5180072

PD-AAA-738-B1

UNCLASSIFIED

DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
ALLIANCE FOR PROGRESS
WASHINGTON, D. C. 20523

CAPITAL ASSISTANCE PAPER

ECUADOR - COOPERATIVE BANK

BEST AVAILABLE

AID-LA/P-50

UNCLASSIFIED

DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington 25, D. C.

UNITED STATES COORDINATOR
ALLIANCE FOR PROGRESS

UNCLASSIFIED

AID-LA/P-50
June 1, 1964

MEMORANDUM FOR THE ADMINISTRATOR

SUBJECT: ECUADOR - Cooperative Bank

The attached Capital Assistance Paper which recommends authorization of a loan of not to exceed $1,200,000 to the Ecuador Cooperative Bank to be used for subloans to members of the Bank to assist in financing the development of the cooperative and credit union movement in Ecuador is under consideration for authorization by this Bureau.

William D. Rogers
Deputy U. S. Coordinator

Attachments:
- Summary and Recommendations
- Project Analysis
- Annexes I-XII

UNCLASSIFIED

UNCLASSIFIED
AID-LA/P-50
June 1, 1964

ECUADOR - COOPERATIVE BANK

TABLE OF CONTENTS

ECUADOR - COOPERATIVE BANK

A. SUMMARY AND RECOMMENDATIONS

1. APPLICANT: The Ecuador Cooperative Bank, privately owned by the stronger and sounder Ecuadorian cooperatives.

2. AMOUNT OF LOAN: Not to exceed $1,200,000.

3. TOTAL COST OF ACTIVITY: $2,004,000, of which 60% is the A.I.D. loan, 3% A.I.D. grant, 29% Ecuadorian cooperative movement local contribution, and 8% GOE contribution.

4. DESCRIPTION OF ACTIVITY: The A.I.D. loan will be utilized exclusively to finance some of the sub-loans which will be made by the Bank [illegible] its cooperative members. The cooperatives and the GOE will also [illegible]nance some sub-loans and all operating expenses. A.I.D. grant will provide coordinated technical assistance which is considered too heavy a burden to include within the loan during the first three years of the Bank's existence.

5. PURPOSE OF ACTIVITY: To increase agricultural and industrial production through private cooperatives which will be composed mainly of lower-middle class Ecuadorians who have almost no access to credit at reasonable terms from existing Ecuadorian financial institutions. To stimulate the further development of the two-year old relatively successful credit union movement. To encourage the development of a revenue-producing and eventually self-financing credit institution which will assist in the economic development of Ecuador.

6. BACKGROUND OF ACTIVITY: The need for Ecuadorian Cooperative Bank has been under consideration for years but recently greatly stimulated by the successful development and strengthening of cooperatives and credit unions through AID, IDB, and Peace Corps technical assistance programs. After a 1963 feasibility study and its indorsement by the National Planning Board, the Ministry of Commerce and Banking took the leadership in passing an

October 1963 GOE law permitting the establishment of a Cooperative Bank under conditions somewhat more liberal than for a regular private bank. This type of activity is also strongly supported under the cooperative and private enterprise, Sections 251(g), 253, and 601 of the Foreign Assistance Act.

7. EXIMBANK INTEREST: On March 10, 1964, the EximBank indicated no interest in the proposed financing.

8. MISSION VIEWS: On May 19, 1964, the original loan paper was approved by the USAID/Embassy Executive Committee for Capital Development.

9. STATUTORY CRITERIA: All statutory criteria have been met.

10. ISSUES: Smaller capitalization and larger debt-equity ratios, particularly in the initial stage, than is normally considered desirable. A spread to the Bank of 5.25%, higher tha[illegible]rmal, is being recommended. Whi[illegible] the financial projectio[illegible]de in the loan paper were base[illegible]hat is believed to be r[illegible]stic demand, they could be up[illegible] the Bank cannot process applications at the projected dem[illegible] level.

11. RECOMMENDATION: Authorization of a loan not to exceed $1.2 million:

   a. Terms - To the Borrower, 25 years with a grace period on repayment of principal for 10 years; to the Government via the two-step procedure, up to 40 years with a 10-year grace period.

   b. Interest - 3/4 of 1% per annum for the first ten years and 2% per annum thereafter for Borrower and Government.

   c. Loan and maintenance of value to be guaranteed by the GOE.

   d. Repayment in U. S. dollars.

   e. Equipment, materials, and services (except marine insurance) financed under the loan shall be procured from the United States of America or Ecuador.

f. United States dollars utilized under the loan to finance local costs will be obtained through the Special Letter of Credit Procedure utilized by A.I.D. and the Central Bank of Ecuador.

g. The Bank will contract for U. S. advisory services satisfactory to A.I.D.

h. The GOE and Cooperative Bank shareholders will make certain minimum grant and paid-in capital contributions agreed to with A.I.D. prior to any disbursements.

i. A maintenance of value reserve system satisfactory to A.I.D. will be developed.

j. The Cooperative B[illegible] will take precautions satisfactory to A.I.D. for [illegible] sub-loans financed by A.I.D. from being mad[illegible] [illegible]atives dominated by the communist movement.

k. Except for the normal Central Bank of Ecuador service charge, the GOE will exempt the Cooperative Bank from taxes in connection with the conversion of foreign exchange.

l. Any other terms and conditions which A.I.D. may deem advisable.

Project Committee: RJApton, USAID/Ecuador, Loan Officer
RPol, USAID/E Cooperative Advisor
MBarnebey, USAID/E Program Officer
GFlood, LA/GC

Drafted: RAPton/USAID/E.

B. History and Background

1. The Cooperative Movement in Ecuador

GOE statistics indicate that as of September, 1963, Ecuador had 850 cooperative institutions with 44,000 members and US$ 2,500,000 capitalization. A previous 1960 GOE report listed 612 cooperatives with US $900,000 capitalization. Thus a significant improvement can be demonstrated during the past three years, particularly because important build-up of capital has been accomplished by some of the stronger cooperatives since 1960. New cooperatives have continued to be formed since the 1963 GOE report. Annex I lists Ecuadorean cooperatives by type and number, their membership totals, and capital.

The USAID Cooperative Section believes that there are about 200 bona fide cooperatives by U.S. standards in the group of 850 cooperatives in Ecuador. The others can be improved in numbers and quality through assistance in management, financing, and cooperative education.

Up to this time, the cooperative movement in Ecuador has had a relatively small impact on the national economy and social welfare, but evidence of a stronger potential for an important and progressive cooperative development can now be seen. Although the Lawrence Feasibility Study states there are only about 150 true cooperatives, the USAID Cooperative Division and Intensive Review Committee would now increase this figure to approximately 200.

The Ecuador Credit Union Federation was organized in June, 1963, by Ecuador's credit unions, with the assistance of a USAID grant-financed contract with the Credit Union National Association which provided the economic and technical services towards this objective. At the time the Federation was organized, there were only 33 legally organized credit unions, with a total membership of nearly 3,000 and a capital of about $110,000. In one year, chartered credit unions have increased to 69, and another 67 groups are in the process of formation and organization; membership has quadrupled to 12,000 (7,000 in the chartered groups and 5,000 in the groups in formation.) Savings and loans have increased to over $225,000.

2. AID, Peace Corps, and IDB Assistance to Ecuadorean Cooperative Movement

Cooperative development in Ecuador, as part of the Alliance for Progress, started in July 3, 1962, when an agreement was signed between the Government of Ecuador and USAID/Ecuador. This initial agreement was aimed primarily at the establishment of a program for the development of credit unions. In March, 1963, the agreement was revised to include an expanded program for cooperative development, aimed to cover all phases of cooperative work, including credit unions.

Prior to that time, little or not organized effort had been made to assist the Ecuadorean cooperative movement in the solution of its problems or in its proper organization. The GOE has neither had the funds for the required technical assistance nor a credit source for financing cooperative enterprises. With the advent of the aforementioned agreement, the USAID took the position that its funds for cooperative development would be used to support the development of the private sector cooperative movement working directly with the people who would be the beneficiaries of their own self-help efforts.

Programs in Specialized Fields

(a) Credit Unions

Initial efforts were made to assist the then weak and [illegible]-directed credit union movement. At the time the program started there were [illegible] credit unions with less than 2,000 members and an accumulated capital of 500,000 sucres ($27,000). Now, almost two years later, there are 111 credit unions, either legally organized or awaiting legal approval, with 6,000 members and an accumulated capital of 3,500,000 sucres ($190,000). During the same period, a credit union federation was established and has begun to assume some of the functions which were begun by and are still being carried on by the USAID in education, accounting, promotional activities, and legal assistance. Over the next five years, the federation is gradually expected to assume all of these functions.

(b) Rural Electrification.- Two surveys were made of Ecuador by NRECA technicians accompanied by USAID and INECEL engineers to determine the most feasible location for a pilot rural electric cooperative. The area in and around Santo Domingo de los Colorados was selected due to the great need for improving and expanding electric service, a strong cooperative spirit, and indicated economic growth.

The cooperative was organized on a sound basis through intensive promotional campaigns, education and training of its leaders, and the obtaining of local participation in the form of membership fees and the purchase of cooperative shares.

The local Municipal electric system was acquired by the cooperative on March 18, 1964. It is now providing 24-hour electric service to over 400 homes and expects to serve a total of 800 members within the next year.

The cooperative has made a loan application to USAID for $650,000 to provide funds for rebuilding the present system, extending electric service to the entire town, and building 110 miles of rural lines. The completed project will serve 3,000 homes and commercial establishments within two years.

(c) Small Grain Marketing and Storage.- A survey of grain marketing and storage in Ecuador has been made by the Farmers Union Marketing Association, Kansas City, Missouri. An analysis of the situation, two proposals for cooperative storage and marketing facilities, and the need for technical assistance in management were presented to the Minister of Development.

(d) Livestock Marketing and Meat Processing.- A survey of livestock marketing in Ecuador has been made by the Farmers Union Marketing Association, and a feasibility study on slaughtering and processing has been presented to ITALCONSULT, an O.A.S. consulting firm analyzing this problem for the National Planning Board.

(e) Production Credit.- A survey on agricultural production credit has been made by a representative of the Kansas cooperative movement. The report explains the importance of agricultural production credit to Ecuador as a measure to increase national productivity.

(f) Present USAID/Ecuador Cooperative Program.- As of May, 1964, the USAID cooperative program consists of:

(1) One direct-hire cooperative advisor to advise the GOE and the USAID on all matters relating to the development of the Ecuadorian cooperative movement.

(2) One contract cooperative educator promoting training and information in the cooperative field.

(3) Two credit union contract consultants and six credit union field workers.

(4) One cooperative editor producing educational and technical material.

(5) Three rural electric cooperative contract technicians.

Several of the USAID direct-hire and contract cooperative technicians have played an active role in the planning stages of the Cooperative Bank. As soon as the proposed loan is authorized, they intend to return to the field of developing the national cooperative movement and providing technical assistance to individual cooperatives and credit unions that plan to utilize the proposed Bank. Together with the continued support by Peace Corps Volunteers, such technical assistance is essential, as the Bank staff will not be able to provide such assistance to its members during the initial stage of its existence and is relying on such support.

Peace Corps Participation.- In the early stages of development of the credit unions program, the need for continual and follow-up phases within this program were evident. Consequently, the Ecuador Credit Union Federation and the GOE proposed that Peace Corps Volunteers be assigned to assist in credit union development. The first group of Volunteers assigned to the Federation received intensive training at the University of Wisconsin and in Puerto Rico in the organization and operation of credit unions. They have since become an important and effective group supporting the extension work which the Federation is conducting in the areas where credit unions operate. The Volunteers conduct regular check-ups on the operations of the four to six credit unions assigned to each of them. They also conduct training sessions and workshops for the directors and committeemen in the individual credit uni[illegible] along with promotion activities for new credit unions. Presently 26 V[illegible]teers are assigned to this work in fourteen provinces of Ecuador.

Inter-American Development Bank

The Inter-American Development Bank has extended a loan to Ecuador which includes substantial support for a cooperative housing program through the Ecuadorian Housing Bank. The amount of the loan is $10.6 million. The IDB has also supplied a three-man technical assistance team to supervise implementation of this loan. However, principally due to the high cost of land and financial and management problems in the Housing Bank, the promotion of housing cooperatives has been moving relatively slowly, particularly until early 1964.

3. A Short History of the Cooperative Bank of Ecuador.

The idea of establishing a cooperative credit system in Ecuador has been under consideration for several years, and has been encouraged by leaders of the individual cooperatives and the Government of Ecuador agencies which are interested in cooperative development.

In a brochure on cooperatives prepared and distributed by the GOE National Directorate of Cooperatives in 1961, the director of that agency pointed out that "all the difficulties encountered by the cooperative movement in Ecuador in obtaining credit.... make it urgently necessary to organize an Ecuadorian Cooperative Bank."

In April, 1962, the GOE and the USAID subscribed to an agreement designed to give greater impetus to the development of cooperative programs in the country, and as a part of this agreement reference was made to the necessity of "granting long and short-term credit to cooperative organizations at low interest rates."

In May, 1963, Mr. Douglas Lawrence, cooperative credit consultant, came to Ecuador under a USAID contract. He made an extensive feasibility survey for organizing an Ecuadorian Cooperative Bank. His recommendations were reviewed and accepted by the GOE, and in July, 1963, the USAID Cooperative Division took the initiative of collaborating with the cooperatives and their leaders who were interested in establishing such a credit system as a private bank to be sponsored by the cooperatives themselves rather than directly by the Government of Ecuador. At that time, a group of cooperative leaders, government officials and USAID representatives met in Quito for the first time and held discussions as to the manner of implementing a private cooperative credit system.

The outcome of the discussions held at this July 17, 1963, meeting was that the organization of a Cooperative Bank would encounter serious difficulties of a legal nature unless a law was passed to provide expressly for the establishment of such an institution. Subsequently, a committee was designated for drafting a proposed law to be submitted to the Government for issuance. When this draft law was completed, it was officially endorsed by the Minister of Commerce and Banking and issued as Decree No. 699 on October 17, 1963. (See Annex II.)

A group of leaders again convened in November, 1963, attended by the original group and a number of cooperative delegates who expressed a desire to be among the founding members. Under the new Decree, on December 12, 1963, they constituted themselves as an Organizing and Promotion Committee for establishing a Cooperative Bank.

On December 19, 1963, the tentative by-laws of the Cooperative Bank of Ecuador were discussed and approved. On January 3, 1964, the Minister of Commerce and Banking, acting for the Government of Ecuador, and Dr. Fernando Pareja, on behalf of the Bank, submitted a joint application for a US$ 2 million loan from AID, exclusively for making sub-loans and not for operating expenses.

To further support the proposed new Bank, the USAID, via grant funds, has provided or is providing:

(a) The Cooperative Bank feasibility study made by Douglas Lawrence.

(b) Continuation of two U.S. Cooperative Advisors and one U.S. Credit Union Advisor within the USAID Cooperative Division.

(c) A contract Cooperative Bank Advisor for two years service with the Ecuadorian Cooperative Bank.

(d) Some initial bank equipment including a safe, office equipment, accounting machinery, and a jeep.

(e) Training of the proposed General Manager in Puerto Rico and Lousiana.

The cooperation of the Ministry of Commerce and Banking of GOE includes:

(a) A total grant of $ 50,000, divided in three equal installments in each of the first three years.

(b) Free office space for a three-year period at the Comisión de Valores.

(c) Technical guidance and the required GOE endorsement and support.

If an AID loan is authorized by June, 1964, it is believed that the Bank can commence operations in September, 1964.

Annex X gives a break-down of the actual and estimated AID grant assistance funding in fiscal years 1963, 1964, and 1965.

C. Objectives and National Priority

The third goal in the Country Assistance Strategy for Ecuador is a major increase in agricultural and industrial production, including as specific targets increasing available agricultural and industrial credit and building up the Ecuadorean credit union and cooperative movements.

As in most underdeveloped countries, credit in Ecuador is scarce, interest rates are high, and local development loans, as opposed to short-term commercial credit, are hard to come by. This is true as well for consumer credit, crop and other agricultural loans, and most other forms of credit.

Alliance for Progress capital loans and new Ecuadorean credit mechanisms should contribute to an eventual reduction of all interest rates in Ecuador, and hopefully, to a less archaic and more progressive attitude toward longer-term development loans at reasonable terms to harness Ecuadorean savings for the nation's agricultural and industrial growth.

As described above, a cooperative bank has recently been established by decree. This $1.2 million loan recommendation will be the seed capital for the first two years' lending operations of the bank and will serve the credit needs of the growing private cooperative movement.

This program will enable cooperatives and their members to make significant contributions to the country's economic and social progress, will permanently create a method for mobilizing additional investment from local resources, and will contribute to the well-being of middle and lower income groups and to their participation in the national economy.

The lack of credit at reasonable terms has been a serious political and social problem, not only for the present government but also for previous ones. The absence or shortage of credit facilities is hampering progress in such key fields as agrarian reform, agricultural and industrial development, artisan development, and credit unions. This proposed loan, as well as other previous and proposed Alliance for Progress loans in industry, housing, and agriculture, is a major step in beginning to bring a favorable political and social impact to the middle and lower income groups of Ecuador. The importance of this and other credit institution loans can also be measured by the continuing major emphasis and publicity which the present government is giving to such loans. This loan will serve to strengthen the slowly growing middle class, create more employment opportunities, and help meet the essential credit requirements of Ecuador's rapidly growing cooperative movement.

This project will directly benefit private cooperatives and their members located throughout the country and is accordingly in the Ecuadorian national interest. The sub-loans will be a source of credit at reasonable rates of interest not now available to cooperatives or credit unions. The credit and the organizational technical assistance that will be made available to the cooperatives will further strengthen their growth and assist in encouraging the practice and habit of saving among middle and lower income groups. Through this project, members of cooperatives and credit unions will be spared from having to rely on unsecured loans at usurious terms reaching 30% or more monthly, and become eligible for loans on reasonable terms, including sound financial planning, that will permit small-scale industrial and agricultural development.

As is set out in the Annex IV letter from the Technical Director of the National Planning Board, this loan is directly related to the National Plan for Economic and Social Development. The operations of the Ecuadorean Cooperative Bank will serve to carry out these general purposes under the Plan: (1) to foster the growth of the cooperative movement in Ecuador; (2) to provide a source of additional agricultural credit; and (3) to provide financing for small-scale industrial and artisan activities. The AID strategy objectives for Ecuador and the Development Plan objectives, as they both relate to this proposed loan, are fully consistent in supporting this type of lending activity.

While a direct contribution will be made by the proposed loan to the agricultural and industrial (including artisan) sectors, and in particular to cooperatives engaged in those sectors, no meaningful quantification can be made as to the eventual increases in production which will be attributable to this loan. Realistically, this loan can be expected to help form new, or expanded, producing entities (i. e. the agricultural, artisan and other cooperatives) which will, for the first time, have access to capital loans for their operations and will have a true incentive to get on with the task of getting organized and marshalling their own--usually meager--savings for increased production. Marginal increases in agricultural and industrial production will occur as a result of implementation of this loan; whatever that marginal increment is will represent a decided plus for Ecuador's economic growth, and will at the same time mean the emergence of new producing entities, the cooperatives themselves, creating thereby new sources of employment and new sources of capital formation.

It is useful in this context to recall the success attained during the last two years by other capital-forming institutions assisted by the AID program in Ecuador. The savings and loan association movement, assisted by the AID $5 million housing loan and limited USAID technical assistance, has so caught on, that despite certain organizational and other problems, eight private saving and loan associations are now operating effectively throughout the country; as of April 1, 1964 with 8,462 depositor-members, over $1.1 million in deposits, and approval of 975 housing loans totaling almost $4 million. Similarly, with USAID-contractual technical assistance, the credit union movement has expanded rapidly; figures on the growth of this institution are presented in Section B of this paper. About $2.8 million of long-term industrial credit loans have been authorized during the past year through the AID and IDB loans to the GOE for this purpose; almost $2 million in additional applications are pending in various stages of processing. Within the next three months, the Comision de Valores will be converted into an industrial Nacional Financiera with authority to make direct loans or through intermediary private commercial banks. The utilization of sub-loans in these three areas augurs well for the capital-formation prospects of the Cooperative Bank, assuming approval of this proposed loan.

The proposed loan represents 60% of total project costs and, when the 25% foreign exchange component is deducted, will cover 55% of total local costs. While the fraction of local costs to be covered by the proposed loan is slightly higher than usual, this is considered justified by the nature of the project. (Actually the proportion of local costs defrayed by actual dollar disbursements would be reduced if AID is successful in channeling some local currency repayments as permitted by a recent amendment to the Foreign Assistance Act, thereby achieving a corresponding reduction in the dollar loan.) The highest practicable local contribution is being obtained from the subsidiary cooperatives -- an estimated $575,000 represented by borrowers' contributions, during the AID loan period. The GOE share is a minimal $169,000. However, it was the Intensive Review Committee's judgment that this is not the ideal proposal on which to push for a maximum GOE contribution since we are desirous of maintaining the completely private nature of the undertaking.

While there is clearly a pent-up demand for credit assistance to cooperatives, no truly reliable approximation can be made as to the effective demand for such credit in the next several years. An element of experimentation is necessarily involved in any such intermediate credit institution when tried for the first time in a country, and in fact a reliable projection of future years' lending operations must await the lending experience actually registered in the first two or three years of the Bank's existence. The GOE and the Intensive Review Committee have therefore accepted and utilized the independent feasibility study projections. This loan proposal must be recognized for what it is, a calculated-risk investment with excellent prospects for acceptance and use by Ecuador's national cooperative movement. Undoubtedly dozens of sub-loans will be sought, and many approved, and the best judgment of the Intensive Review Committee is that the proposed $1.2 million loan program will readily be absorbed by the fast-growing Ecuadorean cooperative movement, with additional funding needs for future years to be weighed and projected on the basis of the actual experiences of the Cooperative Bank in the first approximately two years of its operations. Reinforcing this view, several safeguards have been built into this proposed loan; perhaps most important, the USAID/Ecuador grant-funded technical assistance program of the last two years, and that projected for the next two to three years, has placed increasing stress on provision of highly qualified experts in the cooperative field to encourage and assist individual Ecuadorean cooperatives and their members as to improved org ization and proper financial practices.

If the USAID Mission is to participate a tively in fostering Ecuador's cooperative movement as has been envisaged, both in Quito and in Washington, then AID should give sympathetic consideration for providing a source of capital assistance for the growth of the productive capacity of these cooperatives. Except for the $110,000 PL 480 loan, no other source of credit is available, as a practical matter; neither commercial banks nor the Ecuadorean Government has in the past made significant credits available to cooperatives, and there is little immediate prospect for improvement in this regard except through the proposed loan. As previously stated, the savings and loan and credit union movements have demonstrated that Ecuadoreans of limited means can and will save for their self-improvement. Thousands of such Ecuadoreans have joined, and have placed their faith in, the cooperative movement as a means for seeking economic and social improvements for themselves and their families. As projected in Annex V and Annex VI, the Intensive Review Committee believes that by the fourth year of the Bank's operations, it will be strong enough to commence self-financing loans from surplus representing share purchases or direct saving deposits by the cooperative members who own the Bank.

D. Management of the Bank

Since December 1963, a promotion and organizing committee, including cooperative leaders, members of the USAID staff, and the third ranking officer of the Ministry of Commerce and Banking, have:

Reviewed the Lawrence feasibility study;
Obtained indications of interest from many of the leading Ecuadorian cooperatives and credit unions;
Helped prepare the loan application submitted to AID;
Drafted the proposed by-laws of the new Bank;
Assisted in the drafting of the decree establishing a Cooperative Bank;
and are now in process of obtaining share subscription commitments from existing cooperatives.

This committee will complete its task and be dissolved after the Loan Agreement is signed. The committee will be succeeded by a permanent Board of Directors consisting of seven voting members and one non-voting member. According to the Cooperative Bank Law amendment now being prepared, the following will constitute the Board of Directors: (Annex III)

(a) A representative from the artisan cooperatives.

(b) A representative from the agricultural cooperatives.

(c) A representative from the credit union cooperatives.

(d) An industrial engineer.

(e) A financial representative nominated by the Ecuadorean Monetary Board.

(f) A financial representative nominated by the Comisión de Valores.

(g) A private Ecuadorian banker.

(h) Until 70% of the loan principal is repaid, AID will have the right to send one observer to all Board meetings. [illegible] have a voice but not a vote, for all [illegible].

In order to create a national character for the new credit institution, no more than two members of the Board, nor more than two of the alternates, may be named from any one province of Ecuador. Staggered terms of two years each have been set, together with the right of a member to be re-elected one time. The Board will meet once every two months, or more often if required due to special circumstances. The Intensive Review Committee considers that the Board members will include high quality experienced financial advisors, an engineer, and good diversified representation from the national cooperative movement.

An annual meeting, or more often if required, will be held which will include representatives of every shareholding cooperative in Ecuador. Such a meeting will also be held prior to the official opening of the Ecuadorean Cooperative Bank.

The Credit Committee will consist of the following members:

(a) The Bank General Manager.

(b) The Industrial Engineer on the Board of Directors.

(c) One cooperative member on the Board of Directors.

(d) One financial member on the Board of Directors.

(e) For a period of five years from the day that the bank commences operation, or until all AID loan funds are disbursed a contract U.S. Cooperative Bank Advisor approved by AID or another representative appointed by AID.

The Intensive Review Committee considers that this will constitute a strong and sound Credit Committee.

In order to keep operating expenses at a minimum and to obviate high initial operating costs, it is anticipated that the Bank, until increased business so warrants, will commence operations with a small staff consisting of three officers, a bilingual secretary, and a porter-messenger. To simplify the task of this small group, the USAID has, through grant funds, provided modern office equipment and electrical accounting machinery. In addition, the USAID is funding a two-year Cooperative Bank Advisor who will have a contract directly with the Ecuadorian Cooperative Bank.

Adequate job descriptions for each of the officers have been provided in a supplemental report prepared by Mr. Lawrence. These include additional future staff. Besides the aforementioned three officer personnel (a General Manager, a Deputy Manager-Credit Analyst, and an Accountant-Bookkeeper on a retainer basis), the Bank will utilize the services of a Legal Counsel and an Engineer. When and if warranted, a permanent engineer and legal counsel will be added to the staff.

In addition to providing free office space, the Comisión de Valores will make available members of its technical staff on an as needed and as required basis for a period of three years. This will include the services of the foreign industrial engineer presently engaged by the Comisión de Valores.

Although his nomination is subject to final approval by the still non-existent Board of Directors, the General Manager tentatively selected has excellent qualifications for the position. He is forty-three years of age, and after completion of twelve years of primary and secondary school received a doctorate in economics through attendance at Central University. In addition, he has completed one and one-half years of post-graduate work in finance in the United States. He is fluent in both English and Spanish. Several of the responsible positions which he has already held are: Chief Statistician at the Ministry of Commerce and Banking for six years; Chief of the Statistics Department of the Central Bank of Ecuador for three years; Chief of the Import Department of the Bank for three years; and Financial and Audit Assistant of the USAID Financial Advisor from 1958 to 1960. During this period with the USAID Financial Advisor, he helped develop the application forms utilized for all types of credit by the National Development Bank and its branches, worked on the procedures for conducting audits and examinations of PL-480 loans, and actually directed the auditing of over 250 agricultural and industrial loans made by the National Development Bank totaling over $1 million. This person has also been among those involved in studying the problems connected with the operations and proposed reorganization of the National Development Bank. The proposed General Manager has also had experience in personnel administration and developing the decree and the by-laws of the Ecuadorian Housing Bank. Members of the Intensive Review Committee interviewed the proposed candidate and found him fully acceptable. Until 70% of the loan principal is repaid, AID will recommend that it have the right to approve any General Manager who may be selected.

To further strengthen the capacity of the proposed Cooperative Bank General Manager, the USAID has provided him with a two-month training participantship which includes working with four different cooperative banks in San Juan, Baltimore, New Orleans, and Bogotá. At two of these banks, he will spend an intensive training period of three weeks each; the training will be completed at the end of June.

It has been agreed that no branches would be opened in the near future as this would require additional staff and higher operating expenses. Until 70% of the loan principal has been repaid, AID should reserve the right to approve the opening of any proposed branch.

E. Operations of the Bank

The Lawrence report supports an Ecuadorian Cooperative Bank which will make loans to capital-producing cooperatives including agricultural, fishing, artisan, industrial, and transportation cooperatives. The report additionally supports assistance by the Bank to credit unions.

The Bank organizing and promotion committee and the Ministry of Commerce and Banking, after meetings with AID officials, define all types of cooperatives and credit unions as eligible except as follows:

(a) Housing cooperatives, as these cooperatives should remain as a function of the Ecuadorian Housing Bank.

(b) Transportation cooperatives, unless vehicles are actually owned by the cooperative and profits shared on an equitable basis among the members. The typical transportation cooperative in Ecuador, whereby individual drivers own their own vehicles and perhaps several vehicles, is not considered a true cooperative and therefore ineligible.

(c) Rural electrification cooperatives will generally require large sums of money in the $500, 000 to $1, 000, 000 range; therefore, at this initial stage of the Ecuadorian Cooperative Bank development they will be excluded. However, both the Bank and AID reserve the right to reconsider such a position after the Ecuadorian Cooperative Bank has demonstrated successful operations and the ability to service loans of this magnitude.

(d) Only soundly conceived and relatively strong cooperatives will be accepted for membership by the Board of Directors of the Ecuadorian Cooperative Bank. The [illegible] over 70% of the Ecuadorian cooperatives which are deemed weak will be required to strengthen their management and local organization before receiving favorable consideration for membership in the Bank. Naturally, the existence of the Bank with available loan funds will be an incentive to bring about such reforms.

Ecuadorian Law limits the amount of money which any individual cooperative may borrow to 10% of the Bank's capitalization, except for agricultural or industrial machinery loan limits which may reach 15%. In Ecuador, as in most other Latin American countries, it is today impossible for most cooperatives to borrow from private commercial banks. If it were possible, such loans would be on a short-term bases of from six months to three years at interest rates of from 15% to 18%. Therefore, the need is apparent for a special bank which makes both short and long term loans available only to cooperative organizations. The Bank will be 100% in private hands, fully owned by its member cooperatives and credit unions.

Although the Intensive Review Committee recommends that the Loan Agreement be so drawn as to permit sub-loans at up to 10% interest per annum, the Committee supports the present Ecuadorian plans to make loans at interest rates of 7% per annum plus 2.5% per annum in capital stock subscriptions on any outstanding balance. Stock subscriptions will be used as the primary initial method of building up the capitalization and lending ability of the Bank. Interest payments will build up reserves, cover operating expenses, and eventually also add to the Bank's capitalization and additional lending capacity. As a condition precedent and to insure sound fiscal management, we suggest that AID reserve the right to approve any proposed dividend distribution to stockholders until 70% of the AID loan principal has been repaid. Credit unions will be permitted to re-loan the money which they receive at 1% per month on the unpaid balances, as per their current standards.

In the interest of avoiding any misunderstandings and of ensuring sound financial operations, the Committee would propose that the permanent Board of Directors issue clear sub-loan guidelines, subject to subsequent AID approval.

Except for two-year working capital loans, which might include a six-month grace period, and up to one-year inventory loans, the Committee does not agree with the Lawrence feasibility study recommendation of unsecured loans. (in his second supplemental report, however, Mr. Lawrence modified this recommendation.) Eligible working capital requirements are defined as including raw materials, marketing costs, etcetera, but not daily operating expenses such as wages, rent, power, and fuel. Finished inventory would be eligible for loans of up to one year at a maximum of 75% of value. Regarding longer-term building, machinery, and miscellaneous equipment loans, a term of up to ten years including up to three years grace is the proposed acceptable norm. Security might include the building, machinery, etcetera, which is to be procured, as well as perhaps real estate or other assets as supplemental collateral. The USAID has informed the Committee and Ministry that AID would not agree to the financing of land purchases with its loan funds. Furthermore, on any long-term loans which exceed $10,000, the Committee believes that the loan should not exceed 80% of the value of the goods and services being procured unless reasonable additional collateral is offered.

On August 31, 1968, Mr. Lawrence prepared and submitted to the USAID and to the promotion and organizing committee a second supplementary report which includes a two-page application form, a credit report form, and a cooperative bank loan agreement form. These three documents have been examined by the proposed General Manager and the USAID Intensive Review Committee. While generally sound and certainly the basis for preparing such forms, it is the opinion of all concerned that they still require some minor modifications to fit Ecuadorian conditions. Upon return from his participant trainingship, the proposed General Manager intends to modify these three forms based on his training at three American and one Latin American cooperative bank, together with his experience and understanding of existing Ecuadorian credit formulas and conditions. The forms he develops will then be subject to the approval of the permanent Board of Directors and AID.

When a loan application is submitted to the Bank, it will be reviewed by the Bank officers for financial and technical soundness, completeness of information, and the collateral involved. A determination if the proposed loan is in accordance with the purpose of the particular cooperative involved will also need to be examined. Depending on the size of the loan and the nature of the loan application, a field examination may or may not be necessary. The credit report will be submitted to the Loan Cor ittee as described in Section D of this Loan Paper. If its decision favorable, a standard Loan Agreement setting forth the terms of the particular loan involved will be prepared and submitted to the Legal Counsel for approval. Advances to cooperatives under the Loan Agreement will be made through dollar letters of credit established at a U. S. bank, from Title IV P. L. 480 Funds agreed by the GOE and the USAID for use for this purpose, through P. L. 480 sucre repayment accounts on deposit at a bank in Ecuador, and sucre advances totaling about 60-day requirements which will have been received on a revolving fund basis by the Ecuadorian Cooperative Bank through the new standard Letter of Credit procedure whereby AID loan dollars are converted to sucres through the Central Bank of Ecuador.

The General Manager will be responsible for developing sound standard procedures to implement, monitor, and, if necessary, cancel such loansas the bank will have authorized. AID will approve these procedures prior to the Bank's making any disbursements.

In Ecuador, it is customary in many public and private institutions to appoint an honorary Vigilance Committee who are neither officers of the Bank or members of the Board of Directors. Their function in this case will be to determine that the Bank is well managed. They are encouraged to suggest that the General Manager and his staff take corrective actions or simplify procedures where this may be applicable or necessary. While such a committee is not listed in either the Lawrence feasibility study or the formal loan application, it is under consideration and would be encouraged by AID since it is a sound and traditional Ecuadorian practise. The Vigilance Committee would be elected by shareholding members.

Neither the Lawrence Feasibility Study nor the loan application have made provision for adequate independent audits by an independent accounting firm. Therefore, it is suggested that such language be incorporated into the AID loan agreement.

The Bank will be subject to the normal reviews, audits, and regulations of the Ecuadorian Superintendent of Banking under the Ministry of Commerce and Banking. Although some liberalized conditions have been accorded to the Ecuadorian Cooperative Bank by decree, it is expected that they will follow normal sound banking practices.

The Ministry of Commerce and Banking will arrange for a Government of Ecuador guaranty of the AID loan to the Ecuadorian Cooperative Bank. However, except for the normal supervision of the Superintendent of Banking, the Minister of Commerce and Banking and members of his staff have made it clear that they firmly believe that the GOE should not intervene in this Bank except in providing organizational assistance in the formation period and in the initial three or four month's period of operation of the Bank. However, to further strengthen the Bank, they are providing outright grants of $16,500 per year for three years, as well as free office space within the Comision de Valores building.

F - Financial Analysis

1. Source of Financing

(a) Initial Capitalization

Shareholders (Minimum required)	$ 55,000
GOE Grant in Cash	$ 16,500
AID Grant for Equipment, Auto, etc.	$ 10,000
	$ 81,500

(b) During the Sept. 1964 - December 1966 Period

Shareholders (Estimated) Addl. Contribution	$ 145,000
GOE Grant in Cash Addl. Contribution	$ 33,000
GOE Title IV PL 480 Loan	$ 110,000
GOE Donation of Office space & Util.	$ 9,500
AID Grant for 2 Yr. Coop. Bank Advisor	$ 50,000
AID Loan	1,200,000
	$ 1,547,500

(c) In addition to the above, individual cooperatives will be required to make from 20% to 50% contribution on individual sub-loans. Assuming an average of 30%, this would amount to $375,000.

(d) Summary Totals

AID Loan	$ 1,200,000 or 60%
AID Grants	60,000 or 3%
GOE Grants	59,000 or 3%
GOE Loan	110,000 or 5%
Cooperatives	575,000 or 29%
TOTAL PROJECT	$ 2,004,000

2. Interest Rates, Subsidies and Financial Soundness

With any new credit institution, particularly in an underdeveloped country, the danger period is the first few years. If the loan level anticipated in the Feasibility Study can be reached (and we believe it is a reasonable and acceptable indication of demand), the Bank will be a success from the very first year because of the liberal spread of 6.25% between the AID and GOE loan terms of .075% and the 7% interest being charged the cooperative sub-borrowers. The GOE will guaranty the loan; but it has indicated that it desires no commission for this service as its prime objective is the development of a sound cooperative bank in Ecuador. The GOE is going a step further by providing cash grants of $16,500 per year for three years, plus free office space and utilities for this same period, in order to assist in covering operating expenses in the initial period when income will be low.

The Intensive Review Committee was aware of the usual AID policy to include technical assistance costs within a loan. However, it is recommending AID instead accept the USAID grant funding commitment for a two-year $50,000 Cooperative Bank Advisor contract as an indirect subsidy to the Bank during its initial period of operation. This Advisor, together with the $10,000 in equipment provided to the Bank by the USAID with FY 64 grant funds and the GOE grants, will enable the Bank to commence operations with only normal income and expenditure items on its books rather than being handicapped with the usual heavy one-time expenses required to start operations. Since our objective is to create a sound new permanent credit institution that will stimulate the growth of the private cooperative movement in Ecuador, we believe that these relatively small AID and GOE subsidies to ease the Bank's burden during its infancy period, are fully justified.

The AID interest terms of .75% for ten years with a ten-year grace period on repayment of capital also serve the same purpose of easing the burden during the early and formative stage. After ten years, neither a 2% interest charge nor repayment of the AID loan principal over 15 years should be difficult, as by then, the Bank is expected to have built up adequate reserves. Since a two-step procedure will be offered to the GOE, [illegible] the option of repaying over a 30-year period after a ten-year grace period [illegible], the additional debt-servicing burden should not be a hardship.

The GOE is loaning $[illegible] of Title IV PL 480 proceeds to the Bank at the original AID terms without any surcharge. These terms are .75% interest for [illegible] years, including a two-year grace period on repayment of principal. The small $[illegible] annual repayment of capital commencing in 19[illegible], will place no hardship on the Bank.

The Annex V and VI financial statements demonstrate the strong self-sufficient growth of the Bank which should permit some financing from indigenous resources commencing in the fourth year. This is greatly assisted by the required 2.5% purchase of additional shares whenever the regular 7% interest payment is made. Eventually, the national Ecuadorian cooperative movement, through the Bank which it owns 100%, will be self-financing a major portion of its own needs. By about the tenth year, subject to AID approval, it is anticipated that the Bank may be paying its shareholders dividends from earned surplus or perhaps reduce the additional share purchase per centage requirement.

During the third through sixth years, additional AID loans totalling about $3.7 million, less such GOE PL 480 Title IV loans as may be available at that time, are expected to be requested and are covered in both the Feasibility Study and the financial annexes to this paper.

Ten year industrial and agricultural 8% sub-loans are available from the Comisión de Valores, the National Development Bank, and private commercial banks through major Alliance for Progress loans made to the Government of Ecuador by AID and the Inter-American Development Bank. The standards for these loans, except for small-handicraft and artisan loans of less than $10,000, are not geared to most cooperative needs and exclude credit unions. Private commercial banks with their own reso[illegible]es offer short-term six month to three year suppliers credit and wor[illegible] capital at interest rates to most borrowers of from 15% to 18% per a[illegible]um. A prime ma[illegible]ndustrialist can sometimes obtain short term credit at [illegible]%, but it is d[illegible]ul that any Ecuadorian cooperative or credit union could qualify as a p[illegible]e risk or even as a normal risk. Housing loans through the Social Security system, the Housing Bank, and private savings and loan associations range from 7% to 9%, for about twenty-five years, and generally require about a 20% down payment. Private banks offer 10% to 11% building loans for a period of seven to ten years if a 50% down payment has been made.

The cooperatives eligible to borrow from the Bank, are also its 100% equity shareholders. Because the initial operating period is regarded as the Bank's most difficult one, consideration was given to commencing with an interest rate of higher than 7%. Although this was rejected by the GOE and Organizing Committee, the feasibility study recommendation of requiring a 1.4% additional paid-up share purchase with every interest payment was raised to 2.5%. Besides strengthening the Bank and making it less dependent on future loans, it is anticipated that the shareholders, by the end of the sixth year, will thus have an earned surplus equal to or greater than their paid-in purchases; in other words, the shares may be worth double their original value if the Annex V projections develop as predicted.

To protect its interest and insure sound Bank fiscal policy, AID should reserve the right to approve any proposed dividend or patronage refund and change in either interest rate or the 2.5% additional paid-up share purchase until 70% of the AID loan principal is repaid.

3. Maturity Dates

The AID loan will mature in forty years and not require repayment of any principal for the first ten years. The Cooperative Bank will make long term loans for ten years and also some short-term working capital and inventory loans for periods of one to three years. Thus, the Cooperative Bank sub-loan repayments will commence and continue quite regularly from about the third year. The Intensive Review Committee has no objection to the Bank utilizing the funds as is permitted in the AID industrial credit loan to the Comisión de Valores.

4. Exchange Risk

Ecuador is the only country in Latin America which has had a free market currency appreciation in relation to the dollar during the past two years. The amount has been about 20%. During this period, the official rate of exchange has remained steady at 18.18 to the dollar. At this time, the official rate appears secure. However, it might change for one of two reasons:

(a) A major internal inflation. This is deemed unlikely because of the strict Central Bank of Ecuador fiscal policies and the fact that the cost of living index in Ecuador is increasing at about the same pace as in the United States.

(b) There is always the possibility that the Central Bank of Ecuador may desire to unify the official and free rates by eliminating the former. This might be expected to cause a minor depreciation of perhaps about 5% to 10%.

The Government of Ecuador has agreed to guaranty the exchange risk differential providing the Cooperative Bank sets up a reserve contingency consisting of 1% per annum and within the interest charges collected by the Bank. This portion of the 7% interest collected would be deposited in 8% government bonds to further augment the reserve account. Eventually, the reserve will be sufficiently large, say after it reaches 20% of the outstanding dollar portion of the AID loan, to warrant not being further increased except for the 8% bond interest collected. This same reserve fund, eventually can double as a reserve to repay the AID loan principal and might be utilized partially for this purpose.

The exchange risk will be lessened by whatever portion of the AID loan authorization covers sucres available from GOE repayments of prior and other development loan and PL 480 sucre obligations which are being deposited in a sucre account.

5. Analysis of Financial Statements

Annexes V and VI are a Balance Sheet and Income Statement prepared by a member of the Intensive Review Committee. They may be compared with the feasibility study statements which are shown as Annexes VII and VIII. Relevant footnotes are explained in Annex IX. We are satisfied that the Bank can become as successful as projected, subject only to its being able to efficiently process and make loans. This has been a major bottleneck in other new Ecuadorian credit institutions. To overcome this potential danger, the USAID has already taken the following corrective steps based on the unsuccessful or slow experiences of other Ecuadorian credit agencies:

(a) Management - Has been given reasonable assurance that a strong, non-political diversified Board of Directors will be selected. Participated in the selection of the well-qualified General Manager and sent him on a training participantship in advance of the Bank opening.

(b) Borrowers - Is continuing to give extensive technical assistan to the potential cooperative sub-borrowers in order that sound loa applications can be filed shortly after the Bank opens. A Shareholders Annual Meeting, which will include promotional activities, will be held before the Bank is formally opened.

(c) Application Forms and Assistance in Processing - Through both the U. S. Credit Bank Advisor and the General Manager, from the beginning of this project even before the doors are formally opened, the fostering of the spirit to encourage and meet with sound loan applicants and to actively assist them in presenting their applications will be followed. A simplified application form, consistent with reasonable standards modified to Ecuadorian conditions, is being developed.

The debt-equity ratio will be about 5 to 1 after the first year of operation it will decline to about 6 to 1 three years after the Bank has commenced operations and at the end of the period of the first AID loan. Thereafter, it will strengthen and should reach 3 to 1 by the sixth year or at the end of the period of the final anticipated A.I.D. development loan. While the debt-equity ratio during the initial period is not as strong as normally desired by AID, it must be recognized that this Bank is being started by small private cooperatives with limited means rather than by wealthy families or the government. In spite of this, the financial arrangements that have been planned and outlined should result in reaching the desired AID standard within a reasonable period of six years.

Government subsidies will be eliminated after three years. Development loans are planned for discontinuation after six years. The beginning of some self-financed loans are planned commencing in the fourth year. The strength of this Bank, and the anticipated source of most of its long-range financing, is the continued and increasing shares that will be purchased by its member borrowers at the same time they are paying loan interest and repaying principal.

The exemption of the Bank from all federal and municipal taxes is an important indirect government assist in keeping expenses to a minimum.

While the Intensive Review Committee is fully aware of the difficulties in starting any new credit institution, particularly in Ecuador, we believe that this first AID supported Cooperative Bank in Latin America and perhaps anywhere in the world, has been conceived without haste on a sound financial basis and will succeed. The Bank funding meets the criteria of Section 601 of the FAA, Encouragement of Free Enterprise.

G. Repayment Prospect and Loan Agreement Terms

The Intensive Review Committee believes that this loan can and will be repaid and that the requirements of Section 611 of the Foreign Assistance Act have been met.

It is recommended that the loan be made directly to the Cooperative Bank. The Loan Agreement should be formally accepted by its permanent Board of Directors and then signed by the President of the Board. We believe that the Central Bank of Ecuador should be a party to the Loan Agreement inasmuch as the Special Letter of Credit procedure involving the conversion of dollars to sucres is involved. It is recommended that the two-step procedure be utilized even though it is not requested by the Government of Ecuador, which has waived any two-step commission fees. The two-step procedure provides the GOE with an option to ease Ecuador's total debt-servicing burden. We also recommend that the Minister of Finance and the Minister of Commerce and Banking sign a Guaranty Agreement at the same time the ceremony of the Loan Agreement takes place. A twenty-five year loan to the Borrower with a ten-year grace period on repayment of principal, with interest of .75% during the first ten years and 2% interest thereafter, is recommended. The GOE terms would be identical except that they will go to forty years.

H. Impact on U.S. Economy

All local cost financing required under this loan will be accomplished through the Special Letter of Credit procedure utilized between AID and the Central Bank of Ecuador on other AID loans to insure that the dollars provided by AID are utilized for procurement in the United States.

The spirit of Section 215 of the Foreign Assistance Act encourages local currency financing for this type of loan. Nevertheless, it is anticipated that about 25% of the AID loan, or about $300,000, will be utilized for imports from the United States.

I. Implementation Plan

The Cooperative Bank law has already been issued. An amendment in draft form has been prepared and can be expected to be issued during June 1964.

A tentative General Manager has been selected subject to final approval by the Board of Directors. He will complete an intensive two month training participantship in June 1964.

As soon as word is received that the requested AID loan has been authorized, actions necessary to promptly select a permanent Board of Directors and dissolve the Organization and Promotion Committee will be commenced as well as the announcement to convene a national meeting of cooperatives and credit unions. Assuming the AID loan is authorized in June 1964, completion of the Board selection can be expected by mid-July 1964, and a national cooperative movement convention during late July 1964. The convention would be the ideal time to formally sign the Loan Agreement.

Share subscription pledges from over 20 cooperatives have already been received and more can be expected as soon as the AID loan authorization is announced. The Board of Directors can authorize the actual commencement of collecting the cash for the shares commencing with the national convention. By mid-August 1964, it can reasonable be expected that at least 50 sound and acceptable cooperatives will have deposited the minimum $55,000 required under the Loan Agreement, and that, the Government will have deposited its $16,500 pledge.

The contractual Cooperative Bank Advisor is already under recruitment and two candidates have been suggested. The arrival of the Advisor selected should be no later than August 1964, preferably a month earlier.

The General Manager should select and hire the balance of his staff during August 1964, subject to approval by the Board of Directors. Advance administrative preparations and the printing of stationery and forms should commence in August. Loan applications should be accepted prior to the Bank opening, but not processed. The USAID grant-furnished equipment is already on order and should have arrived by August.

If the above preparations can proceed as planned, the Bank should be able to formally commence operations by about mid-September 1964, with appropriate ceremonies and publicity for this first Alliance for Progress-supported cooperative bank in Latin America.

The anticipated growth of the Bank has been outlined in Annex V.

As set forth in Section K and other parts of this Loan Paper, AID will reserve the right to certain specific approvals until 70% of the loan principal is repaid. These include selection of the General Manager, the right to approve any loan which exceeds $50,000 during the first twelve months of the Bank's operations and any loan which exceeds $100,000 thereafter, etcetera. The Cooperative Credit Advisor or any other AID-selected representative will be a member of the Credit Committee for a period of five years or until the first (and perhaps second) AID loan is fully disbursed, with the right to veto any unacceptable loan during this period. AID will also have the right to appoint a non-voting member with voice to attend the meetings of the Board of Directors until 70% of the AID loan principal is repaid.

The USAID will assign monitoring responsibilities in accordance with the special requirements of this project.

J. Issues

1. A major issue in this loan is the absence of adequate equity capitalization of the Institution, particularly in the initial stage. This has been recognized by the Intensive Review Committee and in the LA/CAEC review of the IRR report.

During its negotiations with the GOE and cooperative leaders, the USAID did succeed in arranging for a higher required paid-in share purchase of 2.5%; with each 7% interest payment, this makes a total payment of 9.5%.

We also obtained a GOE guaranty of the AID principal and interest payments including M.O.V. A GOE grant contribution of $49,500, which is not too large, was substituted for the previous offer of a $16,500 GOE loan. However, neither the GOE nor the cooperative movement had the resources available to make a larger initial capitalization contribution.

As explained elsewhere in this paper, this will result in a higher debt-equity ratio, for a period of about five or six years, than is normally considered desireable.

Despite the inability to obtain an adequate equity capitalization, we still recommend acceptance of the loan as it appears that a satisfactory debt-equity ratio will be reached during the sixth or seventh year. Furthermore, the AID and congressional interest in developing the cooperative movements in Latin America, including sources of financing through new private non-government Cooperative Banks, will require the willingness to accept higher risks than would normally be desireable. Liberal terms were also given during the early days of the U. S. cooperative movement.

2. Generally, [illegible] the best of the knowledge of the Intensive Review Committee, the [illegible] interest spread given to a credit institution by AID is about [illegible] Discounting the 1% maintenance of value account (as this would normally be part of an allowable government risk and profit), the interest spread is 5.25% for the first ten years. Based on our analysis of the balance sheet and income statements, as well as knowledge of the obvious difficult and dangerous infancy period, we support such a high spread resulting from the low AID interest of .75% for a period of ten years. The Intensive Review Committee, however, does not believe that a forty year loan to the Borrower is either necessary or desireable and instead recommends only twenty-five years, the last fifteen years at 2% interest; thus, the spread during the last fifteen years would be 4%.

3. The financial projections made in this paper assumed a lending level of the Bank which we believe is consistent with potential demand. Should the Bank fail to reach this loan level, for whatever reason, net income will drop while expenses will remain fixed. The result would be to reduce the projected surplus and a longer period before the Bank becomes self-sufficient.

K. Conditions and Covenants

1. The Loan proceeds may be utilized to finance:

(a) Equipment or goods whose source and origin is the United States or Ecuador, including their installation.

(b) Buildings and construction which can be considered permanent capitalization.

(c) Working Capital requirements including raw materials, marketing and distribution costs, etcetera, but excluding daily operating expenses such as salaries, fuel, utilities, etcetera.

(d) Inventory loans.

2. Sub-Loan Terms

(a) Loans made for the purposes of 1(a) or 1(b) above may be made for a period of up to ten years, including up to three years grace period on repayment of principal.

(b) Working capital loans described in 1(c) above may be made for a period of up to two years, including up to six months grace period on repayment of principal. No more than 50% of the allowable working capital requirements may be financed.

(c) Inventory loans described in 1(d) above may be made for a period of up to one year. No more than 50% inventory cost value may be considered eligible for a loan.

(d) Credit union loans may be made for a period of up to five years, with up to one year grace on repayment of principal. The individual credit union must demonstrate that it is making at least 50% of its loans with its own deposit resources.

(e) Loans of up to $10,000 need not be secured. Loans in excess of $10,000 will require acceptable collateral and at least a minimum 20% cooperative local contribution.

(f) Subject to AID approval of standards adopted by the Board of Directors to insure against misuse, loans may be refinanced one time for a period not to exceed over one-half of the time periods indicated above.

3. It will be necessary for a minimum of 25% of the total loan proceeds to be utilized for ~~the importation of~~ American equipment or goods.

4. A two-year, Spanish speaking, AID grant-funded Cooperative Bank Advisor will sign a contract with the President of the Bank Board of Directors. At the end of the contract, and until such time as the AID loan funds are fully disbursed, AID reserves the right to require continuation of this type of technical assistance, if it feels such technical assistance is still necessary. If and when such additional funding may be required, it may come from a grant, this loan, or the Bank's own resources, as deemed most appropriate.

5. The Cooperative Bank Credit Advisor, or other AID-appointed representative, will be a member of the Credit Committee with the right to veto any application for a period of five years or until the AID loan funds under this loan, and perhaps a second AID loan, are fully disbursed.

6. During the first twelve months of the Bank's operations, AID will approve any loan which exceeds $50,000. Thereafter, until all AID loan funds are disbursed, AID will approve any loan in excess of $100,000.

7. Housing cooperatives will not be eligible for financing by the Cooperative Bank. Until AID approval is given, rural electric cooperatives will also be ineligible except in those instances where their total loan requirements do not exceed $100,000. Weak cooperatives with poor management or questionable financial promise will not be financed by the Cooperative Bank or considered for a shareholder membership.

8. Up to sixty day estimated loan requirements of the Bank will be drawn through the Special Letter of Credit procedure, including shelf items of U. S. source and origin which may be procured up to a limit of $5,000 per sub-loan. Dollar letters of credit for American imports will generally be drawn in tranches of $150,000.

9. Prior to the disbursement of any funds under the Loan Agreement, conditions precedent must have been met to the satisfaction of AID, including the following:

(a) Ratification of the Loan Agreement by the Bank Board of Directors and the opinion of a legal counsel acceptable to AID that the Loan Agreement is binding.

(b) Ratification of the Guaranty Agreement signed by the Minister of Finance and the Minister of Commerce and Banking in a manner prescribed by AID and the opinion of a legal counsel acceptable to AID that the Guaranty Agreement is binding.

(c) A minimum 1 million sucres ($55,000) of paid-in capital on deposit plus the first GOE contribution of 300,000 sucres ($16,500).

(d) Acknowledgement in writing from the Minister of Commerce and Banking that he will arrange for an additional contribution of 300,000 sucres ($16,500) before June 1965 and again before June 1966. He should also guaranty the provision of acceptable office space and utility service for the Cooperative Bank at no cost to the Bank through December 1966, the anticipated period of the first AID loan.

(e) Approval by the Bank Board of Directors of loan application forms, credit report forms, sample loan agreement forms for different types of loans, which had been approved by AID.

10. Disbursements may not be continued if the debt-equity ratio at any time exceeds 6 to 1.

11. The first 1% of any interest payments collected by the Bank will be deposited in 8% or higher GOE bonds or other securities and held aside, together with the bond interest collected, as a maintenance of value asset reserve account. After this account reaches 20% of the AID loan principal outstanding, only collected bond interest need continue to be added to the account. The mechanics of operating this system will need to be approved by the Bank Board of Directors, the Minister of Commerce and Banking, acting as a guarantor of the loan, and AID.

12. Independent annual audits covering financial statements and an appraisal of the Bank's operations will be prepared at least once per year. These annual audits and any other audits of the Bank will be made available to AID on a confidential basis for internal U. S. Government usage until the full loan principal has been repaid.

13. Until 70% of the loan principal has been repaid, AID reserves the right to:

(a) Appoint an observor to attend all meetings of the Board of Directors.

(b) The right to veto, within a period of one month, any General Manager selected by the Bank Board of Directors, if his qualifications and/or fitness for the position do not appear to be adequate.

(c) Right to approve any change in the interest rate, or in the additional paid-in capital requirement, or in a dividend (patronage fund), prior to a public announcement.

(d) Right to approve any major organizational change, the opening of any branch, or the hiring of additional staff members.

(e) Right to approve any change in the by-laws or a national decree specifically affecting only the Cooperative Bank, pric[illegible]o enactment. (This is not meant to include a general change in the [illegible]ional banking laws affecting all banks).

COOPERATIVES IN ECUADOR

as of September, 1963

	NUMBER	MEMBERSHIP	CAPITAL (in sucres)
Agricultural:			
- Production	225	10,250	10,000,000
- Marketing	115	5,000	4,500,000
- Livestock	15	550	7,000,000
- Colonization	15	600	1,600,000
- Fruits	2	220	25,000
- Irrigation	2	280	10,000
- Poultry	2	40	40,000
- Forestry	1	15	1,500
Total Agricultural	375	18,000	23,800,500
- Housing	135	8,500	15,000,000
- Transportation	160	4,000	5,500,000
- Credit Union	116	10,800	5.000,000
- Consumers	12	1,300	120,000
- Artisan	12	450	115,000
- Fishing	12	300	120,000
- Other	10	700	100,000
TOTAL	850	44,000	50,000,000

A DECREE ISSUED BY THE GOVERNMENT WHEREBY THE ESTABLISHMENT OF COOPERATIVE BANKS IS AUTHORIZED

Following is the text of a Supreme Decree whereby the establishment of Cooperative Banks, as private institutions with a social aim, is authorized:

No. 699

THE MILITARY GOVERNMENT BOARD,
By virtue of the powers vested in them,

Hereby Decrees:

The following Law authorizing the establishment of Cooperative Banks:

CHAPTER I

ESTABLISHMENT AND AIMS

Article 1. There is au ized the establishment of Cooperative Banks as private institutions with cial or public aim and with full legal status, which shall be governed by provisions in this Decree, the General Banking Law, and the Law on Cooperatives insofar as such provisions are not in opposition to the former, and by the Bylaws and Regulations to be issued by the Administrative Council with the prior report of the Superintendent of Banks and the authorization of the Ministry of Commerce and Banking.

The duration of the Cooperative Banks will be indefinite and they will be domiciled in the cities where they are established. They may establish Branch offices and Agencies in any other places in the Republic, at the option of the Administrative Council.

Article 2. The aims of the Cooperative Banks are as follows:

(a) To develop a policy aiming at the solution of the credit problem, at improving the working conditions and productive capacity, in order that the cooperatives which have now been established or to be established hereafter may efficiently achieve their objectives, such as to own an operating capital; to procure materials, machinery and equipment, tools, livestock and other items which are useful for agricultural exploitations, production and marketing, and the gathering of crops; to procure industrial equipment and materials, and to store agricultural products and manufactured articles.

(b) To promote and encourage the establishment of Savings and Loan Cooperatives, as well as Production, Consumption and Mixed Cooperatives.

CHAPTER II

CAPITAL AND STOCK

Article 3. The Cooperative Banks shall be established with a minimum capital of 1,000,000 sucres, divided into nominal shares, payable on demand, which may be transferred in the manner provided in the Law of Cooperatives. Such capital will be contributed as follows:

(a) By means of contribution certificates, subscribed and paid by the Members. Certificates for any number of shares may be issued.

The provisions in Articles 44 and 60 of the General Banking Law do not apply to the Cooperative Banks. They may begin their operation with an initial capital 1,000,000 sucres.

(b) A contribution from the Government of Ecuador in the amount of 300,000 sucres, which will be provided by the Development Credit System as a guarantee, until the respective capital is subscribed and paid.

(c) Domestic or foreign bequests and donations.

(d) Loans granted by domestic or foreign financial agencies.

(e) 20% of the Reserve Fund, which will be indefinitely included from the surplus of the Bank as a result of its operation.

(f) Any other regular or special revenues accruing to the Bank, other than those mentioned above.

Article 4. The Cooperative Banks may increase their capital at any time, subject only to the rules which are established for this purpose by their Bylaws and the Law on Cooperatives.

CHAPTER III

THE OPERATIONS

Article 5. The Cooperative Banks are empowered to perform all functions and operations for achieving their objectives, particularly:

(a) To grant short-, medium- and long-term loans to first, second and third degree Cooperatives which are trying to remedy the lack of adequate availabilities for their development and improvement.

(b) Operating capital, procurement of machinery, seeds, fertilizers, equipment, livestock and other items required for exploitation and gathering of crops, and the marketing of agricultural products.

(c) Procurement of machinery and industrial equipment, transportation equipment, raw materials, tools, and procurement, construction, conditioning and repairs of industrial buildings.

(d) Storage of products and manufactured articles.

(e) Purchasing from, and selling products to, their members.

(f) Establishing warehouses and stores.

(g) Obtaining funds by means of loans from domestic and foreign agencies and making other transactions permitted by law.

(h) Receiving savings and time deposits from the Cooperatives.

(i) To rediscount at the Central Bank the Collateral Portfolio by establishing a guarantee to the satisfaction of the Central Bank of Ecuador, for terms of up to five years.

(j) To act as trustees or depositories of funds owned by any domestic or foreign Cooperative.

(k) To issue guarantees in favor of their members.

(l) To purchase property or to receive same in payment of obligations, in such cases as may be deemed advisable by the Administrative Council.

(ll) To own, let, mortgage or process the title to their property.

Article 6. Loans granted by the Cooperative Bank to any one natural or legal person, as principal debtor, shall not be in excess of 10% of the capital and reserves of the Bank. Likewise, the loans granted for procurement of agricultural and industrial machinery shall not exceed 15% thereof, and shall be controlled by the Administrative Council; provided, however, that in no case shall a total direct loan granted to any one Cooperative be in excess of 15% of the capital and reserves of the Bank.

Article 7. The use of the loans granted shall be strictly controlled. The costs incurred in such control and prior review s' all be paid by the Bank.

CHAPTER IV

ORGANIZATION AND OPERATION

Article 8. The Cooperative Banks shall be managed by their General Meetings, whether regular or special; the by Board of Directors, the Supervisory Council, the General Manager and the Credit Commission, subject to the powers and duties establish for each by the law, the Bylaws and the Regulations.

Article 9. The regular or special General Meeting shall be composed of the member organizations who are registered as Shareholders of the Cooperative Banks, who are in the full exercise of their rights and who are not in default in meeting their obligations. One delegate of each hundred members, or fraction thereof shall be accepted, such members to be active members, who are registered in such organizations.

Article 10. Each Delegate shall be entitled to one vote at the General Meeting.

Article 11. The Administrative Counsil shall be composed of seven members who shall be elected by the General Meeting from among its members. If so required under the terms of a loan granted or guaranteed by domestic or foreign financial agencies, up to three members may be appointed to the Administrative Council by the said agencies, and such appointments will lapse as soon as the loan or guarantee under this provision is repaid by the Bank to the extent of over 70% of its amount.

Article 12. The Administrative Council shall elect, from among its members, a President, a Vice President and two members for the Credit Commission.

Article 13. The Administrative Council shall appoint the General Manager, the Assistant Manager, the Secretary and such other officials as may be required.

Article 14. The Supervisory Council shall be composed of three members elected by the General Meeting from among its members.

Article 15. The Credit Commission shall be composed of the General Manager and two members to be elected from among the members of the Administrative Council, who shall be responsible for reviewing and deciding upon the loan applications in accordance with the Law, the Bylaws and the Regulations.

Article 16. The Bylaws of the Cooperative Banks shall determine the duties, powers and responsibilities of the General Meeting, the Administrative and Supervisory Councils, the General Manager and other officials, and the Credit Commission.

CHAPTER V

PRIVILEGES

Article 17. The Cooperative Banks shall be exempted from payment of all Government taxes and assessments, as well as Municipal any other taxes, including payment of Government stamps and stamp paper, in connection with their establishment.

Article 18. Inasmuch as the Cooperative Banks are authorized by virtue of this Law, it will not be necessary to comply with the requirements determined by the General Banking Law for promotion of this kind of institutions.

CHAPTER VI

TRANSITORY PROVISIONS

Article 19. Upon promulgation of this Decree, organizing committees may be established, which will approve the subscription of capital, draw up the Bylaws of the Bank, which shall be recorded in a public deed with a prior report from the Superintendent of Banks and the authorization of the Ministry of Commerce and Banking, and entered in the Registered of the National Directorate of Cooperatives.

Article 20. All laws and regulations which, either expressly or by implication, are in opposition to this Decree, are hereby revoked.

Article 21. The Minister of Commerce and Banking is responsible for the enforcement of this Decree, which will become operative effective on the date of its promulgation.

Issued in Quito, on October 17, 1963.

(s) Ramón Castro Jijón, Rear Admiral; (s) General Luis Cabrera Sevilla;
(s) General Marcos Gándara Enríquez; (s) Colonel Guillermo Freile Posso;
(s) Enrique Amador Márquez, Minister of Commerce and Banking.

PROPOSED AMENDMENT TO THE LAW AND BY-LAWS OF THE COOPERATIVE BANKS

NOTE: This amendment was not finalized as of May 15, 1964.

One. For the proper development of the Ecuadorian Cooperative Bank, an annual grant of 300,000 sucres will be established during the first three years.

Two. The domestic and foreign loans for the development of the Cooperative Banks may be given a subsidiary guarantee by the Government.

Three A legal provision shall be established for protecting the stability of foreign exchange for the purpose of the loans granted. Such fund is to be constituted by 1% of the loans granted.

Four The Board of Directors the Ecuadorian Cooperative Bank shall be constituted by seven voting members, as follows:

(a) A representative from the artisan cooperatives.

(b) A representative from the agricultural cooperatives.

(c) A representative from the credit union cooperatives.

(d) An Industrial Engineer to be designated by the university engineering faculties.

(e) A representative to be designated by the Ecuadorian Monetary Board.

(f) A representative to be designated by the Comisión de Valores.

(g) A representative to be designated by the private Ecuadorian banks.

(h) International lending agencies will have a representative with voice but not vote until 70% of a loan principal is repaid.

These members will be designated by the respective Bodies of Electors, which will act in accordance with the regulations to be issued for this purpose by the Superintendent of Banks.

The members, both principal and alternate, shall serve during a period of two years and may be re-elected for one additional term.

The principal and alternate members shall be partially replaced, alternatively as 3 and 4.

Article 10 of the law shall be amended to the effect that a vote is given to each member, even though the delegates representing him are many.

The By-Laws should contain a provision whereby the Bank may not operate unless it has a minimum number of 50 Cooperatives, Credit Unions, Federations, or Confederations as Shareholding Associations.

Article 40 of the By-Laws sh[illegible] provide that the meetings of the Administrative Council shall be [illegible] nce every two months.

Article 48 of the By-Laws shall provide that the Credit Commission is to be composed of the Bank General Manager, three members of the Board of Directors, one of the latter to be an Industrial Engineer. A technician, acting for A. I. D., will be a member of the Credit Commission for a five year period from the date when the Bank begins to operate. The Chairman of this Commission shall be one of the members of the Administrative Council.

There may not be more than two representatives from any one Province on the Board of Directors.

NATIONAL ECONOMIC PLANNING AND COORDINATION BOARD

Letter No. 26095-DT

Quito, May 12, 1964

Mr. Ralph J. Apton
Development Loan Officer
USAID Mission
Quito

Dear Mr. Apton.

In reference to your kind letter of May 5, 1964, requesting that we state the final criteria of the Board on the loan application filed with USAID for financing the project for the establishment of the Cooperative Bank of Ecuador, I wish to state the following:

(1) The Planning Board in its initial program for cooperative development included in the General Plan for Economic and Social Development adopted, as an immediate and urgent measure, the programing of a Cooperative Credit Bank to provide a source to finance existing cooperatives.

Such programing was made on the basis of a report submitted to the National Planning Board by Dr. Douglas Lawrence, an expert in cooperative banks who worked for the USAID Cooperative Division last year.

The board accepted practically all of the suggestions made by Dr. Lawrence. While it raised a few objections to the regulations for the operation of the Cooperative Bank, it adopted the financial procedures proposed in the aforesaid report in its entirety.

(2) We understand that the Ministry of Commerce and Banking was the first agency to promote this project by changing the name to the Cooperative Bank of Ecuador; the establishment of this bank is probably being processed through the above named Ministry.

Unfortunately, the Planning Board has not been officially informed as to the details of the financing procedures set forth in the application to which you refer. For this reason, the Board can hardly be expected to refer to such details.

(3) At all events, since the Planning Board is particularly interested in the speedy establishment of an agency which will serve as a source of financing for the national cooperatives, I take the liberty to state that the official criteria of the Board as regards a loan application for capitalizing such agency, are the same as those set forth by Dr. Lawrence in his report, as well as those included in the initial program for cooperative development.

A copy of the report is on file with the Cooperative Division of USAID. However, if this copy should not be available for any reason, you may request the Planning Board to send you its own copy, which is not included now because it is the only one we have.

Trusting that the criteria stated in this letter may serve as basis for the purposes above referred to, I remain,

Very truly yours,

(s) Dr. Germánico Salgado
Technical Director

INTENSIVE REVIEW INCOME STATEMENT
(in thousands of dollars)

	Dec. 65 Year 1	Dec. 66 Year 2	Dec. 67 Year 3	Dec. 68 Year 4	Dec. 69 Year 5
INCOME					
7% Coop. Loans Interest	21	65	114	182	271
8% M.O.V. Govt. Bond Int. (b)		1	2	4	7
4% Plus Other Int. (c)	3	5	10	8	8
Grants (d)	43	16	-	-	-
Total Income	67	87	126	194	286
EXPENSES (f) (g)					
.075% AID Loan Int.	2	7	12	19	26
Bad Debt Losses	6	7	8	12	14
Salaries & Retainers	22	22	26	33	33
Rent, Utilities, Etc.	-	-	-	4	4
Other Oper. Expenses	6	6	8	8	8
Furn. & Equip.	-	-	-	2	3
Total Expenses	36	42	54	76	88
NET INCOME	31	35	72	118	198
Paid-In Shares Purchased	117	78	96	120	152
Self-Financed Loans	-	-	-	200	350

INTENSIVE REVIEW BALANCE SHEET
(in thousands dollars)

	Sep. 64 Beg.	Dec. 65 Year 1 (a)	Dec. 66 Year 2	Dec. 67 Year 3	Dec. 68 Year 4	Dec. 69 Year 5
ASSETS						
Cash Checking Account	11	25	39	50	52	52
M.O.V. Reserve in Govt. Bonds (b)	-	3	13	30	59	105
Savings Deposits, Etc. (c)	57	110	200	340	347	347
Loans to Cooperatives	-	600	1,250	2,000	3,200	4,550
(Less Bad Debt Reserve)	-	(6)	(12)	(20)	(32)	(45)
Furniture, Equip., & Autos	10	10	10	10	12	15
(Less Depriciation)	0	(1)	(2)	(3)	(4)	(6)
TOTAL ASSETS:	81	741	1,497	2,407	3,634	5,017
LIABILITIES						
AID Loan (a) (g)	-	600	1,250	2,000	3,000	4,000
SHAREHOLDERS EQUITY: (e)						
Memberships Paid-In Shares	55	110	165	220	275	330
Addl. Paid-In Shares	-	7	30	71	116	213
Earned Surplus	26	24	52	116	243	474
TOTAL LIABILITIES & EQUITY	81	741	1,497	2,407	3,634	5,017

FEASIBILITY STUDY INCOME STATEMENT
(in thousands of dollars)

	Year 1	Year 2	Year 3	Year 4	Year 5
INCOME					
7% Coop. Loan Int.	14	45	89	141	206
Other Income		4	3		8
Total INCOME	14	49	92	141	214
EXPENSES (f)					
.075% AID Loan Int.	4	7	13	18	25
Operating Expenses	50	50	30	30	30
(Less Subsidies)	(50)	(50)	-	-	-
Bad Debt Loosses	4	5	7	8	11
Total Expenses	8	12	50	56	66
NET INCOME	6	37	42	85	148

FEASIBILITY STUDY BALANCE SHEET
(in thousands of dollars)

	BEG. Year 1	END Year 1	END Year 2	END Year 3	END Year 4	END Year 5
ASSETS						
Cash Checking Account	500	113	164	231	259	267
Loans to Cooperatives		400	900	1,650	2,400	3,500
(Less Bad Debt Reserve)		(4)	(9)	(16)	(24)	(35)
Total Assets	500	509	1,055	1,864	2,635	3,732
LIABILITIES						
AID Loan (a)	500	500	1,000	1,750	2,407	3,314
CAPITAL AND SURPLUS (e)						
Equity Purchases (20% of Int.)		3	12	30	58	99
Equity From Refunds		5	32	64	128	239
Surplus ' 25% of Earnings		2	11	21	43	80
Total Liabilities & Capital	500	509	1,055	1,864	2,635	3,732

AID GRANT ASSISTANCE TO COOPERATIVES

(in thousands of dollars)

	FY 63	FY 64	Est. FY 65
U.S. Direct-Hire Coop. Advisors	-	96	51
National Farmers Union	18	-	-
CUNA Credit Union Contract	92	-	61
Cooperative Educator [illegible]v.	15	35	33
NRECA Rural Elect. Contract	23	59	47
Lawrence Coop. Bank Study	3	-	-
Coop. Bank Equipment	-	9	-
Santo Domingo Excess Prop. Equip.	-	75	-
Cooperative Participant Trng.	2	12	32
Commodities	25	15	13
Other Costs	46	47	30
TOTAL	224	348	267

FOOTNOTES ON STATEMENTS AND THEIR DIFFERENCES

(a) The initial Intensive Review Balance Cheet shows a period of one year and four months from September 1964 to December 1965 while the Feasibility Study Blance Sheet utilizes an undefined period of one year. Thus, the three year Feasibility Study AID loan of $1.75 million is comparable with the Intensive Review recommendation of a $2.0 million AID loan covering a period of three years and four months of operation.

(b) Maintenance of Value will be guaranteed by the Government of Ecuador at no cost. However, the Government is requiring the Bank to set up a reserve account equal to one-seventh of 1% of the 7% loan interest being collected. This Balance Sheet asset account will be invested in 8% government bonds; bond interest collected will be added to the reserve account as well as the income account of the profit and loss statement. This reserve account probably need not exceed 20% of the AID dollar loan principal outstanding and will make it easier for the Bank to repay the AID loan commencing with the eleventh year as the reserve account will be quite large by that time. This matter was not discussed in the Feasibility Study. It is anticipated that a portion of the AID loan will be in sucres, repayable in sucres.

(c) Although the actual practise will be adjusted to operating conditions that will be required by experience, it is anticipated that checking account balances will be maintained at about a $50,000 level and the balance of rapidly needed cash in 4% interest bearing bank savings accounts or higher interest bearing short term securities.

(d) Grants include a cash GOE contribution of $16,500 in 1964, 1965, and 1966 plus an AID grant for furniture, equipment, and an automobile in 1964. Both the 1964 and 1965 GOE payments are shown in the initial one year and four month period of the Bank's operations.

(e) The Feasibility Study Balance Sheet Shareholders Equity was not completely cleared and certain ground rules have been changed since issuance of the study. Therefore the Intensive Review Shareholders Equity shows the initial membership paid-in shares by the founding shareholders at the minimum required $55,000 and assumes that an even growth in new membership of $55,000 per annum will continue. (This makes $110,000 by the end of the first year.) The by-laws of the Bank and the first AID loan Implementation Letter will require the purchase of additional paid-in shares at the rate of 2.5% per annum of any outstanding cooperative loan balance. During at least the initial ten years of the Bank the earned surplus account will back-up the M. O. V. asset reserve account and be utilized for loans self-financed from the Bank's own resources. Eventually, shareholders will commence receiving refunds or dividends based on their paid-in shares.

(f) Based on more recent information available, the Intensive Review Committee feels its operating expenses, which are higher and broken down in more detail than those in the Feasibility Study, can be considered closer to actual anticipated operating expenses. Through December 1967, the GOE will provide free office space and utilities.

(g) Finalization of loan terms had not been completed at the time the Intensive Review Balance Sheet and Income Statement were prepared. It is assumed that the AID loan will include a ten-year grace period. A PL 480 Title IV loan from the GOE to the Cooperative Bank has not yet been completed, but a commitment for 3 million sucres ($165, 000) therefor has been made. The Title IV loan carries .075% interest for 22 years, but the grace period on repayment of principal is only two years. Therefore, commencing with year 2 the Bank may have an additional expense of $8, 750 repayment of principal per year. This amount does not significantly affect the projections made in the Intensive Review statements. It will result in reducing the AID loan to $1, 835, 000. The availability of sucre repayments from prior yea L 480 and development loan transactions, and their potential use with the AID loan, could not be assessed by the Intensive Review Committee as no prior Agency precedent exists.

CHECK LIST OF STATUTORY CRITERIA (ALLIANCE FOR PROGRESS)

1. Foreign Assistance Act of 1961, as amended (hereinafter FAA), Section 102. The loan will further the policy of the Act, as stated in this Section. Every possible precaution will be taken to assure that loan proceeds are not diverted to short-term emergency purposes (such as budgetary purposes, balance of payments purposes, or military purposes) or any other purpose not essential to the long-range economic development of Ecuador.

2. FAA Section 201(d). Loan funds are not to be loaned or re-loaned at rates of interest which are excessive or unreasonable for the Borrower, or higher than the applicable legal rate of interest in Ecuador. (Section F.2).

3. FAA Section 202(c), Foreign Aid and Related Agencies Appropriation Act of 1964 (hereinafter "App."), Section 117. Funds have been appropriated by Congress for this loan.

4. FAA Section 204. The terms and conditions of the loan are in accordance with standards and criteria established by the Development Loan Committee.

5. FAA Section 251(a). The loan will promote economic development in Ecuador and will contribute to the welfare of its people. (Section C.)

6. FAA Section 251(b)(1). Account has been taken of the extent to which Ecuador is adhering to the principles of the Act of Bogota and Charter of Punta del Este and is showing a responsiveness to the vital economic, political, and social concerns of its people, and of the extent to which Ecuador has demonstrated a clear determination to take effective self-help measures. (Section C)

7. FAA Section 251(b)(2). The activity to be financed is economically and technically sound. (Sections D, E, and F).

8. FAA Section 251(b)(3). The activity is consistent with and is related to other development activities being undert n or planned and will contribute to realizable long-range objecti . (Section C)

9. FAA Section 251(b)(4). The loan will have no foreseeable adverse effect on the U. S. economy. (Section H)

10. FAA Section 251(b). Financing from other free world sources (including private sources within the United States) on reasonable terms for the project is not available. (Section C)

11. FAA Section 251(b). The terms of the loan (interest, year amortization) are reasonable under circumstances affecting the loan and the capacity of Borrower to repay. (Section G)

\# 12. FAA Section 251(b). Account has been taken of the extent to which Ecuador is making reasonable efforts to encourage repatriation of capital invested in other countries by its own citizens. (Annex I, Paragraph B.4(a) of Consortium Road Loan - AID-DLC/P-174 Revised).

\# *13. FAA Section 251(b). There are reasonable prospects that the loan will be repaid. (Section G)

* 14. FAA Section 251(e). An application has been received for this loan which gives sufficient information and assurances to indicate reasonably that the funds will be used in an economically and technically sound manner.

15. FAA Section 251(g). This loan will assist in promoting the cooperative movement in Latin America.

\# * 16. FAA Sections 601(b); 621. The loan will be administered in such a manner as to encourage and facilitate participation by private enterprise to the maximum extent practicable. United States private engineering services, and other services of United States private enterprise will be employed whenever practicable. The facilities of other Federal agencies will be utilized only if they are particularly suitable, are not competitive with private enterprise, and can be made available without undue interference with domestic programs.

17. FAA Section 602. American small business shall be assisted to the maximum extent practicable to participate equitably in the furnishing of goods and services for the project, in accordance with the procedures described in this section of the Act.

* 18. FAA Section 604(a). Equipment, materials, and services (except Marine Insurance) financed for the project under the loan shall be procured from the United States or Ecuador . Dollars utilized under the loan to finance procurement in Ecuador shall be made available through appropriate procedures and, except for Marine Insurance, shall be used only for procurement in the United States. (Sections K.1 and H)

* 19. FAA Section 604(b). Any commodities financed by the loan and purchased in bulk will be purchased at prices no higher than prevailing U. S. market prices.

* 20. FAA Section 604(d). Loan funds shall be available for Marine Insurance on commodities shipped when such insurance is placed on a competitive basis, as specified in this section of the Act. In the event that Ecuador discriminates against any U. S. marine insurance company, commodities purchased with loan funds shall be insured against marine risk with a U. S. company, as required by this section.

* 21. FAA Section 611(a)(1). Necessary substantive technical and financial planning for the project has been completed, and a reasonably firm estimate of cost of the project to the United States has been obtained. (Section F)

* 22. FAA Section 611(a)(2). A Cooperative Bank Law, which is legislative action required to implement the project, has been passed. A draft amendment to strengthen the Law has been prepared and is under active study by the GOE (Annexes II and III.)

* 23. FAA Section 611(b), App. Section 101. The project does not involve water or related land resource construction.

* 24. FAA Section 611(c). Construction contracts to be financed by the loan shall to the maximum extent practicable be let on a competitive basis.

* 25. FAA Section 619. Not applicable. Ecuador is not a newly independent country.

* 26. FAA Section 620(a), App. Sections 109(a), 109(b). No assistance will be furnished under this loan to the present government of Cuba, nor does Ecuador furnish assistance to the present government of Cuba. has taken appropriate steps to prevent ships or aircraft under its registry from engaging in any Cuba trade.

* 27. FAA Section 620(b). The Secretary of State has determined that Ecuador is not controlled by the International Communist Movement.

28. AID is satisfied that Ecuador is not in violation of this Sec. which requires that no assistance will be provided to a government which is indebted to any U.S. citizen for goods or services furnished or ordered, where such a citizen has exhausted available legal remedies or where the debt is not denied or contested by or the indebtedness arises under an unconditional guaranty of payment given by Ecuador

* 29. FAA Section 620(d). Loan funds will not finance construction or operation of any productive enterprise which will compete with United States enterprise.

* 30. FAA Section 620(e). Neither the government of Ecuador nor any governmental agency or subdivision thereof has, on or after January 1, 1962, nationalized, expropriated, or seized ownership or control of property of any U. S. citizen or firm, taken steps to repudiate or nullify existing contracts with such citizens or firms, or imposed or enforced discriminatory taxation or other exactions or restrictive conditions, or taken other actions having the effect of nationalizing, expropriating or otherwise seizing ownership or control of property owned by U. S. citizens or firms, as specified in this section of the Act, without taking appropriate steps to discharge its obligations, as specified in this section of the Act.

* 31. FAA Section 620(f), App. Sections 109(a), 109(b). Assistance provided by this loan will not be furnished to any Communist country.

* 32. FAA Section 620(g). Assistance provided by this loan will not be used to compensate for expropriated or nationalized property.

* 33. FAA Section 620(h). Assistance provided by this loan will not be used in a manner which promotes or assists foreign aid projects or activities of the Communist bloc countries. (Section A.11)

* 34. FAA Section 620(i). The President has not determined that Ecuador is engaging in or preparing for aggressive military efforts directed against the United States, or any country receiving assistance from the United States, or against any country to which sales are made under PL 480, nor is any basis for such determination known to A.I.D.

* 35. FAA Section 636(h). Ecuador will contribute local currency in the amount of $744,000 to meet the cost of contractual and other services to be rendered in conjunction with the project. Foreign currency owned by the United States will, to the maximum extent possible, be ut ized to meet the costs of contractual and other serv s for the project. (Section F.1(a)).

* 36. App. Section 102. Obligations of funds in excess of $25,000 for engineering fees to any firms or group of firms financed under the loan will be reported to the committees on appropriations of the Senate and House.

* 37. App. Section 104. Funds obligated by the loan, and local currency generated thereby, will not be used to pay pensions, annunities, etc., as prohibited in this section.

* 38. App. Section 111. U. S. personnel to serve under contracts for services financed by the loan shall have security clearance.

* 39. App. Section 112. Firms which provide engineering, procurement, and construction services financed by the loan for the project, and the terms of their contracts, shall be approved by A.I.D.

* 40. App. Section 114. Loan funds will not be used to make any payment to the U. N.

* 41. App. Section 118. Construction work financed by the loan shall be performed by qualified persons, in accordance with A.I.D. regulations promulgated pursuant to this section.

* 42. App. Section 601. Loan funds will not be used for publicity or propaganda purposes within the United States.

R. J. Apton
Chairman, Project Committee

CLEARANCE: Counsel GFlood
Desk ECoy
Coop. Division RBonham

LOAN AUTHORIZATION

Provided from: Alliance for Progress Funds
ECUADOR: Cooperative Bank

Pursuant to the authority vested in the Deputy U.S. Coordinator, Alliance for Progress, by the Foreign Assistance Act of 1961, as amended, and the delegations of authority issued thereunder, I hereby authorize the establishment of a loan pursuant to Part I, Chapter 2, Title VI, Alliance for Progress, to the Cooperative Bank of Ecuador ("Borrower") of not to exceed one million two hundred thousand United States dollars ($1,200,000) to be used for subloans to members of Borrower to assist in financing the development of the cooperative and credit union movement in Ecuador, this loan to be subject to the following terms and conditions:

1. Interest and Terms of Repayment.

   (a) Borrower shall repay the loan to the Agency for International Development ("A.I.D.") in United States dollars within twenty-five (25) years from the first disbursement under the loan, including a grace period of not to exceed ten (10) years. Borrower shall pay to A.I.D. in United States dollars on outstanding principal of the loan interest of three-quarters of one (3/4 of 1) percent per annum during the grace period and two (2) percent per annum thereafter.

   (b) If, prior to the date when the first interest payment is due, the Government of Ecuador ("Government") so elects, the Borrower shall fulfill its dollar obligations under the loan by paying to Government in the currency of Ecuador the equivalent, determined as of a time and in a manner satisfactory to A.I.D., of the United States dollar amounts payable to A.I.D. under (a) above and in such event the Government shall pay to A.I.D.:

      (i) the equivalent in United States dollars, determined as of a time and in a manner calculated to obtain repayment of all dollars disbursed plus interest, of all amounts paid to Government by Borrower as follows:

(a) All interest immediately upon receipt;

(b) Principal within forty (40) years, including a grace period of not to exceed ten (10) years from the first disbursement under the loan.

(ii) interest in United States dollars of three-quarters of one (3/4 of 1) percent per annum during the grace period and two (2) percent per annum thereafter, on all amounts of outstanding principal paid by Borrower to Government from the respective dates of such payments of principal.

2. Other Terms and Conditions.

(a) Equipment, materials and services (except marine insurance) financed under the loan shall be procured from the United States of America or Ecuador.

(b) United States dollars utilized under the loan to finance local costs shall be made available to the Borrower or its designee through appropriate procedures and shall be used only for procurement in the United States (excepting marine insurance).

(c) Prior to signing the Loan Agreement, Borrower will submit evidence, in form and substance satisfactory to A.I.D., that it has been duly established as a cooperative bank in accordance with Ecuadorean law.

(d) Borrower shall obtain U.S. advisory services satisfactory to A.I.D.

(e) Prior to the first disbursement under the Loan Agreement, and at such later times as A.I.D. shall determine, Government and the members of Borrower shall make contributions to Borrower in amounts agreeable to A.I.D.

(f) Government shall guarantee repayment of the principal of and interest on the loan.

(g) Borrower will adopt measures, satisfactory to A.I.D., for preventing subloans financed by A.I.D. from being made to members dominated by Communists.

(h) The loan shall be subject to such other terms and conditions as A.I.D. may deem advisable.

____
Deputy U.S. Coordinator
Alliance for Progress

____
Date

Clearances:

Chrm.Proj.Com.RApton	________	________
LA/DP:RSternfeld	________	________
LA/GC:DBronheim	________	________
LA/CD:PGlaessner	________	________
A/CONT:EFTennant	________	________

Drafted:GFFlood:cda:LA/GC:6/1/64