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THE DEVELOPMENT BANK AND THE INITIAL FAILURE OF THE INDUSTRIAL PROGRAM IN PUERTO RICO, 1942–1948

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ABSTRACT

The Development Bank and the Development Company were meant to be the two pillars of the industrialization effort implemented in Puerto Rico at the start of the Second World War. It was hoped that this effort would lift the island out of its severe economic and social crisis. The Development Bank was created to take risks and finance industrial loans. However, deeming them too speculative, it concentrated its effort on building its wealth by investing in risk-adverse governmental backed bonds and similar obligations, as well as issuing bonds for infrastructure projects. It therefore ignored or sidetracked the reason for its creation. Over the following sixty years, its successor, the Government Development Bank, continued on this path, shedding its responsibility for promoting industrial loans and development, and instead, concentrating on serving as a governmental bank. This paper examines the origins of the Development Bank and explores the reasons it sidetracked its development functions. [Key Words: Development Banking, Industrialization, Development Company of Puerto Rico, Development Bank of Puerto Rico, Rexford G. Tugwell, Rafael Buscaglia]

Top and bottom: Military planes flying over San Juan during the Second World War. Circa. 1940. All photographs in the essay are courtesy of the photographic collection of the Fundación Luis Muñoz Marín. Reprinted, by permission, from the Fundación Luis Muñoz Marín.

AT THE START OF THE SECOND WORLD WAR,

Puerto Rico began to implement an industrial program. Given the economic crisis of the previous decade and the looming war, it was critical that Puerto Rico get on its feet in order to assist in the war effort. Industrialization was seen as the only solution to this economic dilemma. Newly appointed Governor Rexford G. Tugwell worked with the Popular Democratic Party (PDP) and Senator Luis Muñoz Marín to implement such a program. The two pillars of this program would be the Development Company and the Development Bank. The Development Company was designed to promote the industrial effort, while the Development Bank would be responsible for its finances. Unfortunately, things didn't turn out as planned. This paper analyzes the conflicts that prevented the original plan from being implemented, and points toward its long-term impact on the Puerto Rican economy.

Development banks, such as Mexico's Nacional Financiera, Brazil's Banco Nacional de Desenvolvimento Econômico e Social, and Korea's Development Bank have demonstrated the importance of these institutions to industrial development. In 1942, during the initial stages of its industrial development, Puerto Rico organized a Development Bank to serve as the financial arm of its industrial program. Our research demonstrates that the conflicting views of those implementing the industrial policy of Puerto Rico and those doing the financing severely affected the performance of this institution, to the point where it no longer functioned as the financial arm of the industrial program, but as a governmental bank whose major purpose was to finance infrastructure projects. Financing local and foreign industrial investments was left to the private banking sector.

During the beginning stages of Puerto Rico's industrial development, Rexford G. Tugwell, Governor of Puerto Rico from 1941 to 1946, promoted the creation of a Development Bank. As local entrepreneurs did not want to invest in manufacturing, Governor Tugwell envisioned the Bank as an institution that would be willing to make loans into ventures that were considered too risky by private investors. However, Rafael Buscaglia, the Treasurer of Puerto Rico who ultimately became President of the Board of Directors of the Development Bank, could not have disagreed more with the Governor. He believed that the Bank should not take undue risks and that the industrialization program should be undertaken by private investors, realizing, of course, that the Island's weak infrastructure must be attended to first. Teodoro Moscoso, president of the Development Company —the promotional arm of the industrialization effort—believed that the Development Bank should assume the risks required to implement the industrial plan formulated by the Development Company. According to the laws that created both entities, the Development Company was to be given preferential treatment by the Development Bank.

Another powerful figure in the debate about the Island's political and economic future was the recently elected President of the Senate, Luis Muñoz Marín. During his electoral campaign of 1940, Muñoz, acting as president and founder of the newly minted Popular Democratic Party, promised the creation of a People's Bank, which would safeguard public funds and would provide loans to those in need. This concept certainly did not fit the mold of any development bank, much less one envisioned by Governor Tugwell or Moscoso, or even, for that matter, Buscaglia. As such, the divisions within Puerto Rico's political leadership severely limited the efficacy of this institution right from the start.

Even though the Development Bank was one of the most important manifestations of the state's involvement in economic policy, little has been written about this institution. As a matter of fact, most of what is mentioned in the literature lacks coherence. Thomas Hibben, a U.S. economist, and Rafael Picó, president of the local Planning Board, wrote an influential book entitled *Industrial Development of Puerto Rico and the Virgin Islands of the United States,* in which they pretty much ignored the bank's involvement in economic issues. They also mistake the date the bank commenced operations, an important omission given the short time this bank was in operation (Hibben and Picó 1948: v). In *Puerto Rico's Economic Future: A Study in Planned Development,* Harvey S. Perloff, a prominent economist, limits his discussion of the bank to its industrial loan portfolio, and omits presenting the bank's most outstanding accomplishments, these being the loans to low to middle class housing developments and the bond emissions for infrastructure projects (Perloff 1950: 107–8). Economist Biagio Di Venuti in *Money and Banking in Puerto Rico* limits his discussion of the bank to a superficial presentation of its duties and responsibilities (Venuti 1950: 170–1), while James L. Dietz in the *Economic History of Puerto Rico* limits his discussion to one page in a book whose length exceeds three hundred pages. In *Development Strategies as Ideology,* sociologist Emilio Pantojas-García ignores the Development Bank altogether (Pantojas-Gracía 1990), and José A. Padín, in his doctoral dissertation "Imperialism by Invitation: Causes of a Failed Development State Project in Puerto Rico 1940–1950," discussed the Development Bank only in relationship to the private banking sector (Padín 1998). During the last 58 years, our study has only identified ten publications that included mention of the Development Bank. However, none of these provides a clear and comprehensive picture of the bank's struggle, capabilities, and contributions to the economic development of Puerto Rico during the 1940s and beyond.

The U.S. Government's plan to end poverty in Puerto Rico

Franklin D. Roosevelt was elected President in 1932, amid the worst peacetime crisis in the history of the United States (Schwardz 1993: 70–1). "By 1933, U.S. gross national product (GNP) had dropped from a high of $104.4 billion in 1929 to $56 billion. Consumer prices fell by 25 per cent, and workers' real wages, or their purchasing power, declined about 15 percent. Unemployment reached a staggering 24.9 percent of the work force in 1933, and the real rate of unemployment was certainly even higher. And although the depression was triggered by events in the United States, its effects reverberated thought the world capitalist system" (Dietz 1986: 136–7).

Roosevelt's first action was to close all banks under executive powers conferred by the Great War's Trading with the Enemy Act of 1917. A special session of Congress passed the Emergency Banking Act of 1933, a new banking plan law, in a matter on hours. This was probably the most important New Deal law, and it gave the President the power to safeguard shareholder and depositor interest. The law also concentrated enormous power and responsibility in the hands of the Reconstruction Finance Corporation (RFC), created in January 1932 under former President Herbert Hoover in order to assist insolvent banks (Schwardz 1993: 67–71).

The New Dealers, as they were called during the administration of President Roosevelt, claimed to have transformed the RFC from a safety net for big bankers to a catapult for entrepreneurial growth (Schwardz 1993: 83). The RFC was given a greatly enlarged and diversified lending function, and it was enabled to cooperate with the new recovery agencies. However, "while the RFC boasted that it loaned billions, a cursory examination revealed that most of the money went to banks and railroads tied closely to banks. The Export-Import Bank, dedicated to stimulating overseas sales of American goods, had loaned only $35 million by early 1937.

Eleanor Roosevelt on her first visit to Puerto Rico. Reprinted, by permission, from the Fundación Luis Muñoz Marín.

Typical Puerto Rico Reconstruction Administration (PRRA) housing construction. Circa. 1930. Reprinted, by permission, from the Fundación Luis Muñoz Marín.

As for liberating the housing market, the RFC Mortgage Company's high interest rates discouraged loan applications and then approved a mere 10 percent of the applications it received" (Schwardz 1993: 84).

The New Dealers "sought to create long-term markets by building an infrastructure in undeveloped regions of America" (Schwardz 1993: Introduction). They believed that "the national economic growth was stifled by the monopolization of capital and manufacturing in the Northeast quadrant of the country" (Schwardz 1993: Introduction), and concluded that in order to eradicate the unemployment, economic stagnation, and poverty, "unimaginable quantities of public investment" would be required (Schwardz 1993: Introduction). Rexford G. Tugwell, future Governor of Puerto Rico, served as part of President Roosevelt "Brain Trust" from 1933 to 1936 (Namorato 1988: 95–125). These experiences would greatly influence his approach toward eradicating poverty and stimulating the Puerto Rican economy.

"In Puerto Rico, the decline in output was not as severe as in the United States, at least partly because income and production were so low to begin with. Puerto Rico's GNP fell from $176 million in 1929 to $134 million in 1933, a decrease of 23.9 percent, compared with a 46.4 decrease in the United States" (Dietz 1986: 137). These dislocations came "on the heels of the 1928 hurricane, long before the Island had recovered from that tragedy. Then, in 1932, another hurricane, San Ciprián struck, killing 225 people and causing damage estimated at $30 million. Per capita income worsened during the early 1930's and only began to approach the 1930 level again, in nominal value, toward the end of the decade" (Dietz 1986: 137–9). Even in the late 1930s, poverty, unemployment, poor health conditions, and excessive land concentration were still mayor problems in Puerto Rico (Pantojas-García 1990: 39).

One of the Federal Government's first and most influential efforts to influence the economic state of the Island was the study commissioned by the Department of Agriculture. The results of this study were published on June 14, 1934, when the commission issued its *Report of the Puerto Rico Policy Commission* (Cochran 1959: 44–5).

The highlights of this report include the recommendation that an industrial program be implemented as soon as possible and that studies be conducted to determine the viability of investing in certain industries, such as cement, bottles, corrugated cardboard, textiles, and shoes. These would employ the 150,000 heads of households that were currently unemployed (United States Department of Agriculture 1934: 88–91). The report also recommended that the Reconstruction Finance Corporation extend credit and subsidies to industrial investments (United States Department of Agriculture 1934: 3). On June 16, 1934, two days after the Commission issued its report, President Franklyn D. Roosevelt created an interdepartmental committee in order to coordinate all federal programs in Puerto Rico. Rexford G. Tugwell, who was then the Undersecretary of Agriculture, was appointed to serve on this committee. By the end of 1934, it became apparent that this interdepartmental committee would not achieve the desired results. As such, on June 28, 1935, President Roosevelt created the Puerto Rico Reconstruction Administration (PRRA). By mid-1936, the PRRA employed 60,000 people. The PRRA built and operated a cement factory in San Juan and constructed hydroelectric facilities, but failed in its effort to industrialize Puerto Rico (Pantojas-García 1990: 36–40; Dietz 1986: 154–6).

Given the failure of the PRRA, in June 25, 1938, the U.S. Government approved a federal law allowing public corporations to issue bonds without limiting the Government of Puerto Rico's ability to do the same (United States Statutes at Large 1938: 1203). Prior to the passage of this law, the Insular Government's ability to issue bonds was limited to 10 percent of the net value of the properties owned by the government. This figure was calculated by subtracting the government's debt to the value of the properties owned (ALMM. Development Bank of Puerto Rico, undated report). The Federal Government hoped that by approving this new law, the local government's ability to issue debt would increment substantially, and that this additional income would be used to eliminate the horrific slums that dotted the Island, and to promote the construction of housing projects (United States Statutes at Large 1938: 1203). Surprisingly, the law did not mention the industrial efforts that had been in the forefront of previous U.S. efforts to jump-start the economy. However, Puerto Rico would have to wait until 1941, when Rexford G. Tugwell was appointed Governor of Puerto Rico by President Roosevelt, to truly benefit from this legislation.

Public and private interest collide

Governor Tugwell believed that Puerto Rico needed to industrialize, as its dependence on the sugar industry was one of the causes of the extreme poverty on the island. Manufacturing would provide the necessary capital for the Island to be able to solve its current social and economic crisis (Tugwell 1947: 253). Unfortunately, private capital did not share Tugwell's enthusiasm for manufacturing. A little background helps to understand why this was so. During and after the First World War, sugar prices reached record levels. Prices doubled from 1918 to 1919, reaching their highest mark in 1920. So great was the income provided by this industry, that this period became known as the "Dance of the Millions" (Bird 1937: 113).

There was no reason to believe that the same price cycle would not be repeated as the Second World War approached. Therefore, capital invested in the sugar industry had no incentive to diversify into manufacturing. In fact, their approach would have been to defend their industry against what they would perceive as frontal governmental attacks by the Tugwell Administration (Tugwell 1945: 325), particularly as this administration backed the enactment of the "500-acre law," a law limiting land holdings to 500 acres. The stage was set for a collision course between public and private interests.

The amount of capital deposited in local banking institutions in 1942 was an astonishing $119,324,000. Fifty-four percent of these deposits belonged to private interest groups (Di Venutti 1955: 43–5). As such, capital was available to invest in manufacturing. However, the animosity between the private interest groups and the Tugwell Administration, the perceived income that the sugar industry would generate as a result of the impending war, and the weak internal economic structure made investors uneasy about investing their capital, and banks leery of lending it (Tugwell 1947: 255).

Organizing the Bank

Given the lack of initiative demonstrated by the private sector of the economy to promote the industrialization efforts, the Tugwell Administration had to go about it alone. The Development Bank and the Development Company were organized to promote this effort and to provide "unimaginable quantities of public investment": the New Dealers' answer to economic stagnation and poverty (Schwardz 1993: Introduction). The Development Company was given the responsibility of promoting the industrialization effort, while the bank would be responsible for its financing (Tugwell 1947: 255). It should be noted that both the Development Bank and the Development Company were "conceived within the limits of the colonial relationship with the United States and [were] in keeping with Keynesian economic ideology

TABLE 1: COMMERCIAL BANKS OPERATING IN PUERTO RICO IN 1942 ($000)

	Assets	Deposits	% Assets	Loans	% Loans
Local Banks					
Banco Popular	$22,834	$18,676	81.8%	$5,389	23.6%
Banco Crédito y Ahorro Ponceño	14,025	10,287	73.3%	5,831	41.6%
Banco de Ponce	10,358	8,272	79.9%	5,463	52.7%
Roig Commercial Bank	1,551	1,000	64.5%	784	50.5%
Banco de San Germán	1,033	854	82.7%	277	26.8%
Development Bank	*500*	*500*	*100.0%*	n/a	n/a
Banco de Economías y Préstamos	477	377	79.0%	203	42.6%
Credit Union Bank	365	288	78.9%	164	44.9%
Banco de San Juan	199	110	55.3%	129	64.8%
Subtotal	**$51,342**	**$40,364**	**78.4%**	**18,240**	**35.5%**
U.S. Banks					
National City Bank of New York	62,014	61,407	99.0%	9,186	14.8%
Chase National Bank of New York	8,571	8,548	99.7%	1,819	21.2%
Subtotal	**70,585**	**69,955**	**99.1%**	**11,005**	**15.6%**
Canadian Banks					
Royal Bank of Canada	7,719	7,667	99.3%	4,318	55.9%
Bank of Nova Scotia	7,626	2,834	37.2%	6,671	87.5%
Subtotal	**15,345**	**10,501**	**68.4%**	**10,989**	**71.6%**
Total	**$137,272**	**$120,320**	**88.0%**	**$40,234**	**29.3%**

Sources: Venuti 1955: 32; AHBPPR, Banco Popular de Puerto Rico, Anual Report, 1942: 6,7; Banco de Ponce, *Memoria*, 1942: 9; Law Number 252 May 13,1942, LPR 1942: 1445–7.

Governor Rexford G. Tuwell(Center).To his right: future governor Jesús T. Piñero, Treasurer of Puerto Rico and president of the Development Bank Rafael Buscaglia,Resident Commissioner Antonio Fernós Isern and Representative Ernesto Ramos Antonini. San Juan. 1941–1946. Reprinted, by permission, for the Fundación Luis Muñoz Marín.

widely accepted by the Roosevelt administration. In the United States, Keynesian economic ideology served as a basis for creating regional development companies, such as the Tennessee Valley Authority (TVA)" (Pantojas-García 1990: 44).

Governor Tugwell entrusted James Edward Curry to write the law organizing the Development Bank. Curry, a lawyer by training, was on loan from the Puerto Rico Reconstruction Administration. Since August 1941, he had been working with the Puerto Rico Water Works Authority (ALMM, Sección IV, Presidente del Senado, Cartapacio #152, Documento #6). On March 16, 1942, Curry notified Governor Tugwell he had completed writing the draft of the law that he had requested. Four days later, PDP Senator Vicente Géigel Polanco submitted this draft for senate approval; minor modifications were incorporated (Actas del Senado 1942: 1555). Governor Tugwell signed the Law Number 252, creating the Development Bank of Puerto Rico on May 13, 1942 (LPR 1942: 1445–7).

The law creating the Development Bank was brief and to the point. It consisted of only nine articles. Article Four gave preference and priority to loans and credit extended to the Development Company and to firms sponsored by this Company. Article Six assigned $500,000 to the Bank and Article Five declared that the debts incurred by this institution would not, in any way, mortgage the assets of the People of Puerto Rico (LPR 1942: 1445–7). From the start, the challenges imposed on this organization were enormous, and the capital invested was not sufficient. This would prove to be a recurring problem during the initial stages of this institution.

There were 12 banks operating in Puerto Rico at the time the Development Bank was created. The largest, the National City Bank of New York, had assets of $62 million, an amount equal to 45 percent of all banking assets on the Island.

There were nine locally owned banks, the largest being Banco Popular with $22.8 million in assets, followed by Banco Crédito y Ahorro Ponceño with $14.0 million, and Banco de Ponce with $10.3 million. Two Canadian banks were also doing business in Puerto Rico, though their operations were rather small when compared to the larger stateside or locally owned institutions. The Royal Bank of Canada had, for example, $7.7 million in assets, while the Bank of Nova Scotia had $7.6 million. As such, the Development Bank's assets of $500,000 placed it among the smallest institutions in Puerto Rico. Only the Credit Union Bank, with $365,000 in assets, and the Banco de San Juan, with $199,000, were smaller.

Given that the Development Bank was entrusted with the responsibility of financing the Island's industrial policy (LPR 1942A: 1445–7), the amount of capital assigned to it, as previously stated, was not nearly enough. It is important to realize that during the first months of 1942—as a result of the German U-boat blockade to Puerto Rico—unemployment increased to 237,000 of out an estimated total population of 1,869,255 (Curet Cuevas 1976: 331), food prices increased by 50 percent, and a lack of raw materials practically paralyzed the construction, manufacturing, and transportation industries (Bolívar Fresneda 2007: 27–36). The challenges faced by the Development Bank were enormous. And yet its budget was significantly lower than, say, the Department of Education, which had $6,470,000 assigned to it; the Health Department, which had $2,481,000; and the Insular Police, which had $1,662,000. Only the University of Puerto Rico, the Department of Labor, and the Legislature were assigned lower amounts (ALMM 1942A: 27). However, the Bank overcame this challenge, and capital, or lack thereof, would not play a significant factor in the Bank's performance.

IT IS INTERESTING TO NOTE THAT OUT OF THE NINE MEMBERS OF THIS BOARD, NOT ONE WORKED IN THE MANUFACTURING SECTOR, AND THE DEVELOPMENT BANK WAS, AFTER ALL, AN INSTRUMENT TO PROMOTE INDUSTRIAL POLICY.

The start of operations

On December 9, 1942, the governor's Executive Council nominated the nine members to the Boards of Directors of the Development Bank. Three members were nominated for a period of six years, three for a period of four years and the remaining three for two years. Rafael Buscaglia, Treasurer of Puerto Rico; César A. Toro, a pharmaceutical products representative; and Juan Cabrer, owner of the Cabrer Stores in Ponce and member of the Board of Directors of the Banco de Ponce, were nominated for the longest time period. José Antonio Castillo, a farmer from

Sabana Grande, Vicente Medina, future administrator of the state-run Puerto Rico Glass Corp., and Fernando Rodríguez, executive of the locally owned firm Trigo & Company, were nominated for a period of four years, while Rafael Carrión Pacheco, vice-president of Banco Popular, Pedro Juan Rosaly, executive at Banco de Ponce, and Esteban A. Bird, vice-president of Banco Crédito y Ahorro Ponceño, were nominated for two years (*El Mundo* 1942B: 4; AHBGF 1946: 1). It is interesting to note that out of the nine members of this Board, not one worked in the manufacturing sector, and the Development Bank was, after all, an instrument to promote industrial policy. This blatant omission would adversely affect the decisions made by this institution regarding the loans requested by the manufacturing clientele.

During the first meeting of the Board of Directors, on January 8, 1943, Rafael Buscaglia was unanimously elected president of that institution. From that point on, he would be the driving force of the Bank. According to Buscaglia—one of the founders of the PDP and a firm believer in the eventual independence of Puerto Rico—the Bank should concentrate its efforts in promoting infrastructure programs, as this was an indispensible prerequisite for the implementation of an industrial policy. Buscaglia also believed that any industrial program should be headed by local entrepreneurs, and this point would prove to be a future source of controversy.

On May 4, 1943, the Bank was ready to accept deposits, approve loans, and engage in general banking practices (LPR 1943: 115). Since Buscaglia's main responsibilities lay with his position as Treasure of Puerto Rico, he had little time left to attend the added responsibilities as President of the Development Bank, a position he had been appointed to by Governor Tugwell. Therefore, on October 22, 1943, Buscaglia proposed that the Board of Directors hire the services of an expert in the field of investments that could, in addition, lead the Bank in his absence. Since this kind of expertise was lacking in Puerto Rico, particularity that associated with the issuance of bonds that could be sold in the U.S. (Interview with Roberto de Jesús Toro 2005), Buscaglia proposed hiring Donald R. Bonniwell, an executive with the Chicago-based firm Kneeland & Co. (AHBGF 1943B: 11–4). Bonniwell was eventually hired. He developed a close working relationship with Buscaglia, a relationship that lasted for the following eleven years (Interview with Roberto de Jesús Toro 2005). Also on October 22nd, the Board of Directors nominated Esteban A. Bird to the position of First Vice-President, Juan Cabrer to Second Vice-President, and Fernando Rodriguez to Treasurer (AHBGF 1943C: 15–7). These nominations point to the lack of talent available on the Island required for these highly technical positions, and as previously mentioned, the lack of representation from the industrial sector.

The Development Bank generated a great deal of enthusiasm from the private sector. It received a great number of inquiries regarding its industrial loan approval processes. Most of these inquiries originated from existing business; the remainder, from new ventures. According to Buscaglia, the Development Bank would not be competing with the private banking sector, as the inquiries received by the Bank did not fall into the category of loans that would normally be approved or considered by the commercial institutions. In fact, Buscaglia pictured the Developments Bank's functions more along the lines of the federally funded Reconstruction Finance Corporation (*El Mundo* 1944: 1, 4).

Given that most of the Board of Directors of the Development Bank were in fact bankers, it is not surprising that the loan approval process of the Development Bank was quite similar to that of privately held commercial institutions. The Bank required a critical viability study of the project, a forecast of future growth and the amount of employment it would generate. It also required that 50 percent of the loan be guaranteed with land, buildings, and/or equipment. In spite of the fact that the Board of Directors was chartered by law to approve loans of prudent risks, the Bank's loan approval process dictated that the Bank was not in the business of lending capital to industries it deemed purely speculative in nature, or those it thought possessed a high degree of risk (AGPR 1947A: 7, 9). In addition, the Bank would only evaluate loans that had previously been rejected by commercial institutions. The possibility that the Development Bank would approve loans to the industrial sector, which at the time was considered either highly speculative or risky, was slim.

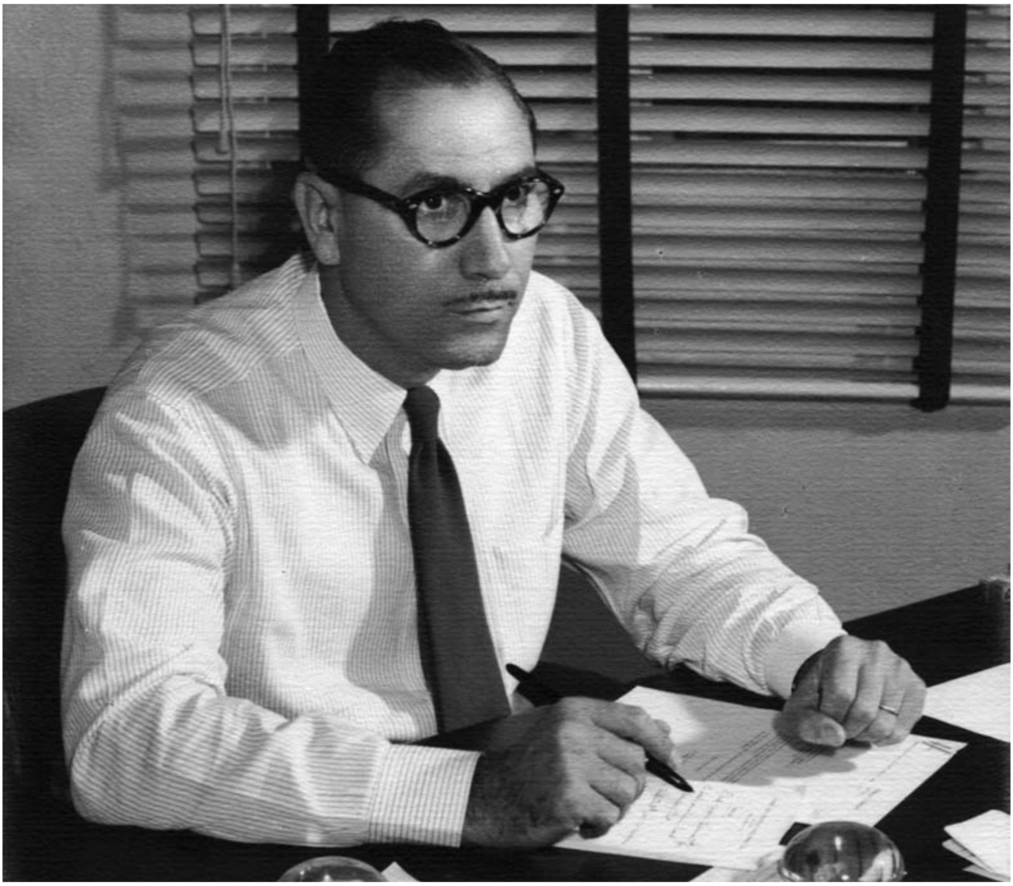
TABLE 2: SOURCES OF CAPITAL — DEVELOPMENT BANK 1943-1948 ($000)

	Legislative Assignments	Legislative Assignments	Deposits: Local Government[4]	Deposits: Local Government	Total
1943	$500 [1]	100%	$	0%	**$500**
1944	5,000 [2]	58%	3,613	42%	**8,613**
1945	15,000 [3]	59%	10,550	41%	**25,550**
1946	-	0%	7,678	100%	**7,678**
1947	-	0%	13,174	100%	**13,174**
1948	-	0%	13,174	100%	**13,174**
Total	**$20,500**	**30%**	**$48,189**	**70%**	**$68,689**

Sources: [1]AHBGF, Law # 252, May 13, 1942:1445–7, [2]AHBGF, Law# 4, March 2, 1944: 9–11, [3]AHBGF, Law # 302, May 15, 1945: 1151–3; [4]Venuti, 1955: 44.

The Development Bank requires more capital

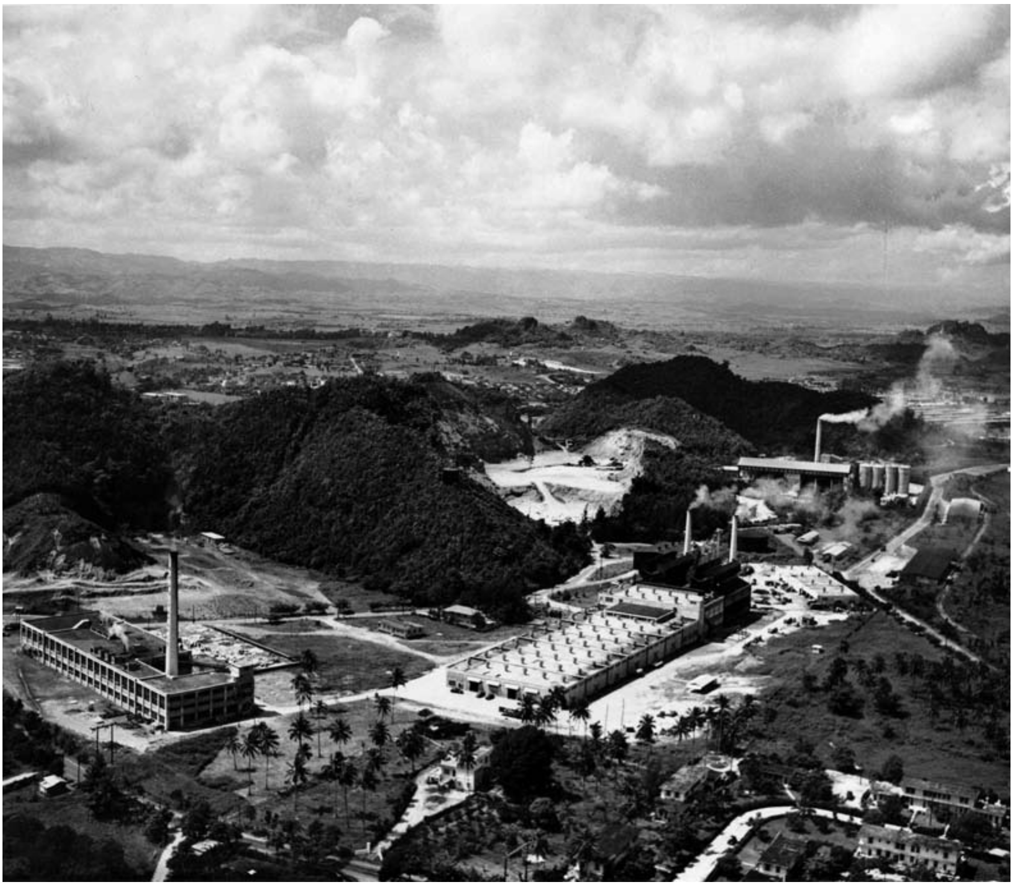
Once[1] the Development Bank commenced operations, on October 22, 1943, it initiated a number of transactions aimed at generating profits. The Bank netted $25,000 by selling $1,000,000 worth of bonds from the Water Works Authority and another $25,000 from a bond issue it was preparing for municipal aqueducts (*El Mundo* 1943B: 1). In spite of these achievements, Buscaglia was of the opinion that the bank did not possess sufficient capital in order to approve industrial loans. Given that this was the reason for creating the Development Bank, during the first week of February 1944, Buscaglia requested an increase in the bank's capital from the Legislative Assembly. On February 15th, Representative Ernesto Ramos Antonini, a member of the PDP, submitted a bill in order to provide $5,000,000 in additional funds to the Bank (Actas de la Cámara de Representantes 1944: 19, 24). The Bill passed the House with 20 in favor and 16 abstentions. It is interesting to note that during the discussions of the Bill, a number of representatives from the private banking sector were called upon to testify. They testified that they did not regard the Development Bank as a competitor. In fact, they were actually in favor of it! According to them, the Development Bank's operations did not affect their business, and they felt the Bank would be of great service to Puerto Rico (Actas de la Cámara de Representates 1944: 90–1).[1] The Senate approved the Bill on February 24th (Actas de la Cámara de Representantes 1944: 122), and Governor Tugwell signed it on March 2nd (AHBGF 1944: 9–11). Five million dollars were therefore added to the bank's capital.



Teodoro Moscoso, president of the Development Company. San Juan. Circa 1940. Reprinted, by permission, from the Fundación Luis Muñoz Marín.

The $5,000,000 the Legislature assigned to the Bank in 1944 was not enough to carry it through 1945. Therefore, on May 15, 1945, Governor Tugwell signed Law Number 302, assigning $15,000,000 in additional capital to the Bank (LPR 1945: 1151–3). Fortunately, for the Bank, the Central Government was flush with an unexpected windfall of income. The federal taxes imposed on the sales of Puerto Rican rum to the mainland, which were rebated to the local government, and the huge military spending on the Island provided the necessary cash to invest in developmental state-sponsored programs (ALMM 1948 Cartapacio# 372, Documento #14).

This infusion of public capital added a substantial competitive advantage to the Development Bank, which, even though it claimed not to compete with the commercial sector, must have sent chilling signs to those executives not accustomed to this sort of favoritism. The capital assigned by the state to the bank was actually free; in other words, the bank did not have to pay it back. However, funds deposited in private institutions were not paid back, as competitive pressures forced private banks to pay interest on their deposits. In addition, private banks needed to open branches throughout the island in order to conduct their business, while the Development Bank conducted all of its transactions from its San Juan office. Not only that, the salaries of the president (Rafael Buscaglia) and the administrator (Jorge Bermúdez) were paid out of the Treasurer's office, where both men were employed. It was therefore in the interest of the private commercial sector that the Development Bank conduct its transactions so as not to compete with them (Interview with Roberto de Jesús Toro 2005).



State run companies owned and operated by the Development Company (Puerto Rico Paper and Pulp, Puerto Rico Glass, and Puerto Rico Cement Corp.) Guaynabo. 1944–1950. Reprinted, by permission, from the Fundación Luis Muñoz Marín.

In addition to the capital assigned by the Legislature, the Development Bank received a deposit of $4,950,000 from the Corporación del Café de Puerto Rico on April 5, 1946. However, in the case of this deposit, the Bank had to pay an annual interest payment of 3.5 percent (LPR 1946: 583–99; AHBGF 1946A: 28). Between 1943 and 1945, the Development Bank was assigned $20,500,000 from the local Legislature. After 1945, the Bank did not receive additional funds from the Legislature. It depended on government deposits to sustain its growth, most of which came at the expense of stateside banking institutions (Bolívar Fresneda 2007: 65, 67).

In 1946, the local government deposited $7,678,000 into the accounts of the Development Bank. It deposited an additional $13,174,000 in 1947 and a similar amount in 1948. Of the $68,689,000 that the Bank received during its short tenure—from 1942 to 1948—70 percent of the capital came from governmental deposits and 30 percent from Legislative Grants (AHBGF, Law # 252 May 13, 1942: 1445–7, AHBGF, Law # 4 March 2, 1944: 9–11, AHBGF, Law # 302 May 15, 1945: 1151–3; Di Venuti 1955: 44). It is interesting to note that the Development Bank's assets grew from $500,000 in 1942 to $46,800,000 in 1948. In comparison, by 1948, Banco Popular had assets worth $58,300,000; Banco Crédito y Ahorro Ponceño, $55,100,000; and Banco de Ponce, $34,700,000. In regard to income, by 1948, the Development Bank's income was $895,000, while Banco de Ponce's was $421,000. No figures were available for Banco Popular and Banco Crédito (Bolívar Fresneda 2007: 272, 279). Lack of capital would not be an obstacle for implementing an industrial program in Puerto Rico.

The conflicts brew

As discussed previously, the four principal participants responsible for the implementation of the industrialization program in Puerto Rico—Governor Tugwell; the president of the Senate, Muñoz Marín; the president of the Development Company, Teodoro Moscoso; and Rafael Buscaglia, the Treasurer of Puerto Rico and president of the Development Bank—differed in their approach to financing and promoting the industrial program. The conflicts, which brewed as a consequence, would have a significant detrimental impact, both short term and long term, on the industrial program implemented in Puerto Rico.

According to Governor Tugwell, the law creating the Development Bank was only a guide. In reality, the members of his administration were not clear as to which functions the Bank should tackle. Therefore, the law was designed to incorporate as much flexibility as possible. The only thing that Tugwell was certain about was that the Development Bank should fill a void created by the failure of the private commercial institutions to facilitate an investment policy that promoted long-term loans, as opposed to agricultural loans, which by definition were approved for a short-term period (Tugwell 1947: 262–3). "Our conception was that the bank should be the credit medium through which the industrialization could be achieved which we believed to be the only hope for real betterment in Puerto Rico. But this meant that it should not try to direct only public funds to these uses: there would always be more private than public capital available. We thought that by covering a margin of risk we might attract these private holdings into new enterprises. Whether this ought to be done by direct loans, by generously rediscounting the loans of private banks, or by making advances to mixed companies, we were not certain" (Tugwell 1947: 262–3). However, the Bank should be a "direct medium for starting new activities" (Tugwell 1947: 262–3). Tugwell, of course, was being influenced by his previous New Deal experiences during the 1930s, as a part of Roosevelt's "Brain Trust." He viewed the Development Bank as an instrument of policy, not as a vehicle for generating profits. This would prove to be an important distinction between himself and members of his administration, particularly the Treasure of Puerto Rico and president of the Development Bank, Rafael Buscaglia.

Senator Muñoz Marín, on the other hand, was more interested in the Bank's ability to issue bonds sidetracking the limits imposed on the Central Government by the Organic Law. Muñoz Marín noted that the PDP programs would cost that much more than what the government could afford. In fact, in a recent issue of the *Inter-American Magazine*—a publication sold in Latin America and in Washington—Muñoz Marín claimed that the Island needed over $700,000,000 in order for the economy to achieve full employment. According to Muñoz Marín, the ability to issue bonds was therefore the only way to help eliminate the hunger that most of Puerto Rico's populations were subject to, to improve the quality of life on the island, and to stimulate the local economy (ALMM 1946 Cartapacio #1, Documento #2).

Moscoso, the president of the Development Company, was more concerned with the Banks commitment to approve loans deemed risky by the commercial institutions, and by risky, he meant industrial loans. Moscoso urged the Development Bank to take certain risks not normally undertaken by the commercial institutions. He alleged that the Development Company was willing to take risks as part of its stated responsibilities, and that the Bank should also be willing to assume similar risks, and not require unreasonable collateral from the investors promoted by the Development Company (ALMM 1947A

Cartapacio #373, Documento #37). Obviously, Moscoso and Governor Tugwell were not concerned with the Bank's profitability.

Moscoso urged Buscaglia to name a committee from the Bank so that it would meet with one in the Development Company, in order for there to be more cooperation between both organizations. This, Moscoso stated, would facilitate the establishment of new industries (ALMM 1942B Cartapacio #373, Documento #33). Moscoso's insistence regarding this issue was the obvious lack of cooperation between both organizations, which, he believed, was debilitating the industrialization efforts (ALMM 1948: 8). He added that both entities should work together to coordinate this effort, since in public opinion, as well as in the opinion of the commercial and industrial sectors and the media, both organizations functioned as one (ALMM 1947B Cartapacio #373, Documento #33). Buscaglia alleged that given the bank's limited resources, the Development Company should not promote U.S. investments by offering to finance them with the Banks capital. On the contrary, Buscaglia claimed Puerto Rico should be intent on attracting capital from the mainland. Though Buscaglia was aware of the Development Company's loans, which he categorized as being highly speculative, he acknowledged that risky loans would have to be approved in order to attract industries to Puerto Rico during the initial stages of the industrial program. However, Buscaglia would rather have the Development Company approve these loans, as he believed that the Bank should act with prudence and abide by industry-approved credit standards (AHBGF 1948: 9–10).

> SENATOR MUÑOZ MARÍN, ON THE OTHER HAND, WAS MORE INTERESTED IN THE BANK'S ABILITY TO ISSUE BONDS SIDETRACKING THE LIMITS IMPOSED ON THE CENTRAL GOVERNMENT BY THE ORGANIC LAW.

Buscaglia believed that the Bank could not and should not be in the business of approving questionable loans that might jeopardize its creditworthiness, or fail to provide the institution with an adequate return on its capital. In other words, Buscaglia believed the Bank was in the business of making money. He also stated that since the Island's infrastructure would not support a full-fledged industrial program, the Bank should concentrate its efforts in promoting the sale of bonds of public corporations that dealt with infrastructure construction (Private library of the Rojas-Buscaglia family).

The Development Bank recommended that Moscoso's Development Company be allowed to make investments in the industries they promoted (AHBGF 1948: 9–10). This would limit the Bank's participation in the approval of industrial loans and give Buscaglia space to concentrate on other priorities (Private library of the Rojas-Buscaglia family). Moscoso did not adhere to this recommendation. His vision was for the Development Company to issue bonds in order to finance his industrial project, and therefore, not depend on loans from the Development Bank, which in any case, were not forthcoming. He could not afford to loan his limited capital on "risky loans," and preferred that the Development Bank take on this responsibility (ALMM 1945 Cartapacio #376, Documento #25). As such, it seems that the struggles between Governor Tugwell, Muñoz Marín, Buscaglia, and Moscoso almost cancelled each other's efforts to industrialize Puerto Rico.

The state of local manufacturing

There were few locally owned manufacturing factories in Puerto Rico between 1942 and 1948. A profile of the 2,300 members of the Puerto Rico Manufacturer's Association (PRMA) reveals that 27 percent were in the cigar industry, 13 percent in the sandwich and bakery industries, and the remaining 60 percent were in other miscellaneous small businesses (Bolívar Fresneda 2007: 220–1). Members were not pleased with the Bank's performance. According to Vicente León, Secretary General of the PRMA, the Development Bank did not approve loans to business that did not own their real estate. León stated that if the Bank was really interested in helping small businesses, they would also accept machinery and equipment as collateral. Ironically, according to León, these were the same requirements needed to qualify for a loan from private commercial institutions. PRMA argued that the Bank should modify its loan requirements in order to benefit small industries, and not cater exclusively to large industries that owned their facility, had a solid financial situation, and were able to negotiate loans with any commercial financial institution (*El Mundo* 1945a: 20).

Buscaglia answered the PRMA's onslaught by declaring that the Development Bank could not and would not approve loans when it thought it could not recoup its investments. Doing so would seal the Bank's future. The Bank should not, under any circumstances, approve loans, private or public, which it thought would fail. In an interview with *El Mundo*, Buscaglia explained that "the Bank is not an institution of subsidies, but a commercial institution that wishes to promote Puerto Rico's economic development through sound and prudent banking practices" (*El Mundo* 1945b: 1).

The Bank acted on Buscaglia's advice, vision, and leadership. He did not place the Bank in financial risk by promoting the approval of speculative loans. In fact, the Bank's loans were highly collateralized and of limited risk. An analysis of the Bank's financial statements confirms this, as it revealed that most of the Bank's income resulted from passive investments, while only a small portion of profits was attributed to interest from the loan portfolio. Between 1944 and 1947, passive investments increased from $9,300,000 to $49,700,000, while loans increased from $900,000 to $6,600,000 (Bolívar Fresneda 2007: 239–41).

TABLE 3: PASSIVE INVESTMENTS — DEVELOPMENT BANK OF PUERTO RICO 1944–1947 ($000)

Passive Investments	1944	1945	1946	1947
U.S. Bonds	0	$18.0	$21.5	$26.0
P.R. Bonds and obligations	$5.7	$7.3	$5.2	$6.6
Cash	$3.6	$10.6	$7.7	$17.1
Total	$9.3	$35.9	$34.4	$49.7
Loans	0	$0.9	$1.5	$6.6
Ratio of loans to passive investments[1]	**0**	**2.5 %**	**4.4%**	**13.3 %**

Sources AHBGF, Puerto Rico Development Bank, Annual Report, 1946–1947, Folio Number 8; [1]Calculated by the author.

As a percentage of its assets, the Development Bank loaned less capital than Banco Popular, Banco de Ponce, and Banco Crédito y Ahorro Ponceño, the three largest locally owned banks operating in Puerto Rico. According to the financial statements made available during our study, from 1944 to 1948—the years in which the Development Bank operated—it approved loans valued at 16.9 percent of its assets. A study of the years 1939–1948 revealed that Banco Popular approved loans valued at 22.0 percent of its assets, while Banco de Ponce approved loans valued at 34.0 percent. For the years 1944–1948, Banco Crédito y Ahorro Ponceño ratio was 27.0 percent. It should be noted, however, that in 1948, the Development Bank's ratio of loans to assets increased to 33.0 percent, lower than Banco de Ponce's 34.0 percent, but higher than Banco Crédito's 30.8 percent and Banco Popular's 29.1 percent. So, what does this information tell us about the Development Bank's commitment to issue and approve loans? Simply put, this institution left the development responsibilities in the hands of the private banking institutions. Ultimately, it became the government's banks, issuing bonds and permanently abandoning its developmental responsibilities.

TABLE 4: LOANS TO ASSET RATIO FOR LOCAL BANKS OPERATING IN PUERTO RICO 1939–1948 ($000)

	DEVELOPMENT BANK			**BANCO POPULAR**		
	Loans	**Assets**	**%**	**Loans**	**Assets**	**%**
1939				$4,219	$10,027	42.1
1940				5,064	13,616	37.2
1941				5,087	17,183	29.6
1942				5,390	22,835	23.6
1943				4,498	30,884	14.6
1944	0	9,143	0	N/A	N/A	N/A
1945	934	27,102	5.5	8,877	59,324	15.0
1946	1,484	29,415	22.4	11,425	67,078	17.0
1947	6,239	41,784	36.9	N/A	N/A	N/A
1948	15,433	46,818	33.0	16,925	58,255	29.1
	Average		**16.9**			**22.0**
	BANCO DE PONCE			**BANCO CRÉDITO**		
	Loans	**Assets**	**%**	**Loans**	**Assets**	**%**
1939				$4,219	$10,027	42.1
1940				5,064	13,616	37.2
1941				5,087	17,183	29.6
1942				5,390	22,835	23.6
1943				4,498	30,884	14.6
1944	0	9,143	0	N/A	N/A	N/A
1945	934	27,102	5.5	8,877	59,324	15.0
1946	1,484	29,415	22.4	11,425	67,078	17.0
1947	6,239	41,784	36.9	N/A	N/A	N/A
1948	15,433	46,818	33.0	16,925	58,255	29.1
	Average		**16.9**			**22.0**

Sources AHBGF, Development Bank of Puerto Rico, Anual Report 1946–47, Folio No. 8, *Government Development Bank for Puerto Rico*, Fiscal Year 1948–49: 47; AHBPPR, Banco Popular de Puerto Rico, Anual Reports, 1939–1948; Banco de Ponce, Anual Reports, 1939, 1940, 1942–1945, 1947,1948; Banco Crédito, Annual Reports, 1944, 1945, 1947, 1948; AHBGF, *Government Development Bank for Puerto Rico*, Fiscal Year 1948–49: 47.

Conclusion

The Second World War, and the disastrous economic and social conditions in Puerto Rico prior to the war, motivated the U.S. government to assist in the Island's economic recovery. In was thought that implementing an industrial program would lift Puerto Rico out of its misery. The Development Company and the Development Bank were to become the pillars of this program. Unfortunately, internal squabbling squandered this opportunity. The Development Bank functioned more like a governmental institution dedicated toward issuing and selling bonds, and ignored its other important function, that of approving loans deemed too risky by the commercial banking sector. Neither did it function as the policy instrument envisioned by Governor Tugwell, assuming risks that the private commercial banks refused to support.

Buscaglia was given full authority to run the bank as he saw fit. In spite of what the law said about the bank's objectives and in spite of Governor Tugwell's view that the bank was an institution that would take risks not covered by the private sector, this did not happen. Buscaglia was able to twist and turn through the political structure, confront accusations by Moscoso's Development Company and by the PRMA, and still hold his ground. His legacy continues. The Development Bank, the precursor of the Governmental Development Bank (GDB), concentrated its efforts on providing governmental services and bond issues, and abandoned its efforts to provide industrial or commercial loans. Its successor, the GDB, continued those policies.

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NOTES

1 In *Imperialism by invitation: Causes of a Failed Developmental State Project in Puerto Rico, 1940–1950*, Padín quotes Mr. Roig, a well-known Puerto Rican banker, expressing consternation about the establishment of a governmental development bank, in part because it would compete with domestic banks for deposits from the governmental Treasury. According to Padín, "a governmental bank threatened private bank prerogatives in two ways. Most obviously, it competed directly for a fixed pool of financial resources. However, there was a less obvious and more far-reaching effect. Once development criteria were introduced in the use of state financial resources, it was possible that what Treasury deposits did continue flowing to private domestic banks were made conditional on the contributions banks made to the industrial program" (Padín 1998: 227–8). Bolívar Fresneda's dissertation disproves this theory, as those most affected by the change in the Treasury's policy were the U.S. banks and not the domestic banks (Bolívar Fresneda 2007: 262–90).

ABBREVIATIONS

- AGPR: Archivo General de Puerto Rico
- AHBGF: Archivo Histórico del Banco Gubernamental de Fomento
- AHCFI: Archivo Histórico Compañía de Fomento Industrial
- ALMM: Archivo de la Fundación Luis Muñoz Marín
- LPR: Leyes de Puerto Rico

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