military.

The raging inflation, which was one of the signs of the economic disorder in the country, had destroyed the earning capacity of the railways. The government wouldn't allow them to raise their rates fast enough to cover their expenses, and they were constantly being subsidized out of the budget. They couldn't afford even proper maintenance. They came to employ masses of labor who were on the payroll for political purposes as much as for accomplishing any useful

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work. The earnings of the railways were scarcely enough to cover their wage bill, let alone to buy supplies, maintain their properties, or provide the new investments necessary to cover rising economic requirements.

The director general of the railways at the time was an Army colonel. I remember watching television one night and seeing him come on to advise people, so far as the passenger services were concerned, not to travel by rail between Rio de Janeiro and Sao Paulo, Brazil's two major cities. He said, "You better go by bus, or you'd better drive your own car. It's just too dangerous to ride on the railways, because we have all these derailments and we cannot assure your safety."

Well, this wasn't exactly a promotional speech on behalf of the railways, but it was probably very sound advice at the time. There had resulted, by reason of inflation and just general

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neglect, what Roberto Campos came to call the "decapitalization" of the railways. This happened also with respect to other public services like water supply and telecommunications. Decapitalization meant that the real capital resources employed were just allowed to depreciate and run down, and the depreciation was hastened by the lack of proper maintenance. No funds were available on the railways to finance modernization and new investment requirements.

MCKINZIE: You mentioned that a number of distinguished Brazilian economists worked on the Brazilian side of it. Did you make changes in the U.S. team after you assumed the co-chairmanship?

KNAPP: No, not really. We still had to recruit some more people, but basically I just took over the team that we had on the United States side. These men may not have been so distinguished in

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terms of their future careers, but they brought to Brazil many types of expertise that simply didn't exist in the country. In other words, you might say the potential of the Brazilians, with the proper technical help and guidance, was very great. But they did need some expert assistance. We had people, for example, in the field of transport. Railway engineers came down to help draw up plans for the railways who were, just by reason of their depth of experience and background, in a position to make quite badly needed contributions to the design of a railways investment program. We had a good team of advisers in general economics, industry, agriculture, and other branches of economic development.

MCKINZIE: To what extent were you concerned with private development, such as U.S. investors putting money into Brazil?

KNAPP: Well, we weren't directly concerned with

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that, because what we found was that the opportunities for private investment, whether by Brazilian or foreign investors, were being stifled through the lack of these basic public services.

We saw it as our task to lay this basic groundwork, or infrastructure. (The word "infrastructure," I believe, was coined in connection with NATO, but it was already being carried over into the field of economic development and in recent years has become a standard part of development jargon.) We were making plans to build the infrastructure which would give support to, and release the energies of, the private investing community in both industry and agriculture.

However, I was drawn into the problems of private investment in a little different way. Aside from being co-president of this joint commission, I was also designated as Minister for Economic Affairs at our Embassy in Brazil. During my stay there, the Brazilian Government

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introduced some highly restrictive regulations with respect to foreign investment. It should be recalled that Brazil was suffering at that time an acute foreign exchange stringency, and the immediate purpose of these actions was to conserve foreign exchange. Very severe restrictions were put upon the remittance of profits by foreign investors in Brazil. They were not only very severe, but very unfair, because they had retroactive effect with respect to past profits. A company was permitted to remit "X" percent on the capital it employed in Brazil -- I think it was 8 percent. But capital employed in Brazil was defined as the original capital minus whatever had been remitted on that capital in the past in excess of 8 percent per annum. In many cases, this meant that the capital base on which these remittances were to be allowed had been eroded to practically nothing.

Well, this precipitated quite a crisis in

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U.S.-Brazil relations. I had to spend some time in negotiating a modification of these regulations to give more opportunities for profit remittances, and thereby to offer more inducements and encouragement to foreign investors. These applied not only to United States investors but to foreign investors generally.

One of the particular problems about trying to draw up a development program in Brazil was the federal nature of the government and administration. The power of the individual Brazilian states is very great today, but in those days it was perhaps even more significant. Each state wanted to have the major part of the cake, if there was any cake to be cut up in terms of investment funds emanating either from the Brazilian Government or from foreign lenders. The reconciliation of these different state interests was a constant problem. To put it in the extreme, every state wanted to have a dam and hydroelectric development. There

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were flat states and there were mountainous states, but even the flat states wanted to have their monuments to economic progress. This sort of haggling intruded upon the planning work in a way that gave the Brazilian members of the commission very serious problems. Politically, that kind of issue sometimes became too hot a potato for the Brazilians to handle, and it would be up to the American side of the joint commission to insist that planning proceed in an orderly way, with due regard to economic and technical considerations rather than to the political considerations that were injected by state demands.

At that time there did not exist any central institution in the Brazilian Government which was concerned with coordinating and financing the different kinds of public investment. Investment by the various public agencies were not coordinated, priorities were not established, and it was, indeed,

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the function of the commission to do something about this. But the commission was a planning commission, supposed to accomplish its task within a finite period of time -- which in the end turned out to be about two years. One of the great successes of the commission, I think, was to establish a Brazilian development bank for the financing of development projects in an orderly way. It was set up when the work of the commission was concluded. This is the so-called Banco Nacional de Desenvolvimento Economico. It was established to provide a central place in the government which, through its control over financial resources, could fix priorities and see that there was an orderly allocation of investment to the different branches of the economy and to the different parts of the country. The BNDE, as it was called, still exists and is one of the very effective instruments of the Brazilian Government. In later years it has proved its worth in following up

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the initial work of the joint commission.

MCKINZIE: Was there any criticism of the existence of this joint commission on the grounds that the American component of the team injected itself unduly into Brazilian internal affairs?

KNAPP: Yes. There was criticism about it, but I would have to say less criticism than might have been expected. We were bitterly criticized in the press for our alleged slowness in coming up with a program and stimulating investments. The fact was that the Brazilian Government -- and Getulio Vargas at that time ran the Government with a pretty strong hand -- had invited the U.S. Government to embark upon this joint effort, and they loyally defended it. I think it is a rather extraordinary thing that a group of Yankees could have come in and touched so closely upon matters of vital national interest, and I think it's remarkable that we didn't have more

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criticism. Aside from concern about our being slow, and the main criticism came from different interested regions and states, that we were not paying adequate attention to their particular affairs and to the projects which they had conceived.

I wore still a third hat during my stay in Rio. Aside from the joint commission, aside from the Embassy, I was also the U.S. head of the so-called Point IV program in Brazil. This had been initiated years before, before the joint commission had been organized, and it consisted essentially of a program of technical assistance, especially in Latin America. In Brazil itself it had a sizeable ongoing program with a large number of American technicians who came and worked, again jointly, with their Brazilian counterparts in such fields as public health; education, particularly technical and agricultural; agricultural extension; and agricultural credit.

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This Point IV program had a budget, which was, in the Brazilian case, drawn up jointly by myself and my counterpart, the Brazilian head of the joint commission. We were charged with the preparation of budgets and with the supervision of the ongoing activities.

It may be remembered that the term "Point IV" comes from an address delivered by President Truman. It was his inaugural address of 1949, in which he outlined a series of measures that he proposed to undertake in both the national and international scene. It just happened that the fourth point that he listed in his speech was the provision of technical cooperation to the developing countries to help promote their economic advancement.

I think I might conclude my remarks on this year of activity by saying that toward the end of the year we received a visit from Secretary Acheson, who had long promised to pay a visit

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to Brazil. He had been attending a NATO meeting in Paris and came back on a triangular trip to Rio on his way back to Washington. After he had discharged some of his diplomatic duties, he came over to our offices to pay a special call on the joint commission. We assembled all our Brazilian and American staff to hear him, and he gave a perfectly delightful speech, full of wit and humor, and also a great deal of good counsel and advice about the work in which we were engaged. I was greatly struck by his reference to the fact that he had just come out of these NATO meetings in Europe. This was at a time when the relations with the Soviet Union and the East-West confrontation in Europe were at a serious pitch. He spoke very inspiringly about how refreshing it was for him to come out of the old world torn by strife and dissension, where the task was to try to hold the fabric of the international system together and where vast sums were being

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spent on armaments to no good purpose, and to visit a new country, not plagued by international confrontations or the burden of tremendous armament expenditures, but devoted, as he put it, "to building a new life." He said that the constructive aspects of this task on which we were engaged contrasted in his mind very sharply with the destructive and frustrating experience that he had had in Europe.

He really managed to convey to this assembled group a sense of new horizons, of great opportunities for economic advancement and welfare that would develop from our work. It gave us all inspiration to get on with the job.

I think I said earlier that my assignment to Brazil was again for a period of one year. The Bank was -- at least they said they were -- very anxious to get me back, and I was anxious to get back to resume what I thought of as my longer term career in the Bank.

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So, after serving in Rio for one year, I was replaced by Ambassador Merwin Bohan, who was an outstanding member of the United States Foreign Service with a great deal of experience in Latin

America and in economic affairs. I turned over my tasks in Rio to him in August 1951 and returned to the United States, this time by boat in order to get a little rest on the way.

In the meanwhile, the World Bank was just inaugurating a new form of organization. They had decided to establish regional offices in the Bank and, whereas I had left the Bank in 1950 as the deputy director of the economic work, I returned to the Bank just in time to become the first director of the Bank's operations in Latin America.

This assignment to Latin American work, as distinct from other parts of the globe, was presumably dictated by the thought that I had

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become an expert on Latin America through being one year in Brazil. I rapidly learned upon taking over my new duties in the Bank that (a) I wasn't yet an expert on Brazil, and (b) Brazil wasn't the whole of Latin America. But just by accident, it happened that my experience in Brazil did start me on a career in Latin American economic affairs, and I served for the next five years as the director of the World Bank's activities in Latin America.

MCKINZIE: Thank you very much.

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